PENNSYLVANIA DEPARTMENT OF TRANSPORTATION

By the Bureau of Public Transportation

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PENNSYLVANIA PUBLIC TRANSPORTATION AUDIT REQUIREMENTS

FOR

FIXED ROUTE, SHARED RIDE AND INTERCITY BUS TRANSPORTATION PROVIDERS

pennsylvania
DEPARTMENT OF TRANSPORTATION

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Background and Applicability

Background

Grantees providing fixed route and/or shared ride/specialized transportation and intercity bus transportation within the Commonwealth of Pennsylvania (Commonwealth or State) receive operating and capital grant funding from Pennsylvania's Department of Transportation (PennDOT or Department). Grantees use these grant funds to subsidize the operating and capital costs of providing transportation to the public. All grant agreements executed between PennDOT as the grantor and the transit provider as the grantee are governed by State legislation that was enacted in order to provide such funding. This legislation enables PennDOT to establish guidelines that sets financial policy with regard to the accounting and reporting for and management of State grant funds provided to grantees. Grantees are required to adhere to these regulations in order to continue receiving funds from the Commonwealth.

All grantees are required to have an annual audit performed by a certified public accounting firm (auditor) at the end of each fiscal year. This audit is to be performed in accordance with *Generally Accepted Government Auditing Standards* (GAGAS) and the financial statements in the audit, comprised of the Statement of Revenues, Expenses and Changes in Net Position, Statement of Net Position and Statement of Cash Flows, are to be prepared and presented in accordance with *Generally Accepted Accounting Principles* (GAAP). Furthermore, the financial statements are to include results for the year being audited and the prior year for comparative purposes. In addition, Notes to the Financial Statements and Other Information serving as Supplementary Information is to be included in the audit. As part of PennDOT's audit requirements, auditors are required to attest to the level of compliance with regard to the accounting and reporting procedures, internal financial controls, and the management of State grant funds pursuant to PennDOT regulations. This document is intended to provide guidance to all grantees and their auditors for the specific auditing, accounting, reporting, and grant management requirements related to State grant funds. The findings of the compliance review conducted by the certified accounting firm are to result in a report that is included as a separate section of the annual financial audit report. While the audit of grantee financial statements will incorporate the auditing, accounting, and reporting procedures required by PennDOT regulations, the PennDOT Grant Compliance Review will focus on compliance with State grant contract provisions and related PennDOT regulations.

The audit requirements for intercity bus operators differ from those of fixed route and specialized transportation service providers. Intercity bus operators and their auditors should make particular note to all program and audit requirements that pertain to these grantees throughout

this Publication. In particular, intercity bus grantees are required to have their accounting firms apply Agreed Upon Procedures – Intercity Bus Operators on the subsidized routes administered by PennDOT as described on page 45 of this Publication.

This Publication serves to identify the primary compliance requirements that PennDOT expects to be fulfilled as part of the annual audit of financial statements and the annual PennDOT Grant Compliance Review.

Applicability

Grantees receive various types of grant funding depending on the type(s) of transportation service that grantees provide. It is mandatory that auditors follow the applicable requirements of this Publication in the course of performing the annual financial statement audit and PennDOT Grant Compliance Review for any Pennsylvania grantee. Auditors shall consider this Publication and the referenced laws and regulations, and PennDOT communications (whether codified by PennDOT implementing the regulations or implemented by other means) in determining the compliance requirements that could have a direct and material effect on the programs included herein.

Update of Requirements

PennDOT is responsible for annually informing grantees of any updates made to this document. Grantees are expected to make sure their respective accounting firms have received these updates prior to the performance of an annual audit. However, auditors should recognize that laws and regulations change periodically and that delays will occur between such changes and revisions to this Publication. Moreover, auditors should recognize that there may be provisions of contract and grant agreements that are not specified in law or regulation and, therefore, the specifics of such may not be included in this Publication. For example, the grant agreement may specify a certain local matching percentage for which the grantee must be in compliance.

Accordingly, the auditor should perform reasonable procedures to ensure that compliance requirements are current and to determine whether there are any additional provisions of contract and grant agreements that should be covered by an audit. Reasonable procedures would be inquiry and review of the contract and grant agreements for programs selected for testing.

Safe Harbor Status

Auditor judgment will be necessary to determine whether the suggested audit procedures are sufficient to achieve the stated audit objectives or whether alternative audit procedures are needed. Therefore, the auditor should **not** consider this Publication to be a “safe harbor” for identifying the audit procedures to apply in a particular engagement.

However, the auditor can consider this Publication a "safe harbor" for identification of compliance requirements to be tested for the programs included herein if, as discussed above, the auditor performs reasonable procedures (1) to ensure that the requirements in this Publication are current and (2) to determine whether there are any additional provisions of contract and grant agreements that should be covered by an audit.

Responsibility for Other Requirements

Although the focus of this Publication is on compliance requirements that could have a direct and material effect on a major program, auditors also have responsibility under *Generally Accepted Government Auditing Standards* (GAGAS) for other requirements when specific information comes to the auditors' attention that provides evidence concerning the existence of possible noncompliance that could have a material indirect effect on a major program.

Internal Control

As a condition of receiving State grants, grantees agree to comply with laws, regulations, and the provisions of contract and grant agreements and to maintain internal control to provide reasonable assurance of compliance with these requirements. This Publication requires auditors to obtain an understanding of the grantee's internal control over State programs sufficient to plan the audit to support a low assessed level of control risk for major programs, plan the testing of internal control over major programs to support a low assessed level of control risk for the assertions relevant to the compliance requirements for each major program, and, unless internal control is likely to be ineffective, perform testing of internal control as planned.

Financial Statement Audit

Applicability

Any office, department, authority, agency, or company that delivers fixed route, demand response, shared ride and/or intercity bus operator in Pennsylvania and receives grant and/or contract funding from PennDOT for these or any other transportation programs and/or from any other Commonwealth department or agency for such transportation services is required to follow the auditing, accounting and reporting requirements contained in this section.

Audit Requirements

REGULATION TITLE: Timing and Performance of Audit

OBJECTIVE: Ensure the timely and professional performance of the financial statement audit

COMPLIANCE REQUIREMENT: All grantees are required to have an annual financial audit performed by a certified public accounting firm at the end of each fiscal year. The audit shall be submitted to PennDOT within six months of the conclusion of each fiscal year.

REGULATION TITLE: Audit Standards

OBJECTIVE: Ensure consistency in all grantee financial audits and the use of standard auditing procedures.

COMPLIANCE REQUIREMENT: The financial audit is to be performed in accordance with GAGAS. Auditors are required to attest to the use of these standards in their audit opinion letter.

Accounting and Reporting Requirements

REGULATION TITLE: Accounting and Reporting Standards

OBJECTIVE: Ensure consistency in all grantee financial audits and the use of standard accounting and reporting conventions.

COMPLIANCE REQUIREMENT: Financial statements are to be prepared and presented in accordance with *Generally Accepted Accounting Principles* (GAAP). Auditors are required to attest to the level of compliance with GAAP accounting and reporting procedures in their audit opinion letter.

REGULATION TITLE: Management Discussion and Analysis (MD&A)

OBJECTIVE: Ensure grantee understanding of, preparation of, communication of, and accountability for annual financial statements.

COMPLIANCE REQUIREMENT: Grantees are solely responsible for the preparation of their financial statements that are then subject to an independent review, examination, and audit by a certified public accounting firm. In addition, each annual financial audit shall include a section entitled "Management Discussion and Analysis" which shall be prepared by grantee management. At a minimum, the MD&A section will include text related to the results of operations for the fiscal year under audit and the changes in financial and operational activity from the prior fiscal year. Auditors are required to clearly disclose a grantee's inability to independently fulfill these requirements.

These requirements are intended to provide a narrative of management's explanation of the grantee's financial statements. In addition to the auditor's findings, the MD&A enhances the overall financial disclosure and provides the context within which the grantee's management analyzes its financial results.

In addition to analyzing the results and changes in financial and operational activity, management may provide information with regard to financial and operational performance indicators as well as trends, demands, commitments, events and uncertainties that are reasonably likely to have a material effect on the grantee's financial condition or operating performance.

REGULATION TITLE: Revenue Recognition and Restricted Cash Classification

OBJECTIVE: Ensure that financial statements properly represent (1) the ***use*** of all government subsidies as non-operating subsidy revenue and (2) ***unused*** subsidies that are carried over to the following year as deferred revenue for future use, restricted for a particular purpose(s).

COMPLIANCE REQUIREMENT: PennDOT classifies State and Federal operating and capital grants that are provided to grantees in the Commonwealth, along with matching contributions from local municipalities, as a non-exchange transaction. In the case of grantees, non-exchange transactions involve the grantees' receipt of a grant(s) without the grantees giving equal value in return. However, in the event that a grantee ceases operations and the entity is dissolved, the grantee is obligated to return all unused/remaining grant funds to the original Federal, State or local grantor.

PennDOT classifies Federal, State and local operating and capital grant funds for public transportation as *government-mandated non-exchange transactions*. Although each grant requires a grantee to use funds for a restricted purpose (operating or capital expenditures incurred in the delivery of public transit service), there are time and eligibility requirements that dictate the timing of revenue recognition of these grant funds.

Timing Requirements and Purpose Restrictions

There are two kinds of stipulations on the use of resources – purpose restrictions and time requirements. Different standards apply for each stipulation:

> *Purpose restrictions* specify the purpose for which grant funds are required to be used. Although purpose restrictions should result in the reporting of restricted net assets, equity or fund balance, purpose restrictions should not affect when such funds are recognized.
>
> *Time requirements*, however, specify the period(s) when grant funds are required to be used or when use may begin (i.e. operating and capital grants for a specific period). Time requirements affect the recognition of non-exchange transactions and their related grant funds.

For all Federal and State grants, along with associated local matching contributions, when there are both purpose restriction ***and*** timing requirements, ***timing requirements take precedent***. Therefore, timing requirements for when grant funds are required to be used dictate when the grant funds are recognized as revenue.

Federal and State *Operating* Grants and Associated Local Match Contributions

Grantees are to recognize operating grant subsidies ***when all applicable eligibility requirements are met***. Eligibility requirements are dictated by both the nature of the grant application and approval process, the resulting executed grant agreement, the timing of when eligible operating expenses are incurred and the timing of when operating grant funds are used to subsidize such expenses.

Grantees in the Commonwealth that provide fixed route public transit service apply for operating assistance each year for the upcoming fiscal year. Operating funds that are granted directly by PennDOT and by PennDOT on behalf of the Federal Transit Administration (FTA) are administered through PennDOT and are part of PennDOT's single operating grant application process. The application process requires grantees to submit a ***balanced*** operating budget. A balanced

operating budget consists of the projected needed amount of operating grant subsidy[1] that would equal the operating loss resulting from expenses exceeding revenue. No surplus or deficit of funds, after the use of such grants, can be shown as part of the operating grant application process in order for the operating grant to be approved.

Once PennDOT has approved a grantee's operating grant application, an operating grant agreement is executed with the grantee. Contained in the operating grant agreement is the amount of State funds that will be distributed to the grantee during the fiscal year. Also stipulated in the operating grant agreement is the minimum matching contribution amount that the grantee is required to obtain from its local contributor(s). Although the grantee may receive State and local funds (and possibly Federal funds) in a particular year pursuant to the operating grant agreement for said year, such funds can only be used to fund ***eligible operating expenses***. Operating expenses only become eligible for subsidization ***once the expense has been incurred***. Once grant funds have been used to subsidize eligible operating expenses for the current fiscal year, any operating grant funds[2] received in excess of grant funds used to subsidize the current year's eligible operating expenses ***are required to be classified as deferred revenue and used in subsequent fiscal years***.

A balanced operating budget requirement is paramount to the operating grant approval process. Grantees' actual financial results at the end of the fiscal year should reflect either a balanced operating result or an operating surplus.[3] Any unused/excess operating grant funds[4] that were received during the year ***are to be classified as deferred revenue since the timing requirement of eligible operating expenses was not met for this portion of the grant funds that were received during the year***.

Interest/Investment Income on Funds from Federal and State Operating Grants, Pennsylvania Transportation Assistance Fund (PTAF), Act 3 of 1997 (Act 3) and Local Match Contributions

Grantees are directed to ***not*** report any interest/investment income generated from the above referenced grant funds and used towards operating expenses as interest/investment income on

[1] Total operating grant subsidy can include both the estimated operating grant allocation for the current year plus the anticipated use of eligible prior year operating grant reserves in order to fully cover the projected operating loss.
[2] Limited to State funds only for the majority of Pennsylvania public transportation grantees. See "Timing Use of Local Matching Contributions – Operating Funds".
[3] Agencies are permitted to show an unbalanced operating result (operating deficit) if it can demonstrate that the deficit is being funded from balance sheet transactions such as, but not limited to, accumulated retained earnings or cash proceeds from loans or line of credit drawdowns. Such assumptiions should be stipulated as part of the grant application.
[4] Limited to State funds only for the majority of Pennsylvania public transportation grantees. See "Timing Use of Local Matching Contributions – Operating Funds".

the audited Statement of Revenues, Expenses, and Changes in Net Position. Interest earnings on these grant funds that are used are considered part of subsidy revenue and are to be reported as such on the audited Statement of Revenues, Expenses, and Changes in Net Position.

The basis for this guidance is that accumulated interest earned on these grants is accounted for and treated as an incremental part of the grant subsidy fund balance available for use. Similar to the State grants and local matching contributions that generated the interest income, interest earnings received are classified as deferred revenue until used. At the time of usage, any interest earnings are recognized on the audited Statement of Revenues, Expenses, and Changes in Net Position as non-operating subsidy revenue. Therefore, subsidy funds that are used consist of used grant funds and used interest earnings generated from such grant funds. All other earnings, including interest related to Non-Fixed and Non-Public transportation activity, should be reported as interest income on the audited Statement of Revenues, Expenses, and Changes in Net Position because they were generated from non-grant funds or from State or local funds that were provided on a trip reimbursable cost basis.

Federal and State Capital Grants and Associated Local Match Contributions

Over the years, due to changes in State legislation, the timing of the distribution of capital grant funds to grantees has differed. This has resulted in differences in grant revenue recognition.

PTAF and Act 3

Act 26 of 1991 (Act 26) included the distribution of State capital grant funding to eligible grantees from PTAF and Act 3, providing similar funding to grantees. Act 3 provided grantees with Base Supplemental Grant (BSG) and Additional Supplemental Grant funds. Both PTAF and Act 3 grant programs required local matching capital funds. Both grant programs distributed State grant funds to grantees prior to or in the fiscal year in which eligible capital project expenditures were incurred.[5] Capital expenditures become eligible once the expenditure has been incurred. Once grant funds have been used to subsidize eligible capital expenditures for the current fiscal year, any capital grant funds in excess of grant funds that were received to subsidize the current year's eligible capital expenditures are required to be classified as deferred revenue and used in subsequent fiscal years.

As grantees incurred expenditures during the year for capital projects that were approved by PennDOT, these capital expenditures became eligible to be subsidized through the use of these capital grant funds and such capital grants should therefore be recognized in the same fiscal year

[5] See page 34 for Restricted Use of State Act 3 BSG and ASG Grants and Associated Local Matching Contributions with regard to the application of such funds towards operating funds for Urban and Rural transit agencies.

to the extent of the amount of grant funds that are used to subsidize the capital expenditures. Any remaining unused capital grant funds that were received during the year are to be classified as deferred revenue since the timing requirement of eligible capital expenses was not met for this portion of the grant funds.

Federal Capital Grants, State Capital Bond Grants, and Act 44 of 2007

With the enactment of Act 44 of 2007 (Act 44), the way grantees were funded for capital projects changed. Grantees no longer receive capital grant funding (i.e., PTAF) in advance of the capital expenditures being incurred for projects that were approved by PennDOT. Similar to the FTA's distribution of capital funds for eligible capital expenditures, the State distributes capital grant funds for projects under the discretionary capital bond program and under Act 44 after eligible capital expenditures are incurred. Recognition of the capital grant therefore occurs in the year in which the grant distribution is received or accrued.

Classification of Restricted Cash

In cases where there are unused/remaining Federal, State, or local operating and/or capital grant funds, such grant funds are to be classified as restricted cash separately by grant program and by funding source and are to be classified as deferred revenue.

REGULATION TITLE: Statement of Revenues, Expenses, and Changes in Net Position

OBJECTIVE: Ensure that the grantee is presenting its Statement of Revenues, Expenses and Changes in Net Position are in accordance with PennDOT accounting and reporting requirements.

COMPLIANCE REQUIREMENT: Grantees are to include in their annual audits a Statement of Revenues, Expenses, and Changes in Net Position presented in a reporting format that has been established by PennDOT. This format is in accordance with GAAP and is consistent across all grantees in the Commonwealth.

Auditors are instructed not to deviate from the reporting standard described in this document (line item summarizations, line item reclassifications, etc.).

Auditors are cautioned to pay close attention to all reporting classifications as specific conditions exist on some of these classifications and transaction testing must occur to confirm that these conditions are being met.

Auditors are to ensure that all amounts are consistently and correctly reported in all PennDOT supporting schedules in accordance with the guidance provided in this document and in, depending on the type of grantee, PennDOT's *Financial Reporting Manual for Urban and Rural*

Fixed Route Transportation Providers, Financial Reporting Manual for Shared Ride and Specialized Transportation Providers or Financial Reporting Manual for Intercity Bus Operators.

The required format and content of the Statement of Revenues, Expenses, and Changes in Net Position is shown and described below:

Required Format for

STATEMENT OF REVENUES, EXPENSES, and CHANGES IN NET POSITION

	FYXX-XX	FYXX-XX
Operating Revenue:		
Passenger fares		
Charter		
Route Guarantees		
State Medical Assistance Transportation Program		
State Shared Ride Program		
State Welfare to Work Program		
State Persons with Disabilities Program		
Area Agency on Aging		
Mental Health/Intellectual & Developmental Disabilities		
Other contract revenue		
Advertising		
Miscellaneous income		
Total operating revenue		
Operating expenses:		
Salaries and Wages		
Fringe Benefits		
Services		
Fuel & Lubricants		
Tires & Tubes		
Other Materials & Supplies		
Utilities		
Casualty & Liability		
Taxes		
Purchased Transportation		
Leases and Rentals		
Miscellaneous expense		
Depreciation		
Total operating expenses		
Loss from Operations		
Non-operating revenue/(expenses):		
Capital funds used for operating assistance and planning grants:		
Federal government		
Commonwealth of Pennsylvania		
Local governments		
Operating grants:		
Federal government		
Commonwealth of Pennsylvania Act 44 Funds		

Local governments Act 44 Matching Funds
Other Commonwealth and Local operating funds

Total government subsidies for operations

Other private/public sources
Interest income
Gain/(loss) on disposal of capital assets
Interest expense

Total non-operating revenue/(expenses)

Loss before capital grant funding

Capital grant funding:
Federal
State
Local

Total capital grant funding

Increase/(decrease) in net position

Net Position at Beginning of Year

Net Position at End of Year

Note that the financial statement above as well as the Statement of Net Position is to reflect financial results for both the year being audited as well as results for the prior year. The applicability of each line item above will vary between grantees particularly fixed route transportation providers compared to stand alone shared ride/specialized transportation providers. Grantees are not expected to include those items that have no activity.

Line Item Definitions

Guidance on the content of each line of the Statement of Revenues, Expenses, and Changes in Net Position follows:

Operating Revenue

Passenger Fares

Passenger fares are revenues earned and collected from carrying passengers. They are the amounts paid by the rider, in the form of cash, tokens, and tickets, to use transit services and amounts paid as special transit fares. Special transit fares are fares from contracts to the grantee in which a grantee or organization pays a set amount in return for unlimited transit service for the persons covered by the contract. Fare revenue that is billed to and paid by any sponsoring agencies or revenue received as part of a fare reimbursement program administered by the Commonwealth or third party grantee sponsor ***is not*** included as part of passenger fares.

Passenger fares may include special programs such as reduced passes or ticket prices for students, the elderly or individuals with disabilities. However, passenger fares reflect the amount of the fare that the passengers pay on their own behalf.

Passenger fares may be collected in several ways, including:

- Before service is provided (e.g., through the sale of media such as passes, tickets and tokens sold to passengers)
- Directly at the point of service (e.g., farebox, turnstile)
- After the service is provided, (e.g., through weekly or monthly billing).

Passenger fares do not include contract revenue, grants, subsidies, or passenger fare assistance from other entities, such as governments to provide a reduced fare or free fare. Grants and subsidies are provided to support the general provision of transit service and are reported as non-operating revenue that is discussed later.

Charter

Charter revenue is revenue earned from operating vehicles under charter contracts.

Route Guarantees

Route guarantees are conditional commitments, either express or implied, by a private or public entity to a local transportation organization to provide financial compensation in return for the provision of public transportation service to a designated area or destination which can only be served with financial compensation.

State Medical Assistance Transportation Program

Medical Assistance Transportation Program (MATP) revenue reflects contract revenue received from MATP for various modes of transportation trips provided to eligible MATP clients by the grantee or its subcontractors under the program. In addition, this amount is to include funds that the grantee receives from MATP (1) as mileage reimbursement for payment to MATP patrons for the use of personal vehicles and (2) for the reimbursement of costs which the grantee incurred to administer the program.

State Shared Ride Program

Shared Ride Program revenue represents the amount of fare reimbursement revenue received from the Pennsylvania State Lottery Program for trips taken by passengers that are age 65 or older.

State Welfare to Work Program

The Welfare to Work (WTW) Program includes fare reimbursement or contract revenue received from the program for all passenger trips provided by the grantee under this program. In addition, this amount is to include funds received from the WTW program for the reimbursement of costs which the grantee incurred to administer the program.

State Persons with Disabilities Program

Revenue received from the Persons with Disabilities (PwD) Program represents the amount of fare reimbursement or contract revenue received for passenger trips provided by the grantee under the PwD program.

Area Agency on Aging

Area Agency on Aging (AAA) revenue reflects fare reimbursement or contract revenue received from AAA for passengers who received trips under the program.

Mental Health/Intellectual & Developmental Disabilities

Revenue received from the Mental Health/Intellectual Developmental Disabilities (MH/ID) Program represents the amount of fare reimbursement or contract revenue received for passenger trips provided by the grantee under the MH/ID Program.

Other Contract Revenue

Contract revenue received from any other third party.

Advertising

Advertising revenue is revenue earned from displaying advertising materials on grantee vehicles and property. The amounts should be net of any fees paid to advertising agencies, which place the advertisement with the grantee.

Miscellaneous income

Revenue derived from other miscellaneous sources include, but are not limited to, rental income, concession income, refund or distribution of insurance premiums, etc.

Operating Expenses

Salaries and Wages

Salaries and wages are the labor expenses for a grantee's employees.

Fringe Benefits

Fringe benefits are expenses for employment benefits or services that an employee receives in addition to his/her basic wages. These payments are the grantee's costs over and above direct

labor costs, but still arising from the employment relationship. Typical benefits include contributions to or providing:

- Retirement plans
- Pension plans
- Medical plans
- Dental plans
- Life insurance and short-term disability plans
- Employer payroll taxes
- Unemployment insurance
- Workers' compensation insurance
- Sick leave
- Holiday leave
- Vacation (and other paid leave such as bereavement leave, jury duty)
- Uniform and work clothing allowances typically for drivers and security personnel
- Tool allowances for mechanics

Services

Services include management services, professional services, and temporary labor services for personnel who are not employees of the grantee, the governmental body, or the multifunctional organization. Services are expenses for the labor and other work provided by outside organizations for fees and related expenses.

Some grantees are organized as a department of local government, or as part of a multifunctional organization. If the grantee is organized this way, the grantee is not deemed to purchase services from other parts of the governmental entity or multifunctional organization. Therefore, the grantee should not report these costs as Service expenses. Instead, the grantee should report all expenses for activities pertaining to the transit services, but performed by other departments or offices within the governmental or multifunctional entity, in the appropriate operating expense. For example, if the grantee is a department of a county government and the county highway department maintains the transit vehicles, the highway department's maintenance labor expenses are to be classified as Salaries and Wages and fringe benefit costs as Fringe Benefit expenses.

Fuel & Lubricants

Fuel and lubricants are the costs of items such as gasoline, diesel fuel, propane, lubricating oil, transmission fluid, and grease for use in vehicles. Taxes levied on fuel and lubricants and paid

by the grantee are not to be classified as part of Fuel and Lubricants but instead are to be classified as Taxes as described below.

Tires & Tubes

Tires and tubes are the lease payments for tires and tubes rented on a time period or mileage basis or the cost of tires and tubes for replacement of tires and tubes on vehicles.

Other Materials and Supplies

Other materials and supplies are the costs of materials and supplies not previously identified. These materials and supplies may be issued from inventory or purchased for immediate consumption and include items such as office supplies and parts used to repair revenue and service vehicles.

Utilities

Utilities costs cover payments made to utility companies for the purchase of utility or related services. Utilities include propulsion power used for electrically driven vehicles, electric power for other uses, water and sewer, natural gas and other fuels for heating, telephone and garbage collection.

Casualty and Liability Costs

Casualty and liability costs are expenses related to losses incurred by the grantee including the costs of loss protection. These expenses include compensation of others for their losses due to acts for which the grantee is liable, the costs of protecting the transit grantee from losses through conventional insurance and other risk financing programs (e.g., self insurance, pools) and grantee losses due to the liable actions of others that are covered by other corporate insurance.

Casualty and liability costs include:

- Physical damage insurance premiums
- Recovery of physical damage losses for public liability and property damage insurance premiums
- Insured and uninsured public liability and property damage settlement pay outs and recoveries, and
- Other corporate insurance premiums (e.g., fidelity bonds, business records insurance)

Taxes

Taxes are the charges and assessments levied against the grantee by Federal, State and local governments.

Expenses include:

- Income taxes
- Property taxes
- Fuel and lubricant taxes
- Electric propulsion power taxes
- Vehicle licensing and registration fees

This classification should not include:

- Sales and excise taxes on materials and services purchased other than fuel and lubricants. Grantees should report these as part of the base price of the material in Other Materials and Supplies or service in Services.
- Rebates and reimbursements of taxes as a credit against an operating expense. Such transactions should be included as rebates and reimbursements paid as revenue and classified as Miscellaneous Income.

Purchased Transportation Service

Purchased transportation (PT) services are expenses, including MATP mileage reimbursement costs, incurred and billed by PT providers (sellers) in the operation of the contracted transit services identified. The PT services expense classification is not included in the expenses associated with directly operated services.

The PT service expense is for the buyer of PT service and covers the payments or accruals made to the PT provider. This expense classification does not include:

- Expenses incurred by an grantee in support of the PT services - for example, salaries and wages of grantee personnel administering or working in some capacity in support of the agreement, fuel and tires if provided to the seller, vehicle maintenance, marketing, advertising, legal services, and ticket sales. These are other costs incurred by the grantee and are classified in the appropriate expense categories.

- Depreciation and lease costs for vehicles and facilities. In some instances, PT providers provide the revenue vehicles as part of their contract and/or the purchased transportation provider operates the service from its own maintenance facility. In these cases, if the PT provider charges total costs - either in absolute dollars and unit charges (e.g., per mile or per trip), the grantee must separate operating costs from any lease and depreciation costs.

Leases and Rentals

Leases are payments for the use of capital assets not owned by the grantee. Leases and rentals are true leases and cover the total cost of the capital asset plus interest.

Leasing often covers two types of costs:

- Capital equipment lease costs
- Operating and maintenance costs

All leases and rental costs are to be included regardless of whether State operating or eligible capital grant funds were used to pay for these costs pursuant to grant regulations.

When reporting leases, costs associated with operating or maintaining the equipment must be segregated from the costs associated with leasing capital equipment. Operating and maintenance costs are to be reflected in the appropriate expense classifications. Only the cost of leasing the capital equipment should be included under Leases and Rentals.

Also included in leases are Purchase Lease Agreements and Related Parties Lease Agreements. Purchase lease agreements are financing transactions, agreements, contracts, or structures that enable a grantee to acquire (own) the capital asset at the end of the lease, sometimes with an additional payment due. The property covered by such leases may or may not have been recorded as owned assets, either during or after the period of the lease, in the grantee's internal accounting records. If purchase leases have not been capitalized in the grantee's internal accounting records, this category includes the lease payments for the purchase lease agreement.

Related parties leases are leases where the terms and amount of payments by the grantee are substantially less than in a true lease because the grantee is related to the lessor. For example, a grantee may lease surplus equipment from another grantee or local government.

Miscellaneous Expenses

Miscellaneous expenses are expenses that cannot be classified in the other expenses that have been discussed.

Miscellaneous expenses include, but are limited to:

- Dues and subscriptions
- Travel and meeting expenses
- Bridge, tunnel and highway tolls
- Entertainment expenses

- Charitable donations
- Fines and penalties
- Bad debt expense
- Advertising and promotion expenses
- Incidental transit services.

Depreciation

Depreciation reflects the loss in service value of the grantee's capital assets. As capital assets, depreciated items have a high initial cost and a useful life of more than one year. To reflect the consumption or use of the asset over its service life, a portion of the asset's cost is expensed each year.

Non-operating revenue/(expenses)

Capital Funds Used for Operating Assistance and Planning Grants

Federal Government

Amounts reflected in this classification include the amount of Federal capital subsidies that are ***used*** to fund eligible expenditures such as preventive maintenance costs, capital cost of contracting, and associated capital maintenance costs. The use of Federal planning grants is also included in this classification.

Commonwealth of Pennsylvania

Amounts reflected in this classification include the amount of State capital subsidies that are ***used*** to fund eligible expenditures such as those used to match Federal funds that were applied to preventive maintenance costs, capital cost of contracting, and associated capital maintenance costs. Auditors must use caution if a grantee is reporting the use of capital funds in this classification if the source of funds that was used was Act 44 Sections 1514, 1515, 1516, or 1517. A waiver to use these Commonwealth funds in this manner must be provided and pre-approved by PennDOT. In addition, auditors should be informed that grantees with remaining PTAF and Act 3 ASG balances are permitted to use these funds towards leases and rentals including lease agreements for tires and tubes.

The use of State planning grants is also included in this classification.

Local Governments

Amounts reflected in this classification include the amount of local capital subsidies that are ***used*** to fund eligible expenditures such as those to match the use of Federal funds that were applied to preventive maintenance costs, capital cost of contracting, and associated capital maintenance costs. Auditors must use caution if a grantee is reporting the use of local capital

matching contribution funds in this classification if the match is for the State source of funds that was used under Act 44 Sections 1514, 1515, 1516, or 1517. A waiver to use these local matching contribution funds in this manner must be provided and pre-approved by PennDOT. In addition, auditors should be informed that grantees with remaining local PTAF and Act 3 ASG balances are permitted to use these funds towards leases and rentals including lease agreements for tires and tubes.

The use of local planning grants is also included in this classification.

Operating Grants

Federal Government
Amount reflects Federal operating assistance funds (i.e. Federal 5311) that the grantee ***used*** towards eligible operating expenses.

Commonwealth of Pennsylvania Act 44 Funds
Amount reflects State Act 44 Section 1513 funds that the grantee ***used*** towards eligible operating expenses.

Local governments Act 44 Matching Funds
Amount reflects local matching contribution funds to State Act 44 Section 1513 funds that the grantee ***used*** towards eligible operating expenses.

Other Commonwealth and Local Operating Funds
Amounts reflect all other State and local operating funds that the grantee ***used*** towards eligible operating expenses.

Other private/public sources
Amount reflects all other private and public funds not previously mentioned that the grantee ***used*** towards eligible operating expenses.

Interest income
Interest income is money received by grantees from banks and financial institutions for deposits that the grantee makes and the balances that it keeps in its accounts throughout the year, including interest/investment income that is received from all fare reimbursement grants /contracts and capital funding sources and balances (i.e. passenger fares, Federal, State and local and capital subsidies).

Auditors are cautioned to pay particular attention to how interest income is reported on the audited Statement of Revenues, Expenses, and Changes in Net Position and on PennDOT's

supporting schedules in accordance with guidance provided in interest/investment income on page 9.

Gain/(loss) on disposal of capital assets

Amount represents the gain or loss on asset dispositions.

Auditors are cautioned to pay particular attention to transactions regarding the gain/loss on asset dispositions. Agencies and their accounting firms must ensure that the asset has reached the end of its useful life and was fully depreciated prior to its disposal. Agencies and their accounting firms should confirm that they are each using PennDOT's Estimated Useful Life asset list. This list can be accessed on PennDOT's website by searching for "Estimated Useful Life" in the search box at the top of PennDOT's homepage located at www.penndot.gov. If this condition is met, all proceeds, including any resulting gain from the transaction, may be used towards operating costs and/or capital expenditures along with the condition that the cost was incurred for the purpose of providing public transportation.

If the agency disposed of the asset prior to the end of its useful life and prior to being fully depreciated, PennDOT approval must be obtained prior to the disposal of the asset.

A loss on an asset disposal immediately raises the issue that the asset was retired prior to the end of its useful life and was not fully depreciated. In this case, agencies should be prepared to provide documentation that prior approval was obtained from PennDOT to dispose of the asset prior to the end of its useful life or that the asset was retired prematurely retired due to other reasons (i.e. accident making the asset unusable for service).

Capital Grant Funding

Federal

Amount reflects Federal capital funding that is ***used*** towards capital expenditures.

State

Amount reflects State capital funding that is ***used*** towards capital expenditures.

Local

Amount reflects local capital matching contributions to Federal and State capital funds that are ***used*** towards capital expenditures.

REGULATION TITLE: PennDOT Supplementary Schedules (Legacy budget reports and schedules)

OBJECTIVE: Ensure that the grantee is including in the audit report the required reports and schedules generated from PennDOT's dotGrants financial reporting system and that this information t is consistent and properly reconciled with the financial statements in the audit.

COMPLIANCE REQUIREMENT: Grantees are to include, as supplementary schedules to the annual financial statement audits, the legacy budget reports submitted in dotGrants for the same fiscal year's financial activity. Reports and schedules to be provided, where applicable to the reporting grantee, include:

Fixed Route Grantees

- Expense Reports
  - Fixed Route Expenses
  - Non-Fixed Route ADA Paratransit Expenses
  - Non-Fixed Route Shared Ride Expenses - Standard Service
  - Non-Fixed Route Demand Response Expenses – Department Approved Service
  - Non-Fixed Route Public Vanpool Expenses
  - Non-Public Expenses - Other Transportation
- Revenue Reports
  - Fixed Route Revenue
  - Non-Fixed Route Revenue
  - Non-Public Revenue - Other Transportation
- Subsidy Reports
  - Fixed Route Subsidies
  - Non-Fixed Route Subsidies
- Budget Summary
- Schedules
  - S1 - Local Match Provided
  - S2 - Local Match Carryover
  - S3 and S4 - Urban and Rural PTAF/BSG/ASG Carryover
  - S5 - Urban and Rural Section 1513 Program Carryover
  - S6 - Shared Ride Expense Allocation Worksheet
  - Shared Ride Retained Earnings

Stand alone Shared Ride/Specialized Transportation Grantees

- Expense Reports
  - Shared Ride Expenses
  - Non-Public Other Transportation Expenses
- Revenue Reports

    - Shared Ride Revenue
    - Non-Public Other Transportation Revenue
- Subsidy Reports
    - Shared Ride Subsidies
- Budget Summary
- Schedules
    - Local Match Provided
    - Shared Ride Expense Allocation Worksheet
    - Shared Ride Retained Earnings

Intercity Bus Grantees

- Expense Reports
    - Intercity Bus Expenses - report for each route
- Revenue Reports
    - Intercity Bus Revenue - report for each route
- Subsidy Reports
    - Intercity Bus Subsidies - report for each route
- Budget Summary
- Schedules
    - Schedule A5 - Intercity Bus Expense Allocation Worksheet
    - Schedule A6 - Intercity Bus Operating Assistance
    - Schedule A7 - Route Financial Statement - schedule for each route
    - Schedule A7 - Consolidated Financial Statement - All Routes

Auditors are expected to possess a detailed knowledge of the financial reporting requirements as stipulated in PennDOT's *Financial Reporting Manual* that are applicable to the grantee that govern the reporting standards of these reports and schedules. Both the grantee and its auditor must ensure that the accounting firm's audit opinion applies to these reports and schedules in a consistent manner as it applies to the grantee's audited financial statements. Furthermore, the accounting firm's audit opinion must include language stating that these reports and schedules were subjected to the same transaction testing that was conducted as part of the overall audit.

State Grant Compliance Review

Applicability

Any office, department, authority, grantee or company that delivers fixed route, demand response, shared ride/community transportation and/or intercity bus service in Pennsylvania and receives grant and/or contract funding from PennDOT and/or any other Commonwealth department or grantee for such transportation services is required to follow the auditing and compliance requirements contained in this section. The auditing requirements should be applied to the overall State Grant Compliance Review while the grant management requirements should be applied to the specific State related programs identified in this section.

Audit Requirements

REGULATION TITLE: Timing and Performance of Audit

OBJECTIVE: Ensure the timely and professional performance of the financial statement audit

COMPLIANCE REQUIREMENT: All grantees are required to have an annual State Grant Compliance Review performed by a certified public accounting firm at the end of each fiscal year. The audit shall be submitted to PennDOT within six months of the conclusion of each fiscal year and shall be submitted with the annual financial statement audit.

REGULATION TITLE: Audit Standards

OBJECTIVE: Ensure consistency in all grantee financial audits and the use of standard auditing procedures.

COMPLIANCE REQUIREMENT: The financial audit is to be performed in accordance with GAGAS. Auditors are required to attest to the use of these standards in their audit opinion letter.

Grant Management Requirements

This section identifies each PennDOT grant program and contains the grant management compliance requirements that apply to each of them.

PROGRAM: Shared Ride Lottery Program

REGULATION TITLE: Receipt of State Grant Funds

AUDIT OBJECTIVE: Ensure that State plus any recorded accounts receivable for uncollected funds are confirmed and consistent with executed grant agreements. Also ensure that funds are deposited and held in an interest bearing account(s) until used.

COMPLIANCE REQUIREMENTS: Grantees must execute annual grant agreements with PennDOT in order to obtain funds to be used towards eligible operating expenses. The following requirements related to the amount:

State Grants Received:

State grant funds received, plus any amount established as an accounts receivable that were due from PennDOT at the end of the fiscal year, must be consistent with the amount of State funds to be granted pursuant to an executed grant agreement. This amount must agree with the amount reported on the Statement of Revenues, Expenses and Changes in Net Position. Any accounts receivable that were established for any amount of State funding that the grantee did not receive during the fiscal year must also be clearly and fully disclosed.

SUGGESTED AUDIT PROCEDURES

Confirm receipt and proper accounting treatment for State grants funds by:

1. Confirming State grant funds actual cash amounts received plus any recorded accounts receivable for the audit period's invoices.
    a. State grant amounts should be compared to, and be consistent with, the sum of all transactions recorded in the grantee's accounting system as well as agree with amounts reflected on the Statement of Revenues, Expenses and Changes in Net Position.
    b. Cash amounts received from PennDOT should be confirmed with actual bank records (bank statements, deposit slips, wire transfers, automatic clearing house transactions (ACH), etc.) Any recorded accounts receivable for the audit period must either be confirmed by identifying the payment clearing the receivable in the subsequent fiscal year or confirmed with PennDOT if payment had not yet been received in the next fiscal year.
2. Confirm that State grant funds are deposited and held in an interest bearing account(s) until used.

PROGRAM: Act 44 Section 1513 Operating Grants

REGULATION TITLE: Receipt of State Grant Funds and Required Local Matching Contributions

AUDIT OBJECTIVE: Ensure that State and local matching contributions, plus any recorded accounts receivable for uncollected funds, are confirmed and consistent with executed grant agreements. Also ensure that funds are deposited and held in an interest bearing account(s) until used and that interest income is separately recorded and accounted for to segregate interest earnings generated from State versus local matching contributions on PennDOT's supporting Schedule S5 – Section 1513 Program Carryover as shown in PennDOT's *Financial Reporting Manual for Urban and Rural Fixed Route Transportation Providers*.

COMPLIANCE REQUIREMENTS: Grantees must execute annual grant agreements with PennDOT in order to obtain funds to be used towards eligible operating expenses. The following requirements related to the amount and source of local matching contributions must be satisfied during the course of an audit:

State Grants and Local Matching Contribution Amounts Received:

1. State grant funds received, plus any amount established as an accounts receivable that were due from PennDOT at the end of the fiscal year, must be consistent with the amount of State funds to be granted pursuant to an executed grant agreement. Any accounts receivable that were established for any amount of State funding that the grantee did not receive during the fiscal year must also be clearly and fully disclosed.
2. The required local matching contributions received during the fiscal year must equal, or exceed, the amount stipulated in the executed grant agreement with PennDOT. The required local matching contributions must be received by the grantee by the end of the fiscal year. Auditors are required to fully disclose any and all occurrences when the minimum required amount of local matching contributions were not received by the grantee during the fiscal year. Furthermore, any accounts receivable that were established for the uncollected amount of local matching contribution must also be clearly and fully disclosed.
3. Both State grant funds and local matching contributions received, plus any applicable accounts receivable, must be consistent with the amounts reported on PennDOT's supporting Schedule S1 –Local Match Provided (Act 44 Section 1513 Local Match for Operating Funds Received) and Schedule S5 – Section 1513 Program Carryover as shown in PennDOT's *Financial Reporting Manual for Urban and Rural Fixed Route Transportation Providers*.

4. Both State and local grant funds must be deposited and held in interest bearing accounts until used. Interest earned on State and local grant funds is to be reported separately on PennDOT's supporting Schedule S5 – Section 1513 Program Carryover as shown in PennDOT's *Financial Reporting Manual for Urban and Rural Fixed Route Transportation Providers*. All interest earnings become part of the respective State and local fund balances and are reported as part of the respective State and local subsidy revenue only when the respective fund balances, or portions thereof, are used towards eligible operating expenses.

SUGGESTED AUDIT PROCEDURES

Confirm receipt and proper accounting treatment for State grants funds and required local matching contributions pursuant to executed grant agreement by:

1. Obtaining a copy of the executed grant agreement from the grantee
2. Comparing State grant funds and required local matching contributions in the agreement with actual cash amounts received plus any recorded accounts receivable to ensure consistency.
    a. State grant and required local matching contribution amounts shown in the executed grant agreements should be compared to, and be consistent with, the sum of all transactions recorded in the grantee's accounting system as well as agree with amounts reflected on PennDOT's supporting Schedule S1 –Local Match Provided (Act 44 Section 1513 Local Match for Operating Funds Received) and Schedule S5 – Section 1513 Program Carryover as shown in PennDOT's *Financial Reporting Manual for Urban and Rural Fixed Route Transportation Providers*.
    b. Cash amounts received from PennDOT and local contributors should be confirmed with actual bank records (bank statements, deposit slips, wire transfers, automatic clearing house transactions (ACH), etc.) Any recorded accounts receivable must be confirmed with PennDOT and local contributors.
3. Confirm that both State and local grant funds are deposited and held in an interest bearing account(s) until used. Ensure separate accounting for and allocation of interest earned from State grant funds and local matching contributions. Amounts must be properly reflected on PennDOT's supporting Schedule S1 – Local Match Provided (Act 44 Section 1513 Local Match for Operating Funds Received) and Schedule S5 – Section 1513 Program Carryover as shown in PennDOT's *Financial Reporting Manual for Urban and Rural Fixed Route Transportation Providers*.

Eligibility of Local Matching Contributions

Auditors are to adhere to the guidance below when determining the eligibility and amount of local matching contributions pursuant to PennDOT regulations:

1. For a private transportation company receiving grants directly from the Department under the act, eligible annual local matching funds shall only consist of contributed cash income that was generated by the transportation company from its nonsubsidized activities.
2. Except for those local transportation organizations using local matching funds from private third-party contractors prior to the enactment of the act, eligible sources of local matching funds for a local transportation organization shall be cash contributions provided by one or more municipalities or private entities in accordance with paragraphs (1) and (10).
    a. The total amount of municipal local match cash contributions for operating assistance cannot be less than the total amount of municipal local match cash contributed in the prior fiscal year.
    b. If the required local match is 15% of the State funding for operating assistance, the municipal local match contribution can be reduced proportionate to any reduction in State operating assistance funding.
3. Advertising revenue may be considered an eligible source of local matching funds for operating assistance grants if the municipalities responsible for providing all of the local matching funds annually pass a resolution which:
    a. Acknowledges their responsibility for providing the local matching funds.
    b. Agrees to offset any shortfall in advertising revenue received during the fiscal year which results in insufficient local matching funds.
    c. Acknowledges that any reduction in service or increase in fares due to the net loss of operating revenue associated with the use of advertising revenue as local match is the responsibility of the municipalities which provide local match.
4. If a shortfall in advertising revenue causes the local transportation organization to obtain less than its required operating assistance local matching funds in any fiscal year and the municipality does not offset the shortfall to bring the local match to the minimum required for State operating assistance funding, the following apply:
    a. Advertising revenue will no longer be considered an eligible source of local matching funds for the affected local transportation organization in future fiscal years.
5. All categories of local transportation organization operating revenue, including passenger fares; public or private payments provided in lieu of fares including route guarantees,

unless the route guarantee revenue is allowed as local match in accordance with paragraph (9); charter or school bus revenue; advertising revenue, unless the advertising revenue is approved for use as local match in accordance with paragraph (3); and interest income or other miscellaneous sources of revenue do not constitute eligible sources of local matching funds.

6. Local bonds issued by local transportation organizations and guaranteed in whole or in part by State funding sources, including interest arbitrage instruments, do not constitute eligible sources of local matching funds for State grants.
7. Income generated from the subsidized public passenger transportation service is not eligible to be used as a source of local matching funds.
8. For a local transportation organization using funds provided by a private third-party contractor as a source of local matching funds prior to the enactment of the act, the following apply with regard to operating assistance:
    a. Local matching funds equal to the local matching funds provided by third-party contractors in State Fiscal Year 2009-10 may continue to come from private third-party contractor sources provided the following requirements are met. The private third-party contractor source of local matching funds must:
        i. Segregate finances for all business entities.
        ii. Maintain separate accounting records for each business entity.
        iii. Submit an independently prepared audit for each business entity. The audit must clearly identify revenue sources used for local matching funds.
    b. Local matching funds in excess of the local matching funds provided in State Fiscal Year 2009-10 must be provided in accordance with paragraph (2). Funding from private third-party contractor sources is not eligible for this portion of the local matching funds.
    c. If the amount of local matching funds provided by the private third-party contractor is ever decreased to an amount less than the local matching funds provided in State Fiscal Year 2009-10, the lower amount will become the maximum amount of local matching funds which can be provided by the private third-party contractor. All local matching funds in excess of the lower amount must be provided in accordance with paragraph (2). Private third-party contractor sources are not eligible for this portion of the local matching funds.
9. For a local transportation organization using route guarantee funds as a source of local matching funds prior to the enactment of the act, the following apply for operating assistance funding:

a. Local matching funds equal to the local matching funds provided by route guarantee funds in State Fiscal Year 2009-10 may continue to come from route guarantee funds.
b. Local matching funds in excess of the local matching funds provided in State Fiscal Year 2009-10 must be provided in accordance with paragraph (2). Route guarantee funds are not eligible for this portion of the local matching funds.
c. If the amount of local matching funds provided through route guarantee funds is ever decreased to an amount less than the local matching funds provided in State Fiscal Year 2009-10, the lower amount will become the maximum amount of local matching funds which can be provided through route guarantee funds. Local matching funds in excess of the lower amount must be provided in accordance with paragraph (2). Route guarantee funds are not eligible for this portion of the local matching funds.

10. Private sources other than funding from private third-party contractors and route guarantees may be eligible as local match provided that a local transportation organization has:
    a. Requested in writing Department approval of the source and amount of the local match from private sources.
    b. Provided a written contract between the private source and the local transportation organization prior to submitting an application for State funding.
11. Local transportation organizations may use uncommitted local match reserves for operating assistance if the following apply:
    a. The total local match reserve amount is identified in the most recent audit report and can be traced through transaction detail to the source of the local match.
    b. The board of the local transportation organization passes a resolution which certifies that the local match reserve to be used for operating assistance is not committed to another project.
    c. The local transportation organization provides to the municipalities responsible for providing the local match written notification of the amount of local match reserve that will be used in a fiscal year to offset shortfalls in local match payments.

SUGGESTED AUDIT PROCEDURES

Eligibility of the source of local matching contribution funds can be determined by examining documentation (i.e. agreements, cancelled checks, bank deposits, bank statements, wire transfers, Automatic Clearing House (ACH) transfers, etc.) in order to confirm the source of the local matching contributions. Components and the respective amounts of local matching contribution(s), in particular any advertising revenue that was applied towards the local matching contribution, must be clearly disclosed in the audit.

REGULATION TITLE: Restricted Use of State Grants and Local Matching Funds

AUDIT OBJECTIVE: Ensure State grant funds and local matching contributions were used for operating assistance in accordance with Act 44 legislation.

COMPLIANCE REQUIREMENTS: State grant funds and local matching contributions are to be used only for any grantee's operating expenses and in accordance with the executed agreements between PennDOT and the grantee.

SUGGESTED AUDIT PROCEDURES

The validity of eligible expenditures can be verified by:

1. Testing expenditures to verify that State grant funds and local matching contributions are used for permitted purposes.

REGULATION TITLE: Exception to Restricted Use of State Grants and Local Matching Funds for Capital Expenditures

AUDIT OBJECTIVE: Ensure the validity of the grantee's use of State grant funds and local matching contributions for capital expenditures. Auditors are required to clearly and fully disclose if any of the conditions described below are not met.

COMPLIANCE REQUIREMENTS: Pursuant to PennDOT's approval, Act 44 Section 1513 grant funds, and the corresponding local matching contributions, may be used for capital expenditures under the following circumstances:

1. The need for the alternative use of these funds is limited to one year
2. The proposed use of operating funds for capital assistance will not result in any of the following:
    a. A reduction in service
    b. An increase in fare levels
    c. An unbalanced operating budget in the year of the transfer and for 3 succeeding fiscal years.

3. The request for approval of the use of operating funds for capital assistance must be supported by written justification documenting that the required level of funds transferred is needed to fund a capital project that cannot be funded from any other available source of State capital assistance including current or carryover PTAF, Act 3, Act 44 Section 1514 Bond, or Section 1517 Capital Improvement assistance.
4. The justification must demonstrate that the proposed capital project, for which the required operating funds will be used, cannot be deferred until a later year without incurring a significant identified hardship.

SUGGESTED AUDIT PROCEDURES: Confirm the validity of the grantee's use of operating assistance funds for capital expenditures by:

1. Obtaining a copy of the grantee's request and PennDOT's approval for the use of these funds for capital expenditures during the fiscal year
2. Confirming that insufficient capital grant funds were available as described in paragraph 3 above in this section
3. Determining that funds for operating assistance were used for capital expenditures within the one year timeframe pursuant to the grantee's request and PennDOT's approval
4. Testing transactions to ensure that expenditures were incurred only for the approved project(s)
5. Confirming that the use of operating assistance funds did not result in an unbalanced operating budget for the grantee for the fiscal year

REGULATION TITLE: Accounting for and Use of State and Local Matching Funds

AUDIT OBJECTIVE: Ensure that the grantee is properly accounting for State grant funds and related local matching contributions, that interest earnings are separately identified and local matching contributions are used in accordance with Commonwealth requirements.

COMPLIANCE REQUIREMENTS: Separate Accounting for State Grant Funds and Local Matching Contributions

State grant funds and local matching contributions must be separately accounted for and reflect distinct and separate fund balances in the grantee's accounting system. These funds are not to be co-mingled with any other accounts used to hold any of the grantee's other operating and/or capital grant funds that are received from any other sources(s). Furthermore, interest income attributed to State grant funds and local matching contributions must be separately identified between the two sources of funds that generated the interest income.

No Ending Local Matching Contribution Balances Permitted

Agencies whose grant agreement requires less than a 15% local matching contribution requirement to State grant funds are required to completely draw down these local matching contributions funds before using any State funds. An exception to this requirement exists under the following conditions:

1. Agencies not yet meeting the 15% threshold are only able to carry over local matching contributions to the extent that they received local matching contributions in excess of the minimum required amount stipulated in the grant agreement and the agency has designated the use of these excess local matching contributions funds. If no excess local matching contributions were received, all prior year Section 1513 funds carried over to the year being reported are to be classified as State funds with zero local match contribution funds on hand.
2. Once an agency reaches the 15% threshold of local matching contributions to State grant funds, the agency is permitted to carry over local matching contributions to the subsequent year even if contributions in excess of the 15% matching requirement were not received. However, local matching contributions spent during the fiscal year must represent at least 15% of State grant funds spent during the fiscal year.

SUGGESTED AUDIT PROCEDURES: Confirm that State grant funds and local matching contributions, including respective accumulated interest earnings, are separately accounted for and segregated by:

1. Ensuring that State grant funds and local matching contributions are deposited and held in separate bank accounts and are properly reconciled with the grantee's general ledger accounts.
2. In an attempt to minimize the number of bank accounts and reduce bank service charges, grantees are permitted to hold State grant funds and local matching contributions in one single bank account only if the following conditions are met:
    a. Grantees must establish and maintain separate general ledger cash accounts in their accounting systems and to "jointly" reconcile such general ledger cash accounts to a bank statement from a single Act 44 Section 1513 State and local matching contributions bank account. Standalone spreadsheets or work papers that are used in the reconciliation process, by themselves and in the absence of establishing separate general ledger accounts, are insufficient and unacceptable.
    b. If the grantee chooses to reconcile two separate general ledger cash accounts to a bank statement from a single Act 44 Section 1513 bank account holding both State and local matching contribution funds, interest income is to be allocated between the State and local general ledger accounts based on the percentage of

each general ledger cash account fund balance as a percentage of the combined total fund balance of the two general ledger cash accounts.

c. If any local matching contributions are on hand at the end of the fiscal year, the auditor must confirm that one of the two aforementioned conditions allowing the exception are met. If the condition allowing the exception involves a grantee grant agreement where the 15% local matching contribution to State grant funds is involved, the auditor must confirm that spending of local matching contributions is at least 15% of State grant funds that were spent.

PROGRAM: ACT 44 SECTION 1516 OPERATING GRANTS – TECHNICAL ASSISTANCE/DEMONSTRATION GRANTS

REGULATION TITLE: Use of Funds and Invoice Submissions

AUDIT OBJECTIVE: Ensure eligibility of expenditures

COMPLIANCE REQUIREMENTS: Funds are to be used for eligible operating expenditures and the percentage of local matching contribution funds used towards each project's total operating expenditures must meet the minimum requirements pursuant to executed State grant agreements.

SUGGESTED AUDIT PROCEDURES: The validity of eligible operating expenditures and local matching contribution usage percentages can be verified by:

1. Transaction testing should result in verifying that State operating grant funds and local matching contributions are used for permitted purposes. Confirm the payments and use of local matching contributions.

Minimum Local Matching Contributions

The percentage of local matching contribution funds used towards total operating assistance must meet the minimum requirements in relation to State operating expenditures pursuant to executed State operating grant agreements.

SUGGESTED AUDIT PROCEDURES: The validity of eligible operating expenditures and local matching contribution usage percentages can be verified by:

1. Testing expenditures to verify that State Act 44 operating grant funds under the relative appropriate section and local matching contributions are used for permitted purposes.
2. Confirming the amount of local matching contributions spent on and the percentage of total funding the local match represented for operating assistance that was funded by the State.

PROGRAM: ACT 44 SECTION 1516: PROGRAMS OF STATEWIDE SIGNIFICANCE – INTERCITY BUS

REGULATION TITLE: Receipt of Federal, State Grant Funds and Required Local Matching Contributions

AUDIT OBJECTIVE: Ensure that Federal, State and local matching contributions, plus any recorded accounts receivable for uncollected funds, are confirmed and consistent with executed grant agreements. Also ensure that funds are deposited and held in an interest bearing account(s) until used and that interest income is separately recorded and accounted for to segregate interest earnings generated from Federal, State and local matching contributions on PennDOT's supporting Schedule A6 – Act 44 Section 1516 and Federal 5311 Transit Operating Assistance as shown in PennDOT's *Financial Reporting Manual for Intercity Bus Operators*.

COMPLIANCE REQUIREMENTS: Grantees must execute annual grant agreements with PennDOT in order to obtain funds to be used towards eligible operating expenses. The following requirements related to the amount and source of local matching contributions must be satisfied during the course of an audit:

Federal 5311 Grant Funds Used:

1. Federal 5311 grant funds received, plus any amount established as an accounts receivable that was due from PennDOT at the end of the fiscal year, must be consistent with the amount of Federal 5311 funds to be granted pursuant to an executed grant agreement. Any accounts receivable that were established for any amount of Federal funding that the grantee did not receive during the fiscal year must also be clearly and fully disclosed.
2. The amount of Federal 5311 grant funds that the grantee can use towards it operations cannot exceed 50% of the fiscal year's *actual* operating deficit. This condition applies regardless if the grantee received Federal 5311 grant funds in excess of 50% of the actual operating deficit that occurred at the completion of the fiscal year. Any remaining Federal 5311 grant funds must be carried over to the following fiscal year and held in an interest bearing account and applied to the subsequent year's operating deficit.

State Grants and Local Matching Contribution Amounts Used:

1. State grant funds received, plus any amount established as an accounts receivable that was due from PennDOT at the end of the fiscal year, must be consistent with the amount of State funds to be granted pursuant to an executed grant agreement. Any accounts receivable that were established for any amount of State funding that the grantee did not receive during the fiscal year must also be clearly and fully disclosed.

2. The amount of State grant funds that the grantee used towards its operations cannot exceed 50% of the fiscal year's remaining operating deficit after Federal 5311 grant funds have been applied. Any remaining State grant funds must be carried over to the following fiscal year and held in an interest bearing account and applied to the subsequent year's operating deficit.
3. Any operating deficit remaining after applying Federal and State grant funds are to be fully funded with local matching contributions. The required local matching contributions received during the fiscal year must equal, or exceed, the amount stipulated in the executed grant agreement with PennDOT. The required local matching contributions must be received by the grantee by the end of the fiscal year. Auditors are required to fully disclose any and all occurrences when the minimum required amount of local matching contributions were not received by the grantee during the fiscal year. Furthermore, any accounts receivable that were established for the uncollected amount of local matching contribution must also be clearly and fully disclosed.
4. Federal, State and local grant funds must be deposited and held in interest bearing accounts until used. All interest earnings become part of the respective Federal, State and local fund balances and are reported as part of the respective Federal, State and local subsidy revenue only when the respective fund balances, or portions thereof, are used towards eligible operating expenses.

SUGGESTED AUDIT PROCEDURES

Confirm receipt and proper accounting treatment for State grants funds and required local matching contributions pursuant to executed grant agreement by:

1. Obtaining a copy of the executed grant agreement from the grantee
2. Comparing Federal, State grant funds and required local matching contributions in the agreement with actual cash amounts received plus any recorded accounts receivable to ensure consistency.
    a. Federal, State and required local matching contribution amounts shown in the executed grant agreements should be compared to, and be consistent with, the sum of all transactions recorded in the grantee's accounting system.
    b. Cash amounts received and accounts from PennDOT and local contributors should be confirmed with actual bank records (bank statements, deposit slips, wire transfers, automatic clearing house transactions (ACH), etc.) Any recorded accounts receivable must be confirmed with PennDOT and local contributors.

3. Confirm that Federal, State and local grant funds are deposited and held in an interest bearing account(s) until used. Ensure separate accounting for and allocation of interest earned from Federal, State and local matching contributions.

REGULATION TITLE: Accounting for and Use of Federal, State and Local Matching Funds

AUDIT OBJECTIVE: Ensure that the grantee is properly accounting for Federal and State grant funds and related local matching contributions, that interest earnings are separately identified and local matching contributions are used in accordance with Commonwealth requirements.

COMPLIANCE REQUIREMENTS: Separate Accounting for Federal and State Grant Funds and Local Matching Contributions

Federal and State grant funds and local matching contributions must be separately accounted for and reflect distinct and separate fund balances in the grantee's accounting system. These funds are not to be co-mingled with any other accounts used to hold any of the grantee's other operating and/or capital grant funds that are received from any other sources(s). Furthermore, interest income attributed to Federal and State grant funds and local matching contributions must be separately identified between the three sources of funds that generated the interest income.

SUGGESTED AUDIT PROCEDURES: Confirm that Federal and State grant funds and local matching contributions, including respective accumulated interest earnings, are separately accounted for and segregated by:

1. Ensuring that Federal and State grant funds and local matching contributions are deposited and held in separate bank accounts and are properly reconciled with the grantee's general ledger accounts.
2. In an attempt to minimize the number of bank accounts and reduce bank service charges, grantees are permitted to hold Federal and State grant funds and local matching contributions in one single bank account only if the following conditions are met:
    a. Grantees must establish and maintain separate general ledger cash accounts in their accounting systems and to "jointly" reconcile such general ledger cash accounts to a bank statement from a single Federal 5311, State Section 1516 and local matching contributions bank account. Standalone spreadsheets or work papers that are used in the reconciliation process, by themselves and in the absence of establishing separate general ledger accounts, are insufficient and unacceptable.
    b. If the grantee chooses to reconcile two separate general ledger cash accounts to a bank statement from a single bank account holding both Federal and State grant funds and local matching contribution funds, interest income is to be

allocated between the Federal, State and local general ledger accounts based on the percentage of each general ledger cash account fund balance as a percentage of the combined total fund balance of the two general ledger cash accounts.

PROGRAM: PTAF Capital Grants

REGULATION TITLE: Authorized Use of Grant Funds Towards Eligible Capital Expenditures

AUDIT OBJECTIVE: Ensure the use of State PTAF grant funds and local matching contributions were used for capital expenditures in accordance with Act 26 legislation and executed Federal and/or State capital grant agreements.

COMPLIANCE REQUIREMENTS: Annual PTAF capital funds were last distributed to grantees under Act 26 during Fiscal Year 2006-07. Many grantees continue to have remaining State PTAF cash balances along with cash balances of related local matching contributions that grantees were required to obtain as part of their agreements with PennDOT. The following requirements related to the restricted use of funds and the percentage of local matching funds used by project must be satisfied during the course of an audit:

Restricted Use of State PTAF Grants and Associated Local Matching Contributions

State PTAF grant funds and local matching contributions are only to be used for a grantee's capital expenditures. Local matching contributions should be on hand at the grantee and the minimum required amount must be used towards capital projects pursuant to Federal and/or State capital grant agreements.

Minimum Local Matching Contributions

The percentage of local matching contribution funds used towards each project's total capital expenditures must meet the minimum requirements in relation to Federal and/or State capital expenditures pursuant to executed Federal and/or State capital grant agreements.

SUGGESTED AUDIT PROCEDURES: The validity of eligible capital expenditures and local matching contribution usage percentages can be verified by:

1. Testing expenditures to verify that State PTAF grant funds and local matching contributions are used for permitted purposes.
2. Confirming the amount of local matching contributions spent on and the percentage of the total funding the local match represented for each capital project that was funded by Federal and State PTAF capital grant funds.

REGULATION TITLE: Accounting for State and Local Matching Contributions

AUDIT OBJECTIVE: Ensure that the grantee is properly accounting for State PTAF grant funds and local matching contributions.

COMPLIANCE REQUIREMENTS: State PTAF grant funds and local matching contributions must be separately accounted for by maintaining separate fund balances in the grantee's accounting system until funds are used. These funds are not to be co-mingled with any other accounts used to hold any of the grantee's other operating and/or capital grant funds that are received from any other sources(s). Furthermore, interest income attributed to State PTAF grant funds and local matching contributions must be separately identified between the two sources of funds that generated the interest income.

SUGGESTED AUDIT PROCEDURES: Confirm that State PTAF grant funds and local matching contributions, including respective accumulated interest earnings, are separately accounted for and segregated by:

1. Ensuring that State PTAF grant funds and local matching contributions are deposited and held in separate bank accounts and are properly reconciled with the grantee's general ledger accounts.
2. In an attempt to minimize the number of bank accounts and reduce bank service charges, grantees are permitted to hold State PTAF grant funds and local matching contributions in one single bank account only if the following conditions are met:
    a. Grantees must establish and maintain separate general ledger cash accounts in their accounting systems and to "jointly" reconcile such general ledger cash accounts to a bank statement from a single State PTAF and local matching contributions bank account. Standalone spreadsheets or work papers that are used in the reconciliation process, by themselves and in the absence of establishing separate general ledger accounts, are insufficient and unacceptable.
    b. If the grantee chooses to reconcile two separate general ledger cash accounts to a bank statement from a single PTAF bank account holding both State PTAF and local matching contribution funds, interest income is to be allocated between the State PTAF and local general accounts based on the percentage of each general ledger cash account fund balance as a percentage of the combined total fund balance of the two general ledger cash accounts.

PROGRAM: ACT 3 BSG AND ASG GRANTS

REGULATION TITLE: Authorized Use of Grant Funds Towards Eligible Expenditures

AUDIT OBJECTIVE: Ensure the use of State Act 3 BSG and ASG grant funds and associated local matching contributions were used in accordance with Act 3 legislation and grant agreements.

COMPLIANCE REQUIREMENTS: Annual Act 3 BSG and ASG funds were last distributed to grantees during Fiscal Year 2006-07. Many grantees continue to have remaining State BSG and ASG cash balances along with cash balances of associated local matching contributions. The following requirements related to the restricted use of funds and the percentage of local matching funds used by project must be satisfied during the course of an audit:

Restricted Use of State Act 3 BSG and ASG Grants and Associated Local Matching Contributions

Both *Urban* and *Rural* transit systems are permitted to use State BSG grant funds for either eligible operating and/or capital expenditures. Urban systems are able to use ASG grant funds only for eligible capital eligible expenditures while Rural systems are permitted to use ASG funds on either eligible operating and/or capital expenditures. These same conditions apply to associated local matching contributions that have been received by the grantee. Local matching contributions should be on hand at the grantee and the minimum required amount must be used towards operating assistance and/or capital projects pursuant to Federal and/or State capital grant agreements.

Minimum Local Matching Contributions

The percentage of local matching contribution funds used towards each project's total operating assistance and/or capital expenditures must meet the minimum requirements in relation to Federal and/or State capital expenditures pursuant to executed Federal and/or State capital grant agreements.

SUGGESTED AUDIT PROCEDURES: The validity of eligible operating and/or capital expenditures and local matching contribution usage percentages can be verified by:

1. Testing expenditures to verify that State Act 3 BSG and ASG grant funds and local matching contributions are used for permitted purposes.
2. Confirming the amount of local matching contributions spent on and the percentage of total funding the local match represented for operating assistance and/or each capital project that was funded by Federal and State capital grant funds.

REGULATION TITLE: Accounting for State and Local Matching Contributions

AUDIT OBJECTIVE: Ensure that the grantee is properly accounting for State Act 3 BSG and ASG grant funds and local matching contributions.

COMPLIANCE REQUIREMENTS: State Act 3 BSG and ASG grant funds and local matching contributions must be separately accounted for by maintaining separate fund balances in the

grantee's accounting system until funds are used. **BSG and ASG funds are not to be comingled** with any other accounts used to hold any of the grantee's other operating and/or capital grant funds that are received from any other sources(s). Furthermore, interest income attributed to State PTAF grant funds and local matching contributions must be separately identified between the two sources of funds that generated the interest income.

SUGGESTED AUDIT PROCEDURES: Confirm that State Act 3 BSG and ASG grant funds and local matching contributions to State Act 3 BSG and ASG funds, including respective accumulated interest earnings, are separately accounted for and segregated by:

1. Ensuring that State Act 3 BSG and ASG grant funds and local matching contributions are deposited and held in separate bank accounts and are properly reconciled with the grantee's general ledger accounts. Act 3 BSG and ASG local matching contributions are not to be co-mingled.
2. In an attempt to minimize the number of bank accounts and reduce bank service charges, grantees are permitted to hold State Act 3 BSG and ASG grant funds and local matching contributions in two bank accounts (one holding State Act 3 BSG funds and the associated local matching contributions and another bank account holding State ASG funds and the associated local matching contributions) only if the following conditions are met:
    a. Grantees must establish and maintain separate general ledger cash accounts in their accounting systems and to "jointly" reconcile such general ledger cash accounts to a bank statement from the single State Act 3 BSG and local matching contributions bank account and the single State Act 3 ASG and local matching contribution bank account. Standalone spreadsheets or work papers that are used in the reconciliation process, by themselves and in the absence of establishing separate general ledger accounts, are insufficient and unacceptable.
    b. If the grantee chooses to reconcile separate general ledger cash accounts to bank statements from separate BSG and ASG bank accounts holding both State Act 3 BSG funds and local matching contribution funds and the other holding State Act 3 ASG funds and local matching contributions, interest income is to be allocated between the State and local general accounts based on the percentage of each general ledger cash account fund balance as a percentage of the combined total fund balance of the separate general ledger cash accounts.

PROGRAM: Act 44 Section 1514: Asset Improvement Program, Section 1515: New Initiatives Program, Section 1516: Programs of Statewide Significance, and Section 1517: Capital Improvements Program

REGULATION TITLE: Use of Funds and Invoice Submissions

AUDIT OBJECTIVE: Ensure eligibility of expenditures and timely submission of invoices

COMPLIANCE REQUIREMENTS: Funds are to be used for eligible capital expenditures and the percentage of local matching contribution funds used towards each project's total capital expenditures must meet the minimum requirements pursuant to executed State grant agreements.

SUGGESTED AUDIT PROCEDURES: The timeliness and validity of eligible capital expenditures and local matching contribution usage percentages can be verified by:

1. Transaction testing should result in verifying that State capital grant funds and local matching contributions are used for permitted purposes. Confirm the payments and use of local matching contributions spent on each capital project that was funded State capital grant funds.

Minimum Local Matching Contributions

The percentage of local matching contribution funds used towards each project's total operating assistance and/or capital expenditures must meet the minimum requirements in relation to Federal and/or State capital expenditures pursuant to executed Federal and/or State capital grant agreements.

SUGGESTED AUDIT PROCEDURES: The validity of eligible operating and/or capital expenditures and local matching contribution usage percentages can be verified by:

1. Testing expenditures to verify that State Act 44 capital grant funds under the relative appropriate section and local matching contributions are used for permitted purposes.
2. Confirming the amount of local matching contributions spent on and the percentage of total funding the local match represented for operating assistance and/or each capital project that was funded by Federal and State capital grant funds.

AGREED UPON PROCEDURES – INTERCITY BUS OPERATORS

Intercity Bus operators are required to submit an annual audit report of their organization's financial results to PennDOT. In addition to the applicability of the audit requirements pertinent to intercity bus operators described throughout this Publication, the Agreed Upon Procedures listed below are to be applied to the subsidized routes in the course of the audit.

Auditors are required to:

1. Ensure that the grantee has established a separate accounting for all transaction activity pertaining to subsidized routes. The grantee is required to establish separate general ledger accounts for all transaction activity including revenue, expenses, assets, liabilities and equity pertaining only to the subsidized routes. At no time is transaction activity for the subsidized routes and the grantee's other operations to be recorded in the same general ledger account(s).
2. Compare all amounts in the grantee's Budget Summary, Schedule A6 – Intercity Bus Operating Assistance, Schedule A7 - Consolidated Financial Statement - All Routes which reflects amounts reported to PennDOT for the fiscal year to the trial balance pertaining to the same reporting period (July 1st to June 30th fiscal year) of the grantee. Auditors are required to disclose all differences in its Report on Applying Agreed Upon Procedures.
3. Confirm that the July 1st to June 30th fiscal year trial balance used in the previous procedure was generated from the grantee's accounting system that generated the trial balance that was used in the annual audit report of the grantee's overall financial results.
4. Ensure that all year end adjusting entries are included in the grantee's trial balance that was used in the grantee's audit report of its financial results and are also included in the July 1st to June 30th fiscal year trial balance, where applicable.
5. Ensure that the grantee is performing interim reporting consistent with Accounting Standards Codification 270.
6. Ensure that grantees submit their annual audit along with the Independent Accountants' Report on Applying Agreed Upon Procedures accompanied by the required reports and schedules shown on page 25 of this publication.