



MICHIGAN

OFFICE OF THE AUDITOR GENERAL

FOLLOW-UP REPORT
ON THE

WORKFORCE DEVELOPMENT AGENCY'S OVERSIGHT
OF THE MICHIGAN WORKS! AGENCIES

MICHIGAN STRATEGIC FUND

December 2014



Doug A. Ringler, C.P.A., C.I.A.
AUDITOR GENERAL

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Auditor General

December 16, 2014

Ms. Christine Quinn, Director
Workforce Development Agency
Michigan Strategic Fund
201 North Washington Square
Lansing, Michigan
and

Mr. Michael A. Finney, President and Chief Executive Officer
Michigan Strategic Fund
300 North Washington Square
Lansing, Michigan

Dear Ms. Quinn and Mr. Finney:

This is our report on our follow-up of the 1 material condition (Finding 1), 4 reportable conditions (Findings 2 through 5), and 5 corresponding recommendations reported in the performance audit of the Bureau of Workforce Transformation's (BWT's) Oversight of the Michigan Works! Agencies (MWAs), Workforce Development Agency, Michigan Strategic Fund. That audit report was issued and distributed in July 2011. Additional copies are available on request or at <http://audgen.michigan.gov>. Executive Order No. 2011-4 transferred any authority, powers, duties, and functions of BWT to the Workforce Development Agency (WDA) within the Michigan Strategic Fund.

This report contains an introduction; our purpose of follow-up; a background; our scope; follow-up conclusions, results, recommendations, and agency responses; and a glossary of abbreviations and terms.

Our follow-up disclosed that WDA had complied with 1 recommendation, had partially complied with 3 recommendations, and had not complied with 1 recommendation. Reportable conditions exist related to the continuous quality improvement (CQI) process (Finding 1), conflicts of interest (Finding 3), MWA expenditure reporting (Finding 4), and program administrative expenditure guidance (Finding 5). As a result, we have issued 1 repeat recommendation and 3 rewritten recommendations.

We appreciate the courtesy and cooperation extended to us during our follow-up. If you have any questions, please call me or Laura J. Hirst, C.P.A., Deputy Auditor General.

Sincerely,

Doug Ringler
Auditor General

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FOLLOW-UP REPORT WORKFORCE DEVELOPMENT AGENCY'S OVERSIGHT OF THE MICHIGAN WORKS! AGENCIES MICHIGAN STRATEGIC FUND

INTRODUCTION

This report contains the results of our follow-up of the material condition*, reportable conditions*, and corresponding recommendations reported in our performance audit* of the Bureau of Workforce Transformation's (BWT's) Oversight of the Michigan Works! Agencies* (MWA), Workforce Development Agency (WDA), Michigan Strategic Fund (641-0820-07), which was issued and distributed in July 2011. That audit report included 1 material condition (Finding 1) and 4 reportable conditions (Findings 2 through 5). This report also contains WDA's plan to comply with our prior audit recommendations, which was required by the *Michigan Compiled Laws* and administrative procedures to be developed within 60 days after release of the July 2011 audit report.

PURPOSE OF FOLLOW-UP

The purpose of this follow-up was to determine whether WDA had taken appropriate corrective measures in response to the 1 material condition, 4 reportable conditions, and 5 corresponding recommendations noted within our July 2011 audit report.

BACKGROUND

Effective April 25, 2011, Executive Order No. 2011-4 transferred any authority, powers, duties, and functions of BWT to the newly created WDA within the Michigan Strategic Fund. WDA is responsible for promoting and overseeing a flexible, innovative, and effective workforce system within the State of Michigan.

* See glossary at end of report for definition.

Title I of the federal Workforce Investment Act of 1998 (WIA) required states to develop a one-stop service center system via local workforce areas to provide employment and training services at centralized locations for use by employers and job seekers. As a result, Sections 408.111 - 408.135 of the *Michigan Compiled Laws* established the Michigan Works! One-Stop Service Center System (Michigan Works! System) to deliver workforce development programs and services tailored to local needs and to provide for consolidated access to employment and retention programs.

The Michigan Works! System includes over 100 Michigan Works! Service Centers, administered by 25 MWAs, that provide a wide range of employment, training, and career education services to employers seeking potential applicants, individuals seeking employment, and those interested in career information. WDA provides federal and State funding to the 25 local MWAs that administer the day-to-day operations of local workforce development programs and services. Funding sources included grants from the U.S. Departments of Agriculture, Labor, Education, Energy, and Health and Human Services.

Section 408.135 of the *Michigan Compiled Laws* (Act 491, P.A. 2006) assigned responsibility for the oversight of the MWAs to WDA. WDA distributes approximately 90% of its funds to MWAs and other subrecipients and expends 10% of its funds directly. Of the amounts that WDA distributes to MWAs and other subrecipients, approximately 80% is distributed to MWAs. For the fiscal year ended September 30, 2013, WDA expended \$309 million, of which \$226 million was distributed to the MWAs.

WDA provides MWA oversight through a variety of methods, including fiscal and programmatic on-site monitoring reviews, MWA U.S. Office of Management and Budget Circular A-133 audit reviews, and technical assistance and training. Fiscal on-site monitoring reviews are conducted annually at each MWA to ensure that the MWAs adhere to applicable federal administrative requirements and cost principles. Programmatic monitoring for the federal WIA program* and Trade Adjustment Assistance (TAA) program* is conducted to ensure that local MWA programs are administered in accordance with the objectives of the program, to ensure that service delivery to job seekers is in accordance with the individual's service plan, and to validate program reporting data submitted to the federal departments.

* See glossary at end of report for definition.

SCOPE

Our fieldwork was primarily performed during May through August 2014. We interviewed WDA personnel and reviewed their corrective action plans to determine the status of compliance with the audit recommendations. We assessed WDA's efforts to implement a continuous quality improvement* (CQI) process. We reviewed WDA's policies and procedures related to conflicts of interest, fiscal oversight of MWAs, and monitoring of MWA performance. We judgmentally selected fiscal and programmatic monitoring reviews to evaluate WDA's process of monitoring MWAs. We also reviewed board members' disclosure report forms and board meeting minutes to verify that local workforce development board members with disclosed conflicts of interest abstained from voting. Our scope did not include visits to individual MWAs or detailed reviews of the MWAs' records.

* See glossary at end of report for definition.

FOLLOW-UP CONCLUSIONS, RESULTS, RECOMMENDATIONS, AND AGENCY RESPONSES

OVERSIGHT OF SELECTED ACTIVITIES OF THE MICHIGAN WORKS! AGENCIES (MWAs)

SUMMARY OF THE JULY 2011 FINDING

1. Continuous Quality Improvement (CQI) Process

BWT needs to establish a comprehensive CQI process to evaluate the successes and shortcomings of its workforce development programs. As a result, BWT could not assess the worthiness of programs and perform qualitative analyses necessary for making informed decisions regarding program improvements.

A comprehensive CQI process includes: performance indicators for measuring outputs* and outcomes*; performance standards* or goals* that describe the desired level of outputs and outcomes based on management expectations and/or benchmarks to peer and historical performance trends; a management information system to accurately gather relevant output and outcome data on a timely basis; a comparative analysis of actual data to desired outputs and outcomes; a reporting of the comparison results to management; and recommendations to improve effectiveness* and efficiency* and/or to change desired performance standards or goals.

RECOMMENDATION (AS REPORTED IN JULY 2011)

We recommend that BWT establish a comprehensive CQI process to evaluate the successes and shortcomings of its workforce development programs.

AGENCY PLAN TO COMPLY*

WDA indicated in its September 26, 2011 plan to comply that it was meeting federal performance goals and engaging in efforts to raise performance levels. However, WDA acknowledged that more extensive evaluation of all participant and fiscal data, a complete review of all individual files, longer-term participant tracking,

* See glossary at end of report for definition.

and access to more current wage-record data would likely generate additional recommendations for program modifications and improvements. WDA stated that it would explore the availability of additional funding for a more extensive evaluation.

FOLLOW-UP CONCLUSION

We concluded that WDA had partially complied with this recommendation and that a reportable condition exists.

FOLLOW-UP RESULTS

Our follow-up disclosed that WDA requested a waiver from the U.S. Department of Labor (USDOL) of the WIA federal requirement to conduct ongoing evaluations of workforce investment activities in order to promote, establish, implement, and utilize methods for continuously improving the activities to achieve high-level performance and outcomes. USDOL granted WDA a waiver of the WIA federal requirement from July 1, 2011 through July 1, 2015.

Although WDA requested a waiver of the federal CQI requirements, WDA took steps toward establishing a more comprehensive CQI process, including:

- WDA developed a five-year strategic plan beginning in fiscal year 2013-14 to assist WDA in implementing its mission, vision, and goals for the workforce development system.
- WDA updated its One Stop Management Information System (OSMIS) and requires MWAs to report employer and wage data for all WIA workers that are noted as employed in OSMIS when exiting the program.
- WDA hired a contractor in April 2014 to evaluate the needs of the MWAs and to assess if OSMIS meets the requirements and needs of the MWAs. WDA informed us that it plans to use the contractor's evaluation to determine which system changes will best meet the needs of WDA and the MWAs.

During our review, we noted that many of WDA's efforts, including those mentioned in the preceding paragraphs, addressed program outputs without providing information necessary to evaluate program outcomes. Further evaluation of

program outcomes related to training, job placement, and employment retention rates could assist WDA in evaluating the successes and shortcomings of workforce development programs.

FOLLOW-UP RECOMMENDATION

We recommend that WDA continue its efforts to establish a comprehensive CQI process to evaluate the successes and shortcomings of its workforce development programs.

FOLLOW-UP AGENCY RESPONSE

WDA provided us with the following response:

WDA agrees and has taken steps to improve the reporting of the 17 common measures, provided additional tools to evaluate programs, and is working towards an interface with wage record data to provide real-time information during a client's participation. WDA will continue to enhance its CQI process for the evaluation of its programs.

SUMMARY OF THE JULY 2011 FINDING

2. On-Site Program Monitoring

BWT needs to improve its efforts to conduct on-site program monitoring to ensure that workforce development activities are sufficient to promote, establish, implement, and utilize methods to achieve high-level performance and outcomes.

Chapter 6, Section (e)(1) of the federal WIA requires states to conduct an ongoing evaluation of workforce investment activities to promote, establish, implement, and utilize methods to achieve high-level performance and outcomes. WIA also states that evaluation should include the identification of methods to promote the efficiency and effectiveness of the workforce investment system to improve jobseeker employability. Also, Title 29, Part 97, section 40 of the *Code of Federal Regulations* requires grantees to monitor grant and subgrant supported activities to ensure compliance with applicable federal requirements and achievement of performance goals.

Our review of BWT's on-site monitoring activities disclosed:

- a. BWT did not conduct regular, on-site program monitoring for the WIA and TAA programs.
- b. BWT did not use a risk-based approach to schedule on-site monitoring visits of MWAs.

RECOMMENDATION (AS REPORTED IN JULY 2011)

We recommend that BWT continue to improve its efforts to conduct on-site program monitoring to ensure that workforce development activities are sufficient to promote, establish, implement, and utilize methods to achieve high-level performance and outcomes.

AGENCY PLAN TO COMPLY

WDA indicated in its September 26, 2011 plan to comply that it had:

- Revised a comprehensive TAA programmatic review guide.
- Began conducting TAA on-site monitoring in March 2010.
- Developed and piloted a new WIA programmatic review guide to help ensure compliance with federal and State regulations.
- Completed two WIA field (trial) reviews performed under consultation with USDOL staff.
- Conducted official review of the Western Upper Peninsula Michigan Works!.
- Scheduled official review of the Detroit Workforce Development Department MWA for November 25, 2011.
- Identified best practices, findings, or concerns with local program design, local staff training needs, and program areas needing additional clarification for each program in WDA.

Also, the plan stated that WDA would schedule annual WIA and TAA visits to each MWA, with additional follow-up based on review outcomes as necessary.

FOLLOW-UP CONCLUSION

We concluded that WDA complied with this recommendation.

FOLLOW-UP RESULTS

Our follow-up disclosed:

- a. Regarding part a. of the finding, WDA implemented on-site program monitoring for the WIA program and TAA program in August 2011 and March 2010, respectively. WDA informed us that starting in August 2014 for the WIA program and in October 2014 for the TAA program, it intends to conduct WIA and TAA program reviews of all MWAs biennially.
- b. Regarding part b. of the finding, WDA is in the process of implementing a risk-based approach. For the WIA program, WDA developed and completed an annual risk assessment form for each MWA to assist in prioritizing which MWAs to visit. WDA informed us that it plans to complete annual risk assessments for the TAA program beginning in September 2014. WDA also informed us that it plans to use the annual risk assessments when scheduling MWA site visits.

SUMMARY OF THE JULY 2011 FINDING

3. Conflicts of Interest

BWT needs to strengthen its disclosure and resolution process regarding potential conflicts of interest for MWA staff, MWA contractors and their employees, and workforce development board members. As a result, BWT could not ensure that key MWA staff, contracted employees, and workforce development board members conducted their responsibilities in a fair and independent manner.

Requiring all MWA staff, MWA contractors and their employees, and workforce development board members to disclose potential conflicts of interest and have a process to ensure the resolution of identified conflicts of interest helps ensure that

decisions and actions are made in the best interests of the workforce development programs and the public good.

Our review of BWT's requirements and processes related to conflicts of interest disclosed:

- a. BWT did not require MWA staff and MWA contractors' employees to periodically disclose and resolve potential conflicts of interest.
- b. BWT did not attempt to verify the completeness of conflicts of interest reported by workforce development boards.
- c. BWT did not follow up on reported conflicts of interest to ensure that they were appropriately resolved.

RECOMMENDATION (AS REPORTED IN JULY 2011)

We recommend that BWT strengthen its disclosure and resolution process regarding potential conflicts of interest for MWA staff, MWA contractors and their employees, and workforce development board members.

AGENCY PLAN TO COMPLY

WDA indicated the following in its September 26, 2011 plan to comply:

MWA Staff and Contractors

WDA's Office of Audit and Financial Compliance annually obtains and reviews a copy of each MWA and select service providers' standards of conduct, which governs the performance of their employees engaged in the award and administration of contracts. MWA standards of conduct monitoring is carried out and complies with the U.S. Office of Management and Budget's Common Rule. WDA requires corrective action if the MWA or service provider is found to be in noncompliance. WDA also advised MWAs that conflicts of interest would be reviewed as part of programmatic on-site reviews.

Workforce Development Board Members

WDA developed a more comprehensive desk audit/site review process and amended the forms used for disclosure of possible conflicts of interest by local

workforce development boards to include the date of the meeting in which the vote in question was taken. WDA staff review the applicable meeting minutes of the local workforce development board to assure that the member actually abstained from voting on the expenditure. In order to address actual versus perceived conflict of interest situations in a timely manner, WDA will update its workforce development board certification policy to include a requirement that each local workforce development board submit a disclosure report form following each meeting. The form will document that a member has abstained from voting due to a perceived conflict of interest and will include the meeting minutes indicating the member's abstention.

FOLLOW-UP CONCLUSION

We concluded that WDA had partially complied with this recommendation and that a reportable condition exists.

FOLLOW-UP RESULTS

Our follow-up disclosed:

- a. Regarding part a. of the finding, although WDA's fiscal and programmatic reviews determine that the MWA standards of conduct include conflict of interest language that is disseminated to MWA staff and that WDA's policy requires MWA staff to disclose conflicts of interest upon hire, we noted the following deficiencies in WDA's processes:
 - (1) WDA's conflict of interest policy did not require MWA staff to periodically update their conflict of interest forms.
 - (2) WDA did not have a policy requiring the MWAs to ensure that MWA contractors' employees periodically disclosed conflicts of interest.
 - (3) WDA did not perform monitoring procedures to determine if:
 - (a) MWAs were in fact requiring staff to disclose potential conflicts of interest or if the MWAs took steps to resolve disclosed conflicts of interest.

- (b) MWAs were monitoring MWA contractors to ensure that the contractors' employees had disclosed conflicts of interest and took steps to resolve disclosed conflicts of interest.

- b. Regarding part b. of the finding, WDA issued a policy in November 2011 requiring local workforce development boards to submit conflict of interest disclosure report forms during the biennial recertification process and after each board meeting.

We noted that WDA did not require board members to make their own conflict of interest disclosures. Rather, WDA required each local workforce development board's chief elected official to make an overall disclosure for all board members at recertification. As a result, WDA did not have sufficient information to verify the completeness of conflicts of interest reported by the local workforce development boards.

- c. Regarding part c. of the finding, WDA informed us that it compares local workforce development board disclosure report forms with board meeting minutes to ensure that board members who disclosed a conflict of interest abstained from voting. We reviewed board meeting minutes and verified that board members with disclosed conflicts of interest did abstain from voting.

FOLLOW-UP RECOMMENDATION

We recommend that WDA continue to strengthen its disclosure and resolution process to require MWA staff and MWA contractors' employees to periodically disclose and resolve potential conflicts of interest and to verify the completeness of conflicts of interest reported by the local workforce development board members.

FOLLOW-UP AGENCY RESPONSE

WDA provided us with the following response:

WDA agrees and will modify its current Conflict of Interest policy to reflect that all employees of MWAs and their service providers complete and sign annual disclosure forms. This will also be required for all members of local Workforce Development Boards. WDA will monitor this process to ensure disclosure forms are maintained and identified conflicts are resolved.

FISCAL OVERSIGHT OF MWAs

SUMMARY OF THE JULY 2011 FINDING

4. **MWA Expenditure Reporting**

BWT did not require MWAs to report budgetary and expenditure information in detail sufficient for appropriate budgetary control. As a result, BWT could not identify variances between budgeted and actual MWA expenditures to evaluate variances and their impact on program results. Also, BWT could not make meaningful comparisons of program activity by expenditure type necessary to effectively evaluate overall and individual MWA performance.

BWT directives for the WIA Adult Program and the WIA Dislocated Worker Program require MWAs to report program expenditures in four categories: administration, core services, intensive services, and training services. Also, BWT policies require MWAs to report all costs incurred by its contractors as program costs (core, intensive, and training services), regardless of the type or nature of the expenditure. BWT did not require further reporting detail within these four categories.

RECOMMENDATION (AS REPORTED IN JULY 2011)

We recommend that BWT require MWAs to report budgetary and expenditure information in detail sufficient for appropriate budgetary control.

AGENCY PLAN TO COMPLY

WDA indicated in its September 26, 2011 plan to comply that it would explore the feasibility of implementing additional budgetary and expenditure reporting controls. However, WDA disputed the assertion that MWAs do not retain sufficient budgetary expenditure detail, as all agencies were providing the information necessary for the State to meet federal fiscal reporting requirements. WDA stated that although monitoring expenditures at the level of detail outlined may assist in the evaluation of programs, implementation costs, such as staffing and other ancillary resources, were not available given the existing funding levels.

FOLLOW-UP CONCLUSION

We concluded that WDA did not comply with this recommendation and that a reportable condition exists.

FOLLOW-UP RESULTS

Our follow-up disclosed that WDA had not implemented any requirements for MWAs to report budgetary and expenditure information in more detail than what was required during the prior audit. We did not note any changes between the budgetary and expenditure information reported during the prior audit and the budgetary and expenditure information reported in fiscal year 2013-14.

FOLLOW-UP RECOMMENDATION

We again recommend that BWT require MWAs to report budgetary and expenditure information in detail sufficient for appropriate budgetary control.

FOLLOW-UP AGENCY RESPONSE

WDA provided us with the following response:

WDA agrees and will work with the MWAs to develop an enhanced budget that will provide detailed planned expenditures with the intent of capturing actual expenditures in the same level of detail. This will be dependent upon available resources to make the necessary system and administrative changes to capture the data.

SUMMARY OF THE JULY 2011 FINDING

5. Program Administrative Expenditure Guidance

BWT did not provide guidance to MWAs regarding the allowability and reasonableness of administrative expenditures. As a result, some MWAs did not exercise sufficient prudence in expending public funds on program administration.

Federal regulations provide general guidance for each federal funding source on allowable funding uses, including categorical spending limitations for administrative activities. However, the regulations do not provide specific guidance regarding the allowability and reasonableness of administrative expenditures in areas, such as MWA staff compensation, travel, lodging, meals, and education, otherwise left to individual discretion and interpretation of each MWA.

Some MWA administrative expenditures that we reviewed raised questions of allowability and reasonableness that could result in federal recovery of funds and sanctions on future grant awards and jeopardize the State's ability to secure future federal funding for job training programs.

RECOMMENDATION (AS REPORTED IN JULY 2011)

We recommend that BWT provide guidance to MWAs regarding the allowability and reasonableness of administrative expenditures.

AGENCY PLAN TO COMPLY

WDA indicated in its September 26, 2011 plan to comply that it issued a policy to the MWAs on July 1, 2011 to address these issues.

FOLLOW-UP CONCLUSION

We concluded that WDA had partially complied with this recommendation and that a reportable condition exists.

FOLLOW-UP RESULTS

Our follow-up disclosed that WDA issued policies giving the MWAs guidance for general allowability of expenditures and outlined federal cost principles. However, for a significant portion of its grants to MWAs, WDA did not provide MWAs with specific guidance regarding administrative expenditures. WDA did not define unallowable expenditures or establish expenditure limits for administrative expenditures, such as staff compensation, travel, lodging, meals, and education.

FOLLOW-UP RECOMMENDATION

We recommend that WDA continue to provide guidance to MWAs by defining unallowable expenditures and establishing expenditure limits for administrative expenditures, such as staff compensation, travel, lodging, meals, and education.

FOLLOW-UP AGENCY RESPONSE

WDA provided us with the following response:

WDA agrees and will provide additional guidance through policy and technical assistance to the MWAs on the allowability and reasonableness of costs charged to grant awards.

Glossary of Abbreviations and Terms

agency plan to comply	The response required by Section 18.1462 of the <i>Michigan Compiled Laws</i> and the State of Michigan Financial Management Guide (Part VII, Chapter 4, Section 100). The audited agency is required to develop a plan to comply with Office of the Auditor General audit recommendations and submit the plan within 60 days after release of the audit report to the Office of Internal Audit Services, State Budget Office. Within 30 days of receipt, the Office of Internal Audit Services is required to review the plan and either accept the plan as final or contact the agency to take additional steps to finalize the plan.
BWT	Bureau of Workforce Transformation.
continuous quality improvement (CQI)	A process that aligns the vision and mission of an organization with the needs and expectations of internal and external customers. It normally includes a process to improve program effectiveness and efficiency by assessing performance measures that evaluate outputs and outcomes related to the program vision, mission, goals, and objectives.
effectiveness	Success in achieving mission and goals.
efficiency	Achieving the most outputs and the most outcomes practical with the minimum amount of resources.
goal	An intended outcome of a program or an entity to accomplish its mission.

material condition	A matter that, in the auditor's judgment, is more severe than a reportable condition and could impair the ability of management to operate a program in an effective and efficient manner and/or could adversely affect the judgment of an interested person concerning the effectiveness and efficiency of the program.
Michigan Works! Agencies (MWAs)	The 25 local agencies that administer the day-to-day operations of local workforce development programs and services.
Michigan Works! System	Michigan Works! One-Stop Service Center System.
OSMIS	One Stop Management Information System.
outcome	An actual impact of a program or an entity.
output	A product or a service produced by a program or an entity.
performance audit	An audit that provides findings or conclusions based on an evaluation of sufficient, appropriate evidence against criteria. Performance audits provide objective analysis to assist management and those charged with governance and oversight in using the information to improve program performance and operations, reduce costs, facilitate decision making by parties with responsibility to oversee or initiate corrective action, and contribute to public accountability.
performance standard	A desired level of output or outcome.

reportable condition	A matter that, in the auditor's judgment, is less severe than a material condition and falls within any of the following categories: an opportunity for improvement within the context of the audit objectives; a deficiency in internal control that is significant within the context of the audit objectives; all instances of fraud; illegal acts unless they are inconsequential within the context of the audit objectives; significant violations of provisions of contracts or grant agreements; and significant abuse that has occurred or is likely to have occurred.
Trade Adjustment Assistance (TAA) program	A program that provides aid, including training for employment in another job or career, to workers who lose their jobs or whose hours of work and wages are reduced as a result of increased imports.
USDOL	U.S. Department of Labor.
WDA	Workforce Development Agency.
WIA	Workforce Investment Act of 1998.
WIA program	A program that supports retraining and helping unemployed and underemployed workers find jobs.

