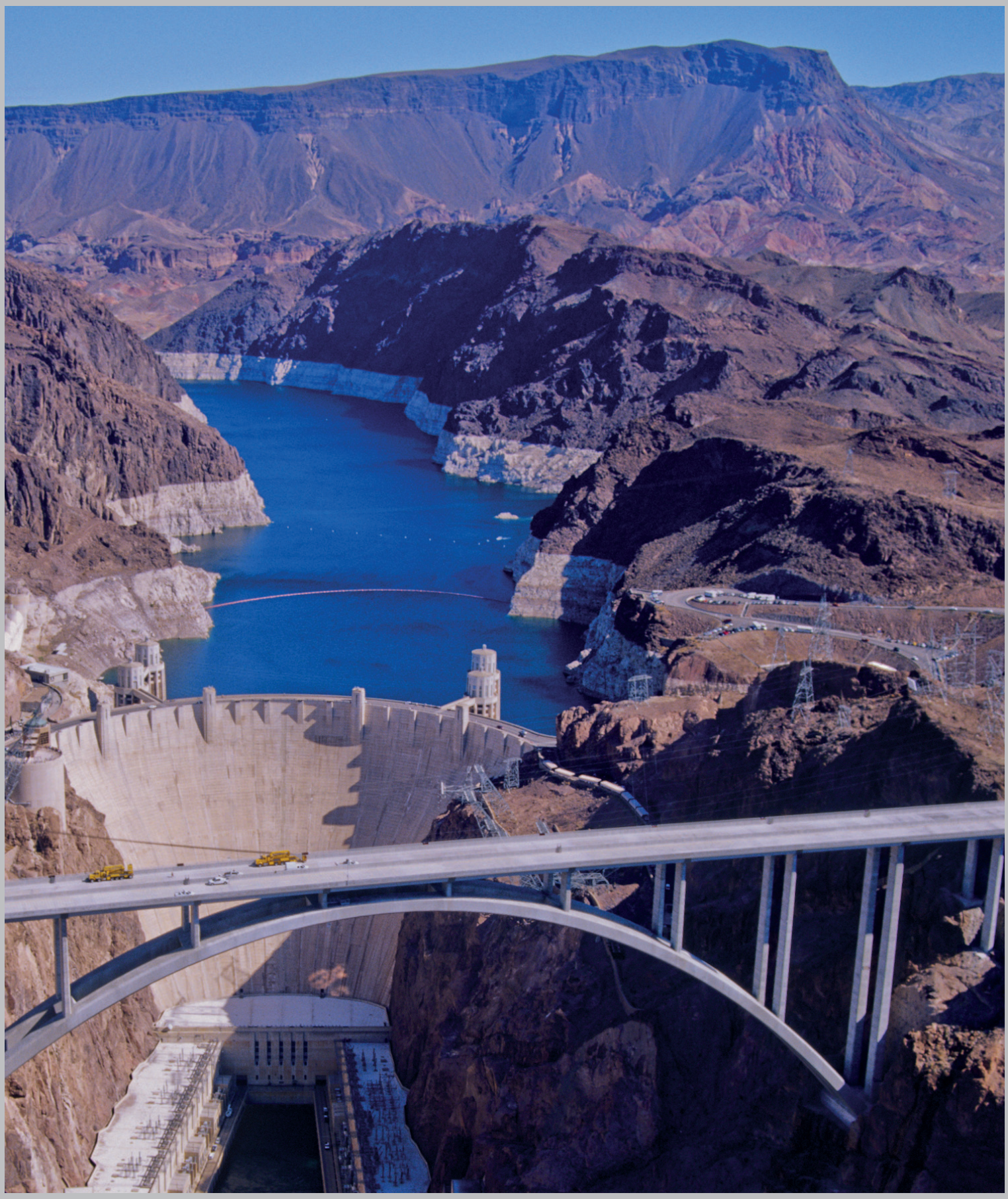

U.S. Department of Transportation
Agency Financial Report Fiscal Year 2010

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Cover and header photograph of the
Colorado Bridge courtesy of
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Federal Highway Administration.

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Other Accompanying Information

FOREWORD

The United States Department of Transportation's (DOT or Department) Agency Financial Report (AFR) for fiscal year (FY) 2010 provides an overview of the Department's financial performance and results to Congress, the President and the American people. The report details information about our stewardship over the financial resources entrusted to us. Additionally, the report provides information about our performance as an organization, our achievements, initiatives and our challenges.

The AFR is the first in a series of reports required under the Office of Management and Budget's Program for Alternative Approaches to Performance and Accountability Reporting. This is the first year that the Department has participated in this voluntary program in an effort to strengthen its annual reporting documents and to present more streamlined and timely information to clarify the relationship between performance, budgetary resources and financial reporting. The Department intends to provide a more meaningful, transparent and easily understood analysis of accountability over its resources. The report provides readers with an overview of the Department's highest priorities, as well as our strengths and challenges.

The Department's FY 2010 annual reporting includes the following three components:

Agency Financial Report (AFR) [available November 2010]

The AFR, the following report, is organized into three major sections:

- The Management's Discussion and Analysis section provides executive-level information on the Department's history, mission, organization, key activities, analysis of financial statements, systems, controls and legal compliance, accomplishments for the fiscal year and management and performance challenges facing the Department.
- The Financial Details section provides a Message From the Chief Financial Officer, consolidated and combined financial statements, the Department's notes to the financial statements and the Report of the Independent Auditors.
- The Other Accompanying Information section provides Improper Payments Information Act reporting details and other statutory reporting requirements.

Annual Performance Report (APR) [available February 2011]

The APR will be produced in conjunction with the FY 2011 President's Budget Request and will provide the detailed performance information and descriptions of results by each key performance measure.

FY 2010 Summary of Performance and Financial Information [available February 2011]

This document will provide an integrated overview of performance and financial information that integrate the AFR and the APR into a user-friendly consolidated format.

This report satisfies the reporting requirements of the following major legislation:

- Reports Consolidation Act of 2000
- Government Performance and Results Act of 1993
- Chief Financial Officers Act of 1990
- Government Management Reform Act of 1994
- Federal Managers' Financial Integrity Act of 1982
- Federal Financial Management Improvement Act of 1996
- Improper Payments Information Act of 2002

All three reports will be available on the Department's Web site at:
http://www.dot.gov/about.html#perfbudgplan

Message from the Secretary

MESSAGE FROM THE SECRETARY

I am pleased to present the U.S. Department of Transportation's (DOT) Agency Financial Report. As required by statute, this material provides reliable and complete data on DOT's financial operations and performance for the fiscal year (FY) that ended September 30, 2010 (FY 2010). Together with our Annual Performance Report that will be released in February 2011, these two documents are presented this year as an alternative to the consolidated Performance and Accountability Report that was prepared and submitted in the past. Our nearly $77 billion budget, summarized below, focuses on DOT's many efforts over the past year to improve safety and reduce congestion in each of the Nation's major transportation systems. We have made significant progress in these areas.

RECOVERY ACT IMPLEMENTATION

Fiscal Year 2010 marks the second year of DOT's implementation of the American Recovery and Reinvestment Act of 2009, and DOT's programs continue to generate worthwhile jobs through careful investments in useful transportation infrastructure. The $48.1 billion appropriated to DOT has been used to support more than 15,000 infrastructure projects. These investments have improved the safety and efficiency of the Nation's system of highways, transit, ports, and airports. Just as important, these projects generated tens of thousands of jobs in transportation and related sectors, in a difficult economic environment.

INCREASE SAFETY

The most important issue DOT addresses is public safety. We have made tremendous strides over the decades through a variety of solutions, such as auto manufacturing safety standards, commercial driver regulations, and public awareness. Our most pressing concern, highway fatalities, accounts for about 95 percent of transportation deaths each year; therefore, we have devoted substantial attention in 2010 to targeted highway safety initiatives. Through these efforts, traffic fatalities in the United States have fallen to a historic 60-year low. The record-breaking decline occurred even while estimated vehicle-miles traveled increased. The data show that the number of people who died on the

nation's roads fell nearly 10 percent from 2008 to 2009, the latest year of available data. This is the lowest total since 1950, when over 33,000 people were killed, with only one-fifth of the number of vehicles on the road. In support of this notable success, some of DOT's initiatives in 2010 included major steps to reduce distracted driving, the development of a new five-star vehicle safety system to assist consumers, and the establishment of a new Transportation Safety Council.

Action to Stop Distracted Driving - Building on the ground-breaking 2009 Distracted Driving Summit, I launched a second Distracted Driving Summit in 2010 with the announcement of several new programs, including regulations to stop commercial truck and bus operators from texting behind the wheel, pilot programs to enforce cell phone bans, and new rules to revoke commercial licenses for school bus drivers convicted of texting while driving. Further, the Department developed tough model distracted driving legislation for States to use in crafting their own bills. I also announced the creation of FocusDriven, the first national nonprofit organization devoted specifically to raising awareness about the dangers of distracted driving.

Tougher Five-Star Safety System - The DOT announced a significant improvement to its five-star vehicle rating system in 2010, which now includes ratings on a vehicle's ability to withstand a frontal crash and a side crash, as well as its resistance to roll-overs during a crash. The new system, which will provide an overall rating score, will be applied to model year 2011 vehicles and beyond. New tests, better crash data, and higher standards are making the ratings tougher and more meaningful for consumers.

New Safety Council - In October 2009, I convened the first DOT Safety Council to address the top safety issues that cut across all modes of transportation. I created this council to serve a broad-based safety leadership role and help break down organizational stovepipes, enabling an even stronger safety culture. Sharing data, research, and best practices among the 10 agencies on the council will result in new ideas and new perspectives on safety issues.

REDUCE CONGESTION

Over many years, we have seen increased mobility among Americans, and we now are seeing the effects of our very mobile society, namely increased congestion. Our ability to move people and goods across the domestic transportation system has become insufficient for modern transportation patterns. Americans already lose over four billion hours and nearly three billion gallons of fuel sitting in traffic jams annually, yet highway vehi-

cle-miles traveled have been projected to grow substantially by 2030. This increases the likelihood of greater congestion. As challenging as the issue of highway congestion is, we see similar issues in air transportation. We know that we are not meeting our targets for on-time performance in air travel, although approximately 70 percent of the delays are caused by weather. By 2025, air traffic is projected to increase at least twofold, placing additional demands on the system. In 2010, DOT has continued to implement several initiatives to address congestion throughout the Nation's transportation system, including the Federal Aviation Administration's (FAA) NextGen program, which is modernizing the air traffic control system, new high-speed rail projects, and a program to promote livable communities around urban transportation hubs.

Next Generation Air Transportation System (NexGen) - Over the next 20 years, NextGen is being deployed to improve our air traffic management procedures so that aircraft can choose more efficient routes and make quicker in-flight decisions to avoid other traffic and weather by replacing World War II-era, ground-based radar technology with satellite operations. As part of this long-term modernization project, in 2010 FAA launched a full-scale, nationwide deployment of the satellite-based surveillance system called Automatic Dependent Surveillance - Broadcast (ADS-B), following its successful roll-out at four key sites. The new system tracks aircraft with greater accuracy, integrity, and reliability than the current radar-based system.

High-Speed Rail - President Obama's bold vision for high-speed rail is a game changer for the U.S. transportation system. With an initial $8 billion investment, the Department laid the groundwork for development of an efficient, high-speed passenger rail network of 100 to 600 mile intercity corridors that represent an essential component of a modernized, nationwide system. The popularity of the program was evident in the 2010 grant announcements, where demand for funding greatly exceeded the money available.

Livable Communities - During 2010, the Administration announced the Nation's first Livable Communities initiative, which will measurably enhance the quality of life for families, workers, and communities across America. This translates into Federal support for more transportation choices, more public transportation, and more commercial and residential development around transportation hubs. In August, DOT and the U.S. Department of Housing and Urban Development jointly announced the availability of $75 million for Community Challenge and Transportation Planning Grants. Communities will use the funds to integrate planning and design for livable communities and the surface transportation systems that are essential to achieving the desired level of livability.

In addition to DOT's programs to enhance safety and reduce congestion, I want to highlight our success during 2010 in taking a significant step toward cleaner air and energy efficiency. Responding to one of the first major directives of the Obama Administration, DOT and the Environmental Protection Agency jointly established a historic new corporate average fuel economy (CAFE) standard that requires cars and light trucks to average 34.1 miles per gallon by 2016. The new standard will conserve about 1.8 billion barrels of oil over the lifetime of the vehicles regulated.

In conclusion, I am proud of the work we are doing at the U.S. Department of Transportation. We have made significant progress in 2010 on some of the most important issues facing our transportation system. As we look to 2011, the Department and its dedicated employees embrace the challenge of continuing this year's record of achievement in addressing the Nation's most pressing transportation and infrastructure needs.

Ray LaHood
November 8, 2010

Management's Discussion and Analysis

UNITED STATES
DEPARTMENT OF TRANSPORTATION

MISSION AND VALUES

MISSION

The Department's mission is to serve the United States by ensuring a fast, safe, efficient, accessible and convenient transportation system that meets our vital national interests and enhances the quality of life of the American people, today and into the future.

VALUES

Professionalism

As accountable public servants, we exemplify the highest standards of excellence, integrity, and respect in the work environment.

Teamwork

We support each other, respect differences in people and ideas, and work together in ONE DOT fashion.

Customer Focus

We strive to understand and meet the needs of our customers through service, innovation, and creativity. We are dedicated to delivering results that matter to the American people.

ORGANIZATION

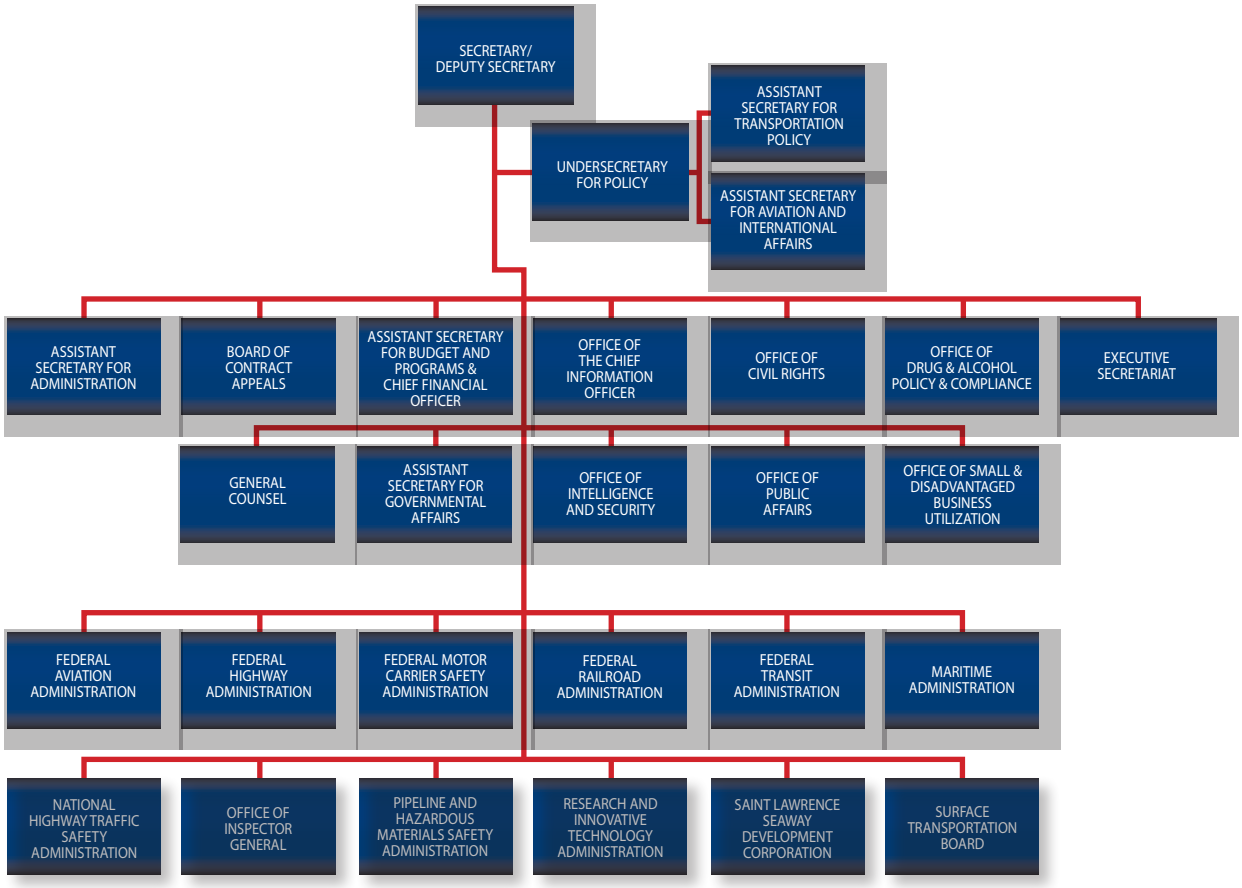
HISTORY

Established in 1967, DOT sets Federal transportation policy and works with State, local, and private sector partners to promote a safe, secure, efficient, and interconnected National transportation system of roads, railways, pipelines, airways, and seaways. DOT's overall objective of creating a safer, simpler, and smarter transportation program is the guiding principle as we move forward to achieve specific goals.

HOW WE ARE ORGANIZED

DOT employs almost 60,000 people across the country, in the Office of the Secretary of Transportation (OST) and through twelve Operating Administrations (OAs) and bureaus, each with its own management and organizational structure.

The Office of the Secretary of Transportation provides overall leadership and management direction, administers aviation economic programs, and provides administrative support. The Office of Inspector General (OIG) and the Surface Transportation Board (STB), while formally part of DOT, are independent by law.



OVERVIEW OF LEGISLATIVE AUTHORITIES

The DOT strategic plan summarizes the legislative authorities of each Operating Administration. To provide a context for the reader, highlights of the responsibilities of each Operating Administration are listed below.

Office of the Secretary. The Office of the Secretary (OST) oversees the formulation of national transportation policy and promotes intermodal transportation. Other responsibilities range from negotiation and implementation of international transportation agreements, assuring the fitness of U.S. airlines, enforcing airline consumer protection regulations, issuance of regulations to prevent alcohol and illegal drug use in transportation systems and preparing transportation legislation.

Federal Aviation Administration. The Federal Aviation Administration's (FAA) mission is to promote aviation safety and mobility by building, maintaining, and operating the Nation's air traffic control system; overseeing commercial and general aviation safety through regulation and inspection; and providing assistance to improve the capacity and safety of our airports.

Federal Highway Administration. The mission of the Federal Highway Administration (FHWA) is to enhance mobility through innovation, leadership, and public service.

Federal Motor Carrier Safety Administration. The Federal Motor Carrier Safety Administration's (FMCSA) primary mission is to prevent commercial motor vehicle-related fatalities and injuries.

Federal Railroad Administration. The Federal Railroad Administration's (FRA) mission is to ensure that our Nation has safe, secure, and efficient rail transportation that enhances the quality of life for all.

Federal Transit Administration. The Federal Transit Administration (FTA) provides leadership, technical assistance, and financial resources for safe, technologically advanced public transportation that enhances mobility and accessibility, improves America's communities, preserves the natural environment, advances economic growth, and ensures that transit systems are prepared to function during and after criminal or terrorist attack.

Maritime Administration. The Maritime Administration's (MARAD) mission is to promote the development and maintenance of an adequate, well-balanced U.S. merchant marine that is sufficient to carry the Nation's domestic waterborne commerce and a substantial portion of its waterborne foreign commerce, and to serve as a naval and military auxiliary in time of war or national emergency.

National Highway Traffic Safety Administration. The National Highway Traffic Safety Administration's (NHTSA) mission is to save lives, prevent injuries and reduce economic costs due to road traffic crashes through education, research, safety standards, and enforcement activity.

Office of Inspector General. The Inspector General Act of 1978, as amended, established the Office of Inspector General (OIG) as an independent and objective organization within the DOT. The OIG's mission is to promote economy, effectiveness, and efficiency and to prevent and detect fraud, waste, and abuse in DOT operations and programs by conducting and supervising independent and objective audits and investigations.

Pipeline and Hazardous Materials Safety Administration. The Pipeline and Hazardous Materials Safety Administration (PHMSA) is dedicated to safety and security by working toward the elimination of transportation-related deaths and injuries in hazardous materials and pipeline transportation, and by promoting transportation solutions that enhance communities and protect the natural environment.

Research and Innovative Technology Administration. The Research and Innovative Technology Administration (RITA) is dedicated solely to the advancement of DOT priorities for innovation and research in transportation technologies and concepts. Innovations that will improve our mobility, promote economic growth, and ultimately deliver a better integrated transportation system.

Saint Lawrence Seaway Development Corporation. The U.S. Saint Lawrence Seaway Development Corporation (SLSDC), a wholly owned government corporation and an OA of DOT, is responsible for the operations and maintenance of the U.S. portion of the St. Lawrence Seaway between Montreal and Lake Erie.

Surface Transportation Board. The Surface Transportation Board (STB) is charged with promoting substantive and procedural regulatory reform in the economic regulation of surface transportation, and with providing an efficient and effective forum for the resolution of disputes and the facilitation of appropriate business transactions.

PERFORMANCE HIGHLIGHTS

The Department of Transportation (DOT) achieved an historic milestone this year: traffic fatalities in the U.S. have fallen to an historic 60-year low. Highway fatalities for 2009 (the latest data available) fell 10% from the previous year to a total of 33,808. Not since 1950, when our roads carried far less traffic, have traffic fatalities been this low.

The Department met nearly 80% of its performance targets for the year. Like every government agency, however, there are areas that we can improve upon. A brief discussion of our results by strategic objective follows.

SAFETY

DOT tracks the safety of Americans on the highways, in the air, on transit systems, and on railroads. In FY 2010 we met 9 out of 10 safety goals. Fatalities in general aviation, particularly from amateur-built aircraft, however, did not decline as quickly as anticipated. To address this issue, FAA has established a Flight Standardization Board for Experimental Amateur-built Aircraft.

REDUCED CONGESTION

One of DOT's strategic objectives is to reduce congestion across the modes of transportation. We do this in a variety of ways, from providing funds that keep our highways in a state of good repair, managing air traffic efficiently, and encouraging the use of mass transit in order to reduce traffic on roadways. For the first time in many years, the Department saw a contraction this year in the number of people across the country using mass transit. Ridership fell for several reasons: a general decline in the economy, relatively high unemployment, and a decline in state and local tax revenues used to support transit. Ridership levels, however, are expected to improve as the economy advances and transit agencies begin to restore services and routes cut during the recession.

GLOBAL CONNECTIVITY

DOT contributes to the economy and American businesses' connection with markets across the world by moving products, goods and vehicles with as little delay as possible. In FY 2010, the St. Lawrence Seaway, which is a vital waterway between the upper Midwest and global markets, was open 99.8% of the shipping season. On the roadways, we continue to make progress in limiting delays at border crossings and improving the flow of traffic in freight corridors.

ENVIRONMENTAL STEWARDSHIP

The transportation system has a significant impact on the environment and DOT mitigates that impact whenever possible. For the third year in a row, there were no violations of air pollution standards in major metropolitan areas. Streamlining the process for completing environmental impact statements, however, continues to be a challenge.

SECURITY, PREPAREDNESS AND RESPONSE

While the Department of Homeland Security has primary responsibility for the security of the transportation system, DOT must ensure it is prepared to continue operating during a crisis. To this end, DOT tracks the readiness of key staff and member agencies. DOT has a role in supporting the Department of Defense during military mobilization. For the third year in a row we have exceeded the readiness requirements for shipping capacity and commercial ports.

ORGANIZATIONAL EXCELLENCE

Mindful of the need to wisely use taxpayer money, DOT tracks the cost and scheduling associated with major system purchases and major infrastructure projects. Although we did not make our cost and schedule targets for major infrastructure projects as a whole, we are seeing improvements within individual projects. DOT agencies will continue to review the finance plans, project management plans, and cost estimates that are required for each major project, and will continue to offer training to engineering and financial management staff on these specific responsibilities.

PERFORMANCE SUMMARY TABLES

SAFETY PERFORMANCE SUMMARY

Performance Measure	2004	2005	2006	2007	2008	2009	2010 Actual	2010 Target	Met/ Not Met
Passenger vehicle occupant highway fatality rate per 100 million passenger vehicle-miles traveled (VMT).	1.17	1.15	1.10	1.04	1.03	.98 – 1.04#	.87#	.99	Met
Large truck and bus fatality rate per 100 million total VMT.	N/A	0.185	0.177	0.169	0.155	0.140 – 0.154#	.108 - .119#	.164	Met
Motorcyclist fatality rate per 100,000 motorcycle registrations.	69.83	73.48	72.42	72.48	71.30	73.75 – 74.96#	65#	78	Met
Non-occupant fatality rate per 100 million VMT	0.19	0.20	0.19	0.18	0.18	0.18 - 0.19#	.16#	.19	Met
Number of commercial air carrier fatalities per 100 million persons onboard	N/A	N/A	N/A	N/A	0.4	6.8*	0.3*	8.1	Met
Fatal Accidents per 100,000 Flight Hours in General Aviation	N/A	N/A	N/A	N/A	N/A	1.17*	1.17#	1.10	Not Met
Rail-related accidents and incidents per million train-miles	19.03r	18.09r	17.59r	17.36r	16.88r	16.71r	15.90*	16.40	Met
Transit fatalities per 100 million passenger-miles traveled	0.467	0.428	0.389	0.437	0.332	0.243*	0.188	0. 458	Met
Number of serious incidents for natural gas and hazardous liquid pipelines	48	41	35	47	41	50	38#	30-43	Met
Number of serious hazardous materials transportation incidents	35	49	32	36	23	29	16#	22-36	Met

(r) Revised; * Preliminary estimate; # Projection from trends; Met; Not Met

REDUCED CONGESTION SUMMARY

Performance Measure	2004	2005	2006	2007	2008	2009	2010 Actual	2010 Target	Met/ Not Met
Percentage of travel on the National Highway System (NHS) meeting pavement performance standards for "good" rated ride.	52	52	54	57	56	57	Data Available December 2010	58	TBD
Percentage of deck area on National Highway System (NHS) bridges rated as deficient, adjusted for average daily traffic.	32.0	29.9	29.2	29.7	29.5	29.2	28.7	28.9	Met
Percentage of total annual urban area travel occurring in congested conditions	28.6	28.6	28.4	27.8	26.3	26.6#	26.8#	27.1	Met
Average percent change in transit boardings per transit market (150 largest transit agencies)	0.7	1.9	2.1	2.5	4.3	2.2	-2.9	2.0	Not Met
Percent of bus fleets compliant with the Americans with Disabilities Act (ADA)	96	96	97	98	98	98	98	98	Met
Percent of key rail stations compliant with the ADA.	82	91	92	93	95	95	95.2	94.5	Met
Percent of all flights arriving within 15 minutes of schedule at the 35 Operational Evolution Partnership airports due to National Airspace System related delays.	79.07	88.44	88.36	86.96	87.29	88.98(r)	90.56#	88.00%	Met

(r) Revised; * Preliminary estimate; # Projection from trends; Met; Not Met

GLOBAL CONNECTIVITY PERFORMANCE SUMMARY

Performance Measure	2004	2005	2006	2007	2008	2009	2010 Actual	2010 Target	Met/ Not Met
Percent of days in the shipping season that the U.S. portion of the St. Lawrence Seaway system is available.	99.1	99.7	99.0	99.4	98.8	99.4	99.8	99.0	Met
Number of freight corridors with an annual decrease in the average buffer index rating.	N/A	N/A	3	5	21	19	14	13#	Met
Number of National Highway System border crossings with a decrease in unexpected delay.	N/A	N/A	N/A	4	3	3	5	5	Met
Percent share of the total dollar value of DOT direct contracts that are awarded to women-owned businesses.	3.8	6.6	8.4	10.4	7.0	9.0	8.0*	5.1	Met
Percent share of the total dollar value of DOT direct contracts that are awarded to small disadvantaged businesses.	15.6	12.7	16.2	18	16	15.5	14.57*	14.5	Met

(r) Revised; * Preliminary estimate; # Projection from trends; Met; Not Met

ENVIRONMENTAL STEWARDSHIP PERFORMANCE SUMMARY

Performance Measure	2004	2005	2006	2007	2008	2009	2010 Actual	2010 Target	Met/ Not Met
Number of areas in conformity lapse	6.3	5.8	1.3	0.0	0.0	0.0	0	3	Met
Number of hazardous liquid pipeline spills with environmental consequences	138	127	106	97	128	110	93#	89-108	Met
Number of Exemplary Human Environmental Initiatives undertaken	N/A	N/A	N/A	N/A	11	16	10	10	Met
Median time in months to complete environmental impact statements for DOT funded infrastructure projects	N/A	56	57	67	63.5	79.3	63.9	48	Not Met

(r) Revised; * Preliminary estimate; # Projection from trends; Met; Not Met

SECURITY PERFORMANCE SUMMARY

Performance Measure	2004	2005	2006	2007	2008	2009	2010 Actual	2010 Target	Met/ Not Met
Percentage of DoD-required shipping capacity complete with crews available within mobilization timelines.	94	95	93	97	97	96*	96	94	Met
Percentage of DoD-designated commercial ports available for military use within DoD established readiness timelines.	93	87	100	100	100	100*	100	93	Met
Percent of DOT personnel with emergency management responsibilities who are prepared to respond to disasters and emergencies.	N/A	N/A	N/A	N/A	N/A	100	100	100	Met
Percent of DOT agencies meeting annual response requirements.	N/A	N/A	N/A	N/A	N/A	96	96	100	Not Met

(r) Revised; * Preliminary estimate; # Projection from trends; Met; Not Met

ORGANIZATIONAL EXCELLENCE PERFORMANCE SUMMARY

Performance Measure	2004	2005	2006	2007	2008	2009	2010 Actual	2010 Target	Met/ Not Met
Percent of major federally funded transportation infrastructure projects with less than 2 percent annual growth in the project completion milestone as reported in the finance plan.	73	89	89	89	79	78	84	90	Not Met
Percent of finance plan cost estimated for major federally funded transportation infrastructure projects with less than 2 percent annual growth in project completion cost.	75	81	84	83	82	84	84	90	Not Met
For major DOT aviation systems, percentage of cost goals established in the acquisitions project baselines that are met.	100	97.00	100	100	96.08	100	97.06	90	Met
For major DOT aviation systems, percentage of scheduled milestones established in acquisition project baselines that are met.	91.50	92.00	97.44	97.00	93.88	93.75	90.74	90	Met

(r) Revised; * Preliminary estimate; # Projection from trends; Met; Not Met

FINANCIAL HIGHLIGHTS

The presentation of the financial statements represents the Department's cumulative efforts to improve financial management and to provide accurate and reliable financial information that is useful for assessing performance. Department management is responsible for the integrity and fair presentation of the financial information presented in these statements.

The financial statements and financial data presented in this Report have been prepared from the accounting books and records of the Department of Transportation in conformity with generally accepted accounting principles (GAAP). GAAP for Federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board (FASAB).

The Hiring Incentives to Restore Employment (HIRE) Act of 2010, the American Recovery and Reinvestment Act of 2009 (ARRA or the Recovery Act) and the Car Allowance Rebate System (CARS) program of 2009 have each had a significant impact on the financial statements of the Department and caused significant fluctuations when comparing FY 2010 to FY 2009 amounts for certain financial statement line items. The HIRE transferred $19.5 billion from the General Fund to the Highway Trust Fund, which is primarily reflected in increased Investments. ARRA provided the Department an additional $48 billion in appropriations in FY 2009, of which $39.6 billion has been obligated and $20.5 billion has been disbursed as of September 30, 2010. The Department received and disbursed an additional $3 billion for the CARS program in FY 2009.

OVERVIEW OF FINANCIAL POSITION

Assets

Overall, the Consolidated Balance Sheet shows Department total assets of $103.8 billion at the end of FY 2010 have remained relatively level with FY 2009. The Fund Balance with Treasury line item decreased by $10.2 billion as ARRA funding provided in FY 2009 continued to be spent down in FY 2010. Conversely, Investments increased by $12.4 billion as a result of new funding provided by HIRE.

The Department's assets reflected in the Consolidated Balance Sheet are summarized in the following table.

ASSETS BY TYPE

Dollars in Thousands	2010	%	2009	%
Fund Balance with Treasury	$52,504,709	50.6	$62,685,783	61.7
Investments	33,050,889	31.9	20,684,481	20.4
General Property, Plant & Equipment	13,907,474	13.4	14,439,603	14.2
Inventory and Related Property, Net	823,603	0.8	797,310	0.8
Direct Loans and Guarantees, Net	2,892,100	2.8	2,219,298	2.2
Accounts Receivable	244,316	0.2	384,754	0.4
Cash and Other Assets	329,250	0.3	294,830	0.3
Total Assets	$103,752,340	100.0	$101,506,059	100.0

Liabilities

The Department's Consolidated Balance Sheet reported total liabilities of $17.3 billion at the end of FY 2010, as summarized in the table below. This represents a slight 2 percent increase from the previous year's total liabilities of $16.9 billion. The largest increase was on the line item Debt and was the result of additional loans made through the Transportation Infrastructure Finance and Innovation Act (TIFIA) program.

LIABILITIES BY TYPE

Dollars in Thousands	2010	%	2009	%
Grant Accrual	$6,965,999	40.4	$6,769,814	40.0
Other Liabilities	4,159,702	24.1	4,444,553	26.3
Accounts Payable	1,717,081	10.0	1,732,169	10.2
Environmental and Disposal Liabilities	1,103,562	6.3	1,195,249	7.1
Debt	3,077,439	17.8	2,478,348	14.6
Loan Guarantees	237,739	1.4	310,710	1.8
Total Liabilities	$17,261,522	100.0	$16,930,842	100.0

Net Position

The Department's Consolidated Balance Sheet and Consolidated Statement of Changes in Net Position report a Net Position of $86.5 billion at the end of FY 2010, a modest 2.3 percent increase from the $84.6 billion from the previous fiscal year. Net Position is the sum of Unexpended Appropriations and Cumulative Results of Operations.

RESULTS OF OPERATIONS

The results of operations are reported in the Consolidated Statement of Net Cost and the Consolidated Statement of Changes in Net Position.

Net Costs

The Department's total net cost of operations for FY 2010 was $78.8 billion.

NET COSTS

Dollars in Thousands	2010	%	2009	%
Surface Transportation	$60,769,477	77.1	$57,597,654	76.4
Air Transportation	16,775,815	21.3	16,288,922	21.6
Maritime Transportation	568,602	0.7	728,687	1.0
Costs Not Assigned to Programs	394,503	0.5	366,041	0.5
Less Earned Revenues Not Attributed to Programs	471	0.001	10,708	0.001
Cross-Cutting Programs	336,506	0.4	327,208	0.4
Net Cost of Operations	$78,844,429	100.00	$75,297,804	100.00

Surface and air costs represent 98.4 percent of the Department's net cost of operations. Surface transportation program costs represent the largest investment for the Department at 77.1 percent of the Department's net cost of operations. Air transportation is the next largest investment for the Department at 21.3 percent of total net cost of operations. The increases in Net Cost are attributed to the Surface and Air Programs.

RESOURCES

Budgetary Resources

The Combined Statement of Budgetary Resources provides information on how budgetary resources were made available to the Department for the year and their status at fiscal year-end. For the 2010 fiscal year, the Department had total budgetary resources of $174.5 billion, which remained on par with FY 2009 levels of $175.6 billion.

RESOURCES

Dollars in Thousands	2010	2009	% Change
Total Budgetary Resources	$174,546,066	$175,644,291	(0.6)
Obligations Incurred	$113,847,631	$117,386,471	(3.0)
Net Outlays	$97,943,743	$80,881,011	21.1

Budget Authority of $164.9 billion consisted of $97.4 billion in appropriations received and $67.5 billion in borrowing and contract authority. The Department's FY 2010 obligations incurred of $113.8 billion were slightly less than FY 2009 obligations incurred of $117.3 billion.

Outlays reflect the actual cash disbursed against previously established obligations. For FY 2010, the Department had net outlays of $97.9 billion, compared to FY 2009 levels of $80.9 billion, an increase of 21.1 percent. As expected, disbursements have increased as the Recovery Act program matures (i.e. as higher levels of obligations from FY 2010 and FY 2009 are liquidated).

HERITAGE ASSETS AND STEWARDSHIP LAND INFORMATION

Heritage assets are property, plant and equipment that are unique for one or more of the following reasons: historical or natural significance; cultural, educational, or artistic importance; or significant architectural characteristics.

Stewardship Land is land and land rights owned by the Federal Government but not acquired for or in connection with items of general property, plant and equipment.

The Department's Heritage assets consist of artifacts, museum and other collections, and buildings and structures. The artifacts and museum and other collections are those of the Maritime Administration. Buildings and structures include Union Station (rail station) in Washington, D.C., which is titled to the Federal Railroad Administration.

The Department holds transportation investments (Stewardship Land) through grant programs, such as the Federal aid highways, mass transit capital investment assistance, and airport planning and development programs.

Financial information for Heritage assets and Stewardship Land is presented under the Financial Report section of this report in the Notes to the Financial Statements and Required Supplementary Information.

LIMITATIONS OF THE FINANCIAL STATEMENTS

The principal financial statements have been prepared to report the financial position and results of operations of the Department of Transportation, pursuant to the requirements of 31 U.S.C. 3515 (b).

These statements have been prepared from the books and records of the Department of Transportation in accordance with GAAP for Federal entities and in formats prescribed by OMB. The statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the U.S. Government.

SYSTEMS, CONTROLS, AND LEGAL COMPLIANCE

FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT (FMFIA)

The FMFIA requires agencies to conduct an annual evaluation of its management controls and financial systems and report the results to the President and Congress. The Secretary of Transportation then prepares an annual Statement of Assurance based on these internal evaluations.

As a subset of the FMFIA Statement of Assurance, DOT is required to report on the effectiveness of internal control over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations, in accordance with the requirements of Appendix A of OMB Circular A-123. A separate discussion on Appendix A is located at the end of this section.

The Secretary of Transportation has provided the President and Congress a qualified Statement of Assurance for FY 2010, based on FISMA results. The Department evaluated its management control systems and financial management systems for the fiscal year ending September 30, 2010. Aside from FISMA results, this evaluation provided reasonable assurance and formed the basis of the Secretary's Statement of Assurance that the objectives of the FMFIA were achieved in FY 2010.

FMFIA ANNUAL ASSURANCE PROCESS

The FMFIA review is an agency self-assessment of the adequacy of financial controls in all areas of the Department's operations – program, administrative, and financial management.

Objectives of Control Mechanisms

1. Financial and other resources are safeguarded from unauthorized use or disposition.
2. Transactions are executed in accordance with authorizations.
3. Records and reports are reliable.
4. Applicable laws, regulations, and policies are observed.
5. Resources are efficiently and effectively managed.
6. Financial systems conform to government-wide standards.

Managers within the Department, being in the best position to know and understand the nature of the problems they face, establish appropriate control mechanisms to ensure

Departmental resources are sufficiently protected from fraud, waste, and abuse, and to meet the intent and requirements of the FMFIA. The head of each Operating Administration and Departmental office submits an annual statement of assurance representing the overall adequacy and effectiveness of management controls within the organization to the Department's Office of Financial Management. FMFIA material weaknesses and material nonconformances are also reported, citing milestones and/or accomplishments. Specific guidance for completing the end of fiscal year assurance statement and reporting on material deficiencies is issued annually by the Department's Office of Financial Management.

CRITERIA FOR REPORTING MATERIAL WEAKNESSES AND NONCONFORMANCES

A material weakness under FMFIA must fall into one or more of the categories below plus merit the attention of the Executive Office of the President and/or the relevant Congressional oversight committees.

Criteria for Reporting a Material Weakness

1. Significant weakness of the safeguards (controls) against waste, loss, unauthorized use or misappropriation of funds, property, or other assets.
2. Violates statutory authority, or results in a conflict of interest.
3. Deprives the public of significant services, or seriously affects safety or the environment.
4. Impairs significantly the fulfillment of the agency's mission.
5. Would result in significant adverse effects on the credibility of the agency.

A material nonconformance under FMFIA must fall into one or more of the categories below plus merit the attention of the Executive Office of the President or the relevant Congressional oversight committees.

Criteria for Reporting a Material Nonconformance

1. Prevent the primary accounting system from centrally controlling financial transactions and resource balances.
2. Prevent compliance of the primary accounting system, subsidiary system, or program system under the Office of Management and Budget Circular A-127.

SUMMARY OF FY 2010 FMFIA MATERIAL WEAKNESSES

Status of Internal Controls (FMFIA Section 2)

The DOT is reporting one material weakness in FY 2010, based on the FY 2009 Federal Information Security Management Act (FISMA) report (the FY 2010 report has not yet been finalized), due to non-compliance with FISMA standards and OMB requirements for information security program and enterprise-level controls.

Status of Financial Management Systems (FMFIA, Section 4)

The DOT is reporting no material weaknesses for FY 2010.

APPENDIX A, INTERNAL CONTROLS OVER FINANCIAL REPORTING

Appendix A of OMB Circular A-123 emphasizes management's responsibility for establishing and maintaining effective internal control over financial reporting. Appendix A requires agencies to maintain documentation of the controls in place and of the assessment process and methodology management used to support its assertion as to the effectiveness of internal control over financial reporting. Agencies are also required to test the controls in place as part of the overall FMFIA assessment process. The assurance statement related to the assessment performed under Appendix A acts as a subset of the Overall Statement of Assurance reported pursuant to Section 2 of the FMFIA legislation. Management's assurance statement as it relates to Appendix A is based on the controls in place as of June 30. The assurance statement is located in the following section of this report.

DOT is reporting a qualified assurance statement on internal controls over financial reporting based on the Department's compliance with FISMA standards. DOT performed in-depth testing of the controls over six focus area business processes for each Operating Administration (OA) including Cost Accounting, Credit Reform and Loans, Financial Reporting, Revenue and Receivables, Environmental Liabilities and Grants Management. Additional testing of high-risk key controls from the remaining eight non-focus area business processes was performed for OAs whose transactions are material to the Department-wide financial statements.

MANAGEMENT ASSURANCES – OMB CIRCULAR A-123

THE SECRETARY OF TRANSPORTATION
WASHINGTON, D.C. 20590
November 8, 2010

The President
The White House
Washington, DC 20500

Dear Mr. President:

I am pleased to report on the effectiveness of the internal controls and financial management systems for the U.S. Department of Transportation (DOT) during Fiscal Year (FY) 2010. This report is based on our successful implementation under the Federal Managers' Financial Integrity Act of 1982 (FMFIA); Office of Management and Budget (OMB) Circular A-123; *Management's Responsibility for Internal Control*; OMB Office of Federal Procurement Policy's (OFPP) Acquisition Assessment; and the 2009 American Recovery and Reinvestment Act (ARRA).

The FMFIA holds Federal managers accountable for establishing and maintaining effective internal controls and financial systems. All DOT organizations are subject to Sections 2 and 4 of the FMFIA, except the Saint Lawrence Seaway Development Corporation, which reports separately under the Government Corporations Control Act.

With the exception noted for compliance with the Federal Information Security Management Act (FISMA), DOT is able to provide reasonable assurance that the internal controls and financial management systems in effect during the period of October 1, 2009 through September 30, 2010 met the objectives of both Sections 2 and 4 of the FMFIA. During FY 2010, DOT conducted its assessment of internal controls and compliance with applicable laws and regulations in accordance with OMB Circular A-123.

FISMA Compliance

In late 2009, the Inspector General (IG) issued a report on DOT's compliance with FISMA. The purpose of this review was to determine the effectiveness of DOT's security program and practices in the areas of policies and procedures, enterprise-level information security controls, management of information security weaknesses, and system-level security controls. As a result of this review, the IG made 27 specific recommendations. During the

year, corrective actions were underway, but at September 30, 2010, many of these actions had not been completed. As a consequence, the Department's compliance with FISMA during 2010 constituted a material weakness in internal controls. A corrective action plan to complete all outstanding FISMA recommendations is being developed and will be implemented.

FMFIA Internal Control Program

For FY 2010, DOT enhanced its standardized and consistent FMFIA Internal Control Program approach for managing control and compliance activities. The DOT identified and documented meaningful Components and Assessable Units (AU). Inherent risk assessments were conducted to classify and prioritize each AU. Management Control Reviews, leveraging the five standards of internal controls, as prescribed by the Committee of Sponsoring Organizations of the Treadway Commission and the U.S. Government Accountability Office, were conducted to identify, assess, document, and communicate key management and programmatic internal controls and related risks or weaknesses.

OMB Circular A-123, Appendix A Internal Control Program

During FY 2010, DOT conducted an assessment of the effectiveness of internal controls over financial reporting, including safeguarding of assets and compliance with applicable laws and regulations in accordance with the requirements of OMB Circular A-123, Appendix A. During FY 2010, DOT assessed and tested controls over key identified business processes, including Cost Accounting, Credit Reform and Loans, Environmental Liabilities, Financial Reporting, Grants Management, and Revenue and Receivables.

The major OMB Circular A-123, Appendix A activities in FY 2010 included evaluating entity level, process level, and in-depth testing at the transaction level of internal controls over financial reporting for the five identified business processes. All deficiencies were communicated to senior management and mitigated using existing remediation procedures.

OMB A-123 Acquisition Assessment

In accordance with guidance from the Office of Federal Procurement Policy and OMB Circular A-123, the DOT Office of Senior Procurement Executive (OSPE) developed a three year assessment reporting cycle of the DOT's acquisition offices and programs, and in FY 2010, OSPE conducted an entity level top-down assessment of 30 percent of component acquisition offices of the Operating Administrations.

American Recovery and Reinvestment Act (ARRA)

The ARRA was signed into law on February 17, 2009. To ensure that ARRA funds are in compliance and meet the objectives of the program, and to ensure that this spending meets unprecedented standards for transparency and accountability, DOT management devised robust risk mitigation strategies for this program. Additionally, DOT management updated key business process documentation and conducted subsequent testing of ARRA transactions as part of OMB A-123 assessment activities to reflect new or modified business processes.

As a result of our FMFIA reviews in FY 2010, I conclude that the Department has made substantial progress in enhancing its internal controls and financial management program. Additional enhancements are planned and underway in FY 2011.

Respectfully,

Ray LaHood

FFMIA OF 1996 FINANCIAL MANAGEMENT SYSTEMS STRATEGY

The Secretary has determined that our financial management systems were in substantial compliance with the Federal Financial Management Improvement Act for FY2010. In making this determination, he considered all the information available, including the auditor's opinion on our FY 2010 financial statements, the report on management's assertion about the effectiveness of internal controls, and the report on compliance with laws and regulations. He also considered the results of the management control reviews and financial management systems reviews conducted by the agency and its independent contractors.

The Federal Financial Management Improvement Act of 1996 (FFMIA) requires that agencies' financial management systems routinely provide reliable and timely financial information for managing day-to-day operations as well as to produce reliable financial statements, maintain effective internal control, and comply with legal and regulatory requirements. Under FFMIA, financial management systems must substantially comply with three requirements: Federal financial management system requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger (SGL) at the transaction level. In addition, CFO Act agencies must determine annually whether their systems meet these requirements. This determination is to be made no later than 120 days after the earlier of (a) the date of receipt of the agency-wide audited financial statement, or (b) the last day of the fiscal year following the year covered by such statement.

Management conducted its assessment of the effectiveness of internal controls over financial systems and compliance with applicable laws and regulations in accordance with FMFIA guidance, OMB Circular A-127, Financial Management Systems, results of OIG and GAO audit reports, annual financial statement audits, the Department's annual Federal Information Security Management Act (FISMA) Report, and other relevant information. Based on the results of DOT's internal control assessment, one material weaknesses was identified in 2010 based on FISMA results.

The Department of Transportation (DOT) uses Oracle Federal Financials software as its agency-wide financial management and accounting system of record (called Delphi). DOT was the first cabinet agency to migrate all of its Operating Administrations (OAs) to a Financial Systems Integration Office (FSIO)-certified, commercial off-the-shelf based financial system. The Oracle system provides real time access to accounting information and fund availability. The consolidation of accounting activities using one financial sys-

tem improves internal controls, reduces redundant processes, improves communications, gains efficiencies, as well as provides monitoring and control of Federal accounting standards and financial policies.

DOT continues to make progress on the financial management modernization initiative to upgrade its current financial management system software from Oracle Release 11i to Oracle Release 12. In order to take advantage of the enhanced functionality offered in Release 12, DOT's Office of Financial Management, in partnership with the Departmental financial community, has decided to use this opportunity to upgrade the system software and to achieve business process improvements and standardizations as well. This multiple-year, Department-wide program has been established to maximize the capabilities of the upgrade and to efficiently and effectively meet internal and external requirements, such as transparency and government-wide accounting structure requirements. This program is led by the Office of the Assistant Secretary for Budget and Programs/CFO, includes participation and support from each Operating Administration (OA) and includes Department-wide executive sponsorship.

In FY 2010, DOT began executing a plan to upgrade Delphi's servers, operating system and database to Intel servers running on a Linux platform which will support the Oracle 11g database. The Oracle 11g database is a requirement for Oracle Federal Financials Release 12; however, certain benefits of the upgrades will be realized before the Release 12 implementation is completed. The new servers will improve Delphi's response times for reports and workflows. Nightly, monthly and year-end processing times will be decreased as well. Additionally, the upgraded system will support clustered computers which allow the Department to run multiple computers on the database. The clustered computers will allow operations to continue if one of the computers in the cluster experiences problems and will also allow additional computers to be added to increase capacity as needed.

In FY 2010, DOT began executing a plan to improve the timeliness of the Delphi instance management process. Completing the full Delphi backup cycle to apply major upgrades or accomplish routine backups currently takes approximately between 14 and 16 hours. The Department is moving to NetApp storage appliances that will reduce the backup cycle to less than 4 hours. This will help reduce system down time due to patches, enhancements and upgrades and will also make the system available to end users much faster during critical times such as month and year end.

FEDERAL INFORMATION SECURITY MANAGEMENT ACT

The Federal Information Security Management Act (FISMA) requires federal agencies to identify and provide security protection commensurate with the risk and magnitude of potential harm resulting from the loss, misuse of, unauthorized access to, disclosure of, disruption to, or modification of information collected to maintained by or on behalf of the an agency. FISMA requires that Inspectors General evaluate agency information security programs and practices. The DOT FISMA report for FY 2010 will not be finalized until after November 15.

The DOT has 13 Operating Administrations that for Fiscal Year 2010 supported a total of 465 information systems, of which 291 belong to the Federal Aviation Administration (FAA). The FAA air traffic control system has been designated by the president as part of the critical national infrastructure. Other systems owned by the Department include safety-sensitive surface transportation systems and financial systems that are used to manage and disburse over $77 billion in federal funds each year.

Last year, the DOT OIG reported that the DOT's information security program did not meet Federal IT security standards and made 27 specific recommendations to improve DOT's controls. At September 30, corrective actions associated with many of these recommendations remain incomplete. However, DOT has made improvements this year by issuing a security policy that addresses all of National Institute of Standards and Technology (NIST) information security control areas. Also, DOT significantly improved its common operating environment's compliance with Federal Desktop Core Configuration (FDCC) which complies with an OMB mandate that requires all federal agencies standardize their desktop and laptops computers configuration settings.

DOT still needs to make progress in other critical areas, e.g., that all operating and database systems have security baseline configurations. Also required is the need for better identification and prioritization of DOT's security weaknesses. Additionally, DOT needs to ensure that all systems and their interfaces have proper certification and accreditation and system recovery controls in the event of a disruption. Completion of protections for sensitive privacy information is the last remaining critical area.

The full FY 2010 FISMA report will be available in early December 2010 and can be found at www.oig.dot.gov.

SAS-70 REVIEW ON DOT'S FINANCIAL MANAGEMENT SYSTEM

The Statement on Auditing Standards (SAS) 70 report summarized the results of a review of general, application, and operational controls over the DOT Enterprise Services Center (ESC). The ESC performs services including accounting; financial management; systems and implementation; media solutions; telecommunications; and data center services for DOT and other Federal organizations.

This is the sixth year that a SAS-70 audit has been conducted on DOT's Delphi financial system. Delphi is hosted, operated and maintained by Federal Aviation Administration employees at the Mike Monroney Aeronautical Center in Oklahoma City, OK, under the overall direction of the DOT Chief Financial Officer.

ESC is one of four Federal Shared Service Providers designated by the Office of Management and Budget to provide financial management systems and services to other government agencies. ESC supports other Federal entities, including the National Endowment for the Arts, the Commodity and Futures Trading Commission, The Institute of Museum and Library Services, The National Credit Union Association, The Consumer Product Safety Commission and the Government Accountability Office. The Office of Management and Budget requires Shared Service Providers to provide client agencies with an independent audit report in accordance with the American Institute of Certified Public Accountants (AICPA) SAS-70.

This year's SAS-70 audit of Delphi was conducted by Clifton Gunderson, LLP of Calverton, MD. Clifton Gunderson concluded that management presented its description of ESC controls fairly in all material respects, and that the controls, as described, were suitably designed for all stated control objectives.

Clifton Gunderson made additional recommendations to DOT management for improving access controls. We agree that implementing these recommendations will further enhance controls over ESC operations. In accordance with DOT Order 8000.1C, the corrective actions taken in response to Clifton Gunderson's recommendations are subject to audit follow-up. Clifton Gunderson performed additional testing and provided a follow-up management letter to OIG on September 30, 2010, reporting no significant changes to the control environment between July 1, 2010, and September 30, 2010.

Effective for reports dated after June 15, 2011, SAS-70 will be replaced the new standard Standards for Attestation Engagements (SSAE) 16. More information can be found at http://www.aicpa.org/Research/Standards/AuditAttest/Pages/SSAE.aspx

DOT'S FINANCIAL MANAGEMENT SYSTEMS IMPROVEMENTS

The Department of Transportation (DOT) continues to forge ahead with a major financial management improvement and modernization effort. This multi-year project, begun in FY 2009, supports the Organizational Excellence strategic goal by transforming and streamlining financial management policies, processes, and systems in an effort to better meet the growing and dynamic mission of the Department in this decade and beyond.

This collaborative effort focuses on three primary goals:

- Comprehensive business process reengineering to improve standardization and consistency across the Department.
- Improving financial data management, including standardization of our accounting classification structure, introduction of business intelligence capabilities, and improved reporting.
- Modernizing DOT's financial management system to better meet financial system standards, transparency requirements, and improved functionality provided by the next Oracle Core Financials release.

This initiative is led by the Office of the Assistant Secretary for Budget and Programs/CFO and includes full participation and support from each Operating Administration (OA) to ensure success of the project. The effort has been structured around "waves" which consist of major targeted solution milestones. As such, the initiative will attain tangible modernization throughout the project, rather than at the end of the project lifecycle, as many projects do. FY 2010 and prior years form the foundation for the effort, with an emphasis on long-term strategic planning. FY 2011 and FY 2012 will focus on realizing strategic planning efforts with the acquisitions of major system applications, analytics (business intelligence), reporting, and hardware components. During this period the project will also implement the first three solution waves: grants payment solution, vendor payment solution, and business intelligence/financial analytics.

DOT has coupled financial management modernization with the transition to Oracle Core Financials Release 12 because the Department has learned through past experience that process improvement and standardization exercises achieve optimal results when done ahead of a major system release. The initiative is a paramount priority for DOT because it will provide a financial management infrastructure (procedures, systems, and reporting capabilities) that will assist the Department in more effectively and efficiently meeting

internal and external requirements, such as transparency and government-wide accounting structure requirements. Additionally, cleaning up aging, non-standard or ineffective processes establishes a better internal control environment, reduces audit findings, limits timely reconciliations, and eradicates the need for costly "work-arounds."

This project uses a collaborative approach to defining and establishing global process and system standardization, with the expectation that optimal standardization will reduce the number and redundancy of ancillary systems and processes.

INSPECTOR GENERAL'S FY 2010 TOP MANAGEMENT CHALLENGES

DEPARTMENT OF TRANSPORTATION OFFICE OF INSPECTOR GENERAL APPROACH

The Office of Inspector General (OIG) issues its annual report on the Department of Transportation's top management challenges to provide a forward-looking assessment for the coming fiscal year. The purpose of the report is to aid Department of Transportation (DOT) agencies in focusing attention on and mapping work strategies for the most significant management and performance issues facing the Department.

In selecting the challenges for each year's list, the OIG continually focuses on the Department's key strategic goals to improve transportation safety, capacity, and efficiency. In addition to the OIG's vigilant oversight of DOT programs, budgetary issues, and progress milestones, it also draws from several dynamic factors to identify key challenges. These include new initiatives, cooperative goals with other Federal departments, recent changes in the Nation's transportation environment and industry, as well as global issues that could have implications for the United States' traveling public. As such, the challenges included on the OIG's list vary each year to reflect the most relevant issues and provide the most useful and effective oversight to DOT agencies.

As required by OMB Circular A-136, the OIG's report briefly assesses DOT's progress in addressing the challenges identified. To track management challenges identified from year to year, the OIG provides an exhibit to the report that compares the current list of management challenges with the list published the previous fiscal year. In addition, the OIG may refine the scope of the management challenge from year to year based on program developments, external factors, or other information that becomes available.

The OIG has not reviewed all of the actions included in this summary.

AFR 2010 MANAGEMENT CHALLENGES

1. Maximizing the Department's Economic Recovery Investments

Issue: Implementing the Office of the Secretary's (OST) $1.5 Billion Dollar TIGER Discretionary Grants Program

I. Why is this an issue?

A new discretionary grants program under the American Recovery and Reinvestment Act of 2009 (ARRA) includes $1.5 billion under the Office of the Secretary (OST). Implementing the program was identified due to a concern over the adequacy of available management resources. To better ensure this program meets its objective, OST was required to develop comprehensive and sound program plans and criteria.

II. Actions taken to date

The Office of Policy within OST is primarily responsible for providing policy direction related to the implementation of infrastructure grant programs, credit programs and regulations that impact infrastructure development and operation. The Office of Infrastructure Finance and Innovation plays the lead role in the implementation, management and administration of the TIGER Discretionary Grant Program. For the application review and selection process, staff was supplemented by over 70 experts drawn from the Department's operating administrations (OAs). Additionally, the Office of Infrastructure Finance and Innovation has partnered with the Federal Highway Administration (FHWA), the Federal Transit Administration (FTA), the Federal Railroad Administration (FRA), Federal Aviation Administration (FAA) and the Maritime Administration (MARAD), to utilize existing grant management staff and resources to appropriately administer the grants and supplement OST grant administration responsibilities.

The OST developed and published project selection criteria and a solicitation for applications. The criteria for TIGER were published in the Federal Register on June, 17, 2009. The criteria are merit-based and address statutory requirements. The OST leads a Department-wide task force charged with evaluating applications and making funding recommendations. The evaluations teams comprised of technical and professional experts from OST and the Department's relevant operating administrations (OAs).

III. Actions remaining and expected completion date

Each project has been assigned to the most appropriate Operating Administration to secure the grant agreement and provide oversight. The OST Office of Policy also concurs on the grant agreement, and will continue to provide guidance on performance measures.

IV. Results or expected results

Successful execution of all project grant agreements.

Issue: Enhancing Oversight of ARRA Spending on Existing and New Programs

I. Why is this an issue?

Enhanced oversight of ARRA spending is necessary to ensure the adequacy of available management resources to administer spending activities.

II. Actions taken to date

In addition to partnering with the FHWA, FTA, FRA, FAA and MARAD, to utilize existing grant management staff and resources, the Office of Infrastructure Finance and Innovation within OST has developed a programmatic structure that is designed to enhance the oversight of ARRA spending activities. The structure includes: (1) Regular reporting requirements from the grantees to the Operation Administrations and from the Operating Administrations to OST; (2) Clear procedures for escalation of issues; and (3) Promoting consistency across relevant Operating Administrations in the management of projects.

III. Actions remaining and expected completion date

The Office of Infrastructure Finance and Innovation, has done the following: (1) Promptly reconciled grantee reported data with internal records; (2) Ensured that the grantee's performance is adequate and properly reported; (3) Worked closely with each of the relevant modal administrations to ensure that the TIGER grants are administered properly; (4) Analyzed and compare the performance of the TIGER program(s) with each appropriation as well as against similar discretionary grant programs.

IV. Results or expected results

Continued reporting and adherence to procedures under the programmatic structure.

Issue: Reporting Accurate and Consistent Job Creation Data

I. Why is this an issue?

Reporting accurate and consistent job creation data on the Department's ARRA program was identified as an issue because the Department did not have a functional system in place designed to capture and report job creation data.

II. Actions taken to date

To coordinate the Department's role in ARRA, the Secretary created a team at DOT. The team ensures that economic recovery act funding is rapidly made available for transportation infrastructure projects and that project spending is monitored and transparent. The team, known as the Transportation Investment Generating Economic Recovery (TIGER) team, is composed of officials from across the Department's Operating Administrations and offices. Early in 2009, the TIGER Team provided guidance to all of the relevant operating administrations – FHWA, FTA, FRA, FAA and MARAD -- on how grantees are required to report the number of paid jobs created by prime recipients, subprime recipients, and vendors (where applicable) as required under Section 1512 of ARRA. The grantees were directed to calculate and report created jobs as "Full-Time Equivalents (FTE)" to http://www.federalreporting.gov. All operating administrations closely monitored the jobs reporting by the recipients to ensure that the data was accurate.

According to data from the Recovery Accountability and Transparency Board, the responsible entity for recipient reports monitoring, DOT has one of the best records for recipient reporting government-wide. DOT has the second largest number of grantees and one of the lowest instances of non-reporting or reporting errors. The TIGER team has monitored and will continue to monitor the collection of jobs data for all ARRA projects administered by the Operating Administrations, as well as for the TIGER Discretionary Grant Program administered by OST.

Department-wide guidance was revised to comply with Office of Management and Budget standards once they were developed for all agencies. The TIGER Team also provided guidance for job reporting under Section 1201 of ARRA, and directed grantees to report direct job-hours for each ARRA grantee. The Department would then use data on direct jobs and expenditures to estimate indirect jobs and total employment, as required by Section 1201 of ARRA.

III. Actions remaining and expected completion date

OST will work closely with each of the relevant modal administrations to ensure that accurate and consistent job creation data are collected, analyzed, and reported for TIGER grants.

IV. Results or expected results

Successful execution of all Recovery Act projects with accurate and complete job reporting.

2. Enhancing Surface Safety Programs to Reduce Injuries and Fatalities While Defining a New Federal Role in Transit Safety

Issue: Promoting Meaningful Performance Indicators to Consistently Measure States' Progress in Improving Safety

I. Why is this an issue?

States and the Federal Government spend large sums of money on highway safety programs and activities. As a data driven organization, the National Highway Traffic Safety Administration (NHTSA) should ensure that states spend money wisely, with a focus on key issues and a positive impact on reducing the number and severity of crashes.

II. Actions taken to date

All states have included core performance measures in their 2010 Highway Safety Plans (HSPs), which outline programs the states will implement and show how they will spend Federal funds. NHTSA and the Governors Highway Safety Association (GHSA) have developed additional attitude and awareness performance measures. NHTSA also convened a working group which developed a consensus speed monitoring performance measure. Additionally, in July 2009, NHTSA's National Center for Statistics and Analysis (NCSA) made fatal crash maps available to the public; these maps use 2007-2009 Fatality Analysis Reporting System (FARS) data to show fatal crash locations within a state via a Google Earth plug-in download. The crash-location maps serve as an extension to the county maps that the State Traffic Safety Information website already delivers.

III. Actions remaining and expected completion date

NHTSA is reviewing the HSPs to assure that they include the requisite performance measures, and continues to work with GHSA on developing guidelines and implementation material for the measures. NHTSA is considering drafting additional developmental measures for enforcement activities.

IV. Results or expected results

During FY 2010, states began to use core performance measures in designing their FY 2010 safety programs. NHTSA and the States will use these data, collected during FY 2010 and out years, to measure the impact of their safety programs, to evaluate safety problems, and to make appropriate modifications to their programs. In future years, States will collect improved speed and injury data, as well as new performance measures (including law enforcement measures, and attitude and awareness surveys). As more years of data become available, States will be able to evaluate the long-term impact of their programs, determine changes in the magnitude of specific safety problems, and

adapt their programs to address the most significant issues. Furthermore, as States measure and report on performance measures, NHTSA will work collaboratively with them to ensure that States meet or exceed their targets. This will include using demonstration projects, technical assistance, and sharing best practices.

Issue: Targeting Unsafe Motor Carriers and Commercial Drivers for Enforcement and Enhancing the Commercial Driver's License (CDL) Program

I. Why is this an issue?

Approximately 1 in 8 overall fatalities in 2008 were related to crashes involving large trucks or buses. The Department must take stringent action against repeat violators of safety regulations, improve its enforcement and data systems, and identify and stop Commercial Drivers License (CDL) holders who are not properly licensed.

II. Actions taken to date

The Agency addressed 73 percent of the total number of recommendations (26) issued by the OIG that pertain to this top management challenge. In FY 2010, the Federal Motor Carrier Safety Administration (FMCSA) closed or requested closure on 12 of the 19 remaining open recommendations pertaining to the OIG's 2010 Top Management Challenges report. FMCSA has several initiatives underway to address the remaining issues identified by the OIG and has taken vigorous action in FY 2010 to target unsafe motor carriers and commercial drivers for enforcement and to enhance the CDL program. FMCSA is committed to resolving and implementing open audit recommendations issued by the OIG.

The OIG recommended that FMCSA take stringent enforcement action against carriers that repeatedly violate safety regulations and improve enforcement and data systems used to oversee the motor carrier industry and commercial motor vehicle drivers. With regards to the OIG recommendation to satisfy the Motor Carrier Safety Improvement Act of 1999 (MCSIA) enforcement requirements and close loopholes for repeat violators, FMCSA closed six of seven recommendations highlighted by the publishing of a very stringent enforcement policy on March 30, 2009, which changed how the Administration assessed maximum fines under section 222 of MCSIA and strengthened the criteria for taking enforcement action against repeat violators.

FMCSA is also establishing quality control procedures to ensure states are reporting Mexican-domiciled Commercial Motor Vehicle (CMV) driver convictions occurring in the United States. This data ensures that the appropriate action is taken against Mexican drivers convicted of disqualifying offenses. Additionally, in response to the OIG's 2009 report, Audit of the Data Integrity of the Commercial Driver's License Information

System (CDLIS), FMCSA issued in the Federal Register (July 2, 2010) guidance to state driver licensing agencies (SDLAs) in support of their efforts to comply with the Federal Commercial Driver's license (CDL) regulations including timely reporting and posting of convictions for traffic offenses. Regarding data security, FMCSA provided grant funds to the States in FY 2010 to implement a new modernized CDLIS, and closed a comprehensive OIG recommendation requiring improved CDLIS information technology security standards.

A program initiated in FY 2010 to ensure that unsafe motor carriers are placed out-of-service and not re-issued authority under new identities includes a robust New Applicant Screening program. The program detects prior unsafe carriers that disband operations before they can reincarnate as new entities in an attempt to avoid their previous safety records. FMCSA also launched a Pre-Employment Screening program in FY 2010, which allows companies to access driver inspection and crash records as part of the hiring process. This program gives companies tools to make informed hiring decisions, which lead to hiring the safest drivers.

In FY 2010, FMCSA also issued a final rule on Electronic On-Board Recorders (EOBRs) that significantly contributes to targeting unsafe motor carriers. The final rule on EOBRs requires carriers with serious patterns of hours of service violations to install EOBRs. The Administration is also proposing stronger CDL standards and testing requirements and anticipates issuing a final rule that will establish revisions to the CDL knowledge and skills testing standards, implement fraud detection and prevention initiatives at SDLAs, and establish new minimum Federal standards for commercial learners permits.

FMCSA also strengthened the New Entrant Safety Assurance program to identify start-up truck and bus companies deficient in key areas that must be addressed in order to continue operations. By the end of calendar year 2010, FMCSA will implement Comprehensive Safety Analysis (CSA) 2010 by replacing the Administration's current motor carrier measurement system, SAFESTAT, with the CSA 2010 Safety Measurement System. Other initiatives to remove truly unfit and unsafe drivers and carriers from the Nation's roads include virtual weigh and inspection stations at the roadside and tools like infrared brake warning detection.

III. Actions remaining and expected completion date

In FY 2011, the Administration anticipates developing and implementing a revised policy on the census updating requirement; fully executing CDLIS modernization and resolving information technology security and data issues; issuing proposed rules on carrier safety fitness determination and the Driver Positive Controlled Substances and Alcohol Test Results Database; and, issuing final rules on restricting the use of cellular phones,

CDL testing and commercial learner's permit standards, and minimum training requirements for entry level commercial motor vehicle operations.

IV. Results or expected results

The safety initiatives implemented in FY 2010 and planned for FY 2011 will improve safety and increase efficiency. These initiatives contribute to the Department of Transportation's overall safety strategic goal and performance target to reduce highway fatalities and support critical motor carrier program activities that will reduce crashes, save lives, and prevent injuries on the Nation's highways.

Issue: Defining a New Federal Role in Transit Safety

I. Why is this an issue?

Historically, rail transit is a safe mode of public transportation. However, recent accidents at major rail transit systems have caused nationwide concern regarding rail transit safety. Secretary LaHood reviewed the existing legal authorities and believes that the current Federal oversight role for rail transit safety should be reformed. The current State Safety Oversight (SSO) structure (with few exceptions) lacks sufficient authority to provide a uniform approach to transit system safety. A multi-modal safety work group chaired by the Deputy Secretary recommended a number of reforms to improve public transportation safety, including submitting a legislative proposal to Congress to enhance the Federal Transit Administration's (FTA) oversight of rail transit safety.

II. Actions taken to date

FTA convened the initial Transit Rail Safety Advisory Committee (TRACS) meeting September 9-10, 2010. The initial focus for TRACs will be recommendations to implement/improve the safety management systems of rail transit systems and improve organization models for SSO agencies. FTA has increased funding for the SSO program and the Bus Safety program to include additional capacity to support an expanded role based on the proposal and to provide additional bus regulatory oversight. FTA increased the number of SSO agency program managers that are certified by the Transportation Safety Institute and decreased the average time to complete SSO agency audit findings.

III. Actions remaining and expected completion date

FTA will integrate safety and security into the New Starts project development phase through more effective use of the Safety and Security Readiness Review process. FTA has worked with transit systems to increase the number of chief safety officers reporting directly to transit agency general managers. FTA continues to provide financial support to the American Public Transportation Association (APTA) in developing voluntary

industry consensus safety, security and emergency management standards. FTA has also provided funding to research rail car crash performance to support the development of future rail car design standards.

Regarding training, FTA is developing a course for rail safety to provide SSO managers, transit personnel and rail safety inspectors with the knowledge of rail transit systems and how safety design, inspections and standards contribute to overall system safety. It is also developing a Training Curriculum for Rail Safety Inspectors that will result in certification. FTA is delivering eight (8) two-day training sessions on track inspection at selected rail transit agencies that will provide instruction on track worker and maintenance safety. This training was developed as a result of recent increases in track worker fatalities. FTA is developing a Safety and Security Strategic Training Plan to promote development and improvement of transportation safety and security, technology management, and operational procedures for educational and training programs that are responsive to modal and intermodal requirements.

TRACS is currently working to provide recommendations for transit systems to implement the best safety planning model, to include but not limited to, Safety Management System (SMS) principles and how those principles might be incorporated into transit safety plans to enhance rail transit safety. It will also provide recommendations for the best State oversight agency organization model, to include identifying the ideal state safety partner and identify the challenges that may be faced in implementing this model along with potential ways the challenges may be overcome. Each of the TRACS recommendations has a projected delivery date of May 2011.

FTA has begun the initial phase of program/project planning to implement elements of the proposed transit rail safety legislation. The initial phase will identify program objectives, resource allocation, and implementation milestones. The initial plans are scheduled for delivery in December 2010.

FTA continues to pursue legislation to strengthen its safety oversight function.

IV. Results or expected results

FTA is projecting improvement in safety based on several actions taken in FY 2010.

The increase in number of Transportation Safety Institute certified SSO agency staff will provide enhanced technical capacity and consistent program capabilities of SSO program management by increasing the number of SSO program managers trained in broad-based knowledge of safety and security principles applicable to transit safety, operations and management. The decrease in the number of days to close out audit findings by 5% of the

2009 average of 219.8 days is a responsive risk reduction process and a tangible means to emphasize commitment to an organizational safety culture. The increase in the number of rail transit agency chief safety officers reporting directly to general managers is anticipated to improve system safety through enhanced senior management leadership and strengthened inter-departmental coordination. The training initiatives underway for transit system employees were developed to promote and improve transportation safety and security, technology management, and operational procedures and should lead to increased safety and security awareness.

3. Maximizing Federal Surface Infrastructure Investments by Helping States Better Allocate Resources and Providing Effective Oversight

Issue: Developing Improved Tools and Techniques to Help States Better Allocate Scarce Resources and Providing Effective Oversight of Federal Investments

I. Why is this an issue?

According to a 2009 report from the American Society of Civil Engineers, one-third of the Nation's major roads are in poor or mediocre condition and more than one-quarter of our bridges are deficient. Maximizing federal investment in surface transportation infrastructure is particularly challenging because the majority of the federally-assisted highway programs are administered by States, which have broad flexibility in deciding how to use their funds, which projects to pick, and how to implement them.

The Department faces the following key challenges:

- Developing improved tools and techniques to help states better allocate scarce resources; and
- Providing effective oversight of Federal investments through better use of data, management tools, and performance measures

II. Actions taken to date

During FY 2010, FHWA developed a Bridge Management Systems (BMS) questionnaire that was used by the FHWA Division Office Bridge Engineers in coordination with their State DOT counterparts to assess the state-of-practice. Based on the questionnaire responses, preliminary results show that 40 States are using their BMS to store bridge information.

Also in FY 2010, FHWA initiated a process to include more detailed project information within bridge projects in the Fiscal Management Information System (FMIS). FHWA drafted detailed criteria that include more than 20 specific metrics linked to the National Bridge Inspection Standards (NBIS) regulatory provisions, such as inspection frequency and inspector qualifications, with defined risk tolerance levels for compliance, substantial compliance, and non-compliance determinations. Application of the defined criteria will improve the consistency in determining compliance with the NBIS. In May, FHWA concluded a pilot evaluation of these criteria and procedures in 12 division offices. The results of the pilot test were evaluated with regard to effectiveness and resource impact. The schedule calls for full implementation in 2011.

FTA is in the process of publishing a notice of proposed rulemaking (NPRM) on project management in the Federal Register for comment. The NPRM will codify FTA's expectations for grantee core project management principles, FTA's risk assessment approach, and enhanced oversight for major capital projects of particular size and complexity. FTA is updating the Project and Construction Management Guidelines, which is a general guidance manual for implementation of New Starts projects. The updated version emphasizes project management principles and risk management concepts. The updated Guidelines will be published by the end of calendar year 2010.

FTA has revised and enhanced its Project Management Oversight Operating Procedures with a special focus on risk management so as to provide better guidance to its staff and oversight contractors in risk assessment and other reviews. FTA developed a new project management course which teaches project sponsors the principles of successful project management. In FY 2010, FTA offered 24 project management courses around the country. The agency initiated an annual conference (New Starts Engineering Workshop) where sponsors of New Starts projects get together to share, among other things, best practices in managing projects successfully with a focus on addressing project scope, schedule, cost and risk.

FTA developed and published a historical database of light and heavy rail project capital costs. This database provides project sponsors with enhanced cost data that supports cost estimation early in project development. This date establishes more reasonable conceptual estimates that will help inform local decision-making and subsequent project development activities.

III. Actions remaining and expected completion date

A bridge management technical assistance plan will be developed once the evaluation of the questionnaire results is completed and a report issued. Based on this plan, the FHWA will provide technical assistance and training to each state.

In FY 2011, FHWA will implement new NBIS compliance processes in all 52 States. In FY 2012, further enhancements to FMIS will be made to collect additional bridge project data. After reauthorization, FHWA will work with States to set performances goals and measures for bridge condition.

FTA will prepare internal standard regional office operating procedures for management of Full Funding Grant Agreements to ensure more active FTA identification and resolution of project scope, schedule, and budget issues during project construction. Finally, FTA will initiate a top-down review of its overall oversight program, intended to address a range of oversight policy, procedural, and management issues to ensure greater grantee

compliance with Federal requirements and the delivery of more efficient and coordinated oversight activities.

IV. Results or expected results

Improvements in future year's condition data are anticipated as a result of bridge investments under the American Recovery and Reinvestment Act of 2009, lower bridge construction unit costs in 2009 and 2010, and the use of the additional $1 billion in dedicated Highway Bridge Program obligation limitation.

FHWA will provide targeted technical assistance to States, based on their current BMS use. Making progress among the States will take time and will require commitment by the leadership of the 52 State DOTs.

FTA expects that the steps it is taking to address this management challenge will improve management of capital projects by project sponsors, improve guidance and tools for FTA and its oversight contractors to provide more responsive and focus oversight of high-risk projects. FTA also expects an increase in the number of projects delivered on time and on budget. In the long-term, it is FTA's expectation that the culture of effective project management will improve significantly in the transit industry, ultimately resulting in improvements in project adherence to baseline scope, schedules, and budget.

4. Addressing Human Factors and Strengthening the Regulatory and Oversight Framework for Aviation Safety

Issue: Increasing Efforts to Address Human Factors

I. Why is this an issue?

Human factors in aviation can affect the safety of users of the National Airspace System (NAS). For example, the effects of fatigue negatively impact human performance through impaired reasoning, attention lapses, and reduced situational awareness. Fatigue can affect both pilots and air traffic controllers.

II. Actions taken to date

In 2010, the Department established an Air Traffic Organization (ATO) Fatigue Risk Management (FRM) program office to address fatigue in air traffic safety by identifying fatigue causes and mitigating its risks. The primary focus of the FRM program office is to build the foundation of an adaptive, evolving Fatigue Risk Management System (FRMS) to promote safety in the National Airspace System (NAS) and enhance the safety and well-being of employees.

In June 2010, FAA developed an initial communication, education, and training plan to increase fatigue awareness for operational employees and management. It also developed an initial report to implement programs to increase content of fatigue risk event information. In collaboration with the National Air Traffic Controllers Association (NATCA), FAA formed a workgroup to address air traffic controller workplace fatigue, and developed collection methodologies to capture and analyze fatigue data from reported air traffic events.

FAA collaborated with its internal stakeholders and NATCA to develop an initial draft of the Fatigue Risk Management System (FRMS) concept. The FRMS will include a broad range of fatigue risk mitigations, such as scheduling, training and education, methods for reporting fatigue, and strategic communications activities.

In September 2010 FAA published a pilot flight and duty time and rest requirements (FDR) notice of proposed rulemaking. FAA use science and information on fatigue, as well as international standards, to develop the proposed rule.

III. Actions remaining and expected completion date

In FY 2011, FAA and NATCA will deliver an initial recommendation for potential policy and procedural changes that address air traffic controller (ATC) fatigue, as well as the

jointly-designed FRMS. FAA will also identify causes of ATC fatigue, associated hazards and risks, and appropriate mitigations to reduce fatigue risk in the NAS.

IV. Results or expected results

The FAA has made substantial progress towards addressing fatigue. FRMS will bring about a sustained focus on fatigue safety through a top-to-bottom approach that incorporates and rests upon fatigue science. The FRMS will also leverage all appropriate fatigue risk mitigation best practices to develop and implement effective improvements in fatigue safety. The results of the Final Rule on pilot flight and duty, and rest requirements will be consistency and standardization in guidance that addresses fatigue, a critical factor in aviation safety. This will mitigate the risks of fatigue and provide the traveling public with reliably-rested flight crews.

Issue: Providing an Equivalent Level of Safety for Passengers Flying On-Demand Carriers by Strengthening FAA Regulations and Oversight

I. Why is this an issue?

FAA has regulatory and statutory authority to provide oversight on air carriers' safety standards. Through our surveillance activities, we are responsible for ensuring that air operators and air agencies provide service with the highest level of safety to the traveling public. FAA is developing a risk-based oversight approach for on-demand operators but it will not be implemented for 4 years.

II. Actions taken to date

In FY 2010, FAA revised internal guidance material to strengthen our oversight of on-demand operators. FAA updated and published the following orders and notice that require principal inspectors to use the Safety Performance Analysis System (SPAS) Surveillance Priority Index (SPI) for work program planning and updating their work.

- August 12, 2010, published FAA Order 1800.56 (National Flight Standards Work Program Guidelines)
- August 12, 2010, published FAA Order 8900.1 (Volume 6, Chapter 2, Section 1 – General Policies and Procedures for Parts 121, 135, and 91 Subpart K Surveillance)
- August 12, 2010, published Notice 8900.132 (Work program Development for 14 CFR Part 135 Certificate Holders).

The FAA is currently considering how best to implement Safety Management System (SMS) for on-demand air carriers. Flight Standards is sponsoring a set of SMS Pilot Projects, through which operators can develop a safety management system that conforms

to International Civil Aviation Organization's requirements using the guidance published in FAA Advisory Circular (AC) 120-92A. SMS enhances the operators' safety by applying risk management and safety assurance processes to their operational systems. On-demand operators of all types, from international jet operators to air tour helicopter operators are participating. One subset of the community that has become especially active is the Helicopter Emergency Medical Service (HEMS) industry. In another segment, an air tour CEO recently stated that "This [SMS] is the best investment that any aviation company can make." The pilot projects are also conducted in close coordination with each operator's FAA certificate management team. Currently, for on-demand operators, the SMS Pilot Project has 53 current participants, 18 of whom joined in FY 2010.

FAA also continued its longer-term strategy to develop and deploy over the next four years a new risk-based oversight approach for on-demand operations as defined by the multi-year Systems Approach to Safety Oversight (SASO) Project Management Plan. SPAS is a major tool for managing a risk-based work program and provides a foundation for a data-driven approach to safety oversight. Mandatory use of the Safety Performance Analysis System Surveillance Priority Index tool aids principal inspectors in using resources more effectively by focusing surveillance on higher priority risks. Inspectors can use information from the Surveillance and Evaluation Program Data Package of each certificate holder to identify areas of risk within the certificate holder's operations. These tools help inspectors prioritize surveillance and focus attention where it is most needed.

Information technology requirements and automation requirements were developed in FY 2010. The functionality of the Safety Assurance System (SAS) was demonstrated with a prototype.

The change management and communications strategies for transition to SAS were established and implemented.

III. Actions remaining and expected completion date

FAA will continue the implementation of change management and communications strategies for the transition to SAS. Wave 1 of the SAS software will be developed by September 30, 2011.

IV. Results or expected results

By the end of FY 2013, deployment of SASO will allow FAA inspectors to provide strengthened, risk-based, and standardized oversight to on-demand carriers. Prior to the deployment of the SAS (2013), the SPAS SPI, the SEP data packages, and the SMS guidance material and pilot project will provide strengthened, risk-based, and standardized oversight of on-demand air carriers.

Issue: Maintaining Momentum in Joint FAA/Industry Efforts to Improve Runway Safety

I. Why is this an issue?

FAA experiences almost 1,000 runway incursions per year, and each one has the potential to result in a collision. The majority of runway incursions (approximately 65 percent) occur when a pilot violates a regulation or fails to adhere to an air traffic controller's instruction. FAA must find near-term solutions to reduce runway incursions and fully vet and set milestones for the plan's mid- and long-term initiatives.

II. Actions taken to date

In June 2010, FAA published the Runway Safety Call to Action Mid-Term and Long-Term Initiatives Action Plan. This plan addresses the status of FAA activities, schedules, and milestones required to implement mid-and long-term initiatives.

FAA's Root Cause Analysis Team (RCAT), chartered by the Runway Safety Council (RSC), reviewed serious runway incursions at seven airports. Full root cause analyses were conducted at four of the seven airports. Formal prioritized recommendations were presented to the RSC for one airport and initial recommendations for three, as well as event review results for three airports.

In December 2009, FAA convened the first-ever FAA International Runway Safety Summit. It conducted nine trade shows and safety conferences that were held throughout the continental United States. At one event alone over 43,000 runway safety publications were distributed. This event raised runway safety awareness globally, improving safety for the flying public, including U.S. citizens traveling abroad.

On June 30, 2010, the FAA instituted an Explicit Taxi Instruction Campaign which implemented new phraseology that will reduce runway incursion risks. Under the new procedure, pilots are required to receive explicit instructions before crossing or taxiing onto a runway.

In 2010 FAA introduced a "Line Up and Wait" Campaign, another significant phraseology change, adopting the international terminology "Line up and wait" in place of the current U.S. phrase "Taxi into position and old". The terminology change will reduce runway incursion risks by establishing a common international standard for this critical air traffic control instruction.

III. Actions remaining and expected completion date

FAA plans to modernize the Notice to Airmen (NOTAM) system to provide current and relevant information to pilots which could prevent runway incursions. NOTAM digitization and dissemination trials are currently running at six airports.

FAA is also developing an "off the shelf" Low Cost Surveillance System (LCGS) for use at smaller airports in order to provide some of the surveillance and conflict alerting capabilities of Airport Surface Detection Equipment – Model X (ASDE-X). LCGS will improve controller surface situational awareness. LCGS is in a two-year test period.

IV. Results or expected results

FAA continues its ongoing outreach, education, and awareness programs to affected groups through mass electronic mail communications, training animations, and a new webpage. Runway safety remains one of our top priorities and we remain committed to mitigating the risks of runway incursions.

As each mid-and long-term item in the action plan is implemented both the number and severity of runway incursions is expected to be reduced.

The recommendations concerning root causes of runway incursions identified by the RCAT were accepted by the Runway Safety Council. The Council assigned a lead organization for each recommendation and is currently tracking the implementation progress for each as well as the effectiveness of the recommendation once implemented.

The International Runway Safety Summit was very successful, attracting over 500 people from almost 20 countries. This has resulted in the FAA presenting a Runway Safety working paper at the International Civil Aviation Organization's (ICAO) High Level Safety Conference. The paper was accepted and ICAO and several states submitted Runway Safety working papers to ICAO's 37th Assembly. This has resulted in ICAO, with FAA support, planning a Global Runway Safety Symposium in May 2011. A second International Runway Safety Summit tentatively will be hosted by EuroControl in 2013.

In addition to the two major fly-in events, FAA participated in over 600 functions where it interacted with pilots and vehicle drivers and distributed safety information. In this way, FAA expects to increase awareness and knowledge of best practices and procedures, resulting in fewer runway incursions.

While it is too soon to evaluate the effect of explicit taxi instructions or the phraseology change to "Line up and wait", we expect these changes to also reduce the number of runway incursions.

Modernizing the NOTAM system will provide current and relevant safety information to pilots concerning airport information that will help them avoid runway incursion situations.

The LCGS systems are operational at two airports and are scheduled to be installed at three additional airports. These systems will provide the basis for a thorough evaluation of this technology. If adopted, these systems will improve the situational awareness of controllers and provide a tool which can be used to prevent runway incursions.

5. Moving Toward the Next Generation Air Transportation System and Improving Performance of the National Airspace System

Issue: Taking Actions to Deliver NextGen Benefits in the Near- and Mid-Term

I. Why is this an issue?

The FAA's Next Generation Air Transportation System (NextGen) is a complex, multi-program undertaking encompassing a portfolio of investments designed to deliver new capabilities to the National Airspace System (NAS) over the next five to ten years. It is a high-risk effort involving billion-dollar investments from both the government and the airline industry. NextGen's challenges are multi-dimensional, involving research and development, complex software development and integration for existing and new systems, workforce changes, and policy decision-making. The integration of new systems, technologies and capabilities impact the workforce and how FAA conducts the air traffic control operation. A key challenge for the Department and FAA involves setting realistic expectations for what NextGen can deliver in the near and mid-term.

II. Actions taken to date

The NextGen Implementation Plan (published annually) summarizes NextGen goals and objectives and provides details on the planned activities required to achieve the desired near and mid-term operational improvements and associated benefits. NextGen implementation projects have been managed and tracked against the planned annual activities and milestones contained in the NextGen Implementation Plan. Moving forward, FAA has continued to integrate RTCA Task Force recommendations into the agency's NextGen planning and implementation activities. Diverse and competing interests of the stakeholders have further reinforced the need for continued government/industry collaboration. As a result, FAA directed RTCA to create a new advisory committee for NextGen. The newly-created NextGen Advisory Committee includes senior industry participants who speak for safety, airport, environmental, global harmonization, and air traffic interests.

The FAA published an updated Enterprise Architecture (EA) in early 2010 that reflects updates to the infrastructure roadmaps such as: Aircraft, Air-Ground, Automation, Weather, Communication, Navigation, Surveillance, Airspace & Procedures, Enterprise Services, Facilities, Human Systems Integration, and Information Systems Security. The NAS EA provides the technical roadmaps for NextGen, and FAA has worked to ensure there are links within the EA from the mid-term through the long-term.

In FY 2010, in conjunction with the National Academy of Public Administration (NAPA) findings and recommendations, FAA developed and implemented an acquisition work-

force plan to ensure the hiring, development, certification and retention of a workforce with enhanced competencies and skills to successfully implement NextGen. The plan contains descriptions of the acquisition workforce, challenges, workforce planning process, current views of the workforce and future demand, staffing/hiring plans, and strategies to address workforce gaps/needs.

III. Actions remaining and expected completion date

FAA will test the Aeronautical Information Management portion of the Special Use Airspace Automated Data Exchange capability for System Wide Information Management by December 2010. Prior to first production sites, terminal separation services will be provided (ADS-B to ADS-B and ADS-B to Radar) for Common Automated Radar Terminal System (Initial Operating Capability (IOC) April 30, 2011).

FAA will provide initial operating capability for En Route separation services with ADS-B integrated into En Route Automation Modernization (ERAM) by April 2011 and En Route separation services with ADS-B integrated into Advanced Technologies and Oceanic Procedures (ATOP) August 2011. Terminal separation services prior to first production sites (ADS-B to ADS-B and ADS-B to Radar) for STARS will have initial operating capability by June 2011.

By the end of FY 2011, FAA will calculate impacts of NAS system performance on passenger exposure in all phases of flight, including delays, using a national flow model for major airports and execute its acquisition workforce plan.

IV. Results or expected results

The FAA will continue to focus on the integration across agency processes, systems and personnel. Under the construct of FAA's portfolio management framework, FAA will conduct detailed integrated program planning to effectively manage NextGen.

Issue: Maximizing the Benefits of Performance-Based Navigation in the National Airspace System and Keeping Airspace Redesign Projects on Track

I. Why is this an issue?

As air travel continues to be a way of life, increasing demands are made on airspace capacity. Although FAA is maximizing the efficiency and safety of our national airspace system (NAS) through performance-based navigation (PBN) and airspace redesign, there is a need to streamline and expedite the implementation processes. Increased awareness and better project management are two key areas that will help achieve the goals of developing integrated, benefit-focused projects.

II. Actions taken to date

FAA has continued to refine the Integrated Airspace and Procedures concept. It has promoted awareness by reaching out to stakeholders to ensure that they understand the full benefits of implementing area navigation (RNAV) and required navigation performance (RNP) initiatives. The goal is to ensure that the system works for everyone, including air traffic controllers, pilots, airports, and the community. To increase awareness amongst the aviation community, in June 2010, FAA initiated a plan to develop material for briefing industry and air traffic controllers.

Industry, through RTCA Task Force 5, recommended that RNAV operations that focus on benefits should be increased and optimized; that a structured and systematic approach to PBN implementation is essential; that environmental concerns and fuel-savings considerations must be a focus; that teams to study the Metroplex issues should be implemented immediately; and that industry should continue to be involved. The primary goal is to produce measurable benefits in reduced flight time & fuel burn by utilizing airspace redesign and performance-based navigation. The team also hopes to deconflict airports in the same Metroplex such as Washington Dulles, Washington National, and Baltimore-Washington International as well as the smaller airports. Anticipated reduction in controller workload will lead to reduced congestion and improved airport and airspace capacity.

To pursue the integrated airspace and procedures concept, FAA held prototype activities, including kick-off meetings, and planning discussions with facilities in Denver in February 2010. On April 19-23, 2010, a design meeting was held with all parties and the initial integrated procedures design was completed in August 2010. Environmental review and human-in-the-loop simulations will further determine refinements to the initial designs.

To improve project management and project tracking mechanisms, FAA initiated development of two databases to track PBN procedures. The first database, the PBN Project Tracking Tool, is a web-based tool that provides a tracking mechanism to expedite the development, review, and implementation of PBN procedures and routes throughout the lifecycle of the PBN project. Additionally, it was developed to align with the new FAA order governing the process for developing and implementing PBN procedures and routes. It provides project management functionality for PBN working group members, along with transparency for those interested in the progress of PBN projects. The PBN Project Tracking Tool is designed to be used by all parties involved with developing PBN procedures and routes. It includes features that are important for compliance with the Safety Management System. The PBN Project Tracking Tool is currently in the initial testing phase. FAA is also developing a new order on the process for development and implementation of PBN procedures

and routes. The second database that was developed in May 2010 is an interim solution to project tracking. It helps track individual procedures and report on procedure counts for our Flight Plan goals.

III. Actions remaining and expected completion date

FAA will approve the new PBN order and release the online procedures tracking database by December 2011. It will also complete the final deliverable DVD briefing material to FAA's Technical Training Organization by July 2011 and update guidance material as needed.

IV. Results or expected results

The expected result is to have an expedited and integrated process for PBN design and implementation. Air traffic controllers and other stakeholders will have a greater understanding of RNAV and RNP, enhancing wider acceptance and technical knowledge.

In FY 2011, FAA will continue to produce PBN routes and procedures at a similar rate as in FY 2010. These procedures and routes will be focused and mainly implemented in Metroplex areas. The FAA's efforts to deconflict arrival and departure traffic around multiple airports in congested metropolitan areas will move RNAV/RNP airspace and procedure design away from individual overlays into an Integrated Airspace and Procedures approach. The agency is also focusing on city pair networks, deconflicting and optimization of procedures serving airports in close proximity.

FAA initiated two databases to increase efficiency in tracking the progress and status of all PBN procedures. This web-based tool will help expedite PBN procedures, aids in Safety Management Systems compliance and expedites coordination with FAA's new more efficient 5 phase development and implementation of PBN procedures and routes.

Issue: Improving Programs for Developing the Next Generation of Air Traffic Controllers

I. Why is this an issue?

Over the next decade, FAA plans to hire and train nearly 11,000 new air traffic controllers to replace those who are close to retirement. Ensuring that these controllers are properly trained and certified at FAA's more than 300 air traffic control facilities requires effective national oversight and accurate metrics for measuring progress of new controllers in training.

II. Actions taken to date

FAA published a report that outlines training failure information by year, type of hire, what stage of training the student failed and completion time. FAA also published a com-

parison study that provides information on transfers, as well as whether or not the transferred controllers were successful or unsuccessful in their new facility. This study made multiple comparisons between en route and terminal air traffic control facilities as well as a comparison of the results of transfers from en route-to-en route facilities, en route-to-terminal facilities, terminal-to-terminal facilities, and terminal-to-en route facilities. The FAA has been analyzing and reporting the time it takes to become a Certified Professional Controller, the number of training failures, and the number of training delays. Enhancements of the methods used for analyzing and reporting on relevant training data continue. A periodic review of these specific indicators has continued through the end of the fiscal year and will continue into subsequent fiscal years.

FAA initiatives to analyze training hours and costs are based on contractor provided invoice data. This ongoing review of training hours and costs has allowed FAA to better monitor training/recruit trends. Also, FAA developed tools to predict contract costing trends for the Air Traffic Control Optimum Training Solution (ATCOTS) contract by May 1, 2010. These tools analyze training hours and weekly invoice data provided by the contractor. In addition, FAA has developed contractor utilization surveillance tools to monitor hours billed for supplemental field training. A program-wide online tool will be deployed in November 2010. As a result of prior recommendations, FAA has aggressively filled multiple ATCOTS program management positions, including Executive Lead, Communications Lead, Management Analyst, and Business Manager. Additionally, contract support vehicles have been utilized to provide contractor support for the Contracting Officer, Program Manager, and Quality Lead. New award fee metrics and goals were established to include individual competency, organizational competency, cost awareness, and customer satisfaction.

III. Actions remaining and expected completion date

Because of the boost in hiring activities since 2006, new air traffic controllers are increasingly brought on with no prior experience. The En Route facilities have established training programs which are able to handle and have been effective handling any type of controller new hire. However, some of the larger terminal facilities have been challenged in meeting the training demand. But since 2007 - and especially in the past year – the FAA has launched several initiatives to update its training methodologies and lesson plans to fit the profile of those who are being hired. The FAA continues to modify its training curriculum to improve its effectiveness for training today's workforce. In addition, periodic review of the stated key performance indicators, measures, and metrics, will continue to assist in determining where additional effort can be targeted, continuously improving the training system, including areas applicable to new hires from the general public.

An ATCOTS program-wide online tool to analyze contractor training hours and weekly costs will be deployed in November 2010.

IV. Results or expected results

The Technical Training Office is positioned to analyze training related data more efficiently with the data sets newly available on a regular basis, allowing for more substantial efforts towards root-cause analysis going into FY 2011. As the metrics and measures mature over the course of the next year, the office will be able to use them to strategically target training support and oversight efforts through weekly tasks, quarterly initiatives, and an annual workplan.

The ATCOTS program office successfully executed the second contract year and remained within the initial and supplemental funding allocation.

By revamping the award fee structure, the FAA now motivates the contractor to perform with added focus in specific program areas. This has resulted in the contractor aligning its initiatives to the FAA's vision for the Technical Training organization and provides a better structure to inform stakeholders on contractor contributions.

By increasing staffing at the FAA ATCOTS Program Office, the Government has improved its capability to support a performance-based, cost-plus contract of this magnitude, scope and complexity. It has built tools to improve day-to-day monitoring of the contract, processes for two-way communications to the field, and an organization structure to improve Program Office efficiency. The program stood up a quality assurance team that now analyzes contractor activities, and established a joint Risk and Opportunity Management Board to guide excellence and efficiency. The FAA participates in the contractor's quality assurance site visits and audits and manages its own instructor evaluation and voucher review programs. To augment existing voucher review processes, the FAA secured third-party audit assistance providing dedicated analyses to ensure direct and indirect costs paid under the ATCOTS contract are allowable and appropriate. The ATCOTS Program Office believes increased scrutiny of quality, cost and price performance could net additional savings that could be redirected to funding training development and delivery.

Once the FAA deploys the first phase of the contractor utilization surveillance tool, expected in November 2010, training managers in the field will be able to forecast and reallocate resources while remaining under established budget. This provides added flexibility for frontline training managers to move resources where they need them without having to go through a lengthy approval process that previously required action from both the FAA and contractor program managers.

6. Improving Contract Management and Oversight

Issue: Recent Government-wide Efforts to Stimulate the Economy and Reduce Spending Heighten the Need for DOT to Address Weaknesses in Contract Planning, Administration and Oversight

I. Why is this an issue?

For the past several years, the Department has had a weakness in its suspension and debarment (S&D) program and internal processes. Significant time delays were occurring for entering Operating Administrations (OAs) S&D decisions into General Services Administration Excluded Party Listing System.

These weaknesses increase the risk that the Department and other Federal agencies may award contracts and grants to irresponsible and/or fraudulent parties. DOT faces the following challenges:

- Strengthening DOT's suspension and debarment program to effectively safeguard against awards to improper parties; and
- Maintaining high ethical standards among DOT employees and fund recipients

II. Actions taken to date

In FY 2010, the Department revised and issued an updated S&D order (5200.E) which clearly defines expectations, processes, timeframes, and responsibilities of the OAs, Office of the Senior Procurement Executive (OSPE), the Office of the Inspector General (OIG), and the Office of General Counsel (OGC). It has also modified and enhanced the utility of the S&D reporting tool to increase tracking and management oversight capabilities. DOT has trained the OAs on the enhanced utility of the S&D tracking and reporting tool. It will continue the direct and formal line of communication with the OIG to ensure that the OSPE receives timely and accurate information regarding S&D activity throughout the Department. Finally, the Department has maintained intra-agency S&D quarterly meetings to share best practices, and updated the OAs on current internal and external developments or issues.

DOT continues to conduct reviews of completed and current Cost Plus Award Fee (CPAF) contracts, and de-obligate unused funds where legally acceptable, practicable and appropriate.

DOT continues to reduce the use of CPAF contracts with only 59 CPAF contracts in FY 2010, which is less than 1% of DOT's contracting activities. DOT had 197 CPAF contracts in FY 2009.

The SPE in conjunction with the modes is developing a Cost Plus Award Fee (CPAF) Guidebook incorporating planning, implementation and administration of CPAF contracts, based on guidance available from best practice agencies. The guidebook will be completed by July 1, 2011.

The Office of the Senior Procurement Executive and the OIG provided supplemental ethics training to the Operating Administration's contract and grant personnel. The training used interactive case studies that addressed a wide range of ethical concerns specific to contract and grant personnel. The Senior Procurement Executive issued a policy on 01/07/2009 APL-2009-01, Preventing Fraud in Contracting, which amplifies the requirement for contractor codes of ethics and conduct and internal controls systems.

The Operating Administrations are currently doing monthly site visits on American Reinvestment and Recovery Act (ARRA) grants. This ensures that internal controls systems are in place and assist in detecting fraud waste and abuse. Non-ARRA contracts are currently being reviewed randomly. The Department has incorporated the Financial Assistance Guidance Manual into TIGER grants to ensure that sound internal controls are in place to prevent and assist in detecting fraud. The Department's risk assessment office set up an internal control work group to assist in developing tighter internal controls for ARRA grants.

III. Actions remaining and expected completion date

The Office of the Senior Procurement Executive has completed the recommended OIG actions to strengthen internal controls, oversight, and transparency into the overall S&D process and program.

Outreach, training, site visits and risk assessments will continue for ARRA. This is an ongoing effort.

IV. Results or expected results

The new S&D Order 5200.E has clearly identified and clarified the roles and responsibilities of the OGC, OIG, OA's, and OSPE. The enhanced S&D reporting tool will be an excellent resource for management's use when inquiring about the status of S&D actions for an individual OA or for the Department as a whole. All S&D liaisons and officials have been trained on the reporting tool's utility and have attended workshops designed to explain the expectations and updates contained in the S&D Order 5200.E. It is anticipated that these enhancements will serve as a strong deterrent for effectively safeguarding the Department against contractor and grantee fraud, waste, and abuse.

The DOT Cost Plus Award Fee (CPAF) Guidebook will incorporate planning, implementation, and administration of CPAF contracts. The guidebook will provide the appropriate training to DOT program managers and contracting personnel involved in the use of CPAF contracts. This training will highlight proper CPAF award and administration and will result in increased knowledge and application and institution of an annual training requirement.

The supplemental training was received by approximately 500 employees. Based on the results of the survey, employees suggested that they now have a better understanding of Government ethics. The risk assessment and the monthly site visits have ensured proper oversight and have dovetailed into preliminary ethical issues and the Office of the Senior Procurement Executive has been able address the issue prior to escalation. This also allows the Government to spot glaring anomalies and mistakes. At this time, the Office is unable to pinpoint any issues directly.

7. Enhancing the Ability to Combat Cyber Attacks and Improving the Governance of Information Technology Resources

Issue: Given the Scope and Complexity of DOT Systems, it is Critical that DOT Effectively Manage and Secure its Information Technology Resources

I. Why is this an issue?

DOT's financial systems manage and disburse over $50 billion in Federal funds each year. At the same time, DOT's information technology (IT) budget covers more than 400 information systems across its 13 Operating Administrations – nearly two-thirds of which belong to the Federal Aviation Administration (FAA).

DOT faces the following management challenges:

- Establishing a robust information security program to support the Department's missions
- Increasing security protection and resilience of the air traffic control system to reduce the risks of cyber attacks

II. Actions taken to date

The Department's Office of the Chief Information Officer (OCIO) led the development of a Comprehensive DOT Strategy Plan. The plan focused on areas such as training, consolidation and integration, remediation, upgrades, governance, and infrastructure protection.

To influence the Operating Administrations (OAs), OCIO has established three control boards (Technology Control Board, Governance & Investment Board and the Cybersecurity & Privacy Board). All of the OAs contributed to the Cybersecurity Strategic Plan focus areas by having representatives work towards the DOT mission. By involving the OAs the Department is collaborating towards a joint solution. The Department has begun to issue PIV cards. Additionally the Departmental OCIO representatives have educated the OAs on the importance of PIV cards and credentialing. The OCIO developed action plans to remediate and mitigate known vulnerabilities by assigning team leads to oversee compliance.

FAA has resolved eighty percent of its web application security issues identified in the FY 2010 DOT Top Management Challenges. Compliance checks for all items were completed ahead of schedule. Meticulous tracking has been performed to document the successful resolution of identified issues. Completion has been slightly delayed due to Traffic Flow Management web asset consolidation at the William J. Hughes Technical Center, which will yield increased security benefits.

III. Actions remaining and expected completion date

The DOT Cybersecurity Strategic Plan is complete; plans of action are on-going initiatives that focus on people, process and technology.

IV. Results or expected results

The DOT CIO strategically developed a plan with mission, vision, goals and action objectives that included collaborative efforts with other Federal agencies and industry partners. The DOT CIO and executives developed a budget plan that concentrated on revamping the infrastructure of DOT to enhance the cyber security efforts. The OCIO conducted several briefings within DOT as well as to the Senate and House Appropriations Committees to present the challenges DOT faces in cybersecurity.

8. Developing a Funding Framework for the Next Surface Transportation Reauthorization

Issue: The Next Surface Transportation Reauthorization Will Need to Provide a Comprehensive Funding Framework for Addressing Infrastructure Needs

I. Why is this an issue?

The Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU), the current authorization law, expired at the end of FY 2009 and since then has been operating under an extension.

DOT faces the following management challenges:

- Ensuring the short-term solvency of the Highway Trust Fund (HTF);
- Assessing the annual federal funding needed to preserve and enhance surface transportation infrastructure; and
- Developing a comprehensive funding framework for the future

II. Actions taken to date

Throughout FY 2010 DOT released weekly cash balance tables for both the Highway Account and the Mass Transit Accounts. Both accounts maintained cash balances that were sufficient for prudent financial management.

DOT maintained outlay projection models for both the Highways and Transit programs to determine how current spending compares to projections. In FY 2010, both FHWA and FTA continued to assess the results of the most recent FY 2008 Conditions and Performance (C&P) Report. The Federal Transit Agency followed up the C&P Report with a special report on Maintaining a State of Good Repair at transit agencies nationwide.

Additionally in FY 2010, DOT conducted outreach events throughout the nation to gather input from stakeholders to develop proposals for the next reauthorization legislation.

III. Actions remaining and expected completion date

Work is ongoing to develop a reauthorization proposal.

IV. Results or expected results

Regular cash balance reporting has maintained a transparent chain of communications with Congress. The Department is on track to release a reauthorization proposal.

9. Strengthening the Department's Acquisition Workforce

Issue: Addressing Acquisition Workforce Retention and Recruitment Concerns

I. Why is this an issue?

Since 2001, human capital management has been identified as a Government-wide high-risk area. With the expanding and increasingly complex acquisition workload, addressing this risk is critical. About 46 percent of contracting specialists are eligible for retirement in less than 5 years. DOT needs to do more to ensure it has the needed size and skill levels to support its mission, especially given its need to oversee billions of dollars in ARRA funds.

II. Actions taken to date

DOT staff volunteered to participate in a government-wide New Hire Immersion Program Focus Group. The purpose of the focus group was to design a course which could be used to quickly train newly hired mid-level (GS9/12 or equivalent) acquisition individuals.

The Intermodal DOT Acquisition Workforce Working Group surveyed DOT Acquisition Directors to get input on rotational exchange and intern programs, designed an acquisition brochure to be distributed at job fairs and career days, conducted a networking Brown Bag where Acquisition Directors networked with new acquisition professionals and colleagues, and drafted requirements for a DOT Rotational Exchange program.

III. Actions remaining and expected completion date

DOT will finalize Rotational Exchange program requirements and implement them by FY 2011. It will also design and implement an intern program in FY 2012.

Based on input from the focus group participants, the Department will develop a final report of the program with specifications including contents, structure and schedule. The final report will be used to develop course materials and select instructors; ensuring that the report is aligned with the acquisition community's vision.

IV. Results or expected results

The above results will increase employee recruitment, engagement and retention.

Issue: Ensuring a Sufficient and Competent Acquisition Workforce to Meet Mission Needs

I. Why is this an issue?

Since 2001, human capital management has been identified as a Government-wide high-risk area. With the expanding and increasingly complex acquisition workload, addressing this risk is critical. About 46 percent of contracting specialists are eligible for retirement in less than 5 years. DOT needs to do more to ensure it has the needed size and skill levels to support its mission, especially given its need to oversee billions of dollars in Recovery Act funds.

FAA faces the same challenges confronting many Federal agencies and acquisition organizations. The number and complexity of acquisitions across the Federal Government have increased significantly at the time when retirement eligibility is on the rise. These combined factors are resulting in an ever-increasing competition for acquisition talent. Currently, about 15 percent of FAA's core acquisition workforce is eligible to retire with a cumulative eligibility of 32 percent by FY 2014. As increasing numbers of acquisition employees retire, FAA's pipeline could shrink. To combat this, FAA has a concerted focus on bringing in and developing new talent.

II. Actions taken to date

In FY 2010, DOT conducted the 2010 Acquisition Workforce Competency Survey. It issued DOT DASH reiterating that all Contracting Officer Technical Representatives (COTRs) must meet the Federal Acquisition Circular (FAC) COTR training requirements to achieve certification. It also issued FAC-COTR Certifications.

In FY 2010, FAA created the centralized Acquisition Career Management Group under the FAA Acquisition Executive. This group had its primary staffing in place by December 2009. The group's focus is workforce planning, workforce development, and the implementation of certification programs specifically designed for the acquisition workforce. The change in organizational infrastructure emphasizes the critical importance of the agency's acquisition workforce to mission accomplishment and transition to the NextGen air traffic control system.

On March 31, 2010, FAA published the Acquisition Career Program Guide under the Acquisition Management System (AMS) policy to further recognize the need for workforce competency. This Guide establishes core requirements related to competencies, training, experience, and certification for multiple acquisition workforce disciplines.

FAA's 2010 Acquisition Workforce Plan provides a profile section for each acquisition-related discipline to provide information about the community, critical competency requirements, training and certification programs, and other workforce-related initiatives. Additionally, FAA carried out reviews of the National Acquisition Evaluation Program (NAEP) in July, 2010. The findings are being used to identify performance gaps within the acquisition workforce. Current training programs and policies are being modified as needed. Areas of review included defining and estimating FAA requirements, making better use of performance-based acquisition, evaluation of proposals and negotiations, Contracting Officer Technical Representative (COTR) communications and management, and administration life-cycle logistics and contracts by program offices.

III. Actions remaining and expected completion date

DOT expects to update the COTR Program Guidance by the 2nd quarter of FY 2011. This will enable COTRs to go to one source to get information regarding the FAC-COTR Certification program. Changes have been made since the initial guidance in 2007 in the form of DOT DASHs and the guidance needs to be updated to reflect these changes. DOT will also update the Transportation Acquisition Manual and Transportation Acquisition Regulations by year end FY 2011 to incorporate required changes made since the last update for DOT-Wide source of information.

FAA has completed all tasks related to this management challenge.

IV. Results or expected results

DOT has a good understanding of its acquisition workforce's competency through the 2010 Acquisition Workforce Competency Survey. It provides clearer guidance to COTRs by clarifying the FAC-COTR requirements for certification. DOT reviewed and approved 454 FAC-COTR certifications and issued seven FAC-Cases DASH Policy Documents.

FAA expects to have the staffing and skill mix to successfully manage NextGen and other major acquisition programs now and into the future. Through the introduction of the Acquisition Career Management Group, documented plans and standards, and proper oversight, FAA will be able to estimate and implement training and support where most needed to effectively achieve its mission.

10. Successfully Implementing the Newly Created Multi-Billion Dollar High-Speed Intercity Passenger Rail Program

Issue: Designing and Implementing the HSIPR Program from the Ground Up

I. Why is this an issue?

The High-Speed Intercity Passenger Rail (HSIPR) Program required the Federal Railroad Administration's (FRA) to undergo organizational transformation, from an agency focused primarily on rail safety issues to a grant-making agency in a relatively short timeframe.

II. Actions taken to date

The HSIPR Program has made significant progress to date in meeting deadlines and obligating funds for both the Recovery Act and the FY 2009 and FY 2010 Appropriations. From a pool of 259 submissions, FRA has reviewed and selected 82 Recovery Act and FY 2009 high-speed rail applications for funding. FRA has obligated $579 million for Recovery Act projects and $9.2 million for FY 2009 Appropriations Act projects.

In addition, FRA has restructured its organization to more effectively manage the program. The Office of Passenger & Freight Programs was reorganized into six divisions to align with the functional responsibilities of administering the new HSIPR Program. FRA hired 11 new staff and filled other vacancies internally to support the HSIPR Program. Additionally, FRA has assigned a "customer support lead" to serve as FRA's primary contact for each State, supported by teams of subject matter experts.

III. Actions remaining and expected completion date

In addition to administering both current and future grants, FRA has identified three key areas essential to the implementation of the HSIPR Program. FRA will continue to hire additional HSIPR Program staff to fill the positions provided for in FY 2010 and future appropriations by the end of FY 2012. It will also develop final guidance to govern the program, rather than issuing interim guidance with each application solicitation – Advanced Notice of Proposed Rulemaking (ANPRM) targeted for FY 2011. Finally, FRA will continue to provide robust technical assistance to States (and other stakeholders) in developing and implementing their proposals.

IV. Results or expected results

Administratively, FRA's staffing increases will allow the agency to provide greater technical support to States, as well as improve the overall efficiency of the program's management. Developing final guidance for the program will provide States, railroads, Congress, and other stakeholders with greater clarity on the program's policies and organizational structure, as well as provide a consistent and predictable framework that allows for sound planning and investment decisions.

Issue: Establishing Policies and Procedures for the Program's Grant Lifecycle Process and Oversight Activities

I. Why is this an issue?

In order to meet the intent of the ARRA to promptly award funds and produce economic stimulus, FRA has operated under a series of interim measures in implementing the new HSIPR Program. While this approach has enabled the agency to stand up the program in a short timeframe greater standardization and documentation of procedures are necessary to ensure the program's long-term success.

II. Actions taken to date

During FY 2010, FRA developed and documented standardized grant management procedures in a new Grant Management Manual. It also drafted new interim program guidance for FY 2010 high-speed rail applications. FRA conducted significant outreach with States and other stakeholders to provide technical assistance in developing high-speed rail proposals, completing required application/award documentation, and complying with Recovery Act reporting requirements.

III. Actions remaining and expected completion date

FRA will need to provide training to grant managers on the application of the Grant Management Manual. This is expected in mid-FY 2011. FRA will also develop and begin implementing a robust oversight and monitoring program, consisting of programmatic, financial, and administrative reviews of grantee-submitted reports and documentation and grantee/project site visits conducted by FRA staff and project management oversight contractors by the end of FY 2011. FRA will also develop final guidance to govern the program that documents application evaluation and selection criteria and methodologies, reporting and oversight conditions, and requirements for supporting application/award documentation. The Advanced Notice of Proposed Rulemaking (ANPRM) is targeted for FY 2011.

IV. Results or expected results

In FY 2011, FRA intends to develop and implement policy changes that will affect both internal program administration and external stakeholder activities. By documenting standardized grant management procedures, FRA staff will be able to apply a consistent approach to grant administration and management. Developing final guidance for the program will provide States, railroads, Congress, and other stakeholders with greater clarity on the program's policies and organizational structure, as well as provide a consistent and predictable framework that allows for sound planning and investment decisions.

Financial Report

MESSAGE FROM THE CHIEF FINANCIAL OFFICER

I am pleased to issue the Department of Transportation's (DOT) Fiscal Year 2010 Agency Financial Report (AFR). This is the first year we have produced the AFR. The Annual Performance Report and the Citizens Report, a short summary of our activities, will be published in February 2011. This new and streamlined three-part format is a helpful reporting improvement for the benefit of the Congress and the public. For the accompanying AFR, we highlight our activities during 2010 on several fronts. We had a positive year, with notable achievements in many areas, including reducing improper payments, a successful financial audit, continuing efforts to modernize our financial systems, and implementation of the Recovery Act, among others.

Improper Payments

DOT has made significant progress in the area of improper payments. During 2010, we tested our largest grant programs, which include the Airport Improvement Program, the Federal-Aid Highway Construction and Planning Program, the Federal Transit Administration's (FTA) Capital Investment Grants, and FTA's Formula and Bus Grants. Together, these four programs represent over 90 percent of DOT's grants. Our analysis found that estimated improper payment rates for these programs did not exceed 1.5 percent, which falls below OMB's 2.5 percent threshold of "significant improper payments." Moreover, the payments cited as improper during testing were non-systemic improper payments, resulting from administrative or documentation errors, which were mistakes having a low-impact.

Annual Financial Audit

During 2010 we continued our emphasis on improved financial management, which contributed substantially to another unqualified audit opinion – DOT's ninth in the last ten years. For the third year in a row, we had no material weaknesses. The audit provides a useful review of our financial processes, and through this annual exercise, we continually strengthen our internal controls and become better stewards of taxpayer dollars.

Financial Systems Modernization

DOT continued to forge ahead with a major financial management improvement and modernization effort in 2010. Our recent focus formed the foundation for this program, with an emphasis on long-term strategic planning. In the coming years, this initiative will center on major system applications, improved financial reporting, and hardware components. During this period we also plan to address some related business process improvements, including such key activities as grant payments, vendor payments, and tools for better financial analysis.

Recovery Act Implementation

In 2010 we made excellent progress in implementing the American Recovery and Reinvestment Act (ARRA). Funding was designated to invest in transportation infrastructure, including transit capital assistance, high speed rail, pavement improvements and bridge repair, as well as to preserve and create jobs, and promote economic recovery. As of September 30, 2010 the second year of the ARRA program, the Department had obligated $39.6 billion and disbursed $20.5 billion.

Extension of the Highway Trust Fund (HTF)

In March 2010, the President signed the Hiring Incentives to Restore Employment (HIRE) Act. The Act extends authority to make expenditures from the HTF through December 31, 2010, and provides additional revenues to the HTF by restoring interest foregone since the fund stopped earning interest on its balances several years ago. The Act transferred $14.7 billion to the Highway Account and $4.8 billion to the Mass Transit Account from the General Fund. Going forward, the trust fund will resume earning interest on its invested balances. Also, refunds and credits of fuel taxes paid on fuel used for exempt purposes will be paid by the General Fund instead of the Highway Trust Fund. DOT worked diligently during 2010 on implementing this key legislation in order to maintain funding for critical transportation programs.

Looking ahead, we will build on our financial management accomplishments, and our critical financial systems and programs will continue to support our Department's strategic goals of Safety, State of Good Repair, Economic Competitiveness, Livable Communities, Environmental Sustainability and Organizational Excellence.

Christopher Bertram
Assistant Secretary for Budget and Programs, and Chief Financial Officer

OFFICE OF INSPECTOR GENERAL QUALITY CONTROL REVIEW

Memorandum

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

Subject: ACTION: Quality Control Review of Audited Consolidated Financial Statements for Fiscal Years 2010 and 2009, Department of Transportation
Report Number: QC-2011-021

Date: November 15, 2010

From: Calvin L. Scovel III
Inspector General

Reply to Attn. of: JA–20

To: The Secretary

I respectfully submit our report on the Quality Control Review of the Department of Transportation's (DOT) audited Consolidated Financial Statements for Fiscal Years (FY) 2010 and 2009.

The audit of DOT's Consolidated Financial Statements as of and for the years ended September 30, 2010, and September 30, 2009, was completed by Clifton Gunderson LLP (Clifton Gunderson), of Calverton, Maryland (see Attachment), under contract to the Office of Inspector General (OIG). We performed a quality control review of the audit work to ensure that it complied with applicable standards. These standards include the Chief Financial Officers Act, as amended; generally accepted government auditing standards prescribed by the Comptroller General of the United States; and Office of Management and Budget Bulletin 07-04, "Audit Requirements for Federal Financial Statements," as amended.

Clifton Gunderson concluded that the consolidated financial statements present fairly, in all material respects, DOT's financial position as of September 30, 2010, and September 30, 2009, and its net costs, changes in net position, and budgetary resources, for the years then ended.

We congratulate DOT for obtaining clean audit opinions with no material weaknesses for 3 consecutive years. Your senior leadership team, including the Chief Financial Officer and Modal Administrators, should be commended for its commitment to improving DOT financial management.

DOT substantially corrected two of the five significant deficiencies in internal control reported in Clifton Gunderson's FY 2009 audit report, but the remaining three significant deficiencies in internal control are again included in this year's report. In addition, there are two new significant deficiencies in internal control presented for FY 2010.

Clifton Gunderson FY 2010 Audit Report

Clifton Gunderson reported five significant deficiencies in internal control and four potential instances of reportable noncompliance with laws and regulations.

Significant Deficiencies

1. **Financial Accounting, Reporting and Analysis** - DOT must continue to reduce the use of journal entries and properly record reclassification and adjustment transactions in the Delphi general ledger system. Furthermore, DOT Operating Administrations (OAs) should follow a formalized systematic fund control process throughout the year to monitor fund status.

2. **Undelivered Orders** - DOT needs to strengthen controls for monitoring inactive obligations and de-obligate an estimated $1.5 billion no longer needed as of September 30, 2010. These funds could potentially be made available for other DOT requirements.

3. **Grant Accruals** - The Federal Highway Administration (FHWA) needs to enhance its review and analysis of grant accruals in order to more reliably measure the cost of grants programs and outstanding liabilities.

4. **Implementation of GrantSolutions Grants Management System** - The Federal Railroad Administration (FRA) needs to improve the effectiveness and functionality of its grants management processes and systems in order to strengthen controls and safeguard obligations.

5. **Controls over Financial Systems and Applications** - DOT's Enterprise Services Center must migrate the Department's accounting application to a new operation system supported by the database vendor, develop a lifecycle plan, and enhance communications with the Department and its OAs. Furthermore, DOT needs to implement effective security controls to protect its financial information from unauthorized access, modification, and disclosure throughout the year.

Noncompliance with Laws and Regulations

> **Anti-Deficiency Act** - DOT management needs to complete its assessment of four potential violations of the Anti-Deficiency Act reported at the Maritime Administration, the Federal Motor Carrier Safety Administration, and FHWA (two potential violations), and report confirmed violations as required by law. These OAs should also enhance their internal control systems for monitoring fund balances.

Clifton Gunderson made 30 recommendations to strengthen financial, accounting, and system controls. We agree with all, and therefore, are making no additional recommendations. DOT officials concurred with Clifton Gunderson's findings on the significant deficiencies and potential instances of noncompliance. The Department also committed to submitting to OIG, no later than December 31, 2010, a detailed action plan to address the findings contained in the audit report. In accordance with DOT Order 8000.1C, the corrective actions taken in response to the findings are subject to follow up. Accordingly, please provide us with quarterly progress reports on the actions taken to reduce the approximately $1.5 billion in unneeded obligations discussed in Clifton Gunderson's "Undelivered Orders" significant deficiency.

Our review disclosed no instances in which Clifton Gunderson did not comply, in all material respects, with applicable auditing standards.

We appreciate the cooperation and assistance of DOT and Clifton Gunderson representatives. If we can answer any questions, please call me at (202) 366-1959; Lou Dixon, Principal Assistant Inspector General for Auditing and Evaluation, at (202) 366-1427; or Earl Hedges, Acting Assistant Inspector General for Financial and Information Technology Audits, at (410) 962-1729.

Attachment

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Clifton Gunderson LLP
Certified Public Accountants & Consultants

Independent Auditor's Report

Secretary and Inspector General,
U.S. Department of Transportation

In our audit of the U.S. Department of Transportation (DOT) for fiscal year (FY) 2010, we found:

- The consolidated balance sheets of DOT as of September 30, 2010 and 2009, and the related consolidated statements of net cost and changes in net position, and the combined statements of budgetary resources for the years then ended (hereinafter referred to as "consolidated financial statements") are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America;
- No material weaknesses in internal control over financial reporting (including safeguarding assets) and compliance with laws and regulations, although internal control could be improved;
- Progress has been made in FY 2010 on the five control deficiency conditions noted in the FY 2009 auditor's report; however, certain matters relating to these conditions continue to exist and are reported herein as significant deficiencies. In addition, two new significant deficiencies were indentified during our FY 2010 audit; and
- Four instances of reportable potential noncompliance with laws and regulations we tested.

The following sections discuss in more detail: (1) these conclusions, (2) our conclusions on Management's Discussion and Analysis (MD&A) and other supplementary information, (3) our audit objectives, scope and methodology, and (4) agency comments and our evaluation.

OPINION ON FINANCIAL STATEMENTS

In our opinion, the accompanying consolidated financial statements including the accompanying notes present fairly, in all material respects, in conformity with accounting principles generally accepted in the United States, DOT's assets, liabilities, and net position as of September 30, 2010 and 2009, and net costs, changes in net position, and budgetary resources for the years then ended.

As discussed in Note 1U, *Summary of Significant Accounting Policies*, and Note 20, *Excise Taxes and Other Non-Exchange Revenue*, the accompanying financial statements reflect actual excise tax revenues collected through June 30, 2010, and excise tax revenues estimated by the Department of Treasury's Office of Tax Analysis for the quarters ended September 30, 2010.

As discussed in Note 1U, *Summary of Significant Accounting Policies*, the Hiring Incentives to Restore Employment (HIRE) Act of 2010 extended authority to make expenditures from the Highway Trust Fund through December 31, 2010. DOT has been developing several reauthorization proposals subject to OMB and Congressional approval. A timely extension of the Highway Trust Fund by December 31, 2010 is expected by DOT.

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CONSIDERATION OF INTERNAL CONTROL

In planning and performing our audit, we considered DOT's internal control over financial reporting as a basis for designing our auditing procedures and to comply with the Office of Management and Budget (OMB) audit guidance 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 entity's internal control over financial reporting and compliance or on management's assertion on internal control included in the MD&A. Accordingly, we do not express an opinion on the effectiveness of the entity's internal control over financial reporting or on management's assertion on internal control included in the MD&A.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency 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 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. We consider the deficiencies summarized below, and described in Exhibit I, to be significant deficiencies in internal control over financial reporting.

Exhibit I

1) Financial Accounting, Reporting and Analysis;
2) Undelivered Orders;
3) Grant Accruals;
4) Implementation of GrantSolutions Grants Management System; and
5) Controls over Financial Systems and Applications

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we do not believe that the significant deficiencies described in Exhibit I are material weaknesses.

We also noted certain other nonreportable matters involving internal control and its operation that we will communicate in a separate management letter to DOT management.

SYSTEMS' COMPLIANCE WITH FFMIA REQUIREMENTS

Under the Federal Financial Management Improvement Act of 1996 (FFMIA), we are required to report whether the financial management systems used by DOT substantially comply with the Federal financial management systems requirements, applicable Federal accounting standards, and the United States Standard General Ledger (SGL) at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements.

The objective of our audit was not to provide an opinion on compliance with FFMIA. Accordingly, we do not express such an opinion. However, our work disclosed no instances in which DOT's financial management systems did not substantially comply with Federal financial management systems requirements, Federal accounting standards, or the SGL at the transaction level.

COMPLIANCE WITH LAWS AND REGULATIONS

Except for potential violations of the Anti-Deficiency Act described in Exhibit II, our tests of DOT's compliance with selected provisions of laws and regulations for FY 2010, disclosed no other instances of noncompliance that would be reportable under United States generally accepted government auditing standards or OMB audit guidance. However, the objective of our audit was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

STATUS OF PRIOR YEAR'S CONTROL DEFICIENCIES AND NONCOMPLIANCE ISSUES

As required by United States generally accepted government auditing standards and OMB Bulletin No. 07-04, as amended, we have reviewed the status of DOT's corrective actions with respect to the findings and recommendations included in the prior year's Independent Auditor's Report dated November 14, 2009. Exhibit III provides a discussion on the status of prior year findings and recommendations.

DOT has made progress in FY 2010 on the five internal control deficiency conditions noted in the FY 2009 auditor's report; two of which are no longer considered Significant Deficiencies for purposes of this report. However, certain matters relating to these conditions continue to exist and further improvement is needed. These conditions are reported in Exhibit I as follows:

1) Financial Accounting, Reporting and Analysis;
2) Undelivered Orders; and
3) Grant Accruals.

With respect to laws and regulations compliance issues reported in FY 2009, the potential Anti-Deficiency Act violation associated with the U.S. Merchant Marine Academy continues to remain unresolved since FY 2007 and is described in more detail in Exhibit II.

CONSISTENCY OF OTHER INFORMATION

DOT MD&A and other required supplementary information (including stewardship information) is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the

methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Other information, exclusive of the MD&A and the Financial Report sections of the FY 2010 Agency Financial Report, is presented for additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

OBJECTIVES, SCOPE AND METHODOLOGY

DOT management is responsible for (1) preparing the financial statements in conformity with accounting principles generally accepted in the United States, (2) establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act (FMFIA), are met, (3) ensuring that DOT's financial management systems substantially comply with FFMIA requirements, and (4) complying with other applicable laws and regulations.

We are responsible for obtaining reasonable assurance about whether the financial statements are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States. We are also responsible for: (1) obtaining a sufficient understanding of internal control over financial reporting and compliance to plan the audit, (2) testing whether DOT's financial management systems substantially comply with the three FFMIA requirements, (3) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements and laws for which OMB audit guidance requires testing, and (4) performing limited procedures with respect to certain other information appearing in the Agency Financial Report.

In order to fulfill these responsibilities, we (1) examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements, (2) assessed the accounting principles used and significant estimates made by management, (3) evaluated the overall presentation of the financial statements, (4) obtained an understanding of DOT and its operations, including its internal control related to financial reporting (including safeguarding of assets), and compliance with laws and regulations (including execution of transactions in accordance with budget authority), (5) tested relevant internal controls over financial reporting, and compliance, and evaluated the design and operating effectiveness of internal control, (6) considered the design of the process for evaluating and reporting on internal control and financial management systems under FMFIA, (7) tested whether DOT's financial management systems substantially complied with the three FFMIA requirements, and (8) tested compliance with selected provisions of certain laws and regulations.

We did not evaluate all internal controls relevant to operating objectives as broadly defined by the FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to controls over financial reporting and compliance. Because of inherent limitations in internal control, misstatements due to error or fraud, losses, or noncompliance may nevertheless occur and not be detected. We also caution that projecting our evaluation to future periods is subject to risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate. In addition, we caution that our internal control testing may not be sufficient for other purposes.

We did not test compliance with all laws and regulations applicable to DOT. We limited our tests of compliance to selected provisions of laws and regulations that have a direct and material effect on the financial statements and those required by OMB audit guidance that we deemed applicable to DOT's financial statements for the fiscal year ended September 30, 2010. We caution that noncompliance with laws and regulations may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

We performed our audits in accordance with auditing standards generally accepted in the United States; the standards applicable to the financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States; and OMB guidance. We believe that our audits provide a reasonable basis for our opinion.

AGENCY COMMENTS AND OUR EVALUATION

In commenting on a draft of this report (Exhibit IV), DOT concurred with the facts and conclusions in our report. We did not audit DOT's response and, accordingly, we express no opinion on it.

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This report is intended solely for the information and use of DOT management, DOT's Office of Inspector General, OMB, the Government Accountability Office, and the U.S. Congress, and is not intended to be, and should not be, used by anyone other than these specified parties.

Clifton Gunderson LLP

Calverton, Maryland
November 12, 2010

EXHIBIT I

DEPARTMENT OF TRANSPORTATION
INDEPENDENT AUDITOR'S REPORT
SIGNIFICANT DEFICIENCIES
September 30, 2010

1. Financial Accounting, Reporting & Analysis

Conditions:
Although DOT management has improved its accounting and financial reporting processes over the past year, certain conditions noted in the prior year continue to exist. The following deficiencies still exist in the DOT's internal controls relating to its financial reporting accounting, reporting and analysis.

a) Over Reliance and Use of Journal Entries, Use of Object Class 00000 and Null Undelivered Orders

Even though DOT has made improvements in this area this year, the problem continues to be substantial and needs more focused attention to ensure reliability of the financial reporting process used by DOT both during the year and at year end.

DOT and its Operating Administrations (OAs) recorded over 8,600 journal entries (JEs) totaling an absolute value of approximately $606 billion during FY 2010. Of the approximately 8,600 JEs used to record transactions, approximately $459 billion in absolute value were period end entries, parent-child reporting entries, and trust fund accounting entries. These entries were made as part of the normal period end accrual entries or because of the general ledger system limitations, for which the use of the JEs is considered necessary. However, many of the JEs in the absolute value of approximately $147 billion appeared to relate to reclassifications and adjustments transactions as a result of entries not being properly recorded in the general ledger system initially. Many of these JEs could have been avoided by processing DOT's normal transactions through its general ledger system, Delphi, modules such as the Budget Execution Module (BEM) or by using Delphi's standard transaction codes. In addition, DOT recorded approximately $2 billion in absolute value of activity and a net balance of $982 million to the 00000 object class code. Furthermore, an absolute value of approximately $1.9 billion of the undelivered order (UDO) balance contained null UDO transactions. The Department describes the object class 00000 as not applicable. Null UDOs are transactions recorded in the general ledger without a specific purchase order number.

DOT, in its effort to achieve standardization of the OAs' use of the JEs, issued a JE policy in May 2010, and DOT, as a whole, has made progress in this area from the prior year. However, more work is still needed to improve in this area. The volume and amount of these adjustments suggest that financial system limitations continue to impede DOT's ability to record certain activities within their Delphi system at the transactional level so that all financial events are properly captured at the time when the transactions occur. This manually intensive process has a high risk of error, is time consuming, and utilizes resources that could be spent on other financial reporting matters.

b) Fund Status Reporting Throughout the Year and at Year-end

DOT's OAs did not follow a formalized systematic fund control reporting and monitoring process throughout the year for their status of funds. Each OA used various tools and resources to monitor their status of funds throughout the year and at year-end. These tools and resources consist of various Delphi web based reports or Excel spreadsheets that may or may not provide the necessary budgetary data to monitor the OAs' fund status and are manually intensive to produce. Much of the financial data included on the Delphi web based reports is limited in nature due to the fact that the information included is as of the report run date instead of a period of time such as at year-end. Certain Delphi web based reports did not include financial data at the allotment level, which is the level at which DOT applies funds control. In addition, the OA personnel responsible for monitoring the status of funds varied amongst OA division offices and level of employees. Such inconsistency in fund control monitoring processes increases the risk that anti-deficiency violations may have occurred and not prevented or detected at the OA level and ultimately reported to DOT in a timely manner. Consequently, DOT management was in the process of evaluating the status of four potential anti-deficiency matters related to Federal Highway Administration (FHWA), Maritime Administration (MARAD) and Federal Motor Carrier Safety Administration (FMCSA) at September 30, 2010 as discussed in Exhibit II.

Recommendations: We commend DOT management for the efforts and improvements they have made in its internal controls, application of accounting principles, and monitoring processes over the past year. However, as evidenced by the conditions noted above, continued diligence in this area is needed to further advance the progress made to date. Accordingly, we recommend that DOT management:

1) Over Reliance and Use of Journal Entries

a) Revise its financial reporting processes so that the majority of the journal entries are not recorded manually. Adjusting journal entries should be used for limited transactions (i.e. quarterly accruals, unusual one-time entries, etc.) In addition, DOT should refine the Departmental JE policy issued in May 2010 to include guidance for budgetary entries.

b) Perform a pro forma analysis to ensure that post closing effects are considered prior to recording significant adjustments (excluding the routine adjustments such as the quarterly or yearend accruals entries) into the general ledger system. For budgetary entries, financial management should review the entries with the budget officials to ensure both are in agreement prior to recording them.

c) Continue with financial management modernization efforts to define and re-engineer business processes which aid in the design and configuration of its next upgrade to Oracle R12. R12 should be configured as a fully integrated financial management system allowing for the use of event driven rules (based on Treasury Transaction codes) in the subsidiary modules. In addition, as part of the Oracle R12 upgrade, management should ensure consistent and standardized data elements and data fields can be utilized to process and record transactions to achieve the greatest efficiency and consistency in its financial reporting for future years.

d) Incorporate the elements of the FSIO Core Financial System Requirements Exposure Draft dated February 2010 and the applicable requirements schedule such as the General Ledger Requirement schedule. Upon implementation of the Oracle R12 update, management should ensure that each requirement included in the General Ledger Requirement schedule is met.

e) Perform a quarterly review to verify whether the use of the 00000 object class is consistent with pre-established policy. If the use is not consistent with policy, the OAs should promptly reclassify amounts to the proper object class.

f) Continue to research the underlying cause of the null UDO activity. The activity recorded in the general ledger should be identified and corrected with a specific document number reported in the Delphi subsidiary system to properly account for the open obligations.
g) Provide training or periodic reminders to users of the Delphi system to ensure that transactions continue to be processed in accordance with Departmental or OA policies and procedures.

2) Fund Status Reporting

a) Develop and implement a process to monitor the status of funds which includes formalizing policies and procedures at the Department level. Accordingly, the information should be disseminated to each OA to ensure that a systematic process is used to monitor the status of funds. The policies at a minimum should include the following:

- OA division/office including the level of the staff responsible for monitoring the status of funds.
- The frequency of the review of the status of funds
- The financial system and the documentation (i.e. reports) that should be used to track and/or monitor the status of funds.

b) Review the current Core Financial System Requirements Exposure Draft released on February 22, 2010 and the applicable functional and subfunctional design specifications such as the Funds Management Requirements. Upon implementation of the Oracle R12 upgrade, management should ensure that the functional and subfunctional requirements for Funds Management have been met.

2. Undelivered Orders

Conditions:
DOT obligates its budgetary resources when it enters into a binding legal agreement such as a grant or a contract with a third party. At the end of the grant or contract period, any previously obligated but not disbursed amounts (also known as undelivered orders, UDO) associated with completed or cancelled projects should be de-obligated enabling the unused funds to potentially become available for other agency program needs. When the unneeded obligations continue to remain on DOT's books, they are considered to be inactive invalid obligations. DOT reported approximately $106.6 billion of UDO at September 30, 2010. Of that amount, approximately $4.1 billion was related to contracts and $4.8 billion was related to grants with no activity for longer than 12 months. It is critical that DOT OAs continue to improve upon their management and monitoring of inactive obligations to ensure the status of the budgetary resources is reported accurately and represent valid obligations of the DOT. The following deficiencies still existed in the DOT's internal controls relating to the UDOs during FY 2010:

a) During our statistically based sample testing of the UDO balances at September 30, 2010, we noted 29 instances out of 60 items tested where the UDO balance should have been de-obligated because the project was completed or the amount recorded could not be substantiated by management. The projected value of the error to the entire UDO population was estimated to be an overstatement of approximately $1.5 billion. DOT recorded an adjustment in that amount to its Statements of Budgetary Resources at September 30, 2010.

b) During our site visits with FHWA and FTA Divisional or Regional offices in FY 2010, we found that certain of those Divisional or Regional offices did not properly monitor the inactive projects and liquidate the unused obligations in a timely manner. Some projects had remained inactive or had been completed with unused obligations carried forward into the current fiscal year. Those projects' period of inactivity ranged from one year to more than ten years.

Recommendations: The projected error in the UDO balance at September 30, 2010 continued to be substantial, and the reasons for the extent of these errors need focused attention to avoid an escalation of the problem in FY 2011. We recommend that DOT take the following actions to immediately reduce the error in the UDO balance and resolve the risk of significant error in the future:

1) Standardize the inactive UDO review process throughout DOT by providing data download of inactive UDOs on a quarterly basis to the OA management and require the OAs to report the status of these inactive UDOs to DOT management. Internal review of the inactive UDOs should focus on the inactive projects and contracts and should be incorporated into DOT's A-123 Appendix A implementation efforts. One technique could include a review of support documentation obtained by using a stratified sampling method. Timely follow up of areas with a higher degree of invalid obligations should be performed to ensure better compliance.

2) Monitor the field offices' quarterly inactive project reviews, particularly on stagnant projects, to ensure that inactive obligations are liquidated in a timely manner throughout the year.

3) Update the policies and procedures to include specific procedures for the timely monitoring and liquidating of inactive obligations. The qualifier "timely" should be clarified in the guidance to ensure consistent implementation of the requirements.

4) Implement policies and procedures which require the OAs to more diligently follow-up with their contracting officers, project managers or grantees to identify and de-obligate unneeded obligations in a timely manner.

3. Grant Accruals

Conditions:
DOT reported approximately $61 billion of grants related expenditures in FY 2010. At September 30, 2010, DOT estimated a grant accrued liability of approximately $7 billion for expenditures incurred by its grantees but not yet reimbursed by DOT. Of the $7 billion reported by DOT, approximately $5 billion were related to FHWA's grant programs. FHWA management did not perform a trend analysis of its grant accrual estimates in FY 2010. The unresolved significant differences between the estimate and actual noted in FY 2009 ranged from a negative $667 million to a positive $404 million, representing a percentage difference range of negative 17% to a positive 16%. In addition, FHWA management did not perform an adequate review of its June 30, 2010 grant accrual calculation resulting in the interim financial statements being understated by approximately $203 million. The lack of adequate review and analysis for the FY 2010 accrued amount coupled with the unresolved significant differences affects FHWA's ability to reliably measure the full cost of its grant programs and the liability it had outstanding with its grantees for costs incurred but not yet reimbursed at September 30, 2010.

Although the Federal Financial Accounting Technical Release (TR) No. 12, *Accrual Estimates for Grant Programs,* does not become effective until the periods beginning after September 30, 2010, the earlier implementation of the guidance is encouraged. TR No. 12 requires federal agencies with significant grant programs to implement adequate and effective internal control procedures to ensure that grant accrual estimates are based on historical transactions and that a trend analysis of grant accrual estimates from year to year be completed. Also, investigations of unusual fluctuations should be performed and the related results should be documented. Due to the lack of available resources, FHWA was unable to perform the grant accrual trend analysis to support the reliability of its grant accrual methodology in FY 2010.

Recommendations:
We recommend that DOT management ensure FHWA:

1) Proactively assess resource constraints well in advance to ensure that the proper attention is given to significant financial management issues such as the validation of the grant accrual estimate. In addition, FHWA management should enhance its oversight and review of the grant accrual calculation to ensure that the amount is properly reported in the financial statements and footnotes.

2) Perform the grant accrual look back analysis on a quarterly basis throughout the fiscal year. Consistent with our prior year recommendation, the application of these methods used to perform the look back analysis should result in providing sufficient evidence to explain unusual variances or support to update the current grant accrual methodology. Such periodic assessment of the adequacy of the grant accrual methodology should be documented and supported by data analysis. The estimated liability amount is subject to risk that actual subsequent disbursement amount may be significantly different than management's estimate. When this occurs, management should further analyze the drivers/factors for such an unexpected occurrence to ensure the validity and reasonableness of the estimation methodology.

3) Implement the FASAB TR No. 12 for grant accrual estimates, consider the prior year recommendation, and assess the reliability and reasonableness of its current grant accrual methodology by performing the following:
    a) Survey sufficient number of grantees due to the waiver of the Paper Reduction Act and update the grant accrual methodology based on the most current and relevant information. Consider reviewing the survey results with the relevant program officials at FHWA to ensure consistency and reliability of information received from the grantees.
    b) Consider using results of the audited grantee information like the accrual amounts reported by its state grantees in their audits and adjust for any programmatic changes that occurred at the grantee level to determine whether the survey information included by the grantee is materially correct or supported. Additionally, the audited information may be used as another tool to validate its grant accrual methodology.
    c) Assess whether an adjustment to the current methodology is warranted based on the various analyses performed by management.

4. Implementation of GrantSolutions Grants Management System

Conditions:
Federal Railroad Administration (FRA) received over $9 billion in funding under the American Recovery and Reinvestment Act of 2009 (Recovery Act). In addition, FRA, with its key role in providing the Federal government's support of the nation's rail transportation activities, receives increased annual appropriations from Congress from approximately $1.8 billion in FY 2009 to over $4 billion in FY 2010. As of September 30, 2010, FRA reported approximately over $9.9 billion of unobligated funds. Though funds have not been obligated, the majority of the amount is appropriated for specific grants programs. In order to strengthen and streamline its controls surrounding the grants management process, FRA implemented the GrantSolutions grants management system and processed one grant in FY 2009. Starting in FY 2010, all new grant awards were processed and obligated through GrantSolutions except for the Amtrak grants. FRA's partial implementation of an automated grant management system is a significant improvement over the manual process previously used. However, we identified several areas for improvements to enhance the effectiveness of the grant management process including the functionality of the grants management systems.

a) Lack of Grant Award Obligations Interface with Delphi
The GrantSolutions system does not interface with the Delphi general ledger system. The lack of an interface requires DOT personnel to manually input obligation data into each of the aforementioned systems separately. This duplication and manual intensive process increases managements' susceptibility to risks that errors will occur and not be prevented nor detected in a timely manner. FRA informed us that they are actively working with the Enterprise Service Center (ESC) and the service provider for GrantSolutions to develop, test, and deploy an interface between Delphi and GrantSolutions. The non-integration of GrantSolutions with Delphi creates redundancy and inefficiency that increases the risks that grant awards are not recorded in the general ledger system accurately or in a timely manner.

b) Lack of Commitment Accounting Implementation
FRA does not use commitment accounting to reserve grant funds that have been approved for award. By not implementing commitment accounting, coupled by the manual obligation recording process, there is an increase risk that funds intended for that grant may no longer be available for obligation.

c) Amtrak and Prior Years Awarded Active Grants not Recorded in GrantSolutions
FRA does not use GrantSolutions to process and obligate grants recorded in Delphi awarded to Amtrak, which amounts to billions of dollars annually. The Amtrak grant awards are manually processed and obligated. In addition, FRA has not migrated any currently active grants awarded in prior years into GrantSolutions, but instead records all subsequent amendments issued in FY 2010 to those active grants as new awards within GrantSolutions. As a result, the original grant is administratively closed-out upon completion of the period of performance, and management has to consult both hard copy files and GrantSolutions to monitor and determine the status of some active projects. This is not an efficient process. When all grants are not recorded in a single grant management system, management cannot readily determine the completeness and accuracy of the grant activities including grant obligations and expenditures. This may result in errors in the financial records and ultimately in the financial statement and related footnotes. In addition, inaccurate reporting to third parties such as OMB may be impacted.

d) **Complete Reconciliation of Cumulative Balances between GrantSolutions and Delphi Not Performed**

FRA does not perform periodic reconciliations between the grant obligations amounts recorded in GrantSolutions to the obligation amounts recorded in Delphi. FRA management stated at the time the grant amount is obligated and recorded in Delphi, a manual review is performed to verify that amount agrees to GrantSolutions. A periodic reconciliation between the two systems would ensure that the grants awarded through GrantSolutions are recorded in Delphi and that the amounts obligated are the same in both systems. Also, a periodic reconciliation would indentify any funding changes that were made in GrantSolutions and not made in Delphi and vice-versa. Not performing periodic cumulative reconciliations between GrantSolutions and Delphi increases the risk that all activities are not accurately reflected in the financial records and ultimately in the financial statements.

e) **Grant Disbursement Data not Recorded in GrantSolutions**

FRA does not record the grant disbursements within GrantSolutions. Instead, FRA's grantees submit Requests for Advance or Reimbursement (SF-270) directly to the ESC in Oklahoma City, for subsequent recording into Delphi. The ESC personnel process the SF-270 in MarkView and forward the request to the appropriate Grant Manager and/or COTR for review and approval. Once approved, the Grant Manager or COTR subsequently updates FRA's administrative records to track the fund status of the grant obligation by updating a manual tracking spreadsheet and filing hard copies of the requests for reimbursement in the official grant file. As a result, FRA uses two separate systems to track the obligations and expenditures, which makes the grant post award monitoring manually intensive, inefficient, and prone to human errors. FRA informed us that they are planning to migrate to DOT's new grant payment system, iSupplier, for processing disbursements. This new system will directly interface with Delphi and subsequently, to GrantSolutions.

f) **Federal Financial and Grant Progress Reports Not Accomplished through GrantSolutions**

FRA does not require its grantees to submit their Federal Financial Reports (SF-425) and Progress Reports through the GrantSolutions system. Currently, all financial and progress reports are submitted to FRA either through the mail or as email attachments. This process requires extra time for staff to download the reports from email accounts, scan the hard copies, and then upload them into GrantSolutions. As a result, the current grant post award monitoring process is manually intensive, inefficient, and prone to delays and human error. FRA confirmed that they will be testing the SF-425 submission functionality in GrantSolutions and anticipate the full implementation of the electronic submission of the SF-425 and progress reports in FY 2011.

g) **Lack of Utilization of Electronic Signatures in GrantSolutions**

In addition to requiring grantees to electronically accept grant awards through GrantSolutions, FRA requires grantees to print the grant document, sign it, and then return the hard copy to FRA. Once FRA receives the signed grant document, it is signed by the FRA Administrator and sent to the ESC for recording the obligation. This administrative process can result in significant delay between the time the grant is approved for funding by the FRA Administrator and when the obligation is actually recorded in Delphi. FRA's manually intensive grants management process heightens the susceptibility of risk of errors being recorded without being detected. Also, there is an increased risk of not recording obligations in a timely manner.

h) Lack of SAS 70 Review for GrantSolutions

FRA has not obtained nor reviewed the latest SAS 70 report that was performed on the GrantSolutions system operated by the Department of Health and Human Services. The review of the SAS 70 will assist FRA in implementing the necessary user controls and in assessing and evaluating certain control risks relating to their utilization of the GrantSolutions as their grants management system.

i) Finalization and Implementation of the Grants Manual

FRA does not have a grant reference manual for use by grant management and program personnel as a day-to-day operational tool to properly process and actively manage and monitor their grant awards. FRA provided a draft copy of a financial guide they are currently drafting and stated that they anticipate publishing an FRA financial guide in FY 2011. Incomplete or inadequate grants management policies and procedures increase management susceptibility to programmatic/operational and financial risk including redundancy, inefficiency, waste, fraud and abuse of budgetary and human capital resources.

Recommendations:

We recommend that DOT management ensure FRA:

1) Implement GrantSolutions capabilities and functionalities that include the integration with the DOT Delphi accounting system or other planned disbursement system such as iSupplier. In addition, management should update the system functionality to include grantee financial and progress reporting submission directly into GrantSolutions. A complete reconciliation between the GrantSolutions and Delphi should be performed on a monthly basis. Any identified differences should be resolved within 60 days at minimum.

2) Consider the implementation and use of commitment accounting to strengthen fund controls. Funds should be reserved at the time the grant is recommended for funding. Grant obligations should occur at the time the grant agreement is electronically approved by the FRA Administrator.

3) Record all active grants in GrantSolutions. This includes grants awarded to Amtrak and any open prior year grants for which only amendments have been processed through GrantSolutions.

4) Identify, assess, and evaluate specific programmatic/operational and financial risk within its grants management process, including the implementation of a grantee risk assessment process to be performed annually to determine whether additional oversight efforts are necessary to mitigate the grantee risks that could result in questioned costs. Management should subsequently implement control activities to address such risks. Control activities should include the development of the grant reference manual that incorporates the operational, programmatic and financial management requirements, and also include management review of the applicable SAS 70 report and consideration of the SAS 70 report results.

5. Controls over Financial Systems and Applications

Background and Control Deficiency Assessment Criteria:

The information systems relevant to financial reporting objectives include automated and/or manual controls over records established to initiate, authorize, record, process, and report entity transactions. These controls also include the processing and maintenance of information in the general ledger accounting system, for the accountability and reporting of budgetary and proprietary accounting information, the related assets, liabilities, and equity. The quality of this information affects management's ability to make appropriate decisions in controlling the entity's activities and to prepare reliable financial reports.

The extent and nature of these risks is dependent upon the effective implementation of internal controls to ensure the integrity of information processed and maintained. For example, multiple users, either external or internal, may access a common database of information that affects financial reporting. In such circumstances, a lack of control at a single user entry point might compromise the security of the entire database, potentially resulting in improper changes to or destruction of data. When IT personnel or users are given, or can gain, access privileges beyond those necessary to perform their assigned duties, a breakdown in segregation of duties can occur. This could result in unauthorized transactions or changes to programs or data that affect the integrity of data used to produce the financial statements.

Monitoring of internal controls is a key control process to determine appropriateness of the design of controls, the effectiveness of the controls, and the need for corrective actions, and whether additional safe guards and/or enhancements should be made to the internal controls as they mature. Monitoring is done to ensure that controls continue to operate effectively. For example, if the timeliness of software patching and upgrades are not monitored, the software may be vulnerable to unauthorized access, modification, disclosure, loss or impairment. Monitoring of controls is accomplished through ongoing monitoring activities, independent evaluations, or a combination of both.

Conditions:

The DOT's ESC provides financial transactions processing and reporting services to DOT. The ESC has provided DOT with the Statement on Auditing Standards (SAS) No. 70, Service Organizations, Report on Controls Placed in Operation and Tests of Operating Effectiveness of the general, applications and operational controls related to the ESC for the nine-month period ended June 30, 2010. The Independent Service Auditor (ISA) qualified its opinion on the operating effectiveness of controls. The ISA found that ESC's configuration management controls did not operate effectively and impacted the Center's access controls. Specifically, the DOT's general ledger system, Delphi, resides on an operating system for which the database vendor stopped providing security patches and those security patches that were applied were not applied timely. This poses additional control risks to DOT, that its general ledger system's database cannot be updated to protect against known security vulnerabilities. ESC did not adequately consider the security of the Delphi application in the system development life cycle to appropriately plan and migrate Delphi to an operating system that will be supported by the database vendor.

DOT was not alerted to the security life cycle risks posed by the impending obsolescence of the Delphi operating system. ESC's monitoring and risk mitigation process was not effective in ferreting out risk implications of the impending software obsolescence. Although, ESC management presented a policy for evaluating individual patches, assessing the suitability to

ESC's environment, level of threat, compensating controls and risk, the ISA found no evidence of compliance with this policy. This deficiency prevented DOT from evaluating the impact of this weakness in a timely manner, and ultimately implementing effective security controls to protect its information from unauthorized access, modification, and disclosure prior to it being alerted of the aforementioned security life cycle risks.

Recommendations: We provide the following recommendations to the respective DOT and OA management:

1) ESC
    a) Promptly migrate the Delphi application to an operating system supported by the database vendor.
    b) Develop and implement a system development life cycle process to plan for the deployment and retirement of information technology resources.
    c) Enhance the communication process with DOT and its OAs to ensure information life cycle issues are adequately addressed and planned for in a timely manner.

2) DOT management should request an action plan from ESC to resolve these matters, and request periodic reports from ESC on the status of the implementation of the above recommendations and apprise its OAs of the status of such action plan.

3) DOT and its OAs' management should continue to assess the impact that these findings have on its financial operations, and continue to focus its efforts on reducing the risk of errors in its financial statements through the use of compensating controls until this matter is resolved.

EXHIBIT II

DEPARTMENT OF TRANSPORTATION
INDEPENDENT AUDITOR'S REPORT
NONCOMPLIANCE WITH LAWS AND REGULATIONS
September 30, 2010

1. Anti-Deficiency Act

Conditions:

a) Maritime Administration (MARAD)

In FY 2009 the Secretary of the Department of Transportation reported Anti-Deficiency Act (ADA) violations related to MARAD's United States Merchant Marine Academy (Academy). In addition to the actual violations reported to the President, the President of the Senate, the Speaker of the House of Representatives, Office of Management and Budget (OMB) Director and the Acting Comptroller General, the Government Accountability Office (GAO) issued an audit report titled "Internal Control Weaknesses Resulted in Improper Sources and Uses of Funds; Some Corrective Actions Are Under Way" in August 2009. The GAO audit report identified additional potential ADA issues for midshipmen fee transactions that occurred during calendar years 2006 and 2007 related to the following:

- fees collected and uses of fees unrelated to goods and services provided to all midshipmen,
- fees collected that exceeded the actual expenses to the Academy for the goods or services provided, and
- the use of accumulated excess midshipmen fees for improper and questionable purposes.

b) Federal Motor Carrier Safety Administration (FMCSA)

During FY 2010, FMCSA identified potential ADA violations related to the following:

- Reprogramming and obligation of funds across Programs, Projects, or Activities without an approved SF-132 reapportionment from OMB in FY 2008. Specifically, it reprogrammed funds from Commercial Vehicle Information Systems and Networks (CVISN) Grant program to the Safety Data Improvement Grants program (SaDIP) in the amount of $0.3 million and to the New Entrant Grant program in the amount of $3.2 million.
- A Motor Carrier Safety Assistance Program grant to the State of New Jersey in the amount of $30,000.
- Deficiencies in the CVISN grant program. The deficiencies indicated that a number of States might have received grant awards that exceeded the statutory amount caps or received grant awards for which they were not eligible.

c) Federal Highway Administration (FHWA)

During FY 2010, FHWA reported that FY 2010 obligations in the American Reinvestment and Recovery Act (ARRA) appropriation account for the Refuge Roads program may be in excess of the amount apportioned under Category B of the Apportionment and Reapportionment Schedule (SF-132) approved by OMB on April 28, 2010. FHWA is currently analyzing the actual obligations for the program to make a proper determination as to whether an ADA violation actually occurred prior to the September apportionment.

d) Federal Highway Administration (FHWA)

FHWA reported that one project obligated for the Transportation Investment Generating Economic Recovery (TIGER) discretionary grant program during FY 2010 was made prior to the allotment advice was provided by DOT's Office of the Secretary (OST) to FHWA. FHWA obligated the funds on July 16, 2010 while the allotment advice from OST was not provided until August 12, 2010.

As of the date of our report, the DOT management had not completed their assessment of these potential violations.

Recommendations: MARAD, FMCSA and FHWA management have taken several corrective actions to address internal controls related to those potential anti-deficiency matters in FY 2010. However, we recommend that DOT management ensure the relevant OAs:

MARAD

1) Continue to implement and monitor the implementation of the recommendations made by GAO in the aforementioned GAO report.
2) Determine whether sufficient appropriations remain available to be charged the official Academy expenses and report ADA violations accordingly if sufficient appropriations are not available to cover those expenses.
3) Establish a formalized and documented process to reimburse midshipmen for overcharged fees.

FMCSA

FMCSA's potential ADA issues indicate internal control weaknesses in the fund control and grants management areas. Management has taken steps to improve upon its fund control monitoring procedures and is in the process of implementing an OMB endorsed automated grants management system to capture the grant transactions through their lifecycle from grant application receipt to grant closeout. This automation will increase the accuracy and accountability of the grant management process. The system will also interface with Delphi to improve upon the grant reconciliation process. We provided recommendations related to DOT's fund controls and fund status reporting and FRA's grant management system implementation in item # 1and #5 of Exhibit I above for FMCSA's implementation. We further recommend the following to address the potential ADA matters:

1) Determine whether ADA violations occurred and report ADA violations accordingly as required by law.
2) Establish comprehensive risk-based internal control systems for fund control and grants management that address the core issues identified. In addition, internal review of the fund controls and grant reconciliation processes should be incorporated into DOT's A-123 Appendix A implementation efforts.

FHWA

1) Determine whether ADA violations occurred and report ADA violations accordingly as required by law.
2) Evaluate the cause for the over-obligations and establish a comprehensive internal control system for monitoring funds control on a real-time basis when an obligation is recorded. Delphi absolute fund control edit checks should be in place to stop the over obligation from occurring.

EXHIBIT III

DEPARTMENT OF TRANSPORTATION
INDEPENDENT AUDITOR'S REPORT
STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2010

Prior Year Condition	Status As Reported at September 30, 2009	Status as of September 30, 2010
Control Deficiencies		
1. Financial Accounting, Reporting & Analysis	***Significant Deficiency:*** The DOT has weaknesses in the following: • Reliance and use of journal entries • Accounting and reporting for Property, Plant and Equipment (PP&E), including the Construction in Progress assets • Timely follow-up of identified Amtrak financial reporting issue	Issues related to FAA and MARAD PP&E accounting, and Amtrak financial reporting have been resolved in FY 2010. The use of journal entry issue is included as part of Significant Deficiency number 1 in Exhibit I.
2. Undelivered Orders (UDO)	***Significant Deficiency:*** • Various testing errors resulting in actual and projected errors of approximately $800 million in UDO at September 30, 2009. • Null UDOs in the absolute value of $2.1 billion and net value of $420 million at September 30, 2009. • Untimely liquidation of inactive projects identified during our FY 09 site visits by FHWA and FTA Divisional or Regional offices	Repeated as a Significant Deficiency number 2 and included in Exhibit I.
3. Grant Accruals	***Significant Deficiency:*** Certain OAs (FHWA and FTA) did not receive sufficient information or perform the look back analysis to either evaluate the accuracy and reliability of the accrual estimate as of September 30, 2009 or update their estimates for FY 2009.	Repeated as a Significant Deficiency number 3 for FHWA in Exhibit I. Remaining issues for FTA are downgraded to a Management Letter deficiency.
4. Financial Management Oversight by MARAD	***Significant Deficiency:*** MARAD has weaknesses in the following areas: • Incorrect reporting of Navy transferred ships • Environmental liability calculation – ship disposal costs • Environmental liability calculation –	Substantial improvements have been made, and the remaining issues relating to the environmental remediation costs have

Prior Year Condition	Status As Reported at September 30, 2009	Status as of September 30, 2010
	environmental remediation costs • Ships not in use	been downgraded to a Management Letter deficiency.
5. Information Technology Controls over Financial Systems and Applications	***Significant Deficiency***: DOT had weaknesses in four systems area: 1) FHWA systems of FMIS and UPACS; 2) FTA systems of TEAM, ECHO and DOTS; and 3) NHTSA system of CARS	Issues related to FHWA & FTA are downgraded to Management Letter deficiencies. The issue for NHTSA has been resolved in FY 2010.
Compliance and Other Matters		
1. Noncompliance with the Anti-Deficiency Act (ADA)	MARAD management reported four ADA matters in FY 09. In addition, GAO identified other potential violations at the U.S. Merchant Marine Academy.	Repeated as a potential non-compliance violation and included in Exhibit II.

DEPARTMENT OF TRANSPORTATION
MANAGEMENT'S RESPONSE TO FY 2010
INDEPENDENT AUDITOR'S REPORT
November 12, 2010

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

Assistant Secretary
for Budget and Programs
and Chief Financial Officer

1200 New Jersey Avenue, SE
Washington, DC 20590

MEMORANDUM TO: Calvin L. Scovell, III
Inspector General

Denise Wu
Partner, Clifton Gunderson, LLP

Sal Ercolano
Partner, Clifton Gunderson, LLP

FROM: Christopher P. Bertram

SUBJECT: Management's Response to the Audit Report on the Consolidated Financial Statements for Fiscal Years (FY) 2010 and 2009

The Department of Transportation (DOT) is pleased to respond to your audit report on the Consolidated Financial Statements for FY 2010 and 2009, and that DOT earned an unqualified audit opinion. For the third consecutive year, no material weaknesses in any agency or at the consolidated department level were identified in the auditor's report on internal controls. This is confirmation of DOT's continued commitment to protecting and managing the resources, assets, and programs entrusted to us. We take great pride in our ability to sustain strong and vigilant financial management, as demonstrated in our achievement of an unqualified audit opinion.

We concur with the five significant deficiencies contained in your report on internal controls over financial reporting, and with the four instances of non-compliance found in certain provisions of applicable laws and regulations. The Department plans to submit a detailed action plan to the Inspector General no later than December 31, 2010, to address the findings contained in your report.

Please convey my sincere appreciation and gratitude to you and your staff for the professionalism and cooperation exhibited during this audit. Our combined efforts and teamwork made the difference in successfully meeting the objectives of the financial audit process. Please refer any questions to David J. Rivait, Deputy Chief Financial Officer.

PRINCIPAL STATEMENTS

U.S. Department of Transportation
Consolidated Balance Sheets
As of September 30, 2010 and 2009
(Dollars in Thousands)

Assets	**2010**	**2009**
Intragovernmental:		
Fund balance with Treasury (Note 2)	$ 52,504,709	$ 62,685,783
Investments, net (Note 3)	33,050,889	20,684,481
Accounts receivable (Note 4)	163,114	285,748
Other (Note 5)	123,418	38,450
Total intragovernmental	85,842,130	83,694,462
Cash	41,882	250
Accounts receivable, net (Note 4)	81,201	99,006
Direct loan and loan guarantees, net (Note 6)	2,892,100	2,219,298
Inventory and related property, net (Note 7)	823,603	797,310
General property, plant and equipment, net (Note 8)	13,907,474	14,439,603
Other (Note 5)	163,950	256,130
Total assets	$ 103,752,340	$ 101,506,059
Stewardship property, plant and equipment (Note 9)		
Liabilities (Note 10)		
Intragovernmental:		
Accounts payable	$ 38,023	$ 20,503
Debt (Note 11)	3,077,439	2,478,348
Other (Note 15)	2,717,013	3,092,982
Total intragovernmental	5,832,475	5,591,833
Accounts payable	700,042	736,223
Loan guarantee liability (Note 6)	237,739	310,710
Federal employee benefits payable (Note 12)	979,016	975,442
Environmental and disposal liabilities (Note 13)	1,103,562	1,195,249
Grant accrual (Note 14)	6,965,999	6,769,814
Other (Note 15)	1,442,689	1,351,571
Total liabilities	17,261,522	16,930,842
Commitments and contingencies (Note 17)		
Net position (Note 18)		
Unexpended appropriations - earmarked funds	1,211,520	1,212,951
Unexpended appropriations - other funds	37,001,417	50,425,385
Cumulative results of operations - earmarked funds	37,822,289	22,481,668
Cumulative results of operations - other funds	10,455,592	10,455,213
Total net position	86,490,818	84,575,217
Total liabilities and net position	$ 103,752,340	$ 101,506,059

The accompanying notes are an integral part of these financial statements.

U.S. Department of Transportation
Consolidated Statements of Net Cost
For the Periods Ended September 30, 2010 and 2009
(Dollars in Thousands)

Program Costs (Note 19)**:**	**2010**	**2009**
Surface Transportation:		
Gross costs	$ 61,555,071	$ 58,120,836
Less: earned revenue	785,594	523,182
Net program costs	60,769,477	57,597,654
Air Transportation:		
Gross costs	17,266,745	16,868,905
Less: earned revenue	490,930	579,983
Net program costs	16,775,815	16,288,922
Maritime Transportation:		
Gross costs	1,094,863	1,113,672
Less: earned revenue	526,261	384,985
Net program costs	568,602	728,687
Cross-Cutting Programs:		
Gross costs	717,840	648,325
Less: earned revenue	381,337	321,117
Net program costs	336,503	327,208
Costs not assigned to programs	394,503	366,041
Less earned revenues not attributed to programs	471	10,708
Net cost of operations	$ 78,844,429	$ 75,297,804

The accompanying notes are an integral part of these financial statements.

U.S. Department of Transportation
Consolidated Statements of Changes in Net Position
For the Periods Ended September 30, 2010 and 2009
(Dollars in Thousands)

	2010			2009		
	Earmarked Funds	All Other Funds	Total	Earmarked Funds	All Other Funds	Total
Cumulative Results of Operations:						
Beginning balance	$ 22,481,668	$ 10,455,213	$ 32,936,881	$ 25,944,043	$ 11,953,114	$ 37,897,157
Budgetary Financing Sources:						
Appropriations used	5,376,150	42,319,961	47,696,111	3,574,704	20,240,117	23,814,821
Non-exchange revenue (Note 20)	45,854,087	63,241	45,917,328	45,875,842	3,829	45,879,671
Donations/forfeitures of cash/cash equivalents	491	452	943	1,102	-	1,102
Transfers-in/(out) without reimbursement (Note 18)	19,477,151	(19,490,004)	(12,853)	7,178,707	(6,970,844)	207,863
Other Financing Sources (Non-Exchange):						
Transfers-in/(out) without reimbursement	(1,603,241)	1,603,235	(6)	(517,922)	364,291	(153,631)
Imputed financing	584,475	120,252	704,727	649,662	106,563	756,225
Other	(671)	(120,150)	(120,821)	(237,241)	68,718	(168,523)
Total financing sources	69,688,442	24,496,987	94,185,429	56,524,854	13,812,674	70,337,528
Net cost of operations	54,347,821	24,496,608	78,844,429	59,987,229	15,310,575	75,297,804
Net change	15,340,621	379	15,341,000	(3,462,375)	(1,497,901)	(4,960,276)
Cumulative Results of Operations	**37,822,289**	**10,455,592**	**48,277,881**	**22,481,668**	**10,455,213**	**32,936,881**
Unexpended Appropriations:						
Beginning balance	1,212,951	50,425,385	51,638,336	1,010,409	7,643,564	8,653,973
Budgetary Financing Sources:						
Appropriations received (Note 1U)	5,437,001	28,891,819	34,328,820	3,879,582	61,003,496	64,883,078
Appropriations transferred-in/(out)	3,608	74,108	77,716	4,916	2,022,133	2,027,049
Other adjustments	(65,890)	(69,934)	(135,824)	(107,252)	(9,657)	(116,909)
Appropriations used	(5,376,150)	(42,319,961)	(47,696,111)	(3,574,704)	(20,234,151)	(23,808,855)
Total budgetary financing sources	(1,431)	(13,423,968)	(13,425,399)	202,542	42,781,821	42,984,363
Total unexpended appropriations	**1,211,520**	**37,001,417**	**38,212,937**	**1,212,951**	**50,425,385**	**51,638,336**
Net position	**$ 39,033,809**	**$ 47,457,009**	**$ 86,490,818**	**$ 23,694,619**	**$ 60,880,598**	**$ 84,575,217**

The accompanying notes are an integral part of these financial statements.

U.S. Department of Transportation
Combined Statements of Budgetary Resources
For the Periods Ended September 30, 2010 and 2009
(Dollars in Thousands)

	2010		2009	
Budgetary Resources (Note 21)**:**	**Budgetary**	**Non-Budgetary Credit Reform Financing Accounts**	**Budgetary**	**Non-Budgetary Credit Reform Financing Accounts**
Unobligated balance, brought forward, October 1	$ 57,993,684	$ 264,137	$ 45,806,953	$ 240,230
Recoveries of prior year unpaid obligations	3,487,556	47,428	713,588	12,240
Budget authority:				
Appropriations received (Note 1U)	97,406,343	-	128,142,339	-
Borrowing authority	127,363	2,476,284	175,000	1,383,169
Contract authority	64,909,999	-	56,717,041	-
Spending authority from offsetting collections				
Earned				
Collected	3,057,377	400,675	2,435,351	202,488
Change in receivables from Federal sources	(86,639)	-	11,725	-
Change in unfilled customer orders				
Advance received	(536,194)	-	(25,133)	-
Without advance from Federal sources	(312,631)	108,377	49,115	47,617
Expenditure transfers from trust funds	4,028,917	-	5,284,320	-
Subtotal	168,594,535	2,985,336	192,789,758	1,633,274
Nonexpenditure transfers, net	51,617	-	2,003,700	-
Temporarily not available pursuant to Public Law	(5,007)	-	(2,251)	-
Permanently not available	(58,581,302)	(291,918)	(67,481,807)	(71,393)
Total budgetary resources	$ 171,541,083	$ 3,004,983	$ 173,829,941	$ 1,814,351
Status of Budgetary Resources:				
Obligations incurred:				
Direct	$ 108,981,763	$ 2,778,188	$ 113,733,058	$ 1,550,214
Reimbursable	2,087,680	-	2,103,199	-
Subtotal	111,069,443	2,778,188	115,836,257	1,550,214
Unobligated balance:				
Apportioned	42,144,037	11,356	49,012,606	8,947
Exempt from apportionment	319,222	-	276,374	-
Subtotal	42,463,259	11,356	49,288,980	8,947
Unobligated balance not available	18,008,381	215,439	8,704,704	255,190
Total status of budgetary resources	$ 171,541,083	$ 3,004,983	$ 173,829,941	$ 1,814,351

The accompanying notes are an integral part of these financial statements.

U.S. Department of Transportation
Combined Statements of Budgetary Resources
For the Periods Ended September 30, 2010 and 2009
(Dollars in Thousands)

	2010		2009	
Change in Obligated Balances:	**Budgetary**	**Non-Budgetary Credit Reform Financing Accounts**	**Budgetary**	**Non-Budgetary Credit Reform Financing Accounts**
Obligated balance, net:				
Unpaid obligations, brought forward, October 1	$ 107,086,559	$ 2,519,805	$ 80,075,300	$ 1,850,080
Uncollected customer payments from Federal sources, brought forward, October 1	(1,512,864)	(216,886)	(1,444,636)	(169,268)
Total unpaid obligated balance, net	105,573,695	2,302,919	78,630,664	1,680,812
Obligations incurred	111,069,443	2,778,188	115,836,257	1,550,214
Gross outlays	(104,054,373)	(1,056,065)	(88,136,410)	(868,249)
Obligated balance transferred, net				
Unpaid obligations	26,344	-	25,000	-
Recoveries of prior year unpaid obligations, actual	(3,487,556)	(47,428)	(713,588)	(12,240)
Change in uncollected customer payments from Federal sources	410,672	(108,377)	(68,228)	(47,618)
Obligated balance, net, end of period:				
Unpaid obligations	110,640,417	4,194,500	107,086,559	2,519,805
Uncollected customer payments from Federal sources	(1,102,192)	(325,263)	(1,512,864)	(216,886)
Total unpaid obligated balance, net, end of period	$ 109,538,225	$ 3,869,237	$ 105,573,695	$ 2,302,919
Net Outlays:				
Net Outlays				
Gross outlays	$ 104,054,373	$ 1,056,065	$ 88,136,410	$ 868,249
Offsetting collections	(6,546,842)	(400,675)	(7,692,821)	(202,488)
Distributed offsetting receipts	(219,178)	-	(188,979)	(39,360)
Net outlays	$ 97,288,353	$ 655,390	$ 80,254,610	$ 626,401

The accompanying notes are an integral part of these financial statements.

NOTES TO PRINCIPAL STATEMENTS

Note 1. Summary of Significant Accounting Policies:

A. Reporting Entity:

The Department of Transportation (DOT or Department) serves as the focal point in the Federal Government's coordinated national transportation policy. It is responsible for helping cities and States meet their local transportation needs through financial and technical assistance, ensuring the safety of all forms of transportation; protecting the interests of consumers; promoting international transportation agreements; and conducting planning and research for the future.

The Department is comprised of the Office of the Secretary and the DOT Operating Administrations, each having its own management and organizational structure, and collectively provides the necessary services and oversight to ensure the best transportation system possible. The Department's consolidated financial statements present the financial data for various trust funds, revolving funds, appropriations and special funds, of the following organizations:

Office of The Secretary (OST) [includes OST Working Capital Fund]
Federal Aviation Administration (FAA)
Federal Highway Administration (FHWA)
Federal Motor Carrier Safety Administration (FMCSA)
Federal Railroad Administration (FRA)
Federal Transit Administration (FTA)
Maritime Administration (MARAD)
National Highway Traffic Safety Administration (NHTSA)
Office of Inspector General (OIG)
Pipeline and Hazardous Materials Safety Administration (PHMSA)
Research and Innovative Technology Administration (RITA) [includes Volpe National Transportation System Center]
Surface Transportation Board (STB)

The Saint Lawrence Seaway Development Corporation (SLSDC) is also a DOT entity. However, since it is subject to separate reporting under the Government Corporation Control Act and the dollar value of its activities is not material to that of the Department, SLSDC's financial data is not included in the DOT consolidated financial statements. However, condensed information about SLSDC's financial position is presented in Note 24.

B. Basis of Presentation:

The consolidated financial statements have been prepared to report the Department's financial position and its results of operations as required by the Chief Financial Officers Act of 1990 (CFO Act) and Title IV of the Government Management Reform Act of 1994 (GMRA). The statements have been prepared from the DOT books and records in accordance with Office of Management and Budget (OMB) form and content requirements for entity financial statements and DOT's accounting policies and procedures. Unless otherwise noted, all dollar amounts are presented in thousands.

The Consolidated Balance Sheets present agency assets and liabilities, and the resulting net position (which is the difference between the two amounts). Agency assets substantially include entity assets (those which are available for use by the agency). Non-entity assets (those which are managed by the agency but not available for use in its operations) are immaterial. Agency liabilities include both those covered by budgetary resources (funded) and those not covered by budgetary resources (unfunded).

The Consolidated Statements of Net Cost present the gross costs of programs less earned revenue to arrive at the net cost of operations for both the programs and the agency as a whole.

The Consolidated Statements of Changes in Net Position report beginning balances, budgetary and other financing sources, and net cost of operations, to arrive at ending balances.

The Combined Statements of Budgetary Resources provide information about how budgetary resources were made available as well as their status at the end of the period. Recognition and measurement of budgetary information reported on this statement is based on budget terminology, definitions, and guidance in OMB Circular No. A-11, "Preparation, Submission, and Execution of the Budget," dated July 2010.

Notes to the Financial Statements

Since DOT custodial activity is incidental to Departmental operations and is not considered material to the consolidated financial statements taken as a whole, a Statement of Custodial Activity has not been prepared. However, sources and dispositions of collections have been disclosed in Note 22 to the consolidated financial statements.

The Department is required to be in substantial compliance with all applicable accounting principles and standards established, issued, and implemented by the Federal Accounting Standards Advisory Board (FASAB), which is recognized by the American Institute of Certified Public Accountants (AICPA) as the entity to establish Generally Accepted Accounting Principles (GAAP) for the Federal Government. The Federal Financial Management Improvement Act (FFMIA) of 1996 requires the Department to comply substantially with (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the U.S. Government Standard General Ledger requirements at the transaction level.

C. Budgets and Budgetary Accounting:

DOT follows standard Federal budgetary accounting policies and practices in accordance with OMB Circular No. A-11, "Preparation, Submission, and Execution of the Budget," dated July 2010. Budgetary accounting facilitates compliance with legal constraints and controls over the use of Federal funds. Each year, Congress provides appropriations to each Operating Administration within DOT to incur obligations in support of agency programs. For FY 2010 and FY 2009, the Department was accountable for trust fund appropriations, general fund appropriations, revolving fund activity and borrowing authority. DOT recognizes budgetary resources as assets when cash (funds held by Treasury) is made available through warrants and trust fund transfers.

Programs are financed from authorizations enacted in authorizing legislation and codified in Title 23 of the United States Code (U.S.C.). The DOT receives its budget authority in the form of contract authority and direct appropriations. Contract authority permits programs to incur obligations in advance of an appropriation, offsetting collections, or receipts. Subsequently, Congress provides an appropriation for the liquidation of the contract authority to allow payments to be made for the obligations incurred. Funds apportioned by statute under Titles 23 and 49 of the U.S.C., Subtitle III by the Secretary of Transportation for activities in advance of the liquidation of appropriations are available for a specific time period.

D. Basis of Accounting:

Transactions are generally recorded on both an accrual accounting basis and a budgetary basis. Under the accrual method, revenues are recognized when earned, and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. Budgetary accounting facilitates compliance with legal constraints and controls over the use of Federal funds. All material intra-departmental transactions and balances have been eliminated for presentation on a consolidated basis. However, the Statement of Budgetary Resources is presented on a combined basis, in accordance with OMB Circular A-136.

Intragovernmental transactions and balances result from exchange transactions made between DOT and another Federal government reporting entity, while those classified as "with the public" result from exchange transactions between DOT and non-federal entities. For example, if DOT purchases goods or services from the public and sells them to another Federal entity, the costs would be classified as "with the public," but the related revenues would be classified as "intragovernmental." This could occur, for example, when DOT provides goods or services to another Federal government entity on a reimbursable basis. The purpose of this classification is to enable the Federal government to prepare consolidated financial statements, and not to match public and intragovernmental revenue with costs that are incurred to produce public and intragovernmental revenue.

DOT accounts for earmarked funds separately from other funds.

E. Funds with the U.S. Treasury and Cash:

DOT does not generally maintain cash in commercial bank accounts. Cash receipts and disbursements are processed by the U.S. Treasury. The funds with the U.S. Treasury are appropriated, revolving, and trust funds that are available to pay current liabilities and finance authorized purchases. Lockboxes have been established with financial institutions to collect certain payments, and these funds are transferred directly to Treasury on a daily (business day) basis. DOT does not maintain any balances of foreign currencies.

F. Investments in U.S. Government Securities:

Investments that consist of U.S. Government Securities are reported at cost and adjusted for amortized cost net of premiums or discounts. Premiums or discounts are amortized into interest income over the term of the investment using the interest or straight-line method. The Department's intent is to hold investments to maturity. Investments, redemptions, and reinvestments are controlled and processed by the Department of the Treasury. The market value is calculated by multiplying the total number of shares by the market price on the last day of the fiscal year.

G. Receivables:

Accounts receivable consist of amounts owed to the Department by other Federal agencies and the public. Federal accounts receivable are generally the result of the provision of goods and services to other Federal agencies and, with the exception of occasional billing disputes, are considered to be fully collectible. Public accounts receivable are generally the result of the provision of goods and services or the levy of fines and penalties from the Department's regulatory activities. Amounts due from the public are presented net of an allowance for loss on uncollectible accounts, which is based on historical collection experience and/or an analysis of the individual receivables.

Loans are accounted for as receivables after funds have been disbursed. For loans obligated prior to October 1, 1991, loan principal, interest, and penalties receivable are reduced by an allowance for estimated uncollectible amounts. The allowance is estimated based on past experience, present market conditions, and an analysis of outstanding balances. Loans obligated after September 30, 1991, are reduced by an allowance equal to the present value of the subsidy costs (resulting from the interest rate differential between the loans and Treasury borrowing, the estimated delinquencies and defaults net of recoveries, the offset from fees, and other estimated cash flows) associated with these loans.

H. Inventory and Related Operating Materials and Supplies:

Inventory primarily consists of supplies that are for sale or used in the production of goods for sale. Operating materials and supplies primarily consist of unissued supplies that will be consumed in future operations. Valuation methods for supplies on hand at year-end include historical cost, last acquisition price, standard price/specific identification, standard repair cost, weighted average, and moving weighted average. Expenditures or expenses are recorded when the materials and supplies are consumed or sold. Adjustments for the proper valuation of reparable, excess, obsolete, and unserviceable items are made to appropriate allowance accounts.

I. Property and Equipment:

DOT agencies have varying methods of determining the value of general purpose property and equipment and how it is depreciated. DOT currently has a capitalization threshold of $200,000 for structures and facilities and for internal use software, and $25,000 for other property, plant and equipment. Capitalization at lesser amounts is permitted. Construction in progress is valued at direct (actual) costs plus applied overhead and other indirect costs as accumulated by the regional project material system. The system accumulates costs by project number assigned to the equipment or facility being constructed. The straight line method is generally used to depreciate capitalized assets.

DOT's heritage assets, consisting of Union Station in Washington, DC, the Nuclear Ship *Savannah* and collections of maritime artifacts, are considered priceless and are not capitalized in the Consolidated Balance Sheets (See Note 9).

J. Prepaid and Deferred Charges:

Payments in advance of the receipt of goods and services are recorded as prepaid charges at the time of prepayment and recognized as expenses or capitalized, as appropriate, when the related goods and services are received.

Notes to the Financial Statements

K. Liabilities:

Liabilities represent amounts expected to be paid as the result of a transaction or event that has already occurred. Liabilities covered by budgetary resources are liabilities incurred which are covered by realized budgetary resources as of the balance sheet date. Available budgetary resources include new budget authority, spending authority from offsetting collections, recoveries of unexpired budget authority through downward adjustments of prior year obligations, unobligated balances of budgetary resources at the beginning of the year or net transfers of prior year balances during the year, and permanent indefinite appropriations or borrowing authority. Unfunded liabilities are not considered to be covered by such budgetary resources. An example of an unfunded liability is actuarial liabilities for future Federal Employees' Compensation Act payments. The Government, acting in its sovereign capacity, can abrogate liabilities arising from other than contracts.

L. Contingencies:

The criteria for recognizing contingencies for claims are (1) a past event or exchange transaction has occurred as of the date of the statements; (2) a future outflow or other sacrifice of resources is probable; and (3) the future outflow or sacrifice of resources is measurable (reasonably estimatable). DOT recognizes material contingent liabilities in the form of claims, legal actions, administrative proceedings and environmental suits that have been brought to the attention of legal counsel, some of which will be paid by the Treasury Judgment Fund. It is the opinion of management and legal counsel that the ultimate resolution of these proceedings, actions and claims, will not materially affect the financial position or results of operations.

M. Annual, Sick, and Other Leave:

Annual leave is accrued as it is earned, and the accrual is reduced as leave is taken. For each bi-weekly pay period, the balance in the accrued annual leave account is adjusted to reflect the latest pay rates and unused hours of leave. Liabilities associated with other types of vested leave, including compensatory, credit hours, restored leave, and sick leave in certain circumstances, are accrued based on latest pay rates and unused hours of leave. Sick leave is generally nonvested, except for sick leave balances at retirement under the terms of certain union agreements, including the National Air Traffic Controllers Association (NATCA) agreement, Article 25, Section 13. Funding will be obtained from future financing sources to the extent that current or prior year appropriations are not available to fund annual and other types of vested leave earned and not taken. Nonvested leave is expensed when used.

N. Retirement Plan:

For DOT employees who participate in the Civil Service Retirement System (CSRS), DOT contributes a matching contribution equal to 7 percent of pay. On January 1, 1987, FERS went into effect pursuant to Public Law (P.L.) 99-335. Most employees hired after December 31, 1983, are automatically covered by FERS and Social Security. Employees hired prior to January 1, 1984, could elect to either join FERS and Social Security or remain in CSRS. A primary feature of FERS is that it offers a savings plan to which DOT automatically contributes 1 percent of pay and matches any employee contribution up to an additional 4 percent of pay. For most employees hired since December 31, 1983, DOT also contributes the employer's matching share for Social Security.

Employing agencies are required to recognize pensions and other post retirement benefits during the employees' active years of service. Reporting the assets and liabilities associated with such benefit plans is the responsibility of the administering agency, the Office of Personnel Management (OPM). Therefore, DOT does not report CSRS or FERS assets, accumulated plan benefits, or unfunded liabilities, if any, applicable to employees.

O. Federal Employees Health Benefit (FEHB) Program:

Most Department employees are enrolled in the FEHB Program, which provides post-retirement health benefits. OPM administers this program and is responsible for the reporting of liabilities. Employer agencies and covered employees are not required to make any contributions for post-retirement health benefits. OPM calculates the U.S. Government's service cost for covered employees each fiscal year. The Department has recognized the entire service cost of these post-retirement benefits for covered employees as an imputed cost and an imputed financing source.

P. Federal Employees Group Life Insurance (FEGLI) Program:

Most Department employees are entitled to participate in the FEGLI Program. Participating employees can obtain basic term life insurance where the employee pays two-thirds of the cost and the Department pays one-third of the cost. OPM administers this program and is responsible for the reporting of liabilities. OPM calculates the U.S. Government's service cost for the post-retirement portion of the basic life coverage each fiscal year. Because OPM fully allocates the Department's contributions for basic life coverage to the pre-retirement portion of coverage, the Department has recognized the entire service cost of the post-retirement portion of basic life coverage as an imputed cost and an imputed financing source.

Q. Federal Employee Compensation Benefits (FECA):

A liability is recorded for actual and estimated future payments to be made for workers' compensation pursuant to the Federal Employees' Compensation Act (FECA). The actual costs incurred are reflected as a liability because DOT will reimburse the Department of Labor (DOL) two years after the actual payment of expenses. Future revenues will be used to reimburse DOL. The liability consists of (1) the net present value of estimated future payments calculated by the DOL, and (2) the unreimbursed cost paid by DOL for compensation to recipients under FECA.

R. Environmental and Disposal Liabilities:

DOT recognizes two types of environmental liabilities: unfunded environmental remediation and unfunded asset disposal liability. The liability for environmental remediation is an estimate of costs necessary to bring a known contaminated site into compliance with applicable environmental standards. The asset disposal liability includes both the cost to remove and dismantle an asset when that asset is no longer in service and the estimated cost that will be incurred to remove, contain, and/or dispose of hazardous materials. DOT estimates the environmental remediation and asset disposal costs at the time a DOT-owned asset is placed in service.

Estimating the Department's environmental remediation liability requires making assumptions about future activities and is inherently uncertain. Costs for estimates of environmental and disposal liabilities are not adjusted for inflation and are subject to revision as a result of changes in technology and environmental laws and regulations.

S. Use of Estimates:

Management has made certain estimates and assumptions when reporting assets, liabilities, revenue, and expenses. Actual results could differ from these estimates. Significant estimates underlying the accompanying financial statements include the allocation of trust fund receipts by Treasury's Office of Tax Analysis (OTA), accruals of accounts and grants payable (including American Recovery and Reinvestment Act funds), accrued workers' compensation, and accrued legal, contingent, environmental and disposal liabilities.

T. Allocation Transfers:

DOT is a party to allocation transfers with other federal agencies as a transferring (parent) entity. Allocation transfers are legal delegations by one department of its authority to obligate budget authority and outlay funds to another department. A separate fund account (allocation account) is created in the U.S. Treasury as a subset of the parent fund account for tracking and reporting purposes. All allocation transfers of balances are credited to this account and subsequent obligations and outlays incurred by the receiving entity (child) are charged to this allocation account as the delegated activity is executed on the parent entity's behalf. Generally, all financial activity related to these allocation transfers (e.g. budget authority, obligations, outlays) is reported in the financial statements of the parent entity, from which the underlying legislative authority, appropriations and budget apportionments are derived.

DOT allocates funds, as the parent, to the following non-DOT Federal agencies in accordance with applicable public laws and statutes: Bureau of Indian Affairs, Bureau of Reclamation, U.S. Forest Service, National Park Service, Bureau of Land Management, Fish and Wildlife Service, Department of the Army, Appalachian Regional Commission, Tennessee Valley Authority, U.S. Army Corps of Engineers, Internal Revenue Service, Department of Housing and Urban Development, Denali Commission, Department of Navy, and Department of Energy.

U. Revenues and Other Financing Sources:

Earmarked Excise Tax Revenues (Nonexchange):

DOT receives funding needed to support its programs through non-exchange earmarked excise tax revenues related to the Highway Trust Fund (HTF) and the Airport and Airway Trust Fund (AATF).

Excise taxes collected are initially deposited to the general fund of the U.S. Treasury. The IRS does not receive sufficient information at the time the taxes are collected to determine how these payments should be distributed to specific earmarked funds. Therefore, the U.S. Treasury makes initial semi-monthly distributions to earmarked funds based on estimates prepared by OTA. These estimates are based on historical excise tax data applied to current excise tax receipts. When actual amounts are certified by the IRS, generally four months after each quarter-end, adjustments are made to the estimated amounts and the difference is adjusted as a transfer of resources to the HTF and AATF accounts.

The DOT September 30, 2010 financial statements reflect excise taxes certified by the IRS through June 30, 2010 and excise taxes estimated by OTA for the period July 1, 2010 to September 30, 2010 as specified by SFFAS Number 7, *Accounting for Revenue and Other Financing Sources* . Actual tax collections data for the quarter ended September 30, 2010 will not be available from the IRS until January 2011. Management does not believe that the actual tax collections for the quarter ended September 30, 2010 will be materially different than the OTA estimate, which would be recorded in the DOT's accounting system.

Appropriations (Financing Source):

DOT receives annual, multi-year and no-year appropriations. Appropriations are recognized as revenues when related program and administrative expenses are incurred. Additional amounts are obtained from offsetting collections and user fees (e.g., landing and registry fees) and through reimbursable agreements for services performed for domestic and foreign governmental entities. Additional revenue is received from gifts of donors, sales of goods and services to other agencies and the public, the collection of fees and fines, interest/dividends on invested funds, loans and cash disbursements to banks. Interest income is recognized as revenue on the accrual basis rather than when received.

On March 18, 2010, the President signed H.R. 2847, the Hiring Incentives to Restore Employment (HIRE) Act. The Act extends authority to make expenditures from the HTF through December 31, 2010 and; provides additional revenues to the HTF by restoring interest foregone since the HTF stopped earning interest on its balances after FY 1998, transferring $14.7 billion to the Highway Account and $4.8 billion to the Mass Transit Account from the General Fund. Going forward, the HTF will resume earning interest on its invested balances. Also refunds and credits of fuel taxes paid on fuel used for exempt purposes will be paid by the General Fund instead of the Highway Trust Fund. (These amounts are reflected in notes 3 and 18).

With the HTF authorization to make expenditures expiring in December 2010, DOT has been developing several reauthorization proposals subject to OMB and Congressional approval. DOT anticipates that there will be a timely extension.

American Recovery and Reinvestment Act:

On February 17, 2009, the President signed into law the American Recovery and Reinvestment Act (ARRA), which designated over $48 billion to the DOT operating administrations. The funding was provided to Federal Highway Administration, the Federal Aviation Administration, the Federal Transit Administration, the Federal Rail Administration, the Office of Secretary Administration and the Maritime Administration. These funds were designated to invest in transportation infrastructure, including transit capital assistance, high speed rail, pavement improvements and bridge repair, as well as to preserve and create jobs, and promote economic recovery that will provide long term economic benefits. As of September 30, 2010, the Department had obligated $39.6 billion and disbursed $20.5 billion.

V. Fiduciary Activities:

Fiduciary assets and liabilities are not assets and liabilities of the Department and as such are not recognized on the balance sheet. In accordance with the provisions of the Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standards (SFFAS) No. 31, Accounting for Fiduciary Activities, this activity is reported separately in a note disclosure. This requirement is effective for reporting periods beginning on or after October 1, 2008. The Maritime Administration Title XI Escrow Fund contains fiduciary activity (See Note 25 for specific required disclosures).

W. Related Parties

The Secretary of Transportation has possession of two long term notes with the National Railroad Passenger Service Corporation (more commonly referred to as Amtrak). The first note is for $4 billion and matures in 2975 and; the second note is for $1.1 billion and matures in 2082 with renewable 99 year terms. Interest is not accruing on these notes as long as the current financial structure of Amtrak remains unchanged. If the financial structure of Amtrak changes, both principal and accrued interest are due and payable. The Department does not record the notes in its financial statements due to the present value of the notes was immaterial at September 30, 2010 discounted according to rates published in OMB M-10-07 Appendix C and the maturity dates of 2975 and 2082.

In addition, the Secretary of Transportation has possession of all the preferred stock shares (109,396,994) of Amtrak. Congress through the Department continues to fund Amtrak since 1981; originally through the purchase of preferred stock, notes receivable and then through grants after 1997. The Amtrak Reform and Accountability Act of 1997 changed the structure of the preferred stock by rescinding the voting rights and eliminating the preferred stock's liquidation over the common stock. The Act also eliminated further issuance of preferred stock to the Department. The Department does not record the Amtrak stock in its financial statements because it is not publicly traded and no fair market value can be placed on it.

Amtrak is not a department, agency or instrumentality of the United States Government or the Department. The nine members of Amtrak's Board of Directors are appointed by the President of the United States and are subject to confirmation by the United States Senate. Once appointed, Board Members, as a whole, act independently without the consent of the United States government or any of its officers to set Amtrak policy, determine its budget and decide operational issues. The Secretary of Transportation is statutorily appointed to the nine member Board. Traditionally, the Secretary of Transportation has designated the Administrator of the Federal Rail Administration to represent the Secretary at Board meetings (See Note 17).

Notes to the Financial Statements

Note 2. Fund Balance with Treasury:

	2010	2009
Fund Balances:		
Trust Funds	$ 7,337,993	$ 3,669,004
Revolving Funds	709,663	764,682
General Funds	44,077,582	57,900,427
Other Fund Types	379,471	351,670
Total	$ 52,504,709	$ 62,685,783
Status of Fund Balance with Treasury:		
Unobligated balance:		
Available	$ 25,560,214	$ 30,866,347
Unavailable	2,474,563	2,294,653
Obligated balance not yet disbursed	24,378,245	29,473,421
Non-Budgetary Fund Balance with Treasury	91,687	51,362
Total	$ 52,504,709	$ 62,685,783

Fund Balances with Treasury are the aggregate amounts of the entity's accounts with Treasury for which the entity is authorized to make expenditures and pay liabilities. Other Fund Types include uncleared suspense accounts, which temporarily hold collections pending clearance to the applicable account, and deposit funds, which are established to record amounts held temporarily until ownership is determined.

The U.S. Treasury processes cash receipts and disbursements. DOT receives appropriations as budget authority, which permits it to incur obligations and make outlays (payments). In addition, DOT also receives contract authority to permit the incurrence of obligations in advance of an appropriation. The contract authority is subsequently replaced with the appropriation or the spending authority from offsetting collections to first cover and then liquidate the obligations. As a result, DOT does not have typical Fund Balance with Treasury amounts as funds remain invested in securities until needed to make payments.

Note 3. Investments:

As of September 30, 2010

	Cost	Amortized (Premium) Discount	Investments (Net)	Market Value Disclosure
Intragovernmental Securities:				
Marketable	$ 44,258	$ 351	$ 44,609	$ 44,825
Non-Marketable Par Value	31,499,950	-	31,499,950	31,499,950
Non-Marketable Market-Based	1,451,884	11,176	1,463,060	1,506,521
Subtotal	32,996,092	11,527	33,007,619	33,051,296
Accrued Interest	43,270	-	43,270	
Total Intragovernmental Securities	$ 33,039,362	$ 11,527	$ 33,050,889	$ 33,051,296

As of September 30, 2009

	Cost	Amortized (Premium) Discount	Investments (Net)	Market Value Disclosure
Intragovernmental Securities:				
Marketable	$ 29,405	$ 122	$ 29,527	$ 29,803
Non-Marketable Par Value	19,313,905	-	19,313,905	19,313,905
Non-Marketable Market-Based	1,289,850	(6,770)	1,283,080	1,317,582
Subtotal	20,633,160	(6,648)	20,626,512	20,661,290
Accrued Interest	57,969	-	57,969	
Total Intragovernmental Securities	$ 20,691,129	$ (6,648)	$ 20,684,481	$ 20,661,290

Investments include non-marketable par value and market-based Treasury securities and marketable securities issued by the Treasury and other Federal entities. Non-marketable par value Treasury securities are issued by the Bureau of Public Debt to Federal accounts and are purchased and redeemed at par exclusively through Treasury's Federal Investment Branch. Non-marketable market-based Treasury securities are also issued by the Bureau of Public Debt to Federal accounts. They are not traded on any securities exchange, but mirror the prices of particular Treasury securities trading in the Government securities market. Marketable Federal securities can be bought and sold on the open market. The premiums and discounts are amortized over the life of the non-marketable market-based and marketable securities using the interest method.

The Federal Government does not set aside assets to pay future benefits or other expenditures associated with earmarked funds. The cash receipts collected from the public for an earmarked fund are deposited in the U.S. Treasury, which uses the cash for Government purposes. Non-Marketable par value Treasury securities are issued to DOT as evidence of these receipts. These securities provide DOT with authority to draw upon the U.S. Treasury to make future expenditures. When DOT requires redemption of these securities to make expenditures, the Government finances those expenditures out of accumulated cash balances by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same way that the Government finances all other expenditures.

Treasury securities are an asset of DOT and a liability of the U.S. Treasury. Because the DOT and the U.S. Treasury are both a part of the Government, these assets and liabilities offset each other from the standpoint of the Government as a whole. For this reason, they do not represent an asset or liability in the U.S. Government-wide financial statements.

Note 4. Accounts Receivable:

As of September 30, 2010	Gross Amount Due	Allowance for Uncollectible Amounts	Net Amount Due
Intragovernmental:			
Accounts Receivable	$ 163,109	$ -	$ 163,109
Accrued Interest	5	-	5
Total Intragovernmental	163,114	-	163,114
Public:			
Accounts Receivable	102,713	(21,696)	81,017
Accrued Interest	405	(221)	184
Total Public	103,118	(21,917)	81,201
Total Receivables	$ 266,232	$ (21,917)	$ 244,315

As of September 30, 2009	Gross Amount Due	Allowance for Uncollectible Amounts	Net Amount Due
Intragovernmental:			
Accounts Receivable	$ 285,717	$ -	$ 285,717
Accrued Interest	31	-	31
Total Intragovernmental	$ 285,748	$ -	$ 285,748
Public:			
Accounts Receivable	123,909	(25,405)	98,504
Accrued Interest	909	(407)	502
Total Public	124,818	(25,812)	99,006
Total Receivables	$ 410,566	$ (25,812)	$ 384,754

Notes to the Financial Statements

Note 5. Other Assets:

	2010	2009
Intragovernmental:		
Advances and Prepayments	$ 123,418	$ 38,450
Total Intragovernmental	$ 123,418	$ 38,450
Public:		
Advances to States for Right of Way	$ 59,188	$ 101,084
Other Advances and Prepayments	104,473	154,778
Other	289	268
Total Public	$ 163,950	$ 256,130

Intragovernmental Other Assets are comprised of advance payments to other Federal Government entities for agency expenses not yet incurred and for goods and services not yet received and undistributed assets and payments for which DOT is awaiting documentation. Public Other Assets are comprised of advances to States, employees and contractors.

Note 6. Direct Loans and Loan Guarantees, Non-Federal Borrowers:

The Federal Credit Reform Act of 1990 divides direct loans and loan guarantees into two groups:

(1) Pre-1992 - the direct loan obligations or loan guarantee commitments made prior to FY 1992 and the resulting direct loans or loan guarantees, and

(2) Post-1991 - the direct loan obligations or loan guarantee commitments made after FY 1991 and the resulting direct loans or loan guarantees.

The Act provides that, for direct loan obligations or loan guarantee commitments made after FY 1991, the present value of subsequent subsidy costs (which arises from interest rate differentials, interest subsidies, delinquencies and defaults, fee offsets, and other cash flows) be recognized in the year the direct or guaranteed loan is disbursed. Direct loans are reported net of an allowance for subsidy at present value, and loan guarantee liabilities are reported at present value. Foreclosed property is valued at the net realizable value. Loans receivable, net, or their value of assets related to direct loans, is not the same as the proceeds that would be expected to be received from selling the loans. DOT has calculated the allowance for pre-1992 loans using the allowance for loss method.

DOT administers the following direct loan and/or loan guarantee programs:

(1) The Railroad Rehabilitation Improvement Program is used to acquire, improve, or rehabilitate intermodal or rail equipment or facilities, including track, components of tract, bridges, yards, buildings, and shops; refinance outstanding debt incurred; and develop or establish new intermodal or railroad facilities.

(2) The Transportation Infrastructure Finance Innovation Act (TIFIA) Loan Program provides Federal credit assistance to major transportation investments of critical national importance such as highway, transit, passenger rail, certain freight facilities, and certain port projects with regional and national benefits. The TIFIA credit program is designed to fill market gaps and leverages substantial private co-investment by providing supplemental and subordinate capital.

(3) The Federal Ship Financing Fund (Title XI) offers loan guarantees to qualified ship owners and shipyards. The guarantee provides the benefit of long term financing at stable interest rates to the approved applicants.

(4) The OST Minority Business Resource Center Guaranteed Loan Program helps small businesses gain access to the financing needed to participate in transportation-related contracts.

An analysis of loans receivable, allowance for subsidy costs, liability for loan guarantees, foreclosed property, modifications and reestimates associated with direct loans and loan guarantees is provided in the following sections:

Direct Loans

Obligated Prior to FY 1992 (Allowance for Loss Method) Direct Loan Programs	2010 Loans Receivable, Gross	Interest Receivable	Allowance for Loan Losses	Value of Assets Related to Direct Loans, Net
(1) Railroad Rehabilitation Improvement Program	$ 3,729	$ -	$ -	$ 3,729

Obligated After FY 1991 Direct Loan Programs	2010 Loans Receivable, Gross	Interest Receivable	Allowance for Subsidy Cost (Present Value)	Value of Assets Related to Direct Loans, Net
(1) Railroad Rehabilitation Improvement Program	$ 411,746	$ 1,105	$ (2,518)	$ 410,333
(2) TIFIA Loans	2,527,782	-	(219,554)	2,308,228
Total	$ 2,939,528	$ 1,105	$ (222,072)	$ 2,718,561

Obligated Prior to FY 1992 (Allowance for Loss Method) Direct Loan Programs	2009 Loans Receivable, Gross	Interest Receivable	Allowance for Loan Losses	Value of Assets Related to Direct Loans, Net
(1) Railroad Rehabilitation Improvement Program	$ 7,053	$ -	$ -	$ 7,053

Obligated After FY 1991 Direct Loan Programs	2009 Loans Receivable, Gross	Interest Receivable	Allowance for Subsidy Cost (Present Value)	Value of Assets Related to Direct Loans, Net
(1) Railroad Rehabilitation Improvement Program	$ 377,437	$ 634	$ (3,729)	$ 374,342
(2) TIFIA Loans	1,879,727	-	(89,770)	1,789,957
Total	$ 2,257,164	$ 634	$ (93,499)	$ 2,164,299

Notes to the Financial Statements

Note 6. Direct Loans and Loan Guarantees, Non-Federal Borrowers: (Cont.)

Total Amount of Direct Loans Disbursed (Post-1991)

Direct Loan Programs	2010	2009
(1) Railroad Rehabilitation Improvement Program	$ 42,575	$ 96,344
(2) TIFIA Loans	564,988	317,164
Total	$ 607,563	$ 413,508

Subsidy Expense for Direct Loans by Program and Component

Subsidy Expense for New Direct Loans Disbursed

Direct Loan Programs	2010 Interest Differential	Defaults	Fees and Other Collections	Other Subsidy Costs	Total
(1) Railroad Rehabilitation Improvement Program	$ -	$ 1,388	$ (1,388)	$ -	$ -
(2) TIFIA Loans	-	85,140	(30,980)	-	54,160
Total	$ -	$ 86,528	$ (32,368)	$ -	$ 54,160

Direct Loan Programs	2009 Interest Differential	Defaults	Fees and Other Collections	Other Subsidy Costs	Total
(1) Railroad Rehabilitation Improvement Program	$ -	$ 2,297	$ (2,297)	$ -	$ -
(2) TIFIA Loans	-	49,078	-	-	49,078
Total	$ -	$ 51,375	$ (2,297)	$ -	$ 49,078

Modifications and Re-estimates

Direct Loan Programs	2010 Total Modifications	Interest Rate Re-estimates	Technical Re-estimates	Total Re-estimates
(1) Railroad Rehabilitation Improvement Program	$ -	$ -	$ (728)	$ (728)
(2) TIFIA Loans	-	-	36,346	36,346
Total	$ -	$ -	$ 35,618	$ 35,618

Direct Loan Programs	2009 Total Modifications	Interest Rate Re-estimates	Technical Re-estimates	Total Re-estimates
(1) Railroad Rehabilitation Improvement Program	$ -	$ -	$ 986	$ 986
(2) TIFIA Loans	-	-	(111,685)	(111,685)
Total	$ -	$ -	$ (110,699)	$ (110,699)

Total Direct Loan Subsidy Expense

Direct Loan Programs	2010	2009
(1) Railroad Rehabilitation Improvement Program	$ (728)	$ 986
(2) TIFIA Loans	90,506	(62,607)
Total	$ 89,778	$ (61,621)

Budget Subsidy Rates for Direct Loans for the Current Year Cohort

Direct Loan Programs	2010 Interest Differential	Defaults	Fees and Other Collections	Other	Total
(1) Railroad Rehabilitation Improvement Program	-0.32%	1.54%	-1.22%	0.00%	0.00%
(2) TIFIA Loans	0.40%	12.27%	0.00%	0.00%	12.67%
Total	0.08%	13.81%	-1.22%	0.00%	12.67%

The subsidy rates disclosed pertain only to the current year's cohorts. These rates cannot be applied to the direct loans disbursed during the current reporting year to yield the subsidy expense. The subsidy expense for new loans reported in the current year could result from disbursements of loans from both current year cohorts and prior year(s) cohorts. The subsidy expense reported in the current year also includes modifications and re-estimates.

Note 6. Direct Loans and Loan Guarantees, Non-Federal Borrowers: (Cont.)

Schedule for Reconciling Subsidy Cost Allowance Balances (Post-1991 Direct Loans)

Beginning Balance, Changes, and Ending Balance	2010	2009
Beginning balance of the subsidy cost allowance	$ 93,499	$ 161,124
Add: subsidy expense for direct loans disbursed during the reporting years by component:		
Default costs (net of recoveries)	86,528	51,375
Fees and other collections	(32,368)	(2,297)
Total of the above subsidy expense components	54,160	49,078
Adjustments:		
Subsidy allowance amortization	6,427	(8,301)
Other	32,368	2,297
Ending balance of the subsidy cost allowance before reestimates	186,454	204,198
Add or subtract subsidy reestimates by component:		
Technical/default reestimate	35,618	(110,699)
Total of the above reestimate components	35,618	(110,699)
Ending balance of the subsidy cost allowance	$ 222,072	$ 93,499

Notes to the Financial Statements

Note 6. Direct Loans and Loan Guarantees, Non-Federal Borrowers: (Cont.)

Defaulted Guaranteed Loans from Post-1991 Guarantees

Loan Guarantee Programs	2010 Defaulted Guaranteed Loans Receivable, Gross	Interest Receivable	Foreclosed Property	Allowance for Subsidy	Value of Assets Related to Default Guaranteed Loans Receivable, Net
(3) Federal Ship Financing Fund (Title XI)	$ 258,383	$ 10,757	$ 28,110	$ (127,440)	$ 169,810

Loan Guarantee Programs	2009 Defaulted Guaranteed Loans Receivable, Gross	Interest Receivable	Foreclosed Property	Allowance for Subsidy	Value of Assets Related to Default Guaranteed Loans Receivable, Net
(3) Federal Ship Financing Fund (Title XI)	$ 68,945	$ 1,974	$ 28,110	$ (51,083)	$ 47,946

Guaranteed Loans Outstanding

Loan Guarantee Programs	Outstanding Principal of Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
(3) Federal Ship Financing Fund (Title XI)	$ 2,028,217	$ 2,028,217
(4) OST Minority Business Resource Center	2,964	2,223
Total	$ 2,031,181	$ 2,030,440

New Guaranteed Loans Disbursed

Loan Guarantee Programs	2010 Outstanding Principal of Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
(3) Fed Ship Financing Fund (Title XI)	$ 22,544	$ 22,544
(4) OST Minority Business Resource Center	2,214	1,661
Total	$ 24,758	$ 24,205

Loan Guarantee Programs	2009 Outstanding Principal of Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
(3) Fed Ship Financing Fund (Title XI)	$ 269,230	$ 269,230
(4) OST Minority Business Resource Center	3,150	2,362
Total	$ 272,380	$ 271,592

Liability for Loan Guarantees (Present Value Method Post-1991 Guarantees):

Loan Guarantee Programs	2010 Liabilities for Post-1991 Guarantees, Present Value
(3) Federal Ship Financing Fund (Title XI)	$ 237,649
(4) OST Minority Business Resource Center	90
Total	$ 237,739

Note 6. Direct Loans and Loan Guarantees, Non-Federal Borrowers: (Cont.)

Subsidy Expense for Loan Guarantees by Program and Component

Subsidy Expense for New Loan Guarantees Disbursed

Loan Guarantee Programs	2010 Interest Supplements	Defaults	Fees and Other Collections	Other	Total
(3) Federal Ship Financing Fund (Title XI)	$ -	$ 1,400	$ (1,037)	$ -	$ 363
(4) OST Minority Business Resource Center	-	41	-	-	41
Total	$ -	$ 1,441	$ (1,037)	$ -	$ 404

Loan Guarantee Programs	2009 Interest Supplements	Defaults	Fees and Other Collections	Other	Total
(3) Federal Ship Financing Fund (Title XI)	$ -	$ 31,257	$ (15,669)	$ -	$ 15,588
(4) OST Minority Business Resource Center	-	58	-	-	58
Total	$ -	$ 31,315	$ (15,669)	$ -	$ 15,646

Modifications and Re-estimates

Loan Guarantee Programs	2010 Total Modifications	Interest Rate Re-estimates	Technical Re-estimates	Total Re-estimates
(3) Federal Ship Financing Fund (Title XI)	$ -	$ -	$ 31,909	$ 31,909
(4) OST Minority Business Resource Center	-	-	(71)	(71)
Total	$ -	$ -	$ 31,838	$ 31,838

Loan Guarantee Programs	2009 Total Modifications	Interest Rate Re-estimates	Technical Re-estimates	Total Re-estimates
(3) Federal Ship Financing Fund (Title XI)	$ -	$ -	$ 51,761	$ 51,761
(4) OST Minority Business Resource Center	-	-	(65)	(65)
Total	$ -	$ -	$ 51,696	$ 51,696

Total Loan Guarantee Subsidy Expense

Loan Guarantee Programs	2010	2009
(3) Federal Ship Financing Fund (Title XI)	$ 32,272	$ 67,349
(4) OST Minority Business Resource Center	(30)	(7)
Total	$ 32,242	$ 67,342

Budget Subsidy Rates for Loan Guarantees for the Current Year Cohort

Loan Guarantee Programs	2010 Interest Supplements	Defaults	Fees and Other Collections	Other	Total
(3) Federal Ship Financing Fund (Title XI)	0.00%	12.28%	-4.89%	0.00%	7.39%
(4) OST Minority Business Resource Center	0.00%	1.86%	0.00%	0.00%	1.86%
Total	0.00%	14.14%	-4.89%	0.00%	9.25%

The subsidy rates disclosed pertain only to the current year's cohorts. These rates cannot be applied to the guarantees of loans disbursed during the current reporting year to yield the subsidy expense. The subsidy expense for new loan guarantees reported in the current year could result from disbursements of loans from both current year cohorts and prior year(s) cohorts. The subsidy expense reported in the current year also includes modifications and re-estimates.

Notes to the Financial Statements

Note 6. Direct Loans and Loan Guarantees, Non-Federal Borrowers: (Cont.)

Schedule for Reconciling Loan Guarantee Liability Balances (Post-1991 Loan Guarantees)

Beginning Balance, Changes, and Ending Balance	2010	2009
Beginning Balance of the loan guarantee liability	$ 310,710	$ 258,050
Add: subsidy expense for guaranteed loans disbursed during the reporting years by component:		
Default costs (net of recoveries)	1,441	31,315
Fees and other collections	(1,037)	(15,669)
Total of the above subsidy expense components	404	15,646
Adjustments:		
Fees Received	7,147	16,541
Foreclosed Property and Loans Acquired	113,080	9,875
Claim Payments to Lenders	(222,967)	(52,837)
Interest accumulation on the liability balance	(10,894)	13,752
Other	8,421	(2,013)
Ending balance of the loan guarantee liability before reestimates	205,901	259,014
Add or subtract subsidy reestimates by component:		
Technical/default reestimate	31,838	51,696
Total of the above reestimate components	31,838	51,696
Ending balance of the loan guarantee liability	$ 237,739	$ 310,710

Interest on the loans is accrued based on the terms of the loan agreement. DOT does not accrue interest on non-performing loans that have filed for bankruptcy protection. DOT management considers administrative costs to be insignificant.

The upward reestimate on the Federal Ship Financing Fund (Title XI) reflects two loan defaults in FY 2010 and a reassessment of risk levels on outstanding loans. The two loan defaults totaling $226 million significantly increased the Federal Ship Financing Fund defaulted guaranteed loans receivable balance in FY 2010. The economic assumptions of the TIFIA upward and downward re-estimates were the result of a reassessment of risk levels as well as estimated changes in future cash flows on loans. The Railroad Rehabilitation Improvement Program's upward reestimate was a result of an update for change in the discount rate between time of loan obligation and disbursement and an update for actual cash flows and changes in technical assumptions.

The downturn in economy has led to volatility in financial markets which could affect loan repayments under direct and loan guarantee programs. Under the Federal Credit Reform Act, upward reestimates are automatically covered by permanent indefinite budget authority, which ensures DOT will have sufficient resources to cover any losses incurred in its existing portfolio without further action by Congress. DOT continues to evaluate the risks to affected markets in light of evolving economic conditions, but the impact of such risks on DOT's loan and loan guarantee portfolio reserves, if any, cannot be fully known at this time. The sufficiency of DOT's portfolio reserves at September 30, 2010 will largely depend on future economic and market conditions and could differ from current estimates.

Note 7. Inventory and Related Property:

As of September 30, 2010

	Cost	Allowance for Loss	Net
Inventory:			
Inventory Held for Current Sale	$ 101,772	-	$ 101,772
Excess, Obsolete and Unserviceable Inventory	12,678	(12,678)	-
Inventory Held for Repair	518,277	(112,840)	405,437
Other	47,166	(10,798)	36,368
Total Inventory	$ 679,893	(136,316)	$ 543,577
Operating Materials and Supplies:			
Items Held for Use	$ 232,835	(1,907)	$ 230,928
Items Held in Reserve for Future Use	30,429	-	30,429
Excess, Obsolete and Unserviceable Items	629	(629)	-
Items Held for Repair	34,954	(16,285)	18,669
Total Operating Materials & Supplies	$ 298,847	(18,821)	$ 280,026
Total Inventory and Related Property			$ 823,603

As of September 30, 2009

	Cost	Allowance for Loss	Net
Inventory:			
Inventory Held for Current Sale	$ 96,485	(84)	$ 96,401
Excess, Obsolete and Unserviceable Inventory	4,984	(4,984)	-
Inventory Held for Repair	493,356	(99,909)	393,447
Other	23,410	(10,591)	12,819
Total Inventory	$ 618,235	(115,568)	$ 502,667
Operating Materials and Supplies:			
Items Held for Use	$ 184,334	(1,881)	$ 182,453
Items Held in Reserve for Future Use	90,797	(165)	90,632
Excess, Obsolete and Unserviceable Items	411	(411)	-
Items Held for Repair	40,764	(19,206)	21,558
Total Operating Materials & Supplies	$ 316,306	(21,663)	$ 294,643
Total Inventory and Related Property			$ 797,310

Notes to the Financial Statements

Note 8. General Property, Plant and Equipment:

As of September 30, 2010

Major Classes	Service Life	Acquisition Value	Accumulated Depreciation	Book Value
Land and Improvements	30	$ 190,310	$ (20,376)	$ 169,934
Buildings and Structures	15-40	5,386,086	(2,981,314)	2,404,772
Furniture and Fixtures	15-20	77,208	(72,487)	4,721
Equipment	15-20	17,778,627	(10,275,214)	7,503,413
ADP Software	15-20	577,430	(294,756)	282,674
Assets Under Capital Lease	6-10	204,580	(104,678)	99,902
Leasehold Improvements	40	125,230	(61,793)	63,437
Aircraft	40	401,353	(324,251)	77,102
Ships and Vessels	11-20	1,950,592	(1,662,816)	287,776
Small Boats	20	26,768	(18,761)	8,007
Construction in Progress		2,950,694	-	2,950,694
Property Not in Use		65,718	(64,823)	895
Other Misc. Property		60,218	(6,071)	54,147
Total		$ 29,794,814	$ (15,887,340)	$ 13,907,474

As of September 30, 2009

Major Classes	Service Life	Acquisition Value	Accumulated Depreciation	Book Value
Land and Improvements	30	$ 102,799	$ (1,355)	$ 101,444
Buildings and Structures	15-40	5,224,590	(2,813,668)	2,410,922
Furniture and Fixtures	15-20	68,760	(67,320)	1,440
Equipment	15-20	18,948,598	(10,580,619)	8,367,979
ADP Software	15-20	365,618	(280,080)	85,538
Assets Under Capital Lease	6-10	204,485	(96,036)	108,449
Leasehold Improvements	40	117,595	(52,435)	65,160
Aircraft	40	397,341	(328,503)	68,838
Ships and Vessels	11-20	1,911,639	(1,561,562)	350,077
Small Boats	20	23,032	(19,044)	3,988
Construction in Progress		2,849,639	-	2,849,639
Property Not in Use		176,282	(150,153)	26,129
Total		$ 30,390,378	$ (15,950,775)	$ 14,439,603

The FAA is currently developing and testing the En Route Automation Modernization (ERAM) system to upgrade the management of air traffic in the en route space and enable the implementation of NextGen capabilities. As of September 30, 2010, construction in progress includes $1.7 billion related to the ERAM system.

While the deployment schedule for ERAM is not finalized and will depend upon results of continued testing of the system, FAA expects to deploy the ERAM system at 20 air route traffic control centers over the next several years. When fully deployed and operational, the ERAM system will replace three legacy air traffic systems currently being depreciated over service lives ranging from 5-20 years.

The net acquisition cost of the three air traffic legacy systems currently in use at September 30, 2010 is $2.1 billion with a net book value of $810 million. Depreciation on these air traffic legacy systems was $136 million and $134 million in FY 2010 and 2009, respectively. As the ERAM deployment schedule becomes more certain, FAA will re-evaluate the remaining service lives of the legacy air traffic systems and its estimated value at disposal. Adjustments will then be made to FAA accounting records in accordance with applicable accounting standards.

FAA conducted an in depth review and validation of its personal property assets in FY2010. The review included a statistical sampling and validation of many personal property assets across the United States and Canada to confirm the asset's existence. As a result of the review, FAA adjusted its property records in FY 2010 for assets previously retired but not recorded in the appropriate year's financial statements. The adjustments made to FAA's accounting records were not material to FAA's FY 2010 or prior year financial statements.

Notes to the Financial Statements

Note 9. Stewardship Property, Plant and Equipment:

Personal Property Heritage Assets

Implied within the Maritime Administration's mission is the promotion of the nation's rich maritime heritage. One aspect of this entails the collection, maintenance and distribution of maritime artifacts removed from agency-owned ships prior to their disposal. As ships are assigned to a non-retention status, artifact items are collected, inventoried, photographed and relocated to secure shore-side storage facilities. This resulting inventory is made available on a long-term loan basis to qualified organizations for public display purposes.

MARAD artifacts and other collections are generally on loan to single purpose memorialization and remembrance groups, such as AMVets and preservation societies. MARAD maintains a web-based inventory system that manages the artifact loan process. The program also supports required National Historical Preservation Act processing prior to vessel disposal. Funding for the maintenance of heritage items is typically the responsibility of the organization requesting the loan. The artifacts and other collections are composed of ships' operating equipment obtained from obsolete ships. The ships are inoperative and in need of preservation and restoration. As all items are durable and restorable, disposal is not a consideration. The artifacts and other collections are removed from inventory when destroyed while on loan. A total of 11,791 units of artifacts and other collections were collected as of September 30, 2010 and 646 units were collected as of September 30, 2009. This upward adjustment in FY 2010 is attributed to capturing the individual assets at the United States Merchant Marine Academy that were not previously reported. For the FY 2010 and 2009 there were 80 and 24, respectively, artifacts and other collections withdrawn from the items in storage.

Real Property Heritage Assets

Washington's Union Station support's DOT's mobility mission, facilitating the movement of intercity and commuter rail passengers through the Washington DC metropolitan area. The Federal Railroad Administration (FRA) has an oversight role in the management of Washington's Union Station. FRA received title through legislation, and sublets the property to Union Station Venture Limited which manages the property.

Washington's Union Station is an elegant and unique turn-of-the-century rail station in which a wide variety of elaborate, artistic workmanship characteristic of the period is found. Union Station is listed on the National Register of Historic Places. The station consists of the renovated original building and a parking garage, which was added by the National Park Service.

The Nuclear Ship *Savannah* is the world's first nuclear-powered merchant ship. It was constructed as a joint project of the Maritime Administration and the Atomic Energy Commission (AEC) as a signature element of President Eisenhower's "Atoms for Peace" program. In 1965, the AEC issued a commercial operating license and ended its participation in the joint program. The ship remains licensed and regulated by the U.S. Nuclear Regulatory Commission (successor to the AEC). The Nuclear Ship *Savannah* is listed on the National Register of Historic Places. The ship is a boldly-styled passenger/cargo vessel powered by a nuclear reactor.

Actions taken by the Maritime Administration since FY 2006 have stabilized the ship and rehabilitated portions of its interior for work-day occupancy by staff and crew. The ship is currently located in Baltimore, MD, where it is being prepared for continued "SAFSTOR" (The NRC method of preparing nuclear facilities for storage and decontamination) retention under the provisions of its NRC license.

Note 10. Liabilities Not Covered by Budgetary Resources:

	2010	2009
Intragovernmental:		
Other Liabilities	$ 368,316	$ 345,840
Total Intragovernmental	368,316	345,840
Federal Employee Benefits Payable	979,016	975,442
Environmental and Disposal Liabilities (Note 13)	1,103,562	1,195,249
Other Liabilities	842,958	809,252
Total Liabilities Not Covered by Budgetary Resources	3,293,852	3,325,783
Total Liabilities Covered by Budgetary Resources	13,967,670	13,605,059
Total Liabilities	$ 17,261,522	$ 16,930,842

Notes to the Financial Statements

Note 11. Debt:

	2009 Beginning Balance	2009 Net Borrowing	2009 Ending Balance	2010 Net Borrowing	2010 Ending Balance
Intragovernmental Debt:					
Debt to the Treasury	$ 1,760,761	$ 715,612	$ 2,476,373	$ 599,357	$ 3,075,730
Debt to the Federal Financing Bank	2,224	(249)	1,975	(266)	1,709
Total Intragovernmental Debt	$ 1,762,985	$ 715,363	$ 2,478,348	$ 599,091	$ 3,077,439

Note 12. Federal Employee Benefits Payable:

	2010	2009
Intragovernmental Liability for FECA (Note 15)	$ 226,974	$ 227,241
Expected Future Liability for FECA	979,016	975,442
Total Federal Employee Benefits Payable	$ 1,205,990	$ 1,202,683

The Department of Labor calculates the FECA liability for DOT as a whole. FECA liabilities include the expected liability for death, disability, medical and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The estimated liability is not covered by budgetary resources and thus will require future appropriated funding.

The intragovernmental FECA liability represents amounts billed to DOT by the DOL for FECA payments made on DOT's behalf. Funding for the liability will be provided by future appropriations. The intragovernmental amount is not an actuarial liability.

Notes to the Financial Statements

Note 13. Environmental and Disposal Liabilities:

	September 30, 2010	September 30, 2009
Public:		
Environmental Remediation	$ 623,799	$ 737,421
Asset Disposal	479,763	457,828
Total Public	$ 1,103,562	$ 1,195,249

Environmental remediation generally occurs under the Resource Conservation and Recovery Act of 1976 (RCRA), the Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA or Superfund), or the Toxic Substances Control Act (TSCA). Environmental remediation includes the fuel storage tank program, fuels, solvents, industrial, and chemicals, and other environmental cleanup activities associated with normal operations or the result of an accident. Cost estimates for environmental cleanup and asset disposal liabilities are not adjusted for inflation and are subject to revision as a result of changes in technology and environmental laws and regulations.

As of September 30, 2010 and 2009, DOT's environmental remediation liability primarily includes the removal of contaminants on the Nuclear Ship Savannah, containment of exfoliating ship paint for the non-retention ships in the National Defense Reserve Fleet (Fleet), and remediation at various sites managed by the FAA and MARAD.

In addition, there is a foreseeable environmental liability related to a site with MARAD and numerous other external parties, where the loss is probable and the estimate cannot be determined.

The National Maritime Heritage Act requires that MARAD dispose of certain merchant vessels owned by the U.S. government, including non-retention ships in the Fleet. Residual fuel, asbestos, and solid polychlorinated biphenyls (PCB) sometimes exist onboard MARAD's non-retention ships. The asset disposal liability at September 30, 2010 includes the estimated cost of disposing 159 ships. In addition, FAA records an asset disposal liability upon the decommissioning of an asset to cover preparatory costs required to meet regulatory standards allowing for the safe disposition of the asset.

Note 14. Grant Accrual:

The grant accrual consists of an estimate of grantee expenses incurred but not yet paid by DOT. Grantees primarily include state and local governments and transit authorities.

Grant accruals by Operating Administration at September 30, 2010 and 2009 are summarized as follows:

	2010	2009
Federal Highway Administration	$ 5,024,636	$ 4,240,468
Federal Transit Administration	1,300,083	1,662,252
Federal Aviation Administration	557,486	775,734
Other	83,794	91,360
Total Grant Accrual	$ 6,965,999	$ 6,769,814

Notes to the Financial Statements

Note 15. Other Liabilities:

September 30, 2010:

	Non-Current	Current	Total
Intragovernmental:			
Advances and Prepayments	$ 1,422,192	$ 749,761	$ 2,171,953
Accrued Pay and Benefits	-	100,395	100,395
FECA Billings (Note 12)	126,010	100,964	226,974
Uncleared Disbursements and Collections	-	142	142
Other Accrued Liabilities	245	217,304	217,549
Total Intragovernmental	$ 1,548,447	$ 1,168,566	$ 2,717,013
Public:			
Other Accrued Unbilled Payments	$ -	$ 56,623	$ 56,623
Advances and Prepayments	-	112,456	112,456
Accrued Pay and Benefits	107,317	835,090	942,407
Deferred Credits	-	37,670	37,670
Legal Claims	-	87,252	87,252
Capital Leases	85,452	21,506	106,958
Other Custodial Liability	-	38,400	38,400
Other Accrued Liabilities	57,633	3,290	60,923
Total Public	$ 250,402	$ 1,192,287	$ 1,442,689

The $1.42 billion in the Non-Current Intragovernmental Advances and Prepayments for FY 2010 is recorded by the Federal Transit Administration and is the remaining advance from the Federal Emergency Management Agency (FEMA) for the construction of Lower Manhattan area in New York. The current portion of the advances and prepayments for this same project is approximately $442.2 million.

Note 15. Other Liabilities: (Cont.)

As of September 30, 2009:

	Non-Current	Current	Total
Intragovernmental:			
Advances and Prepayments	$ 2,293,739	$ 334,334	$ 2,628,073
Accrued Pay and Benefits	36,878	90,594	127,472
FECA Billings (Note 12)	129,994	97,247	227,241
Uncleared Disbursements and Collections	-	156	156
Other Accrued Liabilities	37,123	72,917	110,040
Total Intragovernmental	$ 2,497,734	$ 595,248	$ 3,092,982
Public:			
Other Accrued Unbilled Payments	$ -	$ 44,573	$ 44,573
Advances and Prepayments	-	132,272	132,272
Accrued Pay and Benefits	109,053	729,507	838,560
Deferred Credits	-	53,612	53,612
Uncleared Disbursements and Collections	-	50	50
Legal Claims	10,004	41,374	51,378
Capital Leases	92,548	23,292	115,840
Other Custodial Liability	-	32,028	32,028
Other Accrued Liabilities	80,989	2,269	83,258
Total Public	$ 292,594	$ 1,058,977	$ 1,351,571

Notes to the Financial Statements

Note 16. Leases:

ENTITY AS LESSEE:

Capital Leases:

	2010	2009
Summary of Assets Under Capital Lease by Category:		
Land, Buildings & Machinery	$ 204,580	$ 204,485
Accumulated Amortization	(104,678)	(96,036)
Net Assets Under Capital Lease	$ 99,902	$ 108,449

Future Payments Due:

Fiscal Year	
Year 1 (2011)	$ 14,127
Year 2 (2012)	10,948
Year 3 (2013)	8,340
Year 4 (2014)	8,042
Year 5 (2015)	7,808
After 5 Years (2016+)	82,100
Total Future Lease Payments	$ 131,365
Less: Imputed Interest	24,407
Net Capital Lease Liability	$ 106,958

The capital lease payments disclosed above relate to FAA and are authorized to be funded annually as codified in the United States Code - Title 49 - Section 40110(c)(1) which addresses general procurement authority. The remaining principal payments are recorded as unfunded lease liabilities. The imputed interest is funded and expensed annually.

Operating Leases:

Future Payments Due:

Fiscal Year	**Land, Buildings, Machinery & Other**
Year 1 (2011)	$ 234,400
Year 2 (2012)	213,026
Year 3 (2013)	164,188
Year 4 (2014)	141,149
Year 5 (2015)	129,242
After 5 Years (2016+)	628,352
Total Future Lease Payments	$ 1,510,357

Operating lease expense incurred during the years ended September 30, 2010 and 2009 was $282.8 million and $297 million, respectively, including General Services Administration (GSA) leases that have a short termination privilege; however, DOT intends to remain in the leases. Estimates of the lease termination dates are subjective, and any projection of future lease payments would be arbitrary.

Note 17. Commitments and Contingencies

Legal Claims:

As of September 30, 2010 and 2009, DOT's contingent liabilities, in excess of amounts accrued, for asserted and pending legal claims reasonably possible of loss were estimated at $92.1 million and $96.9 million, respectively. DOT does not have material amounts of known unasserted claims.

In October 2010, the Governor of New Jersey cancelled a major project with FTA, the Access to Regions' Core (ARC) Tunnel. The amount obligated to date was $350 million and payments made were $233 million. FTA management and the State Governor are in the process of determining the amount New Jersey Transit may owe FTA.

Grant Programs:

FHWA pre-authorizes states to establish construction budgets without having received appropriations from Congress for such projects. FHWA does not guarantee the ultimate funding to the states for these "Advance Construction" projects and, accordingly, does not obligate any funds for these projects. When funding becomes available to FHWA, the states can then apply for reimbursement of costs that they have incurred on such projects, at which time FHWA can accept or reject such requests. For the fiscal year ended September 30, 2010 and 2009 FHWA has pre-authorized $40.2 billion and $41 billion, respectively, under these arrangements. These commitments have not been recognized in the DOT consolidated financial statements at September 30, 2010 and 2009.

FTA executes Full Funding Grant Agreements (FFGAs) under its Capital Investment program (New Starts) authorizing transit authorities to establish project budgets and incur costs with their own funds in advance of Congress appropriating New Starts funds to the project. As of September 30, 2010 and September 30, 2009, FTA had approximately $1.87 billion and $4.2 billion respectively, in funding commitments under FFGAs, which Congress had not yet appropriated. Congress must first provide the budget authority (appropriations) to allow FTA to incur obligations for these programs. Until Congress appropriates funds, FTA is not liable to grantees for any costs incurred. There is no liability related to these commitments reflected in the DOT consolidated financial statements at September 30, 2010 and 2009.

FAA's Airport Improvement Program provides grants for the planning and development of public-use airports that are included in the National Plan of Integrated Airport Systems. Eligible projects generally include improvements related to enhancing airport safety, capacity, security and environmental concerns. FAA's share of eligible costs for large and medium primary hub airports is 75 percent with the exception of noise program implementation, which is 80 percent of the eligible costs. For remaining airports (small primary, reliever, and general aviation airports), FAA's share is 95 percent of the eligible costs.

FAA has authority under 49 U.S.C. 47110(e) to issue letters of intent to enter into Airport Improvement Program grant agreements. FAA records an obligation when a grant is awarded. Through September 30, 2010, FAA issued letters of intent covering FY 1988 through FY 2026 totaling $6.5 billion. As of September 30, 2010, FAA had obligated $5.2 billion of this total amount leaving $1.3 billion unobligated. Through September 30, 2009, FAA issued letters of intent covering FY 1988 through FY 2020 totaling $5.9 billion. As of September 30, 2009, FAA had obligated $4.9 billion of this total amount, leaving $1.0 billion unobligated.

Contract Options and Negotiations:

As of September 30, 2010, FAA had contract options of $10.2 billion. These contract options give FAA the unilateral right to purchase additional equipment or services or to extend the contract terms. Exercising this right would require the obligation of funds in future years.

Notes to the Financial Statements

Note 17. Commitments and Contingencies: (Cont.)

Aviation Insurance Program:

FAA is authorized to issue hull and liability insurance under the Aviation Insurance Program for air carrier operations for which commercial insurance is not available on reasonable terms and when continuation of U.S. flag commercial air service is necessary in the interest of air commerce, national security, and U.S. foreign policy. FAA may issue (1) non-premium insurance, and (2) premium insurance for which a risk-based premium is charged to the air carrier, to the extent practical.

Aviation Insurance Program Continued:

During FY 2010, FAA provided premium war-risk insurance to 61 airlines. For these airlines, combined hull and liability per occurrence coverage limits range from $100 million to $4 billion. FAA also provided non-premium war-risk insurance to 33 carriers with 1,577 aircraft for Department of Defense charter operations for Central Command.

As of September 30, 2010, there are no pending aviation insurance claims. There is approximately $1.5 billion available in the Aviation Insurance Revolving Fund to pay claims to carriers covered by premium insurance. If premium insurance claims should exceed that amount, additional funding could be appropriated from the General Fund. The Department of Defense and State Department have agreed to pay claims to the carriers covered by non-premium insurance.

Environmental Liabilities:

As of September 30, 2010, FAA has estimated contingent liabilities, categorized as reasonably possible of $158 million related to environmental remediation. Contingency costs are defined for environmental liabilities as those costs that may result from incomplete design, unforeseen and unpredictable conditions or uncertainties within a defined project scope.

National Railroad Passenger Service Corporation (Amtrak)

The United States and the Department are not at risk if Amtrak fails and they do not guarantee the indebtedness of Amtrak, whose debt is secured primarily by assets of the corporation. Amtrak has been operating with an accumulated deficit and is dependent upon appropriations from Congress to continue operations. Amtrak has been receiving federal funds from Congress through the Department since 1981. For FY 2010 and FY 2009, the Department issued grants to Amtrak for $2.2 billion and $1.5 billion, respectively. These grants were for both operating and capital improvements. Refer to Note 1W (Significant Accounting Policies) for additional disclosure.

Note 18. Earmarked Funds:

DOT administers certain earmarked funds, which are specifically identified revenues, often supplemented by other financing sources, that remain available over time. No new legislation was enacted as of September 30, 2010 that significantly changed the purpose of the earmarked funds or redirected a material portion of the accumulated balance. Descriptions of the significant earmarked funds are as follows:

Highway Trust Fund

The Highway Trust Fund (HTF) is comprised of the Highway Corpus Trust Fund and certain accounts of the Federal Highway Administration, Federal Motor Carrier Safety Administration, Federal Transit Administration, Federal Railroad Administration and the National Highway Traffic Safety Administration. The HTF was created in 1956 by the Highway Revenue Act of 1956 with the main objective of funding the construction of the Dwight D. Eisenhower System of Interstate and Defense Highways. Over the years, the use of the fund has been expanded to include mass transit and other surface transportation programs such as highway safety and motor carrier safety programs. Overall, there are 73 separate treasury symbols in the HTF.

HTF's programs and activities are primarily financed from excise taxes collected on specific motor fuels, truck taxes, and fines and penalties. The Highway Revenue Act of 1982 established two accounts within the HTF, the Highway Account and the Mass Transit Account. During FY 2010, $14.7 and $4.8 billion was transferred from the General Fund to the Highway and Mass Transit Accounts restoring foregone interest earned since 1998. In August 2009 and September 2008, Congress appropriated $7 billion and $8 billion respectively for transfer from the Treasury General Fund to the HTF Highway Account to alleviate the cash shortfall created by increases in fuel prices, and corresponding declines in gas tax revenues.

Airport and Airway Trust Fund

The Airport and Airway Trust Fund (AATF) was authorized by the Airport and Airway Revenue Act of 1970 to provide funding for the Federal commitment to the nation's aviation system and typically includes annual funding for four distinct areas within FAA: Operations; Grant in Aid for Airports; Facilities and Equipment; and Research, Engineering and Development.

Funding currently comes from several aviation related excise tax collections from passenger tickets, passenger flight segments, international arrivals/departures, cargo waybills and aviation fuels.

Notes to the Financial Statements

Note 18. Earmarked Funds: (Cont.)

Mass Transit Account

In FY 2005 and prior, FTA's formula and bus grant programs were funded 80 percent by certain earmarked excise tax revenues and 20 percent from the Treasury general receipts account. These funds are considered earmarked but not reported as part of the HTF.

Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU) legislation (PL 109-59) changed the way FTA programs are funded. Beginning in FY 2006, the FTA formula and bus grant programs are funded 100 percent by the HTF.

The following is a list of other earmarked funds for which the DOT has program management responsibility:

Other Earmarked Funds

Aviation Insurance Revolving Fund
Pipeline Safety
Emergency Preparedness Grant
Aviation User Fees
Essential Air Service and Rural Airport Improvement Fund
University Transportation Centers
Contributions for Highway Research Program
Cooperative Work, Forest Highways
Safety of Cross-Border Trucking Between the United States and Mexico
Payment to Air Carriers
Right of Way Revolving Fund Program Account
Alaska Pipeline Task Force, Oil Spill Liability Trust Fund
Right-of-Way Revolving Fund Trust Fund
Technical Assistance, United States Dollars Advanced from Foreign Governments
Gifts and Bequests, Maritime Administration
Special Studies, Services and Projects
Gifts and Bequests, DOT Office of the Secretary
Equipment, Supplies, etc., for Cooperating Countries

Note 18. Earmarked Funds:

	Highway Trust Fund	Airport & Airway Trust Fund	Mass Transit	Other Earmarked Funds	FY 2010 Total Earmarked
Balance Sheet as of September 30, 2010					
Assets					
Fund Balance with Treasury	$ 4,776,346	$ 881,730	$ 937,341	$ 3,401,502	$ 9,996,919
Investments, Net	24,454,591	7,078,432	-	1,517,866	33,050,889
Accounts Receivable, Net	7,938	-	809	3,606,105	3,614,852
Property, Plant & Equipment	141,781	-	-	2,799,969	2,941,750
Other	318,973	-	784	407,921	727,678
Total Assets	$ 29,699,629	$ 7,960,162	$ 938,934	$ 11,733,363	$ 50,332,088
Liabilities and Net Position					
Accounts Payable	$ 53,446	$ 3,486,898	$ 508	$ 437,381	$ 3,978,233
FECA Liabilities	21,634	-	-	1,120,795	1,142,429
Grants Accrual	4,264,344	-	50,324	576,428	4,891,096
Other Liabilities	271,989	-	2,824	1,011,708	1,286,521
Unexpended Appropriations	-	-	48,480	1,163,040	1,211,520
Cumulative Results of Operations	25,088,216	4,473,264	836,798	7,424,011	37,822,289
Total Liabilities and Net Position	$ 29,699,629	$ 7,960,162	$ 938,934	$ 11,733,363	$ 50,332,088
Statement of Net Cost For the Period Ended September 30, 2010					
Program Costs	$ 39,429,077	$ 10,220,422	$ 391,035	$ 4,890,588	$ 54,931,122
Less Earned Revenue	266,331	-	-	483,528	749,859
Net Program Costs	39,162,746	10,220,422	391,035	4,407,060	54,181,263
Costs Not Attributable to Programs	-	-	-	166,558	166,558
Net Cost of Operations	$ 39,162,746	$ 10,220,422	$ 391,035	$ 4,573,618	$ 54,347,821
Statement of Changes in Net Position For the Period September 30, 2010					
Beginning Net Position	$ 9,733,737	$ 3,899,318	$ 1,276,046	$ 8,785,518	$ 23,694,619
Budgetary Financing Sources	54,473,665	10,794,368	267	5,438,148	70,706,448
Other Financing Sources	43,560	-	-	(1,062,997)	(1,019,437)
Net Cost of Operations	39,162,746	10,220,422	391,035	4,573,618	54,347,821
Change in Net Position	15,354,479	573,946	(390,768)	(198,467)	15,339,190
Net Position End of Period	$ 25,088,216	$ 4,473,264	$ 885,278	$ 8,587,051	$ 39,033,809

Notes to the Financial Statements

Note 18. Earmarked Funds: (Cont.)

	Highway Trust Fund	Airport & Airway Trust Fund	Mass Transit	Other Earmarked Funds	FY 2009 Total Earmarked
Balance Sheet as September 30, 2009					
Assets					
Fund Balance with Treasury	$ 2,607,082	$ (204,227)	$ 1,385,079	$ 3,084,552	$ 6,872,486
Investments, Net	11,484,437	7,829,468	-	1,370,576	20,684,481
Accounts Receivable, Net	46,311	-	6,949	3,966,432	4,019,692
Property, Plant & Equipment	121,162	-	-	3,831	124,993
Other	383,634	46,290	957	3,591,674	4,022,555
Total Assets	$ 14,642,626	$ 7,671,531	$ 1,392,985	$ 12,017,065	$ 35,724,207
Liabilities and Net Position					
Accounts Payable	$ 130,897	$ 3,772,213	$ 401	$ 452,581	4,356,092
FECA Liabilities	22,848	-	-	1,112,446	1,135,294
Grants Accrual	4,501,677	-	113,714	683,946	5,299,337
Other Liabilities	253,467	-	2,824	982,574	1,238,865
Unexpended Appropriation	-	-	41,793	1,171,158	1,212,951
Cumulative Results of Operations	9,733,737	3,899,318	1,234,253	7,614,360	22,481,668
Total Liabilities and Net Position	$ 14,642,626	$ 7,671,531	$ 1,392,985	$ 12,017,065	$ 35,724,207
Statement of Net Cost For the Period Ended September 30, 2009					
Program Costs	$ 44,758,237	$ 11,783,177	$ 747,099	$ 3,190,332	$ 60,478,845
Less Earned Revenue	92,806	-	5,332	531,178	629,316
Net Program Costs	44,665,431	11,783,177	741,767	2,659,154	59,849,529
Costs Not Attributable to Programs	-	-	-	137,700	137,700
Net Cost of Operations	$ 44,665,431	$ 11,783,177	$ 741,767	$ 2,796,854	$ 59,987,229
Statement of Changes in Net Position For the Period Ended September 30, 2009					
Beginning Net Position	$ 12,435,464	$ 4,822,612	$ 2,017,018	$ 7,679,358	$ 26,954,452
Budgetary Financing Sources	42,150,918	10,859,883	795	3,821,301	56,832,897
Other Financing Sources	(187,214)	-	-	81,713	(105,501)
Net Cost of Operations	44,665,431	11,783,177	741,767	2,796,854	59,987,229
Change in Net Position	(2,701,727)	(923,294)	(740,972)	1,106,160	(3,259,833)
Net Position End of Period	$ 9,733,737	$ 3,899,318	$ 1,276,046	$ 8,785,518	$ 23,694,619

Note 19. Intragovernmental Costs and Exchange Revenues:

	For the Period Ended September 30, 2010		
	Intra-governmental	With the Public	Total
Surface Transportation:			
Federal-Aid Highway Program:			
Gross Costs	$ 107,913	$ 30,575,531	$ 30,683,444
Less Earned Revenue	32,019	49,913	81,932
Net Program Costs	75,894	30,525,618	30,601,512
Mass Transit Program			
Gross Costs	31,795	12,565,530	12,597,325
Less Earned Revenue	416,483	1,549	418,032
Net Program Costs	(384,688)	12,563,981	12,179,293
Other Surface Transportation Programs:			
Gross Costs	312,499	17,961,803	18,274,302
Less Earned Revenue	85,003	200,627	285,630
Net Program Costs	227,496	17,761,176	17,988,672
Total Surface Transportation Program Costs	(81,298)	60,850,775	60,769,477
Air Transportation:			
Gross Costs	2,572,942	14,693,803	17,266,745
Less Earned Revenue	182,693	308,237	490,930
Net Program Costs	2,390,249	14,385,566	16,775,815
Maritime Transportation:			
Gross Costs	278,417	816,446	1,094,863
Less Earned Revenue	464,143	62,118	526,261
Net Program Costs	(185,726)	754,328	568,602
Cross-Cutting Programs:			
Gross Costs	44,715	673,125	717,840
Less Earned Revenue	376,785	4,552	381,337
Net Program Costs	(332,070)	668,573	336,503
Costs not assigned to programs	72,511	321,992	394,503
Less: Earned Revenues not attributed to programs	471	-	471
Net Cost of Operations	$ 1,863,195	$ 76,981,234	$ 78,844,429

Notes to the Financial Statements

Note 19. Intragovernmental Costs and Exchange Revenues: (Cont.)

	For the Period Ended September 30, 2009		
	Intra-governmental	With the Public	Total
Surface Transportation:			
Federal-Aid Highway Program:			
Gross Costs	$ 105,064	$ 35,789,451	$ 35,894,515
Less Earned Revenue	32,448	39,807	72,255
Net Program Costs	72,616	35,749,644	35,822,260
Mass Transit Program			
Gross Costs	36,332	11,585,418	11,621,750
Less Earned Revenue	269,677	920	270,597
Net Program Costs	(233,345)	11,584,498	11,351,153
Other Surface Transportation Programs:			
Gross Costs	265,763	10,338,808	10,604,571
Less Earned Revenue	21,332	158,998	180,330
Net Program Costs	244,431	10,179,810	10,424,241
Total Surface Transportation Program Costs	83,702	57,513,952	57,597,654
Air Transportation:			
Gross Costs	2,440,109	14,428,796	16,868,905
Less Earned Revenue	244,329	335,654	579,983
Net Program Costs	2,195,780	14,093,142	16,288,922
Maritime Transportation:			
Gross Costs	61,761	1,051,911	1,113,672
Less Earned Revenue	378,111	6,874	384,985
Net Program Costs	(316,350)	1,045,037	728,687
Cross-Cutting Programs:			
Gross Costs	39,448	608,877	648,325
Less Earned Revenue	316,241	4,876	321,117
Net Program Costs	(276,793)	604,001	327,208
Cost not assigned to a program	85,041	281,000	366,041
Less: Earned Revenues not attributed to programs	15,640	(4,932)	10,708
Net Cost of Operations	$ 1,755,740	$ 73,542,064	$ 75,297,804

Surface Transportation Program costs includes those operating costs incurred by the Operating Administrations authorized by SAFETEA-LU (FHWA, NHTSA, FMCSA, FRA and FTA), to promote safety and mobility of the nation's highways and railroads and among the nation's drivers and auto manufacturers.

Air Transportation Program costs include those operating costs incurred to promote aviation safety and mobility by building, maintaining, and operating the Nation's air traffic control system; overseeing commercial and general aviation safety through regulation and inspection; and providing assistance to improve the capacity and safety of our airports.

Maritime Transportation Program Costs include those operating costs incurred to promote the development and maintenance of a U.S. merchant marine that is sufficient to carry the Nation's domestic waterborne commerce, a substantial portion of which is trade with other nations, and to serve as a naval and military auxiliary in time of war and national emergency.

Cross-cutting Program costs include those operating costs incurred to provide goods and services on a reimbursable basis for those Operating Administrations whose mission is primarily cross modal.

Note 20. Excise Taxes and Other Non-Exchange Revenue:

The Internal Revenue Service (IRS) collects various excise taxes that are deposited in the HTF and AATF. Monthly, the United States Treasury, Office of Tax Analysis (OTA) estimates the amount collected/revenue recognized, and adjusts the estimates to reflect actual collections quarterly. The IRS submits certificates of actual tax collections to DOT three months after the quarter-end and, accordingly the DOT financial statements are adjusted to reflect such actual amounts at that time. Total taxes recognized for the year ended September 30, 2009 and 2008 includes OTA estimates as follows:

	9/30/2009	9/30/2008
Actual	12,437,337	12,861,000
Estimate	12,408,576	13,047,000
Under (Over) accrual	28,761	(186,000)

These differences were reflected as an adjustment in the DOT subsequent year's financial statements. During FY 2010, DOT continued to experience differences between its estimated and actual excise tax collections as follows:

	Quarter Ended		
	12/31/09	3/31/2010	6/30/2010
Actual	11,491,000	11,061,360	12,334,798
Estimate	11,993,000	10,896,563	12,519,765
Under (Over) accrual	(502,000)	164,797	(184,967)

Excise taxes estimated by OTA in the 1st, 2nd and 3rd quarters of FY 2010 fluctuated with the certified as actual by the IRS by $502 million, ($164) million and $184 million, respectively. Total taxes recognized in DOT FY 2010 financial statement included the OTA estimate of $11.5 billion the for quarter ended September 30, 2010.

For the years ended September 30, 2010 and 2009, respectively, excise taxes and associated nonexchange revenue, which are reported on the Statement of Changes in Net Position, were as follows:

Non-Exchange Revenue:

Highway Trust Fund **Excise Taxes and Other Non-Exchange Revenue**	**2010**	**2009**
Gasoline	$ 24,836,919	$ 24,626,848
Diesel and Special Motor Fuels	9,135,819	9,323,118
Trucks	2,767,199	3,166,825
Investment Income	17,325	-
Fines and Penalties	24,918	25,586
Total Taxes	36,782,180	37,142,377
Less: Transfers	(1,203,149)	(1,135,367)
Gross Taxes	35,579,031	36,007,010
Less: Refunds of Taxes	(569,069)	(1,045,767)
Total Excise Taxes	35,009,962	34,961,243
Other Non-Exchange Revenue	161	1,151
Net Highway Trust Fund Excise Taxes & Other Non-Exchange Revenue	35,010,123	34,962,394
Federal Aviation Administration **Excise Taxes and Other Non-Exchange Revenue:**		
Passenger Ticket	7,261,070	7,465,647
International Departure	2,324,017	2,187,182
Fuel (Air)	651,475	556,570
Waybill	395,119	469,881
Investment Income	181,415	281,994
Tax Refunds and Credits	(18,728)	(110,034)
Other	35,379	34,532
Net Federal Aviation Administration Excise Taxes & Other Non-Exchange Revenue	10,829,747	10,885,772
Other Miscellaneous Net Non Exchange Revenue	77,458	31,505
Total Non-Exchange Revenue	$ 45,917,328	$ 45,879,671

Notes to the Financial Statements

Note 21. Combined Statement of Budgetary Resources:

The amount of direct and reimbursable obligations incurred against amounts apportioned under Category A, B and Exempt from apportionment, as defined in OMB Circular No. A-11, Part 4, Instructions on Budget Execution, are as follows:

	2010			2009		
	Direct	Reimbursable	Total	Direct	Reimbursable	Total
Category A	$ 7,192,018	$ 836,297	$ 8,028,315	$ 8,185,100	$ 992,716	$ 9,177,816
Category B	104,494,200	1,000,490	105,494,690	107,055,097	1,110,483	108,165,580
Exempt from apportionment	73,733	250,893	324,626	43,075	-	43,075
Total	$ 111,759,951	$ 2,087,680	$ 113,847,631	$ 115,283,272	$ 2,103,199	$ 117,386,471

The information presented in the DOT's Statement of Budgetary Resources reconciles with information submitted in its year-end Reports on Budget Execution and Budgetary Resources (SF-133s) with one material difference. The difference is caused by the reversal of a $767 million adjustment recorded at the end of FY 2009, for which DOT consulted with OMB on its reporting of the FY 2010 Report on Budget Execution and Budgetary Resources (SF 133). In FY 2011, the $767 million will be a reconciling item in the reconciliation of the Statement of Budgetary Resources to the President's Budget due to the timing of the release of the information.

	2010	2009
Available Contract Authority at year-end	$ 26,432,116	$ 28,959,336
Available Borrowing Authority at year-end	$ 2,603,647	$ 335,573
Undelivered Orders at year-end	$ 106,634,884	$ 101,592,347

The amounts reported for undelivered orders only include balances obligated for goods and services not delivered and does not include prepayments.

Terms of Borrowing Authority Used:

Under the provisions of the Federal Credit Reform Act of 1990, DOT direct loan and loan guarantee programs are authorized to borrow funds from Treasury to support its credit programs. All loan draw downs are dated October 1 of the applicable fiscal year. Interest is payable at the end of each fiscal year based on activity for that fiscal year. Principal can be repaid at any time funds become available. Repayment is effectuated by a combination of loan recoveries and upward re-estimates.

Existence, Purpose, and Availability of Permanent Indefinite Appropriations:

DOT has permanent indefinite appropriations for the Facilities and Equipment, Grants in Aid and Research, Development and Engineering appropriations to fully fund special projects that were on-going and spanned several years.

Unobligated Budgetary Resources:

Unobligated balances of budgetary resources for unexpired accounts are available in subsequent years until expiration, upon receipt of an apportionment from OMB. Unobligated balances of expired accounts are not available.

Statement of Budgetary Resources vs Budget of the United States Government:

The reconciliation for the year ended September 30, 2009 is presented below. The reconciliation for the fiscal year ended September 30, 2010 is not presented, because the submission of the Budget of the United States (Budget) for FY 2012, which presents the execution of the FY 2010 budget, occurs after publication of these financial statements. The Department of Transportation Budget Appendix can be found on the OMB website (http://www.gpoaccess.gov/usbudget) and will be available in early February 2011.

(Dollars in millions)

	Budgetary Resources	Obligations Incurred	Distributed Offsetting Receipts	Net Outlays
Combined Statement of Budgetary Resources	$ 175,644	$ 117,386	$ (228)	$ 80,881
Funds not Reported in the Budget				
Expired Funds	(350)	(87)	-	-
Recovered subsidy costs	(17)			
Distributed Offsetting Receipts	-	-	228	225
Other	1	(4)	-	(4)
Budget of the United States Government	$ 175,278	$ 117,295	$ -	$ 81,102

Other differences represent financial statement adjustments, timing differences and other immaterial differences between amounts reported in the Department's Statement of Budgetary Resources and the Budget of the United States.

Note 22. Incidental Custodial Collections:

Revenue Activity:

Sources of Cash Collections:	**2010**	**2009**
Miscellaneous Receipts	$ 19,068	$ 26,184
Fines, Penalties and Forfeitures	-	6,136
Total Cash Collections	19,068	32,320
Total Custodial Revenue	19,068	32,320
Disposition of Collections:		
Transferred to Treasury's General Fund	19,068	32,320
Net Custodial Activity	$ -	$ -

Notes to the Financial Statements

Note 23. Reconciliation of Net Cost of Operations to Budget:

	2010	2009
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations Incurred	$ 113,847,631	$ 117,386,471
Less: Spending Authority from Offsetting Collections and Recoveries	10,194,866	8,731,311
Obligations Net of Offsetting Collections and Recoveries	103,652,765	108,655,160
Less: Distributed Offsetting Receipts	(219,178)	(228,339)
Net Obligations	103,433,587	108,426,821
Other Resources		
Donations and Forfeitures of Property	-	-
Transfers In/Out Without Reimbursement	(6)	(153,631)
Imputed Financing From Costs Absorbed by Others	704,727	756,225
Other	(120,821)	(168,523)
Net Other Resources Used to Finance Activities	583,900	434,071
Total Resources Used to Finance Activities	104,017,487	108,860,892
Resources Used to Finance Items Not Part of the Net Cost of Operations:		
Change in Budgetary Resources Obligated for Goods, Services and Benefits Ordered but not yet Provided	4,921,176	26,709,777
Resources That Fund Expenses Recognized in Prior Periods	231,453	238,485
Credit Program Collections That Increase Liabilities for Loan Guarantees or Allowances for Subsidy	(404,267)	(209,856)
Other/Change in Unfilled Customer Orders	645,292	(75,777)
Anticipated Resources not yet realized	(18,602)	-
Resources That Finance the Acquisition of Assets	2,142,542	1,712,741
Other Resources or Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations	19,403,513	6,999,368
Total Resources Used to Finance Items Not Part of the Net Cost Of Operations	26,921,107	35,374,738
Total Resources Used to Finance the Net Cost of Operations	$ 77,096,380	$ 73,486,154

Note 23. Reconciliation of Net Cost of Operations to Budget: (Cont.)

	2010	2009
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Periods:		
Increase in Annual Leave Liability	$ 6,461	$ 14,084
Increase in Environment and Disposal Liability	-	366,360
Upward/Downward Reestimates of Credit Subsidy Expense	(43,394)	(58,536)
Increase in exchange revenue receivable from the public	4,228	(23,370)
Change in Other Liabilities	174,084	56,513
Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods	141,379	355,051
Components Not Requiring or Generating Resources:		
Depreciation and Amortization	1,173,561	1,209,740
Revaluation of Assets or Liabilities	291,694	12,924
Other Expenses and Adjustments not Otherwise Classified Above	141,415	233,935
Total Components of Net Cost of Operations That Will Not Require or Generate Resources	1,606,670	1,456,599
Total Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Period	1,748,049	1,811,650
Net Cost of Operations	$ 78,844,429	$ 75,297,804

Notes to the Financial Statements

Note 24. Reporting on DOT Affiliated Activities

Saint Lawrence Seaway Development Corporation

The U.S. Saint Lawrence Seaway Development Corporation (SLSDC), a wholly owned Government corporation and operating administration of the Department, is responsible for the operation and maintenance of the U.S. portion of the St. Lawrence Seaway. This responsibility includes maintaining and operating two U.S. locks, controlling vessel traffic and promoting trade development activities on the seaway.

Condensed Information:

	2010	2009
Cash and Short-Term Time Deposits	$ 34,283	$ 28,529
Long-Term Time Deposits	2,839	1,271
Accounts Receivable	86	113
Inventories	266	267
Other Current Assets	1	27
Property, Plant and Equipment	75,687	73,533
Deferred Charges	3,546	3,457
Other Assets	600	622
Total Assets	**$ 117,308**	**$ 107,819**
Current Liabilities	$ 3,825	$ 3,465
Actuarial Liabilities	3,546	3,457
Total Liabilities	**7,371**	**6,922**
Invested Capital	90,818	88,661
Cumulative Results of Operations	19,119	12,236
Total Net Position	**109,937**	**100,897**
Total Liabilities and Net Position	**$ 117,308**	**$ 107,819**
Operating Revenues	$ 29,375	$ 30,639
Operating Expenses	25,226	22,652
Operating Income (loss)	4,149	7,987
Other Financing Sources	2,734	2,768
Operating revenues and other financing sources over (under) operating expenses	**6,883**	**10,755**
Beginning cumulative results of operations (deficit)	12,236	1,481
Ending cumulative results of operations (deficit)	**$ 19,119**	**$ 12,236**

MARAD Non-Appropriated Fund Instrumentality (NAFI)

The Non-Appropriated Fund Instrumentality (NAFI) operate using their own funds generated from the proceeds received from various non-governmental sources, rather than appropriated funds. At DOT, NAFI's operate as a separate fiscal entity under MARAD to provide or assist the U.S. Merchant Marine Academy in providing programs and services for students, personnel and authorized civilians from sources other than Congressional appropriations. Although considered Governmental, NAFI cash balances and operating expenses are separate and distinct from those recorded in the books of the Federal Government. For the fiscal years September 30, 2010 and September 30, 2009, NAFI operating revenues and proceeds from midshipmen fees totaled $10 million and $13 million respectively.

Note 25. Fiduciary Activities

The Title XI Escrow Fund was authorized pursuant to the Merchant Marine Act of 1936, as amended. The fund was originally established to hold guaranteed loan proceeds pending construction of MARAD approved and financed vessels.

The Act was recently amended to allow the deposit of additional cash security items such as reserve funds or debt reserve funds. Individual shipowners provide funds to serve as security on MARAD guaranteed loans. Funds deposited and invested by MARAD remain the property of individual shipowners. In the event of default, MARAD will use the escrow funds to offset the shipowners' debt to the Government.

Fund investments are limited to U.S. Government securities purchased by MARAD through the Treasury.

Schedule of Fiduciary Activity
For the quarter ended September 30, 2010 and 2009

	2010	2009
Fiduciary Net Assets, beginning of year	$ 141,756	$ 28,396
Contributions	-	113,360
Disbursements to and on behalf of beneficiaries	(113,562)	-
Increases/(Decreases) in fiduciary net assets	(113,562)	113,360
Fiduciary net assets, end of year	**$ 28,194**	**$ 141,756**

Fiduciary Net Assets
As of September 30, 2010 and 2009

Fiduciary Assets		
Fiduciary Fund Balance with Treasury	$ 295	$ 75
Investments in Treasury Securities	27,899	141,681
Total Fiduciary Net Assets	**28,194**	**141,756**

REQUIRED SUPPLEMENTARY INFORMATION

Deferred Maintenance:

DOT Entity	Major Class of Asset	Method of Measurement	Asset Condition*	2010 Cost to Return to Acceptable Condition**	2009 Cost to Return to Acceptable Condition**
FAA	Buildings	Condition Assessment Survey	4 & 5	$ 74,155	$ 111,298
	Other Structures and Facilities	Condition Assessment Survey	4 & 5	194,000	151,000
MARAD	Vessels, Ready Reserve Force (Various Locations)	Condition Assessment Survey	3	9,191	6,285
	Real Property, Buildings (Anchorage)	Condition Assessment Survey	4	7,672	40
	Other (Fleet Craft)	Condition Assessment Survey	2&3	-	350
	Other (Pier and Berthing Surveys and Studies)	Estimate	2	-	35
	Other (Heritage Assets)	Condition Assessment	3&4	-	200
			Total	$ 285,018	$ 269,208

*Asset Condition Rating Scale:

1 - Excellent
2 - Good
3 - Fair
4 - Poor
5 - Very Poor

**Acceptable Condition is:

FAA Buildings	3 - Fair
FAA Other Structures and Facilities	3 - Fair
MARAD Vessels, Ready Reserve Force	1 - Excellent - Ships are seaworthy and ready for mission assignments within prescribed time limits.
MARAD Real Property, Buildings	3 - Fair - Buildings are safe and inhabitable.
MARAD Real Property, Structures	3 - Fair - Adequate water depth, shore power, and mooring capabilities.
MARAD Heritage Assets	3 - Fair

Deferred Maintenance is maintenance that was not performed when it should have been or was scheduled to be performed and delayed until a future period. Maintenance is keeping fixed assets in acceptable condition, and includes preventative maintenance, normal repairs, replacement of parts and structural components, and other activities needed to preserve assets in a condition to provide acceptable service and to achieve expected useful lives.

U.S. Department of Transportation
Required Supplementary Information
Combining Statements of Budgetary Resources By Major Account
For the Period Ended September 30, 2010
(Dollars in Thousands)

Budgetary Resources:	**Federal-Aid**	**FAA**	**FTA**	**MARAD**	**All Other**	**TOTAL**
Unobligated balance, brought forward, October 1	$ 25,819,161	$ 3,598,143	$ 8,953,472	$ 543,188	$ 19,343,857	$ 58,257,821
Recoveries of prior year unpaid obligations	-	425,738	542,305	20,483	2,546,458	3,534,984
Budget authority:						
Appropriations received	41,943,123	15,526,737	11,789,581	610,268	27,536,634	97,406,343
Borrowing authority	-	-	-	319,363	2,284,284	2,603,647
Contract authority	51,750,152	3,515,000	8,360,565	-	1,284,282	64,909,999
Spending authority from offsetting collections						
Earned						
Collected	247,666	916,686	436,306	524,404	1,332,990	3,458,052
Change in receivables from Federal sources	(11,188)	(92,865)	(7,760)	18,741	6,433	(86,639)
Change in unfilled customer orders						
Advance received	1,785	(817)	(410,065)	(25,287)	(101,810)	(536,194)
Without advance from Federal sources	(165,864)	(27,370)	(10,375)	(98,578)	97,933	(204,254)
Expenditure transfers from trust funds	-	4,000,000	-	487	28,430	4,028,917
Subtotal	93,765,674	23,837,371	20,158,252	1,349,398	32,469,176	171,579,871
Nonexpenditure transfers, net	(1,406,637)	(48,627)	1,561,151	50,000	(104,270)	51,617
Temporarily not available pursuant to Public Law	-	-	-	-	(5,007)	(5,007)
Permanently not available	(44,046,000)	(3,521,002)	(9,401,608)	(221,502)	(1,683,108)	(58,873,220)
Total budgetary resources	$ 74,132,198	$ 24,291,623	$ 21,813,572	$ 1,741,567	$ 52,567,106	$ 174,546,066
Status of Budgetary Resources:						
Obligations incurred:						
Direct	$ 41,536,569	20,218,239	$ 11,308,034	895,647	$ 37,801,462	$ 111,759,951
Reimbursable	70,271	751,479	4,683	367,936	893,311	2,087,680
Subtotal	41,606,840	20,969,718	11,312,717	1,263,583	38,694,773	113,847,631
Unobligated balance:						
Apportioned	16,881,341	1,704,024	10,015,855	231,710	13,322,463	42,155,393
Exempt from apportionment	-	-	-	15,526	303,696	319,222
Subtotal	16,881,341	1,704,024	10,015,855	247,236	13,626,159	42,474,615
Unobligated balance not available	15,644,017	1,617,881	485,000	230,748	246,174	18,223,820
Total status of budgetary resources	$ 74,132,198	$ 24,291,623	$ 21,813,572	$ 1,741,567	$ 52,567,106	$ 174,546,066

U.S. Department of Transportation
Required Supplementary Information
Combining Statements of Budgetary Resources By Major Account
For the Period Ended September 30, 2010
(Dollars in Thousands)

Change in Obligated Balances:	**Federal-Aid**	**FAA**	**FTA**	**MARAD**	**All Other**	**TOTAL**
Obligated balance, net:						
Unpaid obligations, brought forward, October 1	$ 52,631,073	$ 9,680,164	$ 22,058,387	$ 402,202	$ 24,834,538	$ 109,606,364
Uncollected customer payments from Federal sources, brought forward, October 1	(516,259)	(463,179)	(84,750)	(153,110)	(512,452)	(1,729,750)
Total unpaid obligated balance, net	52,114,814	9,216,985	21,973,637	249,092	24,322,086	107,876,614
Obligations incurred	41,606,840	20,969,718	11,312,717	1,263,583	38,694,773	113,847,631
Gross outlays	(31,031,619)	(20,938,189)	(13,113,796)	(1,276,041)	(38,750,793)	(105,110,438)
Obligated balance, transferred, net						
Unpaid obligations	-	-	-	-	26,344	26,344
Recoveries of prior year unpaid obligations, actual	-	(425,738)	(542,305)	(20,483)	(2,546,458)	(3,534,984)
Change in uncollected customer payments from Federal sources	181,512	120,235	18,136	79,836	(97,424)	302,295
Obligated balance, net, end of period:						
Unpaid obligations	64,706,294	9,285,955	19,715,003	369,261	22,258,404	116,334,917
Uncollected customer payments from Federal sources	(334,747)	(342,944)	(66,614)	(73,274)	(609,876)	(1,427,455)
Total unpaid obligated balance, net, end of period	$ 64,371,547	$ 8,943,011	$ 19,648,389	$ 295,987	$ 21,648,528	$ 114,907,462
Net Outlays:						
Net Outlays						
Gross Outlays	$ 31,031,619	$ 20,938,189	$ 13,113,796	$ 1,276,041	$ 38,750,793	$ 105,110,438
Offsetting collections	(253,414)	(4,915,870)	(26,241)	(499,604)	(1,252,388)	(6,947,517)
Distributed offsetting receipts	-	(12,776)	93	(85,402)	(121,093)	(219,178)
Net outlays	$ 30,778,205	$ 16,009,543	$ 13,087,648	$ 691,035	$ 37,377,312	$ 97,943,743

U.S. Department of Transportation
Required Supplementary Information
Combining Statements of Budgetary Resources By Major Account
For the Year Ended September 30, 2009
(Dollars in Thousands)

Budgetary Resources:	**Federal-Aid**	**FAA**	**FTA**	**MARAD**	**All Other**	**TOTAL**
Unobligated balance, brought forward, October 1	$ 35,439,498	$ 2,822,280	$ 4,456,802	$ 499,971	$ 2,828,632	$ 46,047,183
Recoveries of prior year unpaid obligations	-	385,377	37,871	59,833	242,747	725,828
Budget authority:						
Appropriations received	41,440,266	16,830,694	19,040,663	599,202	50,231,514	128,142,339
Borrowing authority	-	-	-	209,000	1,349,169	1,558,169
Contract authority	43,186,476	3,900,000	8,360,565	-	1,270,000	56,717,041
Spending authority from offsetting collections						
Earned						
Collected	86,112	829,788	280,061	494,245	947,633	2,637,839
Change in receivables from Federal sources	1,573	70,202	3,228	(21,834)	(41,444)	11,725
Change in unfilled customer orders						
Advance received	7,667	66,512	(260,677)	45,174	116,191	(25,133)
Without advance from Federal sources	76,146	(39,911)	(18,828)	30,188	49,137	96,732
Expenditure transfers from trust funds	-	5,238,005	25	15,956	30,334	5,284,320
Subtotal	84,798,240	26,895,290	27,405,037	1,371,931	53,952,534	194,423,032
Nonexpenditure transfers, net	(977,819)	(46,300)	1,265,065	-	1,762,754	2,003,700
Temporarily not available pursuant to Public Law	-				(2,251)	(2,251)
Permanently not available	(53,342,158)	(3,744,234)	(8,770,000)	(234,066)	(1,462,742)	(67,553,200)
Total budgetary resources	$ 65,917,761	$ 26,312,413	$ 24,394,775	$ 1,697,669	$ 57,321,674	$ 175,644,292
Status of Budgetary Resources:						
Obligations incurred:						
Direct	$ 40,049,960	$ 21,971,269	$ 15,420,778	$ 787,413	$ 37,053,852	$ 115,283,272
Reimbursable	48,640	743,001	20,525	367,068	923,965	2,103,199
Subtotal	40,098,600	22,714,270	15,441,303	1,154,481	37,977,817	117,386,471
Unobligated balance:						
Apportioned	19,186,099	1,707,455	8,946,604	247,783	18,933,612	49,021,554
Exempt from apportionment	-	-	-	2,027	274,347	276,374
Subtotal	19,186,099	1,707,455	8,946,604	249,810	19,207,959	49,297,928
Unobligated balance not available	6,633,062	1,890,688	6,868	293,378	135,898	8,959,894
Total status of budgetary resources	$ 65,917,761	$ 26,312,413	$ 24,394,775	$ 1,697,669	$ 57,321,674	$ 175,644,292

U.S. Department of Transportation
Required Supplementary Information
Combining Statements of Budgetary Resources By Major Account
For the Year Ended September 30, 2009
(Dollars in Thousands)

Change in Obligated Balances:	**Federal-Aid**	**FAA**	**FTA**	**MARAD**	**All Other**	**TOTAL**
Obligated balance, net:						
Unpaid obligations, brought forward, October 1	$ 48,973,366	8,904,431	18,025,560	369,343	5,652,680	$ 81,925,380
Uncollected customer payments from Federal sources, brought forward, October 1	(438,541)	(432,888)	(100,351)	(144,756)	(497,368)	(1,613,904)
Total unpaid obligated balance, net	48,534,825	8,471,543	17,925,209	224,587	5,155,312	80,311,476
Obligations incurred	40,098,600	22,714,270	15,441,303	1,154,481	37,977,817	117,386,471
Gross outlays	(36,440,893)	(21,553,160)	(11,370,605)	(1,061,789)	(18,578,212)	(89,004,659)
Unpaid obligations	-	-	-	-	25,000	25,000
Recoveries of prior year unpaid obligations, actual	-	(385,377)	(37,871)	(59,833)	(242,747)	(725,828)
Change in uncollected customer payments from Federal sources	(77,718)	(30,291)	15,601	(8,354)	(15,084)	(115,846)
Obligated balance, net, end of period:						
Unpaid obligations	52,631,073	9,680,164	22,058,387	402,202	24,834,538	109,606,364
Uncollected customer payments from Federal sources	(516,259)	(463,179)	(84,750)	(153,110)	(512,452)	(1,729,750)
Total unpaid obligated balance, net, end of period	$ 52,114,814	$ 9,216,985	$ 21,973,637	$ 249,092	$ 24,322,086	$ 107,876,614
Net Outlays:						
Net Outlays						
Gross Outlays	$ 36,440,893	$ 21,553,160	$ 11,370,605	$ 1,061,789	18,578,212	$ 89,004,659
Offsetting collections	(93,779)	(6,134,305)	(19,409)	(555,375)	(1,092,441)	(7,895,309)
Distributed offsetting receipts	-	(49,703)	(568)	(39,806)	(138,262)	(228,339)
Net outlays	$ 36,347,114	$ 15,369,152	$ 11,350,628	$ 466,608	$ 17,347,509	$ 80,881,011

REQUIRED SUPPLEMENTARY STEWARDSHIP INFORMATION

NON-FEDERAL PHYSICAL PROPERTY
ANNUAL STEWARDSHIP INFORMATION, September 30, 2010
TRANSPORTATION INVESTMENTS
(Dollars in thousands)

Surface Transportation:	**FY 2006**	**FY 2007**	**FY 2008**	**FY 2009**	**FY 2010**
Federal Highway Administration					
Federal Aid Highways (HTF)	$ 32,190,231	$ 32,800,748	$ 34,470,595	$ 37,618,049	$ 29,649,943
Other Highway Trust Fund Programs	452,022	366,672	481,762	136,002	155,061
General Fund Programs	14,240	51,119	31,740	3,228,008	11,616,036
Appalachian Development System	366,816	329,161	185,316	321,480	90,091
Federal Motor Carrier	117,004	196,967	144,455	837	-
Total Federal Highway Administration	33,140,313	33,744,667	35,313,868	41,304,376	41,511,131
Federal Transit Administration					
Discretionary Grants	$ 91,961	$ 11,719	$ 27,174	$ 16,424	$ 17,171
Formula Grants	3,376,068	2,086,876	1,329,811	743,604	428,696
Capital Investment Grants	3,073,294	2,662,845	2,473,141	2,175,758	1,930,185
Washington Metro Area Transit Authority	4,255	28,430	46	33	-
Interstate Transfer Grants	206	1,774	360	316	-
Formula and Bus Grants	1,862,772	4,193,989	5,968,651	7,264,278	7,345,804
Total Federal Transit Administration	8,408,556	8,985,633	9,799,183	10,200,413	9,721,856
Total Surface Transportation Nonfederal Physical Property Investments	$ 41,548,869	$ 42,730,300	$ 45,113,051	$ 51,504,789	$ 51,232,987

NON-FEDERAL PHYSICAL PROPERTY
ANNUAL STEWARDSHIP INFORMATION, September 30, 2010
TRANSPORTATION INVESTMENTS
(Dollars in thousands)

Air Transportation:	**FY 2006**	**FY 2007**	**FY 2008**	**FY 2009**	**FY 2010**
Federal Aviation Administration					
Airport Improvement Program	$ 3,852,141	$ 3,923,719	$ 3,753,840	$ 4,034,970	$ 4,015,463
Total Air Transportation Nonfederal Physical Property Investments	$ 3,852,141	$ 3,923,719	$ 3,753,840	$ 4,034,970	$ 4,015,463
Total Nonfederal Physical Property Investments	$ 45,401,010	$ 46,654,019	$ 48,866,891	$ 55,539,759	$ 55,248,450

The Federal Highway Administration reimburses States for construction costs on projects related to the Federal Highway System of roads. The main programs in which the States participate are the National Highway System, Interstate Systems, Surface Transportation, and Congestion Mitigation/Air Quality Improvement programs. The States' contribution is ten percent for the Interstate System and twenty percent for most other programs.

The Federal Transit Administration provides grants to State and local transit authorities and agencies.

Formula grants provide capital assistance to urban and nonurban areas and may be used for a wide variety of mass transit purposes, including planning, construction of facilities, and purchases of buses and railcars. Funding also includes providing transportation to meet the special needs of elderly individuals and individuals with disabilities.

Capital investment grants, which replaced discretionary grants in FY 1999, provide capital assistance to finance acquisition, construction, reconstruction, and improvement of facilities and equipment. Capital investment grants fund the categories of new starts, fixed guideway modernization, and bus and bus-related facilities.

The Washington Metropolitan Area Transit Authority provides funding to support the construction of the Washington Metrorail System.

Interstate Transfer Grants provided Federal financing from FY 1976 through FY 1995 to allow States and localities to fund transit capital projects substituted for previously withdrawn segments of the Interstate Highway System.

The Federal Aviation Administration (FAA) makes project grants for airport planning and development under the Airport Improvement Program (AIP) to maintain a safe and efficient nationwide system of public-use airports that meet both present and future needs of civil aeronautics. FAA works to improve the infrastructure of the nation's airports, in cooperation with airport authorities, local and State governments, and metropolitan planning authorities.

HUMAN CAPITAL INVESTMENT EXPENSES
ANNUAL STEWARDSHIP INFORMATION, September 30, 2010
(Dollars in thousands)

Surface Transportation:	**FY 2006**	**FY 2007**	**FY 2008**	**FY 2009**	**FY 2010**
Federal Highway Administration					
National Highway Institute Training	$ 14,123	$ 4,083	$ 1,205	$ 375	$ 109
Federal Motor Carrier Safety Administration					
California Highway Patrol	-	127	722		
Safety Grants	-	748	426	1,230	845
Idaho Video	-	-	302	399	9
Kentucky IT Conference	175	-	-	-	-
Massachusetts Training Academy	-	172	-	-	-
Minnesota Crash Investigation	1	-	-	-	-
New York Crash Reconstruction	-	36	180	-	-
Tennessee Crash Investigation	-	165	167	-	-
Federal Transit Administration					
National Transit Institute Training[(1)]	3,961	3,879	4,577	3,440	3,886
National Highway Safety Administration					
Section 403 Highway Safety Programs	221,523	235,382	162,038	143,639	138,221
Highway Traffic Safety Grants	279,244	416,241	485,721	566,790	565,787
Pipeline and Hazardous Materials Safety Administration					
Hazardous Materials (Hazmat) Training	7,800	7,798	13,263	13,263	13,153
Total Surface Transportation Human Capital Investments	526,827	668,631	668,601	729,136	722,010

Maritime Transportation:	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
Maritime Administration					
State Maritime Academies Training[1]	7,528	8,978	9,406	11,041	10,810
Additional Maritime Training	134	555	800	1,751	2,365
Total Maritime Transportation Human Capital Investments	7,662	9,533	10,206	12,792	13,175
Total Human Capital Investments	$ 534,489	$ 678,164	$ 678,807	$ 741,928	$ 735,185

The National Highway Institute develops and conducts various training courses for all aspects of Federal Highway Administration**.** Students are typically from the State and local police, State highway departments, public safety and motor vehicle employees, and U.S. citizens and foreign nationals engaged in highway work of interest to the Federal Government. Types of courses given and developed are modern developments, technique, management, planning, environmental factors, engineering, safety, construction, and maintenance.

The California Highway Patrol educates the trucking industry for the Federal Motor Carrier Safety Administration about Federal and State commercial motor vehicle/carrier inspection procedures, and to increase CMV driver awareness. The Idaho Video Program develops video training material utilized by the FMCSA National Training Center for the purpose of training State and Local law enforcement personnel. The Massachusetts Training Academy provides training to State law enforcement personnel located in the northeast region of Massachusetts. The Minnesota Crash Investigation program provides training and develops processes and protocols for commercial motor vehicle crash investigations.

The National Transit Institute of the Federal Transit Administration develops and offers training courses to improve transit planning and operations. Technology courses cover such topics as alternative fuels, turnkey project delivery systems, communications-based train controls, and integration of advanced technologies.

The National Highway Safety Administration's programs authorized under the Highway Trust Fund provide resources to State and Local governments, private partners, and the public, to effect changes in driving behavior on the nation's highways to increase safety belt usage and reduce impaired driving. NHTSA provides technical assistance to all states on the full range of components of the impaired driving system as well as conducting demonstrations, training and public information/education on safety belt usage.

The Pipeline and Hazardous Materials Safety Administration administers Hazardous Material Training (Hazmat). The purpose of Hazmat Training is to train State and local emergency personnel on the handling of hazardous materials in the event of a hazardous material spill or storage problem.

[1] Does not include funding for the Student Incentive Payment (SIP) program which produces graduates who are obligated to serve in a reserve component of the United States armed forces. Does not include funding for maintenance and repair (M&R).

RESEARCH AND DEVELOPMENT INVESTMENTS
ANNUAL STEWARDSHIP INFORMATION, September 30, 2010
(Dollars in thousands)

Surface Transportation:	**FY 2006**	**FY 2007**	**FY 2008**	**FY 2009**	**FY 2010**
Federal Highway Administration					
Intelligent Transportation Systems	$ 129,219	$ 152,799	$ 128,931	$ 111,219	$ 129,993
Other Applied Research and Development	105,336	74,942	63,906	28,259	159,389
Federal Railroad Administration					
Railroad Research and Development Program	$ 11,681	$ 5,551	$ 3,049	$ 3,349	$ 5,647
Federal Transit Administration					
Applied Research and Development					
Transit Planning and Research	$ 6,543	$ 3,144	$ 6,076	$ 6,914	$ 7,228
Pipeline and Hazardous Materials Safety Administration					
Applied Research and Development					
Development Research and Development Pipeline Safety					
Applied Research and Development Pipeline Safety	$ 12,953	$ 5,494	$ 12,762	$ 9,198	$ 7,362
Applied Research and Development Hazardous Materials	2,225	1,072	1,084	1,593	1,622
Research and Innovative Technology Administration					
Applied Research and Development					
Research and Technology	$ 1,110	$ 1,036	$ 1,036	$ 1,936	$ 10,737
Total Surface Transportation Research and Development Investments	$ 269,067	$ 244,038	$ 216,844	$ 162,468	$ 321,978

Air Transportation:	**FY 2006**	**FY 2007**	**FY 2008**	**FY 2009**	**FY 2010**
Federal Aviation Administration					
Research and Development Plant	$ 3,821	$ 4,217	$ 3,498	$ 3,381	$ 5,590
Applied Research	106,390	102,782	88,114	95,764	103,042
Development	587	844	814	1,102	2,008
Administration	30,566	32,050	33,519	35,055	36,723
Total Air Transportation Research and Development Investments	$ 141,364	$ 139,893	$ 125,945	$ 135,302	$ 147,363
Total Research and Development Investments	$ 410,431	$ 383,931	$ 342,789	$ 297,770	$ 469,341

The Federal Highway Administration's research and development programs are earmarks in the appropriations bills for the fiscal year. Typically these programs are related to safety, pavements, structures, and environment. Intelligent Transportation Systems were created to promote automated highways and vehicles to enhance the national highway system. The output is in accordance with the specifications within the appropriations act.

The Federal Transit Administration supports research and development in the following program areas:

Research and development in Transit Planning and Research supports two major areas: the National Research Program and the Transit Cooperative Research Program. The National Research Program funds the research and development of innovative transit technologies such as safety-enhancing commuter rail control systems, hybrid electric buses, and fuel cell and battery-powered propulsion systems. The Transit Cooperative Research Program focuses on issues significant to the transit industry with emphasis on local problem-solving research.

Transit University Transportation Centers, combined with funds from the Highway Trust Fund, provide continued support for research, education, and technology transfer.

Capital investment grants, which replaced discretionary grants in FY 1999, provide capital assistance to finance acquisition, construction, reconstruction, and improvement of facilities and equipment. Capital investment grants fund the categories of new starts, fixed guideway modernization, and bus and bus-related activities.

The Office of the Secretary's Office of Emergency Transportation is involved in research and development of mapping software for the Crisis Management Center, transportation policy, and outreach efforts.

The Pipeline and Hazardous Materials Safety Administration funds research and development activities for the following organizations and activities.

The Office of Pipeline Safety is involved in research and development in information systems, risk assessment, mapping, and non-destructive evaluation.

The Office of Hazardous Materials is involved in research, development, and analysis in regulation compliance, safety, and information systems.

The Research and Innovative Technology Administration's key mandate is to coordinate research across DOT to maximize and leverage the taxpayers' $1.2 billion annual investment in research, development and technology (RD&T) activities.

The Federal Aviation Administration (FAA) conducts research and provides the essential air traffic control infrastructure to meet increasing demands for higher levels of system safety, security, capacity, and efficiency. Research priorities include aircraft structures and materials; fire and cabin safety; crash injury-protection; explosive detection systems; improved ground and in-flight de-icing operations; better tools to predict and warn of weather hazards, turbulence and wake vortices; aviation medicine, and human factors.

Other Accompanying Information

SUMMARY OF FINANCIAL STATEMENT AUDIT AND MANAGEMENT ASSURANCES

Table 1. Summary of Financial Statement Audit

Summary of Financial Statement Audit						
Audit Opinion	Unqualified					
Restatement	No					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None	0					0
Total	0	0	0	0	0	0

Table 2. Summary of Management Assurances

Effectiveness of Internal Control over Financial Reporting (FMFIA, Section 2)						
Statement of Assurance	Unqualified					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Total Material Weaknesses	0					0

Effectiveness of Internal Control over Operations (FMFIA, Section 2)						
Statement of Assurance	Unqualified					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
FISMA Noncompliance	0	1				1
Total Material Weaknesses	0	1				1

Conformance with Financial Management System Requirements (FMFIA, Section 4)						
Statement of Assurance	Unqualified					
Non-Conformances	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Total Non-Conformances	0					0

Conformance with Federal Financial Management Improvement Act (FFMIA)		
	Agency	Auditor
Overall Substantial Compliance	Yes	Yes
1. System Requirements	Yes	Yes
2. Accounting Standards	Yes	Yes
3. USSGL at Transaction Level	Yes	Yes

INSPECTOR GENERAL'S FY 2011 TOP MANAGEMENT CHALLENGES

TOP MANAGEMENT CHALLENGES

Department of Transportation

Report Number: PT-2011-010

Date Issued: November 15, 2010

Memorandum

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

Subject: INFORMATION: DOT's Fiscal Year 2011 Top Management Challenges Department of Transportation Report Number PT-2011-010

Date: November 15, 2010

From: Calvin L. Scovel III
Inspector General

Reply to Attn. of: J-1

To: The Secretary
Deputy Secretary

As required by law, we have identified the Department of Transportation's (DOT) top management challenges for fiscal year 2011. The Nation's economy and the quality of life for all Americans rely heavily on a safe and vital transportation system. The Department spends approximately $79 billion annually on a wide range of programs and initiatives to meet this objective, and we continue to support its efforts through our audits and investigations.

Improving safety across all modes of transportation remains DOT's overarching goal. Significant challenges remain for policymakers as they seek to continue enhancing safety in the air and on the ground. This includes advancing new regulations for pilot training and rest requirements, strengthening the process for granting special permits and approvals for transporting hazardous materials, and ensuring pipeline operators identify and repair defects in oil and gas pipelines in a timely manner. Longstanding concerns that demand sustained attention include establishing realistic plans for the Next Generation Air Transportation System, securing viable financing for future surface transportation infrastructure investments, bolstering Federal oversight of transit safety, and addressing the Nation's aging surface infrastructure. At the same time, DOT must continue to improve contract management and safeguard its complex information and technology systems from cyber threats.

Budget constraints and uncertain financial markets exacerbate these challenges. With the passage of the American Recovery and Reinvestment Act of 2009 and the Consumer Assistance To Recycle and Save (CARS) Program, DOT was tasked with rapidly disbursing billions of dollars to thousands of transportation projects and to consumers who were encouraged to trade in their vehicles for new, more fuel-efficient

vehicles. Thus far, DOT has obligated almost $41 billion in Recovery Act funds. The commitment of the Secretary and his staff to the success of DOT's initiatives is evidenced by their response to our ARRA reports and advisories and the prompt implementation of the CARS Program.

We continue to build a body of work to assist DOT with its critical mission; improve the management and execution of programs; and protect its resources from fraud, waste, abuse, and violations of law. We considered several criteria in identifying the following nine challenges, including their impact on safety, documented vulnerabilities, large dollar implications, and DOT's ability to effect change in these areas:

- Ensuring Transparency and Accountability in the Department's Recovery Act Programs
- Maintaining Momentum in the Department's Oversight of Highway, Motor Vehicle, Hazardous Materials, and Transit Safety
- Maintaining Momentum in Addressing Human Factors and Improving Safety Oversight of the Aviation Industry
- Improving the Department's Oversight of Highway, Transit, and Pipeline Infrastructure
- Identifying Sufficient Funding Sources To Support Future Federal Investment in Surface Transportation Infrastructure
- Transforming the Federal Railroad Administration To Address Significantly Expanded Oversight Responsibilities
- Advancing the Next Generation Air Transportation System While Ensuring the Safe and Efficient Operation of the National Airspace System
- Implementing Processes To Improve the Department's Acquisitions and Contract Management
- Improving the Department's Cyber Security

Given the fiscal pressures facing the Federal Government, strong leadership and careful stewardship of taxpayer dollars are critical to successfully addressing DOT's top challenges. Trade-offs among diverse programs will likely be required, but there are important opportunities to minimize these trade-offs by setting priorities and establishing sound management policies, practices, and procedures.

We are committed to keeping decision makers informed of emerging and longstanding issues identified through our audits and investigations. We appreciate DOT's responsiveness to our findings and recommendations and the commitment to taking prompt corrective action.

This report and DOT's response will be included in the Department's Performance and Accountability Report, as required by law. DOT's response is included in its entirety in the appendix to this report.

If you have any questions regarding the issues presented in this report, please contact me at (202) 366-1959. You may also contact Lou E. Dixon, Principal Assistant Inspector General for Auditing and Evaluation, at (202) 366-1427.

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Table of Contents

CHAPTER 1

Ensuring Transparency and Accountability in the Department's Recovery Act Programs

Source: Federal Highway Administration

Since February 2009, the Department and its Operating Administrations have obligated nearly $40 billion American Recovery and Reinvestment Act (ARRA) funds for more than 14,600 highway, bridge, transit, shipyard, airport, and rail projects across the Nation. In February 2010, the Office of the Secretary of Transportation (OST) awarded Transportation Investment Generating Economic Recovery (TIGER) discretionary grants to 51 recipients for multimodal surface transportation projects. Now the Department and its Operating Administrations will need to address a number of challenges associated with ensuring those funds are spent effectively.

Key Challenges

- Overseeing ARRA projects and expenditures
- Executing OST's TIGER discretionary grants program
- Collecting quality data from award recipients

CHAPTER 1

Ensuring Transparency and Accountability in the Department's Recovery Act Programs

Overseeing ARRA Projects and Expenditures The Department must ensure adequate oversight and accountability to meet ARRA goals. Our June ARRA Advisory reported that the Federal Highway Administration (FHWA) did not ensure states conducted federally required "value engineering" studies[1] on highway and bridge projects prior to contract award. Further, the Government Accountability Office (GAO) recently reported that staffing shortages may limit states' ability to properly implement and manage ARRA programs.[2] With limited staff, it is critical that the Department identify high-risk areas and target its resources accordingly. Additionally, the Office of Management and Budget (OMB) directed agencies to use single audit reports to identify high-risk grantees, ensure resolution of audit findings, and consider additional monitoring and inspections of these grantees.[3] This is consistent with our August 2009 ARRA Advisory that proposed to FAA that it enhance its risk-based approach to ensuring new ARRA grant recipients, that historically have not administered funds effectively, receive increased oversight. FHWA's national review teams (NRT) also have the potential to enhance oversight of ARRA funds. Through NRT assessments of state ARRA management processes and compliance with Federal requirements, FHWA aims to identify problems needing corrective action as well as national trends and potential new risks. However, FHWA needs to follow through and implement the corrective actions identified by the NRTs to effectively use this new oversight tool. Finally, vigilant oversight is needed to ensure that ARRA recipients meet ARRA's goal to complete projects within 3 years because nearly 2 years after ARRA was enacted, a significant number of projects have yet to begin, including approximately 1,400 highway projects.

Management attention is also needed to protect ARRA funds from fraud, waste, and abuse. As of September 2010, we have 50 criminal investigations open for alleged crimes such as false statements, false claims, prevailing wage violations, disadvantaged business enterprise (DBE) fraud, and bid rigging. DBE fraud accounts for more than 30 percent of our ARRA-related investigations, compared to 10 percent for our non-ARRA investigations. Underbidding on ARRA-funded transportation projects is also a concern. Many winning bids are 20 to 30 percent below engineer's estimate, increasing the risk that some contractors

[1] Value engineering studies are objective reviews of reasonable design alternatives. Bridges and highways with costs equal to or above $20 million and $25 million, respectively, are required to have value engineering studies.

[2] GAO, *State and Local Governments: Fiscal Pressures Could Have Implications for Future Delivery of Intergovernmental Programs*, GAO-10-899, July 2010.

[3] OMB Memorandum, "Updated Guidance on the American Recovery and Reinvestment Act," March 22, 2010.

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may attempt to make up the difference by submitting false claims or committing another form of fraud.

Executing OST's TIGER Discretionary Grants Program In February 2010, OST awarded $1.5 billion in TIGER discretionary grants to 51 recipients for multimodal surface transportation projects. As OST moves from grant selection and award into TIGER program execution, it must provide the enhanced oversight that ARRA and OMB require. Yet, OST does not have direct experience administering grant programs and overseeing capital investments in surface transportation infrastructure. OST is leveraging oversight expertise within the Department by delegating grant oversight to the Operating Administrations. However, OST must provide stewardship by clearly defining its role and oversight strategy—including the levels of authority and accountability it will retain—and allocate adequate resources and expertise to ensure that TIGER program goals are achieved and ARRA funds are spent wisely.

Collecting Quality Data From Award Recipients On behalf of the Recovery Accountability and Transparency Board, we assessed the Department's and six other agencies' oversight of ARRA recipient data. Each agency identified inaccuracies in recipient data in significant areas, including award type, date, and amount or the number of jobs created. Several factors contributed to these errors, including misinterpretation of guidance and technical challenges. While surveyed agencies have taken steps to address these problems, continued vigilance will be needed to meet the level of accountability called for in ARRA.

Related Products The following related reports and testimonies can be found on the OIG website at http://www.oig.dot.gov.

- Letter to Ranking Member Issa on DOT's Use of ARRA Signage, August 17, 2010
- ARRA Advisory: FAA's Process for Awarding ARRA Airport Improvement Program Grants, August 6, 2009
- ARRA Advisory: FHWA's Oversight of the Use of Value Engineering Studies on ARRA Highway and Bridge Projects, June 28, 2010

CHAPTER 1

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- Federal Railroad Administration Faces Challenges in Carrying Out Expanded Role, April 29, 2010
- Weaknesses in DOT's Suspension and Debarment Program Limit Its Protection of Government Funds, March 18, 2010
- Recovery Act Data Quality: Errors in Recipients' Reports Obscure Transparency, February 23, 2010
- Letter to Senator Mark Pryor on DOT OIG's Recovery Act Oversight Activities, February 19, 2010
- Final Report on DOT's Suspension and Debarment Program, January 7, 2010
- Final Report on DOT's Implementation of the American Recovery and Reinvestment Act: Continued Management Attention Is Needed To Address Oversight Vulnerabilities, November 30, 2009

For more information on the issues identified in this chapter, please contact Madeline Chulumovich, Chief of Staff, at (202) 366-1959 or Joseph W. Comé, Assistant Inspector General for Highway and Transit Audits, at (202)-366-5630.

CHAPTER 2

Maintaining Momentum in the Department's Oversight of Highway, Motor Vehicle, Hazardous Materials, and Transit Safety

Source: Julie Nixon, John A. Volpe National Transportation Systems Center

Over the last 5 years, fatalities and injuries related to motor vehicle crashes declined by 22.3 percent and 18.5 percent, respectively. This decline is noteworthy; now, the Department must tackle persistent challenges to maintain this trend and address longstanding concerns with vehicle, motor carrier, pipeline, and transit safety concerns.

Key Challenges

- Addressing motor vehicle safety defects
- Strengthening motor carrier enforcement programs and commercial driver's license (CDL) standards
- Strengthening the Pipeline and Hazardous Materials Safety Administration's (PHMSA) special permits and approvals program to achieve its safety mission
- Addressing potential issues if Congress enhances Federal oversight authority for transit safety

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Addressing Motor Vehicle Safety Defects The National Highway Traffic Safety Administration (NHTSA) conducts tests, inspections, and investigations to identify motor vehicles and equipment that contain safety-related defects and ensure the public is notified so defects can be corrected. In 2002 and 2004, we reported that NHTSA had weaknesses in its defect investigation systems and processes, including a lack of reliable early warning reporting information.[4] In response, NHTSA revised its defect assessment processes and established an Early Warning Division to analyze manufacturer data for identifying potential safety-related defects.

In 2010, NHTSA's defects investigation program came under increased media and congressional scrutiny due to complaints of sudden unintended acceleration and crashes involving Toyota Motor Corporation vehicles. For example, in August 2009, a Lexus sped out of control and crashed, killing its driver and three passengers. NHTSA's investigations of the complaints resulted in 3 Toyota recalls, affecting 8 million vehicles. NHTSA also enlisted the National Aeronautics and Space Administration and the National Academy of Sciences to investigate the sudden unintended acceleration issue. We are currently determining whether there are lessons learned from Toyota recalls as well as any improvements needed in NHTSA's processes, procedures, and recourses for investigating safety defects. This work is based in part on a request from the Secretary of Transportation and Members of Congress.

Strengthening Motor Carrier Enforcement Programs and CDL Standards From 2008 to 2009, the number of fatalities related to crashes involving large trucks or buses dropped by 20 percent.[5] To ensure this trend continues, the Federal Motor Carrier Safety Administration (FMCSA) must follow through on previous commitments, maintain its efforts to enforce safety regulations, and remove motor carriers and drivers who do not comply. FMCSA has begun several initiatives to ensure new and existing operators in the motor carrier industry operate safely. For example, the Agency implemented a more stringent safety assurance process that new entrants must complete before receiving permanent operating authority as well as a new vetting process for passenger and household goods carriers to prevent unsafe carriers from continuing operations under a

[4] OIG Report Number MH-2002-071, "Review of the Office of Defects Investigation, National Highway Traffic Safety Administration," January 3, 2002, and OIG Report Number MH-2004-088, "Report on Follow-Up Audit of the National Highway Traffic Safety Administration's Office of Defects Investigation," September 23, 2004.

[5] Motor Carrier Safety Progress Report, Federal Motor Carrier Safety Administration, as of June 30, 2010.

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new identity. FMCSA still needs to expand this vetting process to all new entrant applicants in the motor carrier industry. In 2011, FMCSA plans to fully implement its Comprehensive Safety Analysis 2010 (CSA 2010) model, which is designed to identify high-risk carriers with safety issues that could reasonably lead to crashes. CSA 2010 will rely heavily on crash, inspection, and census data.

While FMCSA has made progress in improving crash and inspection data, it has yet to implement a longstanding Office of Inspector General recommendation to improve carrier census data reporting,[6] which would improve its ability to rank the safety performance of motor carriers and target inspection and enforcement activities. Other areas that require action include improving knowledge and skills testing standards for CDLs, new minimum standards for states to issue commercial drivers' permits, and CDL fraud prevention efforts. Delays in implementing these recommendations are largely due to the complexity of coordinating with states and other stakeholders. Taking timely action to implement fraud prevention efforts is especially important as Office of Inspector General investigations have uncovered various schemes by individuals to circumvent FMCSA standards for issuing commercial drivers' licenses. For example, a Louisiana-registered third-party CDL tester admitted that he conspired and fraudulently conducted approximately 250 CDL skills tests for $200 per test. The tester was sentenced to 5 years probation and ordered to make restitution of over $7,300. Additionally, the Louisiana Department of Public Safety, Office of Motor Vehicles recalled and retested all CDL drivers tested by this individual.

Going forward, the Department must complete ongoing efforts and resolve issues related to finalizing CDL standards to improve the safety of the motor carrier industry operating large trucks and buses on our Nation's highways.

[6] Census data are to be provided by motor carriers on the number of drivers they employ and commercial vehicles (power units) they own or lease.

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Strengthening PHMSA's Special Permits and Approvals Program To Achieve Its Safety Mission PHMSA regulates up to 1 million movements of hazardous materials a day. Many of these materials are transported under special permits and approvals that allow relief from the Hazardous Materials Regulations under certain conditions.[7] Our work has pointed to longstanding concerns about PHMSA's process for assessing risks and granting special permits and approvals as well as its fundamental operating procedures for promoting the safe movement of hazardous materials. In 1 case, PHMSA granted a special permit to a company that had 53 incidents within 10 years—12 of which were serious—and 22 violations issued by PHMSA's or FMCSA's enforcement office. Also of concern is PHMSA's practice of granting special permits to trade associations—effectively giving "blanket authorization" to thousands of member companies without any assessment of their safety histories or need for the permit.

PHMSA has established action plans to address the safety concerns we identified. To successfully implement these plans, PHMSA must proactively identify safety risks, work with partner safety agencies to resolve safety and operational matters, and set targeted oversight priorities.

Addressing Potential Issues if Congress Enhances Federal Oversight Authority for Transit Safety In 2009, 3 rail-to-rail crashes in different cities killed 9 people and injured 159 others; in separate incidents, 3 transit employees were killed while working on rail tracks. While transit remains a relatively safe mode of travel, these recent rail incidents brought renewed attention to transit safety.

In December 2009, the Department proposed legislation that would shift its role from providing guidance for state-managed oversight programs to directly overseeing transit safety. An enhanced Federal role may create significant challenges for the Department, including (1) collecting data necessary to conduct effective transit safety oversight, (2) establishing standards to improve transit safety among a diverse set of systems across the country, and (3) conducting enhanced transit safety oversight and enforcement. The Secretary has established the Transit Rail Advisory Committee for Safety (TRACS)—a Federal

[7] *Special permits* authorize a holder to vary from specific provisions of the Hazardous Materials Regulations; identify the section(s) from which relief is provided; and include provisions, conditions, and terms that must be followed in order for the special permit to be valid. An *approval* means written consent from PHMSA's Associate Administrator to perform a function that requires prior consent under the Hazardous Materials Regulations.

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advisory committee comprised of rail safety experts from transit agencies, state safety oversight agencies, labor unions, and other key constituencies—which could provide an important forum for addressing the challenges associated with enhanced oversight.

Related Products The following related reports and testimonies can be found on the OIG website at http://www.oig.dot.gov.

- Actions Taken and Needed To Improve Management and Oversight of PHMSA's Hazardous Materials Special Permits and Approvals Program, April 22, 2010
- New Approaches Needed in Managing PHMSA's Special Permits and Approvals Program, March 4, 2010
- PHMSA's Process for Granting Special Permits and Approvals for Transporting Hazardous Materials Raises Safety Concerns, September 10, 2009
- Audit of the Data Integrity of the Commercial Driver's License Information System, July 30, 2009
- Use of Income Derived from the Commercial Driver's License Information System for Modernization, July 10, 2008
- Best Practices for Improving Oversight of State Highway Safety Programs, March 25, 2008
- Effectiveness of Federal Drunk Driving Programs, October 25, 2007
- Audit of the National Highway Traffic Safety Administration's Alcohol-Impaired Driving Traffic Safety Program, March 5, 2007
- Follow-Up Audit on National Highway Traffic Safety Administration's Office of Defects Investigation, September 23, 2004
- Review of the National Highway Traffic Safety Administration's Office of Defects Investigation, January 3, 2002

For more information on the issues identified in this chapter, please contact Joseph W. Comé, Assistant Inspector General for Highway and Transit Audits, at (202) 366-5630 or Jeffrey B. Guzzetti, Assistant Inspector General for Aviation and Special Program Audits, at (202) 366-0500.

CHAPTER 3

Maintaining Momentum in Addressing Human Factors and Improving Safety Oversight of the Aviation Industry

The aviation industry continues to experience one of the safest periods in its history due to both Federal Aviation Administration (FAA) and industry efforts to advance safety. However, the crash of Colgan Air flight 3407 in February 2009 confirmed the need for constant vigilance.

Key Challenges

- Advancing industry and Government efforts to address pilot training and fatigue issues
- Enhancing risk-based oversight of Part 121 air carriers[8] and foreign and domestic repair stations
- Ensuring FAA provides effective oversight of mainline and regional air carriers operating under domestic code share agreements

[8] 14 CFR Part 121 governs the operations of large, scheduled commercial passenger and cargo carriers.

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Advancing Industry and Government Efforts To Address Pilot Training and Fatigue Issues According to the National Transportation Safety Board (NTSB), pilot fatigue has been associated with air carrier accidents resulting in 250 fatalities over the last 16 years. Although NTSB has identified this issue as an area of concern for all air carriers, it is particularly critical for regional carriers. NTSB has cited pilot performance and fatigue as findings in four of the last six fatal accidents involving regional carriers, including the fatal crash of Colgan Air flight 3407 in February 2009. Under the FAA Administrator's leadership, FAA took swift action by creating the Call to Action plan to refocus and accelerate air carriers' safety efforts. The plan consists of 10 short- and mid-term initiatives to enhance pilot performance and training, increase air carrier participation in voluntary safety programs, and expand pilot records review. FAA also set goals to develop new safety oversight guidance for its inspectors, conduct regional safety forums, develop programs addressing pilot professionalism, and establish new rules on pilot fatigue and training.

FAA has issued two Notices of Proposed Rule Making to address pilot fatigue and training. The first rule would require airlines to enhance FAA-required pilot training programs, including training on hazards, such as loss of control, and recovery from approach to stalls. The rule also calls for enhanced training for flight attendants and dispatchers. The second proposed rule would require a single set of scientifically based flight, duty, and rest requirements for all Part 121 carriers. However, this proposed rule does not address NTSB's recommendation to require air carriers to address fatigue risks associated with pilot commuting—a key finding NTSB identified in its investigation into the Colgan accident. Maintaining positive momentum on these rulemakings will be an important watch item for the Department, industry, and Congress.

Enhancing Risk-Based Oversight of Part 121 Air Carriers and Foreign and Domestic Repair Stations FAA has made noteworthy progress in improving safety oversight, such as clarifying guidance for inspectors who monitor air carriers. However, we continue to find weaknesses in FAA's Air Transportation Oversight System (ATOS)—a systematic approach for identifying high-risk safety areas and targeting inspections to those areas. Specifically, FAA's oversight of ATOS inspections has been ineffective at the national level, in large part because FAA does not track unassigned inspections or fully use collected inspection data.

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At the same time, we have repeatedly highlighted weaknesses since 2003 in FAA's oversight of aircraft maintenance and called for safety enhancements. While FAA has made a number of procedural changes to improve its oversight of repair stations, it has not addressed our most significant and longstanding recommendations to identify facilities performing safety-critical repairs and target its surveillance accordingly. Given air carriers' increasing reliance on repair stations, it is imperative that FAA provide more rigorous oversight of this industry.

Ensuring FAA Provides Effective Oversight of Mainline and Regional Air Carriers Operating Under Domestic Code Share Agreements Mainline and regional air carriers have increasingly turned to domestic code share agreements—a marketing arrangement in which one air carrier sells and issues tickets for the flight of another carrier as if it were operating the flight itself. Through these arrangements, passengers receive lower fares and more seamless air travel, regional carriers benefit from joint promotion and advertising, and mainline carriers gain access to additional and smaller aircraft with no ownership stake for bringing passengers to their hub.

Domestic code share agreements are an integral part of the aviation system. While they can help mainline and regional carriers expand their markets and increase revenue, they also present challenges. For example, we have identified differences between the hiring, training, professionalism, and safety programs of most regional and mainline carriers. While FAA initiated a Call to Action for airline safety to encourage mainline and regional carriers to reconcile these differences, progress has been mixed. FAA and the Department must make oversight of the operators involved in these arrangements a top priority to ensure the safety of passengers who depend on those flights. This is particularly critical given that since 2003, seven commercial airline accidents have involved regional air carriers.

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Maintaining Momentum in Addressing Human Factors and Improving Safety Oversight of the Aviation Industry

Related Products The following related reports and testimonies can be found on the OIG website at http://www.oig.dot.gov.

- FAA's Process for Reviewing Air Transportation Oversight System (ATOS) Inspection Data, March 19, 2010
- Progress and Challenges with FAA's Call to Action for Airline Safety, February 4, 2010
- Letter to Senator Claire McCaskill Regarding FAA's Progress in Implementing Past OIG Recommendations To Improve Oversight of Outsourced Maintenance, January 11, 2010
- The Federal Aviation Administration's Role in Safety Oversight of Air Carriers, June 10, 2009
- Review of FAA's Oversight of Airlines and Use of Regulatory Partnership Programs, June 30, 2008

For more information on the issues identified in this chapter, please contact Jeffrey B. Guzzetti, Assistant Inspector General for Aviation and Special Program Audits, at (202) 366-0500.

CHAPTER 4

Improving the Department's Oversight of Highway, Transit, and Pipeline Infrastructure

Source: U.S. Department of Transportation

The Department faces significant challenges in overseeing highway, transit, and pipeline infrastructures, especially given current fiscal constraints. According to the American Society of Civil Engineers, $186 billion is needed each year to substantially improve the Nation's roads that are in poor or mediocre condition—well above the $70 billion spent annually on highway improvements.[9] At the same time, the Department projects shortfalls in the Highway Trust Fund, which provides most of the funding for highway and transit programs.[10] Recent gas pipeline ruptures also point to a need for program improvements to identify and repair defective pipes and ensure public safety.

Key Challenges

- Tracking and monitoring states' and localities' use of Federal funds
- Ensuring infrastructure safety and protecting federally funded highway and transit projects from fraud
- Ensuring pipeline operators identify and repair defects in oil and gas pipelines in a timely manner

[9] American Society of Civil Engineers, "2009 Report Card for America's Infrastructure," 2009.
[10] See chapter 5 for a discussion of Highway Trust Fund issues.

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Tracking and Monitoring States' and Localities' Use of Federal Funds

With the Nation's highway and transit infrastructure needs increasing faster than funding resources, the Department must maximize the return on its surface transportation investments. The Federal Highway Administration's (FHWA) Fiscal Management Information System (FMIS) lacks sufficient detail on states' use of Highway Bridge Program (HBP) funds.[11] For example, Michigan used almost $3 million in HBP funds on a project that involved multiple bridges, but FHWA could not use FMIS to determine how much Federal funding went toward improving the condition of the project's structurally deficient bridges. Expanding FMIS's capabilities would allow FHWA to better assess the effectiveness of current programs and enable it to stretch every available infrastructure dollar.

The Department's large portfolio of transit infrastructure projects also demands rigorous oversight to ensure projects stay on schedule and within budget. While the Federal Transit Administration (FTA) has required sponsors of major projects to develop project management, project execution, and financial plans, it has not always fully used these plans to monitor project progress. For example, FTA approved an early systems work agreement last year to expedite the Access to the Region's Core (ARC) project[12] in New York and New Jersey, and awarded $130 million in ARRA funds for project activities. However, FTA had not received a final project management plan, project execution sub-plans, a master schedule, or a financial plan that described strategies for mitigating risks. The lack of finalized plans has hindered FTA's oversight of the project sponsor's efforts to mitigate risks that could increase costs or cause schedule delays.

Ensuring Infrastructure Safety and Protecting Federally Funded Highway and Transit Projects From Fraud The 2007 bridge collapse in Minnesota highlighted the need for FHWA to focus on the safety of the Nation's surface transportation infrastructure. According to FHWA, about one-quarter of the Nation's more than 600,000 bridges have major deterioration, cracks in their structural components, or other deficiencies.[13] Our work has identified weaknesses in FHWA's enforcement of National Bridge Inspection Standards and called for sustained management attention to ensure that planned improvements in the

[11] HBP is the primary Federal program that funds the replacement and rehabilitation of bridges nationwide.
[12] ARC involves the construction of a 9-mile commuter rail line between Secaucus, New Jersey, and Manhattan, New York. It includes construction of two tunnels under the Hudson River. The estimated cost is $9.23 billion.
[13] This estimate is based on 2009 data.

inspection oversight program are implemented. Given the potentially catastrophic risks of not properly inspecting bridges, FHWA must determine with greater consistency whether states complied with the National Bridge Inspection Standards and define procedural steps for enforcing compliance.

Enhanced FHWA oversight is also needed for new highway projects to ensure they comply with all relevant standards and requirements. After the Central Artery/Tunnel (CA/T) Project in Boston was declared substantially complete in January 2006, 26 tons of improperly secured concrete ceiling panels fell in one of the project's tunnels and killed a motorist in July of that year. While the Commonwealth of Massachusetts initiated a "Stem to Stern" safety review that included the CA/T Project, FHWA did not always follow its protocols for conducting independent field verifications to assess the Commonwealth's progress in resolving safety risks.

With the number of highway and transit projects receiving Federal assistance, it is imperative that the Department and Operating Administrations aggressively combat fraud, waste, and abuse. Fraud awareness education and vigilant oversight are needed to identify and prevent common fraud schemes, such as bid rigging, price fixing, product substitution, bribery and kickbacks, conflicts of interest, false statements and false claims, labor and materials overbilling, and disadvantaged business enterprise fraud. Of particular concern are schemes that compromise safety. For example, a Utah corporation specializing in the installation of highway safety devices was sentenced to 36 months of probation, ordered to pay a fine of $10,000, and $31,485.45 in restitution for falsifying certificates of compliance related to the installation of highway crash cushions of a FHWA-funded project. The company admitted to submitting false certificates even though it knew that the installation of these devices did not meet contract specifications.

Ensuring Pipeline Operators Identify and Repair Defects in Oil and Gas Pipelines in a Timely Manner The Nation's aging oil and gas pipelines are vulnerable to ruptures caused by corrosion and pipe defects. Federal regulations require pipeline operators to maintain integrity management programs, which are regulated and inspected by the Pipeline and Hazardous Materials Safety Administration (PHMSA) or its state partners. However, recent pipeline ruptures—including the explosion of a 54-year old gas pipeline in California that killed 8 people and destroyed 37 homes—call into question the effectiveness of operator programs as well as Federal and state oversight. For example, in

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July 2010, a 41-year-old Enbridge Energy interstate pipeline in Michigan leaked more than 800,000 gallons of oil. Although the company had reported nearly 330 integrity threats (including defects) on this pipeline segment, Enbridge's remediation plan requested a 30-month extension to complete needed repairs. However, the rupture occurred before PHMSA responded to this request. Going forward, PHMSA and its state partners need to closely scrutinize pipeline operator integrity management programs to ensure that defects are identified and repaired before catastrophic ruptures occur.

Related Products The following related reports and testimonies can be found on the OIG website at http://www.oig.dot.gov.

- Actions Needed To Mitigate Risks Associated with the Access to the Region's Core Project, May 17, 2010
- The Commonwealth of Massachusetts's Safety Review of the Central Artery/Tunnel Project Was Comprehensive, but FHWA's Oversight Approach Has Shortcomings, April 20, 2010
- Assessment of FHWA Oversight of the Highway Bridge Program and the National Bridge Inspection Program, January 14, 2010
- DOT's Implementation of the American Recovery and Reinvestment Act: Continued Management Attention Is Needed To Address Oversight Vulnerabilities, November 30, 2009

For more information on the issues identified in this chapter, please contact Joseph W. Comé, Assistant Inspector General for Highway and Transit Audits, at (202) 366-5630 or Jeffrey B. Guzzetti, Assistant Inspector General for Aviation and Special Program Audits, at (202) 366-0500.

CHAPTER 5

Identifying Sufficient Funding Sources To Support Future Federal Investment in Surface Transportation Infrastructure

Source: Federal Highway Administration

The Department has worked with Congress to maintain the Highway Trust Fund's (HTF) solvency, but the current short-term fixes are unsustainable and make future cash shortfalls inevitable. The Safe, Accountable, Flexible, Efficient, Transportation Equity Act: A Legacy for Users (SAFETEA-LU) of 2005—the most recent surface transportation authorization act—was due to expire at the end of fiscal year 2009 but continues to operate under a series of short-term extensions. Most recently, the Hiring Incentives To Restore Employment Act extended SAFETEA-LU through December 2010 and transferred $19.5 billion from the General Fund to preempt foreseeable cash shortfalls in the HTF.

Key Challenges

- Replacing short-term fixes for HTF solvency with long-term solutions
- Achieving consensus among stakeholders on Federal infrastructure needs, spending levels, and a funding framework for the next surface transportation reauthorization

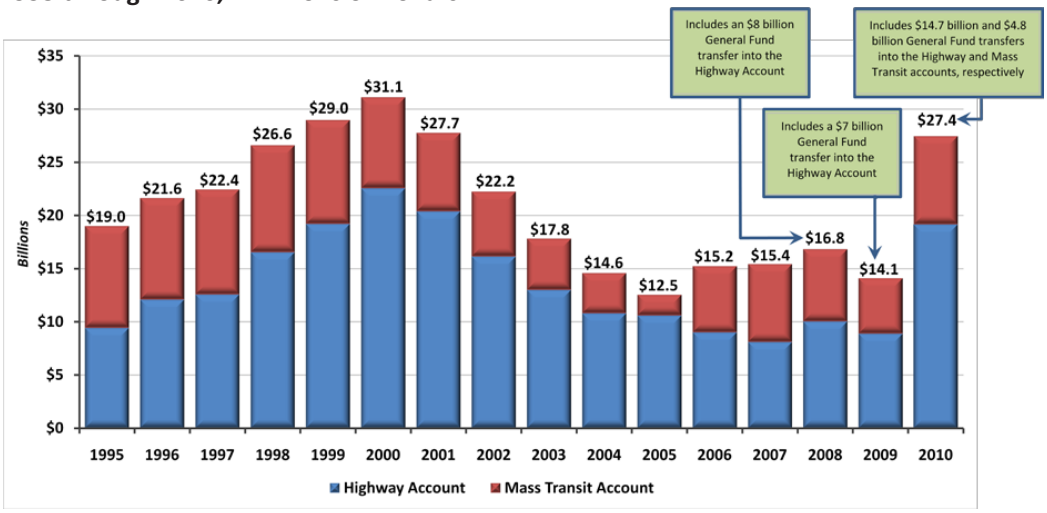
CHAPTER 5

Identifying Sufficient Funding Sources To Support Future Federal Investment in Surface Transportation Infrastructure

Replacing Short-Term Fixes for HTF Solvency With Long-Term Solutions

Historically, cash receipts into HTF's Highway and Mass Transit Accounts exceeded outlays, leading to a surplus that peaked at $31.1 billion at the end of fiscal year 2000 (see figure 5.1). However, with the enactment of the Transportation Equity Act for the 21st Century (TEA-21) in 1998, outlays began to outpace receipts, eroding the surplus. SAFETEA-LU further eroded the surplus by increasing contract authority over TEA-21 levels without an associated increase in funding. High fuel prices and a lagging economy resulted in an unforeseen decline in vehicle miles travelled (VMT) and a more rapid decline in the Highway Account balance than anticipated. Prior to receiving the $4.8 billion cash infusion into the Mass Transit Account earlier this year, the Federal Transit Administration projected that the account would experience a shortfall in fiscal year 2011.

Figure 5.1. Historical Cash Balances in Highway and Mass Transit Accounts, Fiscal Years 1995 through 2010, in Billions of Dollars



Source: Federal Highway Administration, Federal Transit Administration
Note: In 1999, $8 billion was transferred from the Highway Account to the General Fund. Fiscal year 2010 amounts are preliminary and subject to adjustment.

Without cash infusions from the General Fund, the Federal Highway Administration would have been forced to reduce or suspend disbursements to states for eligible surface transportation expenses.

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Achieving Consensus Among Stakeholders on Federal Infrastructure Needs, Spending Levels, and a Funding Framework for the Next Surface Transportation Reauthorization Citing the critical role surface transportation infrastructure plays in the Nation's quality of life and economic productivity, the House Transportation and Infrastructure Committee unveiled legislation in June 2009 that proposed $500 billion in funding to support state surface transportation programs over 6 years. This proposed spending level is significantly higher than the $244 billion authorized by SAFETEA-LU over a 5-year period. Of this amount, $450 billion is proposed for highway, public transportation, and safety programs and $50 billion for high speed rail.

The Administration recently issued its framework for the next surface transportation authorization bill. The plan envisions 150,000 miles of roads rebuilt, 4,000 miles of rail constructed and maintained, and 150 miles of runway rehabilitated or reconstructed over the next 6 years. However, the Department has yet to define the spending levels needed to meet the Nation's surface transportation infrastructure requirements.

Yet, the current funding mechanism—which relies heavily on excise taxes on fuel and the sales of trucks and tires—does not generate the cash receipts needed to meet current outlays, let alone the larger outlays proposed in the next authorization. Further, given the current economic environment, the Administration opposes an increase in fuel tax rates or the establishment of a VMT-based fee, both of which Congress has discussed as methods of increasing the HTF's cash receipts. The next authorization must establish a funding framework that aligns proposed spending levels with the HTF's cash receipts. Without this alignment, the HTF will continue to experience shortfalls and risk reducing state and local investments in surface transportation infrastructure projects.

The solution to ending the HTF's funding gap is neither obvious nor imminent. As the Department and congressional and other stakeholders evaluate alternative funding mechanisms and enact the next surface transportation authorization, the Department must also work with Congress to ensure the HTF is adequately funded during any extensions of SAFETEA-LU. Failure to do so could significantly impact the solvency of the Highway and Mass Transit Accounts and their ability to continue reimbursements to states and transit authorities for eligible highway and transit expenses.

CHAPTER 5

Identifying Sufficient Funding Sources To Support Future Federal Investment in Surface Transportation Infrastructure

Related Products The following related reports and testimonies can be found on the OIG website at http://www.oig.dot.gov.

- Letter to Senate Budget Committee Ranking Member Gregg Regarding DOT's Projections of Highway Trust Fund Solvency, June 24, 2009
- Growth in Highway Construction and Maintenance Costs, September 26, 2007

For more information on the issues identified in this chapter, please contact Mitch Behm, Assistant Inspector General for Rail, Maritime, and Economic Analysis, at (202)-366-9970.

CHAPTER 6

Transforming the Federal Railroad Administration To Address Significantly Expanded Oversight Responsibilities

Source: Federal Railroad Administration

The 2008 Railroad Safety Improvement Act (RSIA) and Passenger Railroad Investment and Improvement Act (PRIIA)—two of the most comprehensive pieces of railroad legislation in 30 years—dramatically realigned and expanded the Federal Railroad Administration's (FRA) roles and responsibilities. In addition, the American Recovery and Reinvestment Act (ARRA) infused an unprecedented amount of new capital into these new passenger rail programs and drastically accelerated timeframes for implementation.

Key Challenges

- Providing sufficient oversight of the implementation and management of the High Speed Intercity Passenger Rail (HSIPR) Program
- Addressing new PRIIA requirements to enhance passenger rail
- Ensuring the safe and secure movement of people and goods while undertaking increased passenger rail responsibilities
- Balancing an increased and diversified workload with the continuing need to oversee Amtrak operations

CHAPTER 6

Transforming the Federal Railroad Administration To Address Significantly Expanded Oversight Responsibilities

Providing Sufficient Oversight of the Implementation and Management of the HSIPR Program Historically, FRA's responsibilities have focused on promoting and overseeing railroad safety and providing grants and loans. The new HSIPR program—authorized under PRIIA—greatly expanded the Agency's responsibilities to include distributing $10.5 billion in grants for passenger rail-related projects in a compressed timeframe. To manage its expanded grants solicitation and award process, FRA requested and received 27 additional staff resources in its fiscal year 2010 budget. The Agency also requested 31 staff positions to support its additional requirements in fiscal year 2011. Although FRA has not fully positioned itself to address the challenges it faces with implementing the HSIPR program, it has moved forward with soliciting, accepting, and awarding grants for states' high-speed rail projects.

Securing these grants could be a significant challenge for states. According to FRA interim guidance, funding will not be disbursed until states finalize agreements with freight railroads that specify the passenger rail service improvements the projects are designed to achieve. The freight railroads have, however, voiced concerns about certain service outcome requirements in these agreements; specifically, that the requirements would be unduly burdensome to their operations. Chief among these service outcome requirements are rigid on-time performance metrics that require the freight railroad to incur any and all expenses necessary to ensure the passenger rail service operating on the freight tracks runs according to schedule.

Addressing New PRIIA Requirements To Enhance Passenger Rail PRIIA tasked FRA with numerous other responsibilities, including initiatives to improve or establish intercity passenger rail service; design a long-range national rail plan that promotes an integrated, efficient, and optimized national rail system; and develop metrics for passenger rail service quality. These responsibilities require FRA to perform a variety of tasks and coordinate with a number of public and private entities. For example, in developing a national rail plan, FRA must work with the rail industry and other stakeholders to address interconnectivity with other modes of transportation, identify rail projects of national significance, and consider sustainable funding options. To develop the final metrics for assessing passenger rail service quality, FRA teamed with rail industry entities, including Amtrak management and labor, the Surface Transportation Board, the freight railroads, state rail departments, and non-profit rail passenger organizations. Yet, to ensure railroads adhere to these metrics, which were effective beginning May 2010, FRA must collaborate

with passenger rail service providers to identify a standardized mechanism for collecting and reporting train performance data.

All of these new tasks and requirements must be balanced against FRA's traditional responsibilities to administer its existing grant and loan programs: the Rail Line Relocation discretionary grant program, the Railroad Rehabilitation and Improvement Financing loan program, and the Amtrak grant program. These programs alone accounted for 37 percent of FRA's $4.4 billion fiscal year 2010 budget.

Ensuring the Safe and Secure Movement of People and Goods While Undertaking Increased Passenger Rail Responsibilities Recent railroad legislation also expanded FRA's traditional safety role. Specifically, RSIA requires FRA to develop a long-term strategy for improving railroad safety, which includes an annual plan to address the following six goals:

- Reduce the number and rates of accidents, incidents, injuries, and fatalities involving railroads caused by train collisions, derailments, and human factors.
- Improve the consistency and effectiveness of enforcement and compliance programs.
- Improve the identification of high-risk highway-rail grade crossings and strengthen enforcement and other methods to increase grade crossing safety.
- Improve research efforts to enhance and promote railroad safety and performance.
- Prevent railroad trespasser accidents, incidents, injuries, and fatalities.
- Improve the safety of railroad bridges, tunnels, and related infrastructure to prevent accidents, incidents, injuries, and fatalities caused by catastrophic failures and other bridge and tunnel failures.

RSIA further requires FRA to establish a discretionary grant program, with authorized funding of $50 million per year for fiscal years 2009 through 2013, to support the development and deployment of positive train control (PTC) technologies.[14] While these technologies may help FRA achieve RSIA's safety goals, FRA has noted some concern on the

[14] "Positive train control" means a system designed to prevent collisions between trains, overspeed derailments (derailments caused when a train exceeds speed limits), incursions into established work zone limits, and the movement of a train through an improperly positioned switch.

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part of freight railroads that investing in PTC will divert capital from near-term capacity enhancements and lead to delays that cause more freight to shift onto already congested highways. Such concerns place an even heavier burden on FRA to balance interests of freight rail companies with the renewed focus and investment in the expansion of passenger rail service throughout the United States.

Balancing an Increased and Diversified Workload with the Continuing Need To Oversee Amtrak Operations In addition to its new and expanded responsibilities, FRA must remain vigilant in its traditional role of overseeing Amtrak's operations and disbursing Amtrak's annual grant funds.[15] This oversight role is reinforced in several provisions of PRIIA. For example, PRIIA requires FRA to produce quarterly reports on the performance and service quality of intercity passenger train operations, including Amtrak's cost recovery, ridership, on-time performance and minutes of delay, causes of delay, on-board services, stations, facilities, equipment, and other services. Similarly, FRA must oversee Amtrak's compliance with applicable sections of the Americans with Disabilities Act of 1990 and the Rehabilitation Act of 1974 to ensure that Amtrak's services and facilities are accessible to individuals with disabilities to the extent required by law.[16]

PRIIA not only expanded FRA's responsibilities but also added significantly to Amtrak's workload. For example, PRIIA requires Amtrak to implement a new cost accounting system and spearhead a committee of various stakeholders to design and develop specifications for a next generation train equipment pool. As Amtrak undertakes these new initiatives, FRA will need to enhance its Amtrak oversight capabilities.

Related Products The following related reports and testimonies can be found on the OIG website at http://www.oig.dot.gov.

- Amtrak Cascades and Coast Starlight Routes: Implementation of New Metrics and Standards Is Key To Improving On-Time Performance, September 23, 2010
- Semiannual Report on Amtrak's Financial and Operating Performance and Savings From Reform, May 17, 2010

[15] These grant funds totaled nearly $1.6 billion in fiscal year 2010.

[16] Amtrak was mandated to comply with requirements under the Americans with Disabilities Act of 1990 (ADA) by July 26, 2010. Amtrak is not yet in full compliance but has recently submitted an ADA compliance plan to Congress requesting additional funding and an extension of the ADA deadline.

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- "Federal Railroad Administration Faces Challenges in Carrying Out Expanded Role," statement of Ann Calvaresi Barr, Deputy Inspector General, U.S. Department of Transportation before the Committee on Appropriations Subcommittee on Transportation, Housing and Urban Development, and Related Agencies, United States Senate, April 29, 2010
- DOT's Implementation of the American Recovery and Reinvestment Act: Continued Management Attention Is Needed To Address Oversight Vulnerabilities, November 30, 2009
- American Recovery and Reinvestment Act of 2009: Oversight Challenges Facing the Department of Transportation, March 31, 2009

For more information on the issues identified in this chapter, please contact Mitch Behm, Assistant Inspector General for Rail, Maritime, and Economic Analysis, at (202)-366-9970.

CHAPTER 7

Advancing the Next Generation Air Transportation System While Ensuring the Safe and Efficient Operation of the National Airspace System

Source: Federal Aviation Administration

The Federal Aviation Administration (FAA) estimates there are around 7,000 aircraft in the air over the United States at any given time. To better manage this capacity, FAA is developing the Next Generation Air Transportation System (NextGen)—a satellite-based air traffic control system intended to replace the current ground-based system. At the same time, FAA must operate and sustain the existing National Airspace System (NAS).

Key Challenges

- Establishing realistic plans and setting expectations for NextGen
- Addressing problems with ongoing modernization projects that are essential to NextGen's success

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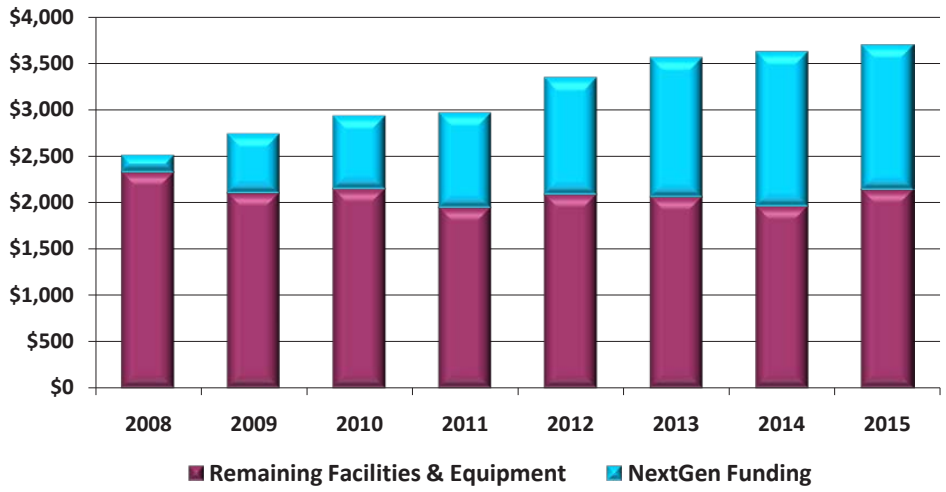
- Maximizing the delivery and implementation of new performance-based navigation initiatives that can enhance capacity and reduce delays
- Ensuring a sufficient number of certified professional controllers at facilities that are critical to the NAS

Establishing Realistic Plans and Setting Expectations for NextGen

NextGen is vital to revolutionizing our aviation system and the Nation's long-term economic growth. Yet, the Department and FAA have struggled with setting expectations for what can reasonably be achieved in the near, mid, and long term. FAA plans to spend almost $9 billion between fiscal years 2008 and 2015 specifically on NextGen-related programs, which include a new satellite-based surveillance system and an information sharing system (see figure 7.1).

Figure 7.1. FAA Capital Funding for Fiscal Years 2008 through 2015, in Millions of Dollars



Source: FAA

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Last September, a government-industry task force made a series of recommendations for advancing NextGen in the midterm.[17] These included leveraging equipment already on aircraft, enhancing information sharing among FAA and airspace users, and reducing delays. FAA is incorporating the task force's recommendations into its plans, but it has not yet established detailed milestones to complete initiatives at high-activity locations that affect delays nationwide, like New York. Earlier this year, the task force identified 20 gaps between its recommendations and FAA's plans. Many of these relate to differences in milestones and locations as well as the need for FAA to develop more specific plans. In addition, while FAA has endorsed the recommendations, it still faces several barriers with respect to organizational culture, unresolved policy issues, and controller training that could impede implementation and expected benefits.

In June 2010, we reported that FAA had made progress in developing a vision for NextGen in the midterm but that it still needed to make a number of critical decisions to keep NextGen on track. Specifically, FAA has not decided how to allocate new capabilities for controllers among various automation systems or to what extent FAA facilities can be realigned, co-located, or consolidated due to new technology. Much work also remains to refine requirements and costs and establish metrics for measuring progress. These decisions will materially affect the cost of NextGen. In addition, FAA has not fully leveraged other Federal agencies' existing research and development programs, including research at the Department of Defense that could significantly reduce NextGen development costs.

Addressing Problems with Ongoing Modernization Projects That Are Essential to NextGen's Success Central to achieving NextGen's goals is the successful implementation of ongoing modernization projects that will provide platforms for new NextGen capabilities. Of particular concern are problems with the $2.1 billion En Route Automation Modernization (ERAM) program, which is intended to replace hardware and software at facilities that manage high-altitude traffic. FAA originally planned to deploy ERAM to 20 en route facilities by the end of 2010. However, during testing at ERAM's initial operating site, FAA encountered significant software-related problems, including radar processing failures and handing off traffic between controllers. As a result, FAA stopped ERAM testing in March 2010 to reexamine plans and develop corrective actions. FAA is working with its contractor to address the more than 200 problems identified so far and to

[17] *NextGen Mid-Term Implementation Task Force Report*, September 9, 2009.

improve system stability. The cost and schedule to complete ERAM are uncertain, but delays could be 2 years or longer. Delays with ERAM have serious consequences—FAA will have to maintain aging systems longer, limit capacity enhancing improvements in the high-altitude environment, and provide refresher training for controllers and maintenance technicians who must be certified on two different systems. Prolonged problems with ERAM could also have a cascading effect on implementing NextGen now and in the future, including key systems such as the Automatic Dependent Surveillance-Broadcast (ADS-B)[18] and Data Communications.[19]

Maximizing the Delivery and Implementation of New Performance-Based Navigation Initiatives That Can Enhance Capacity and Reduce Delays A fundamental building block of FAA's NextGen efforts is establishing new performance-based navigation routes and procedures, using Area Navigation (RNAV) and Required Navigation Performance (RNP) specifications.[20] The potential benefits of RNAV and RNP are significant and include shorter, more direct flight paths; improved airport arrival and departure efficiency; enhanced controller productivity; fuel savings; and reduced aircraft noise and carbon emissions.

However, FAA has not widely implemented efficient RNP procedures, clarified the role of non-government third parties in developing RNAV/RNP procedures, or developed metrics to measure expected benefits. For example, FAA does not plan to rely on its two qualified third-party vendors to design and implement public RNP procedures, but airline officials stated that third parties may be needed to provide technical expertise for developing more efficient RNP procedures. FAA has instead focused on producing a targeted number of procedures—most of which are overlays of existing routes that do not provide shorter paths to alleviate airspace congestion or are incompatible with existing air traffic policies at airports with parallel runways. As a result, airlines that are equipped and approved for RNP are not widely using FAA's RNP procedures.

[18] ADS-B offers surveillance, like radar, but with more precision. ADS-B provides air traffic controllers and pilots with more accurate information to help keep aircraft safely separated in the sky and on runways.

[19] Data Communications will provide comprehensive data connectivity, including ground automation message generation and receipt, message routing and transmission, and aircraft avionics requirements.

[20] RNAV is a method of navigation in which aircraft use avionics, such as Global Positioning Systems, to fly any desired flight path without the limitations imposed by ground-based navigation systems. RNP is a form of RNAV that adds on-board monitoring and alerting capabilities for pilots, thus allowing aircraft to fly more precise flight paths.

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Since we reported last year, FAA has stated that it will adjust its goals to focus on implementing beneficial procedures rather than producing a targeted number of procedures. In response to the recommendations of a joint government-industry task force, FAA is also creating joint agency-industry teams tasked with deploying enhanced procedures at delay-plagued airports in metropolitan areas, but this effort is in the early stages. FAA's key challenges to realizing the benefits of new procedures include integrating new routes with airspace redesign efforts, streamlining its procedure development process, modifying the equipment that controllers rely on to manage traffic, and properly training air traffic controllers and pilots on procedures before implementing them.

Ensuring a Sufficient Number of Certified Professional Controllers at Critical Facilities FAA estimates that it will need to hire and train nearly 11,000 new air traffic controllers by fiscal year 2019 to replace controllers hired after the 1981 strike who are now eligible to retire. Because of the surge in attrition, FAA must assign newly hired controllers to complex air traffic control facilities, such as the Southern California Terminal Radar Approach Control, the Atlanta Terminal Radar Approach Control, the Chicago O'Hare Airport Traffic Control Tower, and facilities controlling the New York area airspace. In fiscal year 2009, 61 percent of all newly hired controllers were placed at Level 10 through 12 facilities, which are the busiest and most complex in the Nation and critical to NAS operations. In addition, 26 percent of FAA's controller workforce is currently in training—compared to 15 percent in 2004—creating the potential for fewer certified controllers in the workforce to control air traffic while providing on-the-job training for new controllers. While FAA has ongoing actions or plans to improve controller training and placement, the Agency will need to minimize the risks that less experienced controllers impose on the most critical facilities in the NAS. Key challenges will be ensuring adequate staffing, training resources, and other support to maintain continuity of facility operations.

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Advancing the Next Generation Air Transportation System While Ensuring the Safe and Efficient Operation of the National Airspace System

Related Products The following related reports and testimonies can be found on the OIG website at http://www.oig.dot.gov.

- Timely Actions Needed To Advance the Next Generation Air Transportation System, June 16, 2010
- Challenges in Meeting FAA's Long-Term Goals for the Next Generation Air Transportation System, April 21, 2010
- Actions Needed To Meet Expectations for the Next Generation Air Transportation System in the Midterm, October 28, 2009
- Challenges in Implementing Performance-Based Navigation in the U.S. Air Transportation System, July 29, 2009
- Training Failures Among Newly Hired Air Traffic Controllers, June 8, 2009
- Progress and Remaining Challenges in Reducing Flight Delays and Improving Airline Customer Service, May 20, 2009
- Aviation Industry Performance: A Review of the Aviation Industry in 2008, May 6, 2009
- Controller Staffing at Key California Air Traffic Control Facilities, April 23, 2009
- Federal Aviation Administration: Actions Needed To Achieve Mid-Term NextGen Goals, March 18, 2009
- Key Issues for Reauthorizing the Federal Aviation Administration, February 11, 2009
- FAA Faces Significant Risks in Implementing the Automatic Dependent Surveillance-Broadcast Program and Realizing Benefits, October 12, 2010

For more information on the issues identified in this chapter, please contact Jeffrey B. Guzzetti, Assistant Inspector General for Aviation and Special Program Audits, at (202)-366-0500.

CHAPTER 8

Implementing Processes To Improve the Department's Acquisitions and Contract Management

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In fiscal year 2010, the Department obligated approximately $5.8 billion[21] on contracts for goods and services, including information technology services, training, road maintenance, and professional services to plan and implement key NextGen systems. Additionally, more than $60 billion was budgeted for grants to states, transit agencies, and other partners to help meet departmental strategic goals. To ensure it maximizes these dollars, the Department needs to strengthen its acquisition and contract management practices. While it has made some progress in this area, such as completing oversight reviews of the Federal Aviation Administration's (FAA) compliance with its acquisition policy guidance,[22] our audits continue to find weaknesses in how the Department plans, administers, and oversees its contracts.

[21] Based on data from the Federal Procurement Data System-Next Generation provided by DOT.
[22] Completed regularly by FAA's National Acquisition Evaluation Program Team.

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Key Challenges

- Strengthening processes to govern the appropriate use of non-competitive or risky contracts and maximize use of competition
- Strengthening the acquisition function and workforce to provide leadership for the Department's acquisitions
- Maintaining programs to help ensure high ethical standards among the Department's contractors and employees

Strengthening Processes To Govern the Appropriate Use of Non-Competitive or Risky Contracts and Maximize Use of Competition Recent Office of Management and Budget (OMB) contracting initiatives underscore agency use of competition and fixed-price contracts and require agencies to perform effective price analysis to mitigate risks for noncompetitive contract awards.[23] However, the Department annually awards over $1.8 billion using sole-source, cost-reimbursable, time-and-materials, and labor hours contracts, which represent the greatest risk to the Government because they are inefficient and subject to misuse. The Department was required to reduce the amount obligated for new awards of these contracts by more than 10 percent in fiscal year 2010.[24] However, our recent work on contracting at FAA and the Federal Motor Carrier Safety Administration (FMCSA) and award fee contracts illustrates that the Department needs to further improve its controls over high-risk contracts.

In fiscal year 2009, FAA obligated $541 million on more than 16,500 noncompetitive contract actions.[25] Our ongoing review of FAA's processes for awarding these sole-source contracts revealed that acquisition planning was inadequate and responsible officials were not sufficiently trained to perform price analyses. As a result, program and contracting officials took shortcuts when completing price analyses to meet compressed timeframes. Improved planning, training, and documentation are essential to ensure that prices are fair and reasonable for these contracts.

[23] OMB Memorandum, *Increasing Competition and Structuring Contracts for Best Results,* October 27, 2009.

[24] DOT did not provide us with the analysis to show if it met the 10-percent reduction required by OMB for these contracts in fiscal year 2010.

[25] These include actions for awards of new contracts, modifications, task orders, and delivery orders. Not all of these contract actions required competitive awards, but when the action exceeds $10,000 FAA requires price analysis to ensure the Government receives the best value for dollars spent.

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FMCSA spends about 40 percent of its procurement dollars on high-risk time-and-materials contracts—compared to 5 percent Government-wide. In August 2010, we reported that FMCSA's contract pre-award processes leave it vulnerable to using ineffective business arrangements and ultimately hinder its ability to maximize competition.[26] For example, FMCSA does not prepare required acquisition plans, follow its recommended procurement lead times for planning and awarding contracts, or perform adequate market research to identify qualified vendors. While FMCSA concurred with our recommendations to follow sound procurement practices and maximize competition, FMCSA must fully implement planned actions to ensure it reduces its reliance on high-risk contracts and receives the best value for its procurement dollars.

Weaknesses in the Department's use of cost-plus-award-fee (CPAF) contracts further put its contract dollars at risk. CPAF contracts can encourage excellence by providing financial incentives based on performance, but they require effective monitoring to ensure contract dollars are spent wisely and award fees are justified. In August 2010, however, we reported that Operating Administrations did not use measurable evaluation criteria or payment structures to motivate exceptional performance. Ultimately, Operating Administrations consistently gave contractors high ratings and substantial award fees, despite lacking adequate support for their actual performance, as measured by award-fee evaluation criteria and directed by OMB.[27] These award fees totaled about 92 percent of the awards for the rating periods we reviewed. Based on our audit sample, we estimated that more than $140 million was paid in award fees without proper justification.[28] To improve its use of award fee contracts at operating administrations, the Department is developing a guidebook incorporating best practices for planning, implementing, and administering CPAF contracts and training contracting and program personnel.[29] Effective implementation of Office of the Secretary (OST) and FAA measures will be critical to ensuring the Department does not pay improper award fees to contractors.

[26] OIG Report Number ZA-2010-093, "Federal Motor Carrier Safety Administration Lacks Core Elements for a Successful Acquisition Function," August 24, 2010.
[27] OIG Report Number ZA-2010-092, "Improvements in Cost-Plus-Award-Fee Processes Are Needed To Ensure Millions Paid in Fees Are Justified," August 25, 2010.
[28] We audited the performance periods for award fee contracts as of December 31, 2007. Our estimate was based on extrapolating our contract sample to the universe of DOT's 41 CPAF contracts.
[29] FAA issued separate award fee guidance in September 2007.

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Strengthening the Acquisition Function and Workforce To Provide Leadership for the Department's Acquisitions To maintain an effective acquisition function, OMB provided agencies with standard guidance that emphasizes organizational alignment and leadership, policies and procedures, a workforce of the appropriate size and needed skills, and information management and stewardship.[30] However, key acquisition leadership positions within OST have been vacant or filled as collateral duties, and a strategic vision is needed to guide acquisition operations successfully throughout the Department. Also, OST's Senior Procurement Executive (SPE) does not report directly to the Chief Acquisition Officer (CAO), contrary to legislative requirements[31] and the intent of OMB guidance. Because the SPE does not have a direct line of communication with the CAO and is not formally part of the Department's top-level management discussions and meetings, the SPE's ability to elevate acquisition issues and position the acquisition function to play a strategic role is diminished. For example, OST is not sufficiently performing critical oversight of acquisitions at Operating Administrations. OST also lacks a comprehensive set of updated policies to effectively manage its acquisitions. The Department's Transportation Acquisition Regulations and Transportation Acquisition Manuals, maintained by OST, were last updated in 2005 and 2006, respectively. Finally, OST lacks the basic internal controls needed to minimize the risk of unauthorized users accessing and manipulating the Department's procurement data. The lack of internal controls compromises the data's integrity, security, and usefulness in forming management decisions and ultimately exposes the Department to fraud, waste, and abuse.

OST has begun steps to strengthen its acquisition function. However, until OST fully commits to needed reform, it will be limited in its ability to provide clear direction and vision to acquisitions across the Department. Strong acquisition direction is essential to ensure the billions of dollars the Department spends on contracting each year are used in the most efficient and effective manner and help accomplish the Department's mission.

In addition to lacking an effective acquisition function, the Department is challenged to maintain an acquisition workforce that can effectively oversee its expanding and complex contracts for goods and services. Retention and recruitment concerns, as well as the need to ensure a competent workforce, pose risks to the Department's ability to meet its

[30] OMB Memorandum, *Conducting Acquisition Assessments under OMB Circular A-123,* May 21, 2008.
[31] Service Acquisition Reform Act of 2003 (Pub. L. No. 108-136 § 1421(c).

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acquisition workload demands.[32] Between fiscal years 2008 and 2018, the percentage of employees in the Department's contracting series eligible to retire will more than triple to 63 percent—a rate about 10 percent higher than the average for civilian agencies. According to FAA, its acquisition workforce is currently 6 percent understaffed, and this shortage could grow to 26 percent by 2014. Despite these concerns, the Department has yet to develop adequate plans to address this challenge. For example, the Department's 2009 Strategic Acquisition Workforce Succession Plan is based on survey responses from less than half of its workforce. In addition, Operating Administrations have not made sufficient progress in implementing the specific strategies and goals in the Department's first Acquisition Workforce Strategic Human Capital Plan, issued in April 2010, for increasing the capacity and capability of the acquisition workforce through fiscal year 2014.[33] This year, FAA—whose procurement function is autonomous from the Department's—updated its 2009 Acquisition Workforce Plan to project workforce needs through 2014 and broaden the definition of acquisition workforce.

Maintaining Programs To Help Ensure High Ethical Standards Among the Department's Contractors and Employees Our audits and investigations have identified the need for more vigilant oversight to detect and prevent procurement fraud, waste, and abuse within the Department and among its fund recipients. The Department's oversight of over $40 billion in Recovery Act funds heightens the importance of safeguarding against awarding funds to those with a record of wrongdoing and abuse.

Contract and grant fraud cases currently comprise about 42 percent of active Office of Inspector General investigations. Between June 2009 and September 17, 2010, contract grant fraud cases resulted in 27 indictments, 34 convictions, and $72 million in recoveries. For example, an airport owner and recipient of FAA Airport Improvement Program grants was sentenced to 2 years probation for diverting approximately $375,000 in grant funds—provided by FAA to pay contractors who completed airport improvements—for his personal use. Similarly, a Chicago engineering firm owner was sentenced to 41 months in prison and ordered to pay $10 million in restitution for overstating overhead expenses on various engineering and architectural projects. The overpayments were due to invalid charges on

[32] OIG Report Number PT-2010-008, "DOT's Fiscal Year 2010 Top Management Challenges," November 16, 2009.
[33] DOT's plan was in response to an October 27, 2009, Office of Federal Procurement Policy requirement that civilian agencies develop an annual acquisition human capital plan.

projects funded by the Federal Transit Administration, the Federal Highway Administration, and FAA.

In January 2010, we reported that the Department's ability to safeguard against awarding contracts and grants to improper parties was limited by delays in its suspension and debarment (S&D) decisions and reporting, as well as deficiencies in its policies, procedures, and internal controls.[34] In response to our recommendations, OST and FAA revised their S&D policies to require timely action on S&D decisions and accurate and timely reports on these cases. However, neither OST nor FAA has fully implemented the reporting system and corresponding internal controls used to collect and manage S&D information across the Department. Until the Department fully implements these improvements to its S&D Program, it will have incomplete information on its S&D caseloads and risk awarding contracts and grants to parties that have been suspended or debarred.

[34] OIG Report Number ZA-2010-034, "DOT's Suspension and Debarment Program Does Not Safeguard Against Awards to Improper Parties," January 7, 2010.

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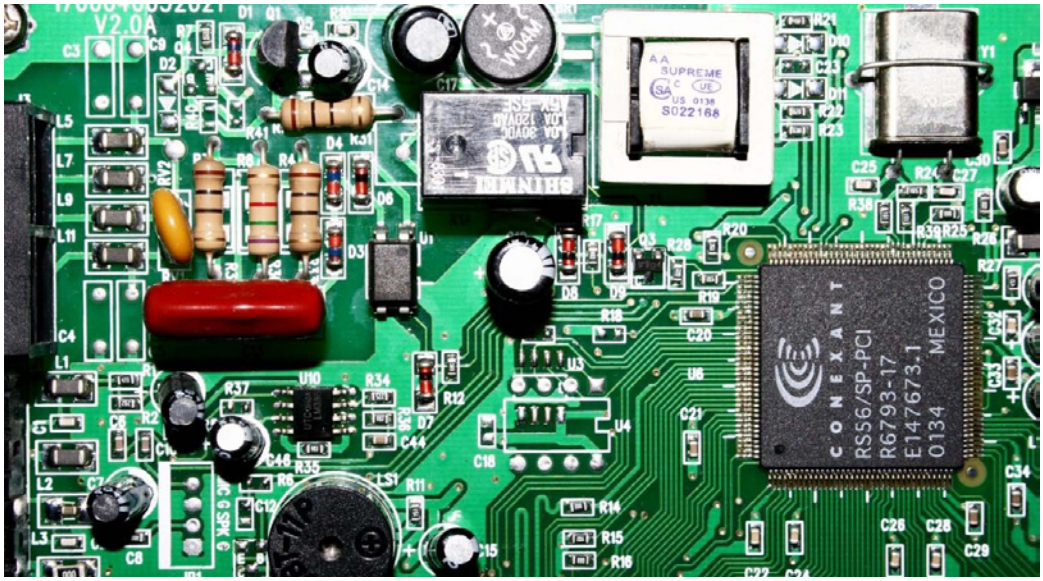
Related Products The following related reports, testimonies, and advisories can be found on the OIG website at http://www.oig.dot.gov.

- Improvements in Cost-Plus-Award-Fee Processes Are Needed To Ensure Millions Paid in Fees Are Justified, August 25, 2010
- Federal Motor Carrier Safety Administration Lacks Core Elements for a Successful Acquisition Function, August 24, 2010.
- Weaknesses in DOT's Suspension and Debarment Program Limit Its Protection of Government Funds, March 18, 2010
- DOT's Suspension and Debarment Program Does Not Safeguard Against Awards to Improper Parties, January 7, 2010
- ARRA Advisory–DOT's Suspension and Debarment Program, May 18, 2009

For more information on the issues identified in this chapter, please contact Tony Wysocki, Acting Assistant Inspector General for Acquisition and Procurement Audits, at (202)-493-0223 or Timothy Barry, Principal Assistant Inspector General for Investigations, at (202) 366-1967.

CHAPTER 9

Improving the Department's Cyber Security



Source: freepixels.com

As part of its Accountable Government Initiative, the Administration seeks to enhance Federal cyber security[35] while closing information technology (IT) gaps between the Government and private sector. With new cyber threats constantly arising, automated tools are essential to continuously monitor security-related information. With more than 400 systems—nearly two-thirds of which belong to the Federal Aviation Administration (FAA)—and an approximately $3 billion annual technology investment, the Department is working to incorporate new technologies and meet the Administration's cyber security goals.

Key Challenges

- Establishing a robust information security program
- Strengthening air traffic control system protections
- Increasing protection of personally identifiable information (PII)

[35] Cyber security is the branch of security that pertains to computers and networks, including the Internet.

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Establishing a Robust Information Security Program The Federal Information Security Management Act (FISMA) of 2002 requires agencies to establish an information security program to protect agency information and systems. Last year, we reported that the Department's information security program was not as effective as it should be and did not meet key FISMA and Office of Management and Budget (OMB) requirements.[36] With limited progress during fiscal year 2010, several challenges remain.

First, security deficiencies still exist in key control areas, including management of information, system authorization, configuration management, and contingency planning. For example, we determined that the Department's Recovery Act websites made user information and departmental systems vulnerable to attack. To build an information security program that adequately protects against cyber threats, the Department needs to address security deficiencies in a sustainable and flexible manner so it can quickly adapt to and avert new threats.

Second, the Department's Office of the Chief Information Officer (OCIO) could do more to guide and oversee the Operating Administrations in building and sustaining strong information security practices. In 2009, OCIO issued its Department-wide information security policy—the first step in building an information security program. The next step for OCIO is to enhance this policy and develop Department-wide procedural guidance. In addition, OCIO needs to conduct quality assurance reviews of modal cyber security efforts and assess the use of technology to facilitate timely management of the Department's cyber security. At present, the Department does not have central, automated systems to enable the timely assessment of its information security program. Until the OCIO can better guide and oversee Operating Administrations' information security, the Department cannot ensure that policy is properly implemented or deploy automated tools to quickly and continuously monitor its cyber security posture.

Finally, the Department has yet to meet OMB's requirement for issuing Personal Identity Verification (PIV) cards to employees and contractors—a key Government-wide initiative to secure Federal information and information systems. OCIO and the Assistant Secretary of

[36] OIG Report Number FI-2010-023, "Audit of DOT's Information Security Program and Practices," November 18, 2009.

Administration share the responsibility of managing PIV card issuance. More than a year after OMB's October 2008 deadline, less than 30 percent of the Department's approximately 112,000 employees and contractors had a PIV card. The Department has yet to develop an actionable plan to complete issuance of PIV cards to its remaining employees and contractors. In addition, the Department needs a better process for securing the information systems used to store, process, and transmit personally identifiable information. Until it takes action to address these weaknesses, the Department not only risks issuing PIV cards to non-DOT employees and contractors, it cannot secure personal information such as Social Security numbers (SSN).

Strengthening Air Traffic Control System Protections FAA's planned Next Generation Air Transportation System (NextGen) system relies on a number of new technologies to achieve its goals. The Automatic Dependent Surveillance-Broadcast (ADS-B), a key NextGen system, uses satellite-based surveillance to more precisely track the location of aircraft.[37] While ADS-B offers many benefits over traditional ground-based radar systems, some aspects are vulnerable to certain types of cyber attack. Also, as part of the transition to NextGen, FAA is increasingly relying on the use of Internet Protocol (IP)-based commercial products and web applications rather than proprietary software. While this strategy will enable FAA to efficiently facilitate air traffic control services, it poses a higher security risk due to the vulnerabilities inherent in using commercial IP-based products. In addition, FAA is outsourcing more of its operations to contractors. ADS-B is the first operational Air Traffic Control (ATC) system to be owned and operated by a contractor. Because FAA only owns the data, not the system, it could have little control over security challenges encountered with ADS-B.

As FAA develops NextGen, it must continue to protect its current ATC systems, which are located at hundreds of operational facilities, such as en route centers, Terminal Radar Approach Control (TRACON) facilities, and airport control towers. Yet, FAA has not established adequate Intrusion Detection System (IDS) capabilities to monitor and detect potential cyber security incidents at key ATC facilities. Instead, FAA relies on the Department's Cyber Security Management Center to monitor cyber incidents only for administrative systems, such as email at these facilities. To collect critical information for

[37] See chapter 7 for a discussion of NextGen.

CHAPTER 9

Improving the Department's Cyber Security

security analyses, FAA needs to install IDS sensors at key locations.[38] During the past year, FAA has taken steps to identify key ATC facilities that need IDS monitoring and has begun deploying IDS at certain TRACON facilities. However, without comprehensive NAS-wide IDS capabilities, FAA cannot effectively monitor ATC systems for possible cyber attacks or take timely action to stop them. FAA management is developing an implementation strategy to address this issue but has not developed or identified a timetable for deploying IDS beyond the specified TRACON facilities.

Increasing Protection of Personally Identifiable Information To minimize the risks associated with the unauthorized disclosure of PII, OMB required agencies to eliminate the unneeded use of SSNs by November 2009. In fiscal year 2010, the Department stabilized its inventory of systems containing PII, provided advanced training sessions for modal privacy personnel, and continued its analysis to reduce the use of SSNs in PII systems. Despite this progress, PII remains vulnerable to misuse. The Department has preliminarily identified 70 systems that need to be evaluated for SSN elimination but does not plan to complete the elimination until 2013. To protect the public's privacy and comply with OMB requirements, the Department must assign a priority to meet the OMB mandate of eliminating unneeded use of SSNs in a timelier manner.

Our review of the Airmen Medical Support Systems (MSS) found that airmen's PII was not properly secured to prevent unauthorized access due to serious security lapses in FAA's management of user access to the system.[39] For example, medical examiners' former staff continued to have access to MSS. At the same time, FAA has not fully implemented security controls required by OMB and the Department to protect PII. In addition, FAA has not ensured secure configuration of MSS computers in accordance with the Department's baseline standards to reduce the risk of unauthorized access and corruption. We found vulnerabilities on MSS computers, such as the configuration allowing intruders to install malicious codes on FAA user computers. These weaknesses make airmen's PII vulnerable to unauthorized access and use and potential falsification of medical certificates that could lead to unfit airmen being medically certified to fly. During our review, FAA took immediate

[38] Sensors are a combination of hardware and software that serve as the "eyes and ears" of the IDS. Ideally, they are placed at key network locations (e.g., Internet access points) to detect threats such as viruses.

[39] OIG Report Number FI-2010-069, "Information Security and Privacy Controls over the Airmen Medical Support Systems," June 18, 2010.

action to enhance security protection by working with doctors to remove thousands of separated medical staff's access to MSS and retracting millions of PII records from the contractor's site. However, additional improvements are needed to adequately secure PII data from unauthorized use.

Related Products The following related reports and testimonies can be found on the OIG website at http://www.oig.dot.gov.

- Review of FAA's Progress in Enhancing Air Traffic Control Systems Security, November 2, 2009
- Final Report on the Department of Transportation's Information Security Program and Practices, November 18, 2009
- Information Security and Privacy Controls Over the Airmen Medical Support Systems, June 18, 2010

For more information on the issues identified in this chapter, please contact Earl Hedges, Acting Assistant Inspector General for Financial and Information Technology Audits, at (410)-962-3612.

EXHIBIT

Comparison of Fiscal Year 2011 and 2010 Top Management Challenges

Fiscal Year 2011 Challenges	Fiscal Year 2010 Challenges
• Ensuring Transparency and Accountability in the Department's Recovery Act Programs	• Maximizing the Department's Economic Recovery Investments
• Maintaining Momentum in the Department's Oversight of Highway, Motor Vehicle, Hazardous Materials, and Transit Safety	• Enhancing Surface Safety Programs To Reduce Injuries and Fatalities While Defining a New Federal Role in Transit Safety
• Maintaining Momentum in Addressing Human Factors and Improving Safety Oversight of the Aviation Industry	• Addressing Human Factors and Strengthening the Regulatory Oversight Framework for Aviation Safety
• Improving the Department's Oversight of Highway, Transit, and Pipeline Infrastructure	• Maximizing Federal Surface Infrastructure Investments by Helping States Better Allocate Resources and Providing Effective Oversight
• Identifying Sufficient Funding Sources to Support Future Federal Investment in Surface Transportation Infrastructure	• Developing a Funding Framework for the Next Surface Transportation Reauthorization
• Transforming the Federal Railroad Administration to Address Significantly Expanded Oversight Responsibilities	• Successfully Implementing the Newly Created Multi-Billion Dollar High-Speed Intercity Passenger Rail Program
• Advancing the Next Generation Air Transportation System While Ensuring the Safe and Efficient Operation of the National Airspace System	• Moving Toward the Next Generation Air Transportation System and Improving Performance of the National Airspace System
• Implementing Processes To Improve the Department's Acquisitions and Contract Management	• Improving Contract Management and Oversight • Strengthening the Department's Acquisition Workforce
• Improving the Department's Cyber Security	• Enhancing the Ability To Combat Cyber Attacks and Improving the Governance of Information Technology Resources

APPENDIX. DEPARTMENT RESPONSE

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

Memorandum

Subject: **ACTION:** Response to Office of Inspector General (OIG) draft report, "Top Management Challenges for Fiscal Year 2011"

Date: November 3, 2010

From: Christopher Bertram
Assistant Secretary for Budget and Programs, and Chief Financial Officer

Reply to Attn. of:

To: Calvin L. Scovel III
Inspector General

Throughout FY 2010, the Department of Transportation (DOT) has maintained its long-standing record of excellence in delivering a world-class transportation system for our Nation. Many of our recent accomplishments demonstrate the Department's continued commitment to ensuring safe and reliable transportation for today, while at the same time planning for the transportation needs of tomorrow. The Department continues to promote intermodal solutions utilizing the best that each transportation mode has to offer for solving current transportation challenges, as well as an even more holistic or systems approach that builds transportation efficiency into communities from the start. This new systematic focus encourages livable communities by incorporating consideration of the important role that transportation plays into development decision-making to help make neighborhoods safe, accessible and efficient.

Transportation Safety is the Department's First Priority

The Department's commitment to maintaining and further improving transportation safety in all modes is unequivocal. The results of our safety culture continue to be demonstrated in recent metrics. Working together with state and local authorities, we have achieved further reductions in the annual highway fatality rates. This includes reductions in motorcycle fatalities which had been steadily rising. We raised public awareness around the Nation about the dangers posed by distracted driving from the unsafe use of cell phones, texting, and the use of other electronic devices. The Secretary personally highlighted the risks associated with distracted driving at events throughout the country and hosted a Distracted Driving Summit here at the Department to focus on this important issue. The Secretary also moved

forward with a bold initiative to extend the Department's safety culture to the transit systems millions of people depend on each day to travel to and from work. After a recent string of safety failures across the Nation, the Secretary determined that it is time for the Federal Transit Administration to take a stronger, more proactive role in transit safety, and has been working with the Congress to bring an increased Federal focus on transit safety.

The Department's combined efforts through each of its operating administrations continue to advance transportation safety through improvements in systems, processes, and oversight. Through the Pipeline and Hazardous Materials Administration, the Department has significantly improved its oversight of hazardous materials transportation over the past year, with the application of improved procedures, better interaction with organizations throughout the Department, and increased management focus on the issues. The National Highway Traffic Safety Administration demonstrated its commitment to ensuring vehicle safety through its introduction of new and tougher vehicle safety rating systems, its enforcement of vehicle recall requirements, and its use of new and creative ways to inform the public. Its continued emphasis on proven public information campaigns, such as "Click it or Ticket," combined with targeted enforcement activities led to further improvement in the rate of seat belt use across the country, which is saving lives today. The Federal Aviation Administration (FAA) has demonstrated continued success in its use of safety data to better focus safety inspections and affect appropriate actions by air carriers to continue achieving a strong safety record, even through difficult economic times. As a result of these and other actions throughout the Department, we continue to make significant strides in achieving our safety goals.

DOT Recovery Act Implementation Generates Tens of Thousands of Jobs with More than 15,000 Infrastructure Projects

FY 2010 marks the second year of the Department's implementation of the American Recovery and Reinvestment Act of 2009 (Recovery Act) and the Department's programs continue to generate worthwhile jobs with careful investments in useful transportation infrastructure. The $48.1 billion appropriated to DOT has been used to support more than 15,000 infrastructure projects. This investment has improved the safety and efficiency of the Nation's system of highways, transit, ports, and airports. Just as important, these projects generated tens of thousands of jobs in transportation and related sectors, during a difficult economic environment.

In addition to enhanced funding for the Department's traditional programs, the Recovery Act included $1.5 billion for the Secretary's Discretionary Grant program known as TIGER Grants, and $8 billion to begin addressing the President's vision for a world class high speed intercity passenger rail system for America. The TIGER Grant program focused on projects that apply intermodal solutions and innovative strategies to address demonstrated transportation needs. Early in 2010, the Secretary selected 51 projects nationwide that promote greater mobility, a cleaner environment and more livable communities. Through the Federal Railroad Administration (FRA), the Department has devoted significant time and

resources over the past year for successful implementation of the new High Speed rail initiatives. These efforts require nothing less than building an entirely new program including identifying programmatic requirements, identifying and obtaining necessary resources, and creating oversight structures, while implementing the program with unprecedented speed. Using a truly intermodal approach, FRA identified best practices from operating administrations throughout the Department and is modeling the program based-on best practices from the Department's established grant programs.

Implementing the Recovery Act also generated unanticipated benefits, including new business processes, increased focus on new measures of results, and ever growing expectations for expeditious program implementation with unprecedented transparency to the public. We identified new ways to collect, analyze, and convey data. As we implemented the Recovery Act, our innovative staff created capabilities that bring nationwide transportation data to a level of granularity that is meaningful and accessible to local communities. For the first time, the public can log onto the internet and with a few clicks of a mouse, gain a clear sense of what the Recovery Act meant to their community, their state and the Nation. We developed new training methods that helped the transportation community understand and comply with the Recovery Act's requirements. We developed new programs, like the TIGER program from the ground up, based on virtual teams and existing resources that can be quickly assembled, utilized, and then deconstructed, to get things done quickly and expertly, with a minimum cost to the taxpayer. We will continue to assess and analyze the lessons from Recovery Act implementation to determine how they can be applied to increase the efficiency and effectiveness of the Department's future endeavors.

Preparing for the Next Generation of Air Travel

FAA continues its efforts to effect a major change in the management of the Nation's airspace with its NextGen initiative. NextGen is intended to replace aging radar-based air traffic management systems with a new state-of-the-art satellite-based technology that holds the potential to improve system performance, address airspace congestion, and provide the airline community with significant operational benefits. Implementing this "system of systems" into an integrated air traffic management tool is a major undertaking and one of the Department's highest priorities. Ensuring that each NextGen segment moves forward in a synchronized way and effectively addresses the interdependencies among the various systems presents an enormous technical challenge to the Department. We must also keep in mind, that as the development and implementation of NextGen proceeds, FAA must also ensure that today's airspace continues to meet operational goals, such as reducing tarmac delays, increasing on-time arrivals, and maintaining strong safety performance throughout the National Airspace System.

Planning for the Surface Transportation Needs of the Future

The Department's surface transportation programs are due to be authorized by Congress. Throughout FY 2010, we have been working to delineate the Administration's priorities for

surface authorization and reflect the President's vision for meaningful investment in transportation infrastructure to facilitate economic growth, enhance safety, and improve the environment. In identifying these priorities we continue to build on a focus of intermodal solutions and enhancing the systems approach for improving livability with effective transportation solutions. We look forward to working with the Congress to explore the potential for new and better ways to fund transportation infrastructure investment, including innovative financing tools that will further leverage limited Federal resources and maximize our return on investments for the public.

Overall, the nature of the Department's mission with its focus on transportation safety and guiding wise investments in transportation infrastructure leads to a continuous cycle of management challenges. Even as progress is achieved, new challenges arise. For example advances in automotive electronics led to new advances in safety such as advanced vehicle stability control that is saving lives today. At the same time, we recognize that advanced electronics also lead to new challenges that resulted in the Secretary's initiative to reduce distracted driving. Nonetheless, the Department has established a clear record of accomplishment throughout the operating administrations and in the Office of the Secretary over the past year. As we begin FY 2011, we will once again bring to bear the talent, energy and commitment of the Department to help Transportation meet its goals. Thank you for sharing the Office of Inspector General's perspectives on the challenges facing the Department. This information will be helpful in planning for FY 2011 and beyond.

IMPROPER PAYMENTS INFORMATION ACT OF 2002

In FY 2010, the Department fully implemented the Improper Payments Information Act of 2002 (IPIA), which requires that agencies (1) review and identify programs susceptible to significant improper payments, (2) report to Congress the amount, and causes of, improper payments, and (3) develop approaches for reducing improper payments.

As part of the IPIA review, the Department successfully examined the following grant programs:

- Federal Highway Administration (FHWA) Federal-aid Highway Program
- Federal Aviation Administration (FAA) Airport Improvement Program
- Federal Transit Administration (FTA) Formula Grants Program
- Federal Transit Administration Capital Investment Grants Program

In an effort to adhere to IPIA requirements, the Department engaged Deloitte & Touche, LLP to develop nationwide sampling plans, test sampled invoice line items for improprieties, and extrapolate nationwide improper payments estimates for the Department's major grant programs.

Relative to FY 2009, and in direct response to the Office of the Inspector General's (OIG) recommendations, the Department obtained all data extracts from a single source, DOT's financial system of record. Additionally, to ensure both sample validity and the accuracy of extrapolated programmatic improper payment estimates, the Department collaborated closely with OIG's IPIA statistician to develop sampling and extrapolation methodologies mutually agreed upon by both parties.

Regarding transaction testing, the Department designed all test plans, specific to each Operating Administration, to scrutinize a range of administrative and contractual elements related to each invoice line item. Testing of administrative elements includes determining whether grantees properly approved payments, billed at the correct Federal participation rate, and determining whether billings and payments are mathematically accurate. Testing of contractual elements includes determining whether payments are in accordance with contract rates/prices for specified materials and whether material quality tests indicate materials' compliance with contractual requirements.

Samples for all reviewed grant programs are of sufficient size to yield an estimate with a minimum 90 percent confidence interval within 2.5 percentage points above and below

the estimated percentage of erroneous payments, as prescribed by OMB. The following sections discuss the results of these efforts.

FHWA Federal-aid Highway Program

The Department developed and executed a sampling methodology and test plan to review project payments and estimate the dollar amount of the Federal-aid Highway Planning and Construction Grant Program's improper payments. FHWA executed the nationwide testing program using FHWA division office personnel. The sample of tested line items originated from Federal disbursements to grantees within the twelve-month period April 1, 2009 through March 31, 2010.

The IPIA sampling methodology involved a risk-based multi-staged statistical approach that included the selection of 141 Federal disbursements totaling $582,923,902.62 and 282 line items from supporting invoices totaling $648,647,751.17. As in FY 2009, the Department designed the FY 2009 sample to extrapolate a nationwide estimate of improper payments and this sample does not support an estimate for individual states or territory grantees. FHWA subjects states and territories not selected as part of the IPIA sample to a similar sampling and testing process under FHWA's annual Financial Integrity Review and Evaluation (FIRE) program.

After accounting for duplicate line items, improper payments totaling $550,740.15 were found in the sample of 240 tested items. The projection of known improper payments to the population of program payments for the twelve-month period results in an improper payment estimate of $616,796,231.70 +/- $504,847,189.67. The estimated improper payment rate is 1.40% +/- 1.14%. This projection does not meet OMB's definition of significant improper payments ($10 million and 2.5 percent of total program payments).

Reported improper payments resulted from non-systemic administrative, clerical, and documentation errors. FHWA, in coordination with DOT's Office of Financial Management, will develop and distribute a Best Practices Guide for grantees in an effort to work towards a reduced programmatic improper payment rate. Furthermore, FHWA will continue to review for improper payments within its FIRE Program which ensures all grantees, including grantees not selected within the IPIA sample, test for improper payments annually. Additionally, FHWA will advise grantees regarding the importance of proper documentation maintenance for programmatic reviews and audits.

FTA Formula Grants Program

FTA executed the nationwide testing program using contractor personnel. The sample of tested line items originated from Federal disbursements to grantees within the twelve-month period April 1, 2009 through March 31, 2010.

The IPIA sampling methodology involved a risk-based multi-staged statistical approach that included the selection of 53 Federal disbursements totaling $590,953,605.00, and 106 line items from supporting invoices totaling $532,108,823.28. As in FY 2009, the Department designed the FY 2010 sample to extrapolate a nationwide estimate of improper payments and this sample does not support an estimate for individual states or transit agencies.

After accounting for duplicate line items, one improper payment with a value of $3,803.00 was found in the sample of 90 tested items. The projection of known improper payments to the population of program payments for the twelve-month period results in an improper payment estimate of $14,289,025.31 +/- $16,431,730.77. The estimated improper payment rate is 0.16% +/- 0.19%. This projection does not meet OMB's definition of significant improper payments ($10 million and 2.5 percent of total program payments).

The cited improper payment resulted from a non-systemic administrative error. FTA, in coordination with DOT's Office of Financial Management, will develop and distribute a Best Practices Guide for grantees in an effort to work towards a reduced programmatic improper payment rate. Additionally, FTA will advise grantees regarding the importance of proper documentation maintenance for programmatic reviews and audits.

FTA Capital Investment Grants Program

FTA executed the nationwide testing program using contractor personnel. The sample of tested line items originated from Federal disbursements to grantees within the twelve-month period April 1, 2009 through March 31, 2010.

The IPIA sampling methodology involved a risk-based multi-staged statistical approach that included the selection of 53 Federal disbursements totaling $1,284,256,775.57 and 106 line items from supporting invoices totaling $288,016,902.57. As in FY 2009, the Department designed the FY 2010 sample to extrapolate a nationwide estimate of improper payments and this sample does not support an estimate for individual states or transit agencies.

After accounting for duplicate line items, testing yielded no improper payments within the sample of 78 tested items. The projection of known improper payments to the population of program payments for the twelve-month period results in an improper payment estimate of $0.00 + $70,537,743.33. The estimated improper payment rate is 0.00% + 2.17%. This projection does not meet OMB's definition of significant improper payments ($10 million and 2.5 percent of total program payments).

Despite the lack of cited improper payments, FTA, in coordination with DOT's Office of Financial Management, will develop and distribute a Best Practices Guide (compiled from best practices identified within the Department's largest grant programs). Additionally, FTA will advise grantees regarding the importance of proper documentation maintenance for programmatic reviews and audits.

FAA Airport Improvement Program (AIP)

FAA executed the nationwide testing program using contractor personnel. The sample of tested line items originated from Federal disbursements to grantees within the twelve-month period April 1, 2009 through March 31, 2010.

The IPIA sampling methodology involved a multi-staged statistical approach that included the selection of 120 Federal disbursements totaling $190,184,028.22 and 240 line items from supporting invoices totaling $102,303,139.08. As in FY 2009, the Department designed the FY 2010 sample to extrapolate a nationwide estimate of improper payments and this sample does not support an estimate for individual states or airport sponsors.

After accounting for duplicate line items, improper payments totaling $1,312.10 were found in the sample of 219 tested items. The projection of known improper payments to the population of program payments for the twelve-month period results in an improper payment estimate of $1,313,317.36 +/- $1,425,670.47. The estimated improper payment rate is 0.03% +/- 0.04%. This projection does not meet OMB's definition of significant improper payments ($10 million and 2.5 percent of total program payments).

Reported improper payments resulted from non-systemic administrative, clerical, and documentation errors. FAA, in coordination with DOT's Office of Financial Management, will develop and distribute a Best Practices Guide for grantees in an effort to work towards a reduced programmatic improper payment rate. Additionally, FAA will advise grantees regarding the importance of proper documentation maintenance for programmatic reviews and audits.

PROGRAM	PY OUTLAYS (M)	PY IP%	PY IP $ (M)	CY OUTLAYS (M)	CY IP%	CY IP $ (M)	CY+1 EST. OUTLAYS (M)	CY+1 IP%	CY+1 IP $ (M)	CY+2 EST. OUTLAYS (M)	CY+2 IP%	CY+2 IP $ (M)	CY+3 EST. OUTLAYS (M)	CY+3 IP%	CY+3 IP $ (M)
FAA Airport Improvement Program	N/A	N/A	N/A	$4024	0.03%	$1.3	$3606	0.5%	$18.0	$3297	0.5%	$16.5	$2731	0.5%	$13.7
FHWA Highway Planning / Construction	N/A	N/A	N/A	$44187	1.40%	$616.8	$48010	1.0%	$480.1	$45238	1.0%	$452.4	$45087	1.0%	$450.9
FTA Capital Investment Grants Program	N/A	N/A	N/A	$3251	0.00%	$0.0	$2424	0.5%	$12.1	$2200	0.5%	$11.0	$2199	0.5%	$11.0
FTA Formula Grants Program	N/A	N/A	N/A	$8868	0.16%	$14.3	$9168	0.5%	$45.8	$8777	0.5%	$43.9	$9038	0.5%	$45.2

Recovery Audit

DOT's Recovery Auditor, Horn and Associates, worked to both recover identified departmental overpayments, and identify departmental payment process weaknesses. DOT granted Horn and Associates full access to the Department's financial system in order for Horn and Associates to efficiently review payment records.

The Recovery Auditor did not uncover or identify any departmental systemic payment process weakness as overpayments resulted from individual cases of duplicate payments, prompt payment interest payment errors, sales tax on utility billings, and open credits on statements.

Agency Component	Amount Subject to Review for CY Reporting	Actual Amount Reviewed and Reported CY	Amounts Identified For Recovery CY	Amounts Recovered CY	Amounts Identified for Recovery PY	Amounts Recovered PY	Cumulative Amounts Identified for Recovery (CY +PY)	Cumulative Amounts Recovered (CY +PY)
TOTAL	18,544,293,726	18,544,293,726	961,178	913,119	305,680	299,568	1,266,858	1,212,687

U.S. Department of Transportation

Office of the Secretary of Transportation

Assistant Secretary for Budget & Program Performance

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