

STATE AUDITOR AND INSPECTOR

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December 28, 2010

Gary Ridley, Director
Oklahoma Department of Transportation
200 NE 21st Street
Oklahoma City Oklahoma 73105

Dear Mr. Ridley:

This communication is provided pursuant to the parameters of the 2010 Office of Management and Budget (OMB) pilot project. Such project requires auditors of entities that volunteer for the project to issue, in writing, an early communication of significant deficiencies and material weaknesses in internal control over compliance for certain federal programs having expenditures of American Recovery and Reinvestment Act of 2009 (ARRA) funding at an interim date, prior to the completion of the compliance audit. Accordingly, this communication is based on our audit procedures performed through November 30, 2010, an interim period. Because we have not completed our compliance audit, additional significant deficiencies and material weaknesses may be identified and communicated in our final report on compliance and internal control over compliance issued to meet the reporting requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

In planning and performing our audit procedures through November 30, 2010, of the Formula Grants for Other Than Urbanized Areas program, CFDA 20.509, we are considering the Oklahoma Department of Transportation's compliance with activities allowed or unallowed, allowable costs and cost principles, cash management, eligibility, reporting, and special tests and provisions-R1-separate accounting for funds provided under the Recovery Act, as described in the *OMB Circular A-133 Compliance Supplement* for the year ended June 30, 2010. We are considering the Oklahoma Department of Transportation's internal control over compliance with the requirements previously described that could have a direct and material effect on the Formula Grants for Other Than Urbanized Areas program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Oklahoma Department of Transportation's internal control over compliance.

Our consideration of internal control over compliance is for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the entity's internal control that might be significant deficiencies as defined in the following paragraph. However, as discussed subsequently, based on the audit procedures performed through November 30, 2010, we identified deficiencies in internal control over compliance that we consider to be a significant deficiency.

A *control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings to be significant deficiencies.

The Oklahoma Department of Transportation's response to our finding is described in the accompanying schedule. We did not audit the Oklahoma Department of Transportation's response and, accordingly, we express no opinion on it.

This interim communication is intended solely for the information and use of management, the Director, the Director of Finance and Administration, the Oklahoma Department of Transportation Commission, others within the entity, federal awarding agencies, and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,



Steve Burrage, CPA
State Auditor and Inspector

Schedule of Findings

STATE AGENCY: Oklahoma Department of Transportation

FEDERAL AGENCY: United States Department of Transportation

CFDA NO: 20.509

FEDERAL PROGRAM NAME: Formula Grants for Other than Urbanized Areas

FEDERAL AWARD NUMBER: OK-86-X002-00

FEDERAL AWARD YEAR: 2009

CONTROL CATEGORY: Activities Allowed or Unallowed and Allowable Costs/Cost Principles

Criteria: 2 CFR § 215.21 (b)(3) states, "Recipients' financial management systems shall provide for the following: Effective control over and accountability for all funds, property, and other assets. Recipients shall adequately safeguard all such assets and assure they are used solely for authorized purposes."

A basic component of adequate internal controls is the segregation of duties so that one individual cannot perpetuate and conceal errors and irregularities in the normal course of his/her duties. Strong internal controls require the segregation of responsibilities for authorizing transactions and the related record keeping.

Condition: Proper segregation of duties do not exist between the approval of invoices and the preparation and approval of claims. Subrecipients submit claims for reimbursement through the Transit Programs Division's MYLEO.NET system. Four individuals in the Transit Programs Division that have access to print, review, and manually approve the subrecipient invoices from MYLEO.NET also have signing authority on claims. One of those four individuals is also responsible for preparing and transmitting claims for reimbursement.

Cause: The Department does not have formal policies and procedures in place to ensure proper segregation of duties exist in the internal control process for claims.

Effect: The possibility of inappropriate payments or misappropriation of assets exists when the same individual can both review and approve an invoice for payment and approve a claim for reimbursement without a second individual verifying the claim. Allowing an individual to review and approve an invoice for payment, approve a claim for reimbursement, and prepare and transmit the claim to the Comptroller Division increases the possibility of inappropriate payments or misappropriation of assets.

Recommendation: We recommend the Department assign signing authority on the claims to someone without signing authority on the invoices. We further recommend the Department develop formal policies and procedures to ensure proper segregation of duties exist in the internal control process for claims.

Views of Responsible Official(s): The Department concurs with this finding.

Contact Person: Kenneth R. LaRue

Anticipated Completion Date: 11/01/2010

Corrective Action Planned: All four employees will retain claim signing authority. However, if one of these four employees approves the invoice, that person should not approve the claim as well. Segregation of duties for invoice and claim approvals has been added to division internal policies and procedures.

Contact Person and contact information for high level management official who will assume overall responsibility for ensuring appropriate corrective action:

David Streb – Director of Engineering
dstreb@odot.org
405.521.6916

STATE AGENCY: Oklahoma Department of Transportation

FEDERAL AGENCY: United States Department of Transportation

CFDA NO: 20.205; 20.509

FEDERAL PROGRAM NAME: Highway Planning and Construction; Formula Grants for Other than Urbanized Areas

FEDERAL AWARD NUMBER: CFDA #20.205 – N/A; CFDA #20.509 - OK-86-X002-00

FEDERAL AWARD YEAR: 2009

CONTROL CATEGORY: Activities Allowed or Unallowed and Allowable Costs/Cost Principles

Criteria: 2 CFR § 215.21 (b)(3) states, “Recipients’ financial management systems shall provide for the following: Effective control over and accountability for all funds, property, and other assets. Recipients shall adequately safeguard all such assets and assure they are used solely for authorized purposes.” A basic component of adequate internal controls is the authorization/approval of claims. Approval authority is delegated to specific individual(s). In the event that a signature stamp is used for approval, access to the signature stamp should be limited to those specific individual(s), and the signature stamp should be secured when not in use.

Condition: The Comptroller Division authorizes claims with a rubber stamp of the Director’s signature. The signature stamp also displays the initials of the Central Office Accounting Supervisor. During our review, we noted two identical stamps were in use, but were not in the custody of either the Director or the Central Office Accounting Supervisor. In addition, the stamps were not kept in a secure area when not in use; thus, access to the signature stamps was not limited.

Cause: The Department does not ensure the use of the signature stamps is appropriately restricted. Additionally, the Department does not ensure access to the signature stamps is limited to specific individuals with delegated authority at all times.

Effect: The signature stamps could be used by unauthorized individuals.

Recommendation: We recommend the Department ensure access to the signature stamp is limited to those specific individuals with delegated authority and design adequate procedures to ensure the signature stamp is secured when not in use.

Views of Responsible Official(s): We concur.

Contact Person: Chelley Hilmes, Comptroller

Anticipated Completion Date: Completed

Corrective Action Planned: The Accounting Manager has reminded the staff of the policy regarding safeguarding the signature stamp with the accounts payable staff. The Comptroller Division will continue in its efforts to ensure access to the signature stamp is limited when not in use.

Contact Person and contact information for high level management official who will assume overall responsibility for ensuring appropriate corrective action:

Mike Patterson – Deputy Director
mpatterson@odot.org
405.521.4768

STATE AGENCY: Oklahoma Department of Transportation

FEDERAL AGENCY: United States Department of Transportation

CFDA NO: 20.205; 20.509

FEDERAL PROGRAM NAME: Highway Planning and Construction; Formula Grants for Other than Urbanized Areas

FEDERAL AWARD NUMBER: CFDA #20.205 – N/A; CFDA #20.509 - OK-86-X002-00

FEDERAL AWARD YEAR: 2009

CONTROL CATEGORY: Activities Allowed or Unallowed and Allowable Costs/Cost Principles; Cash Management; Matching and Earmarking; Reporting; Separate Accountability for American Recovery and Reinvestment Act (ARRA) Funds

Criteria: Control environment, risk assessment, control activities, information and communication, and monitoring are the five components of internal controls. The agency should be control conscious; identify, analyze and manage risks; and implement policies and procedures to help ensure necessary actions are taken to address the potential risks involved in accomplishing the entity's objectives. The agency should also assess the quality and effectiveness of the organization's internal control process over time, and implement appropriate actions when necessary.

Basic components of effective internal controls include appropriate segregation of duties and ensuring procedures for performing essential duties are adequately documented to facilitate an efficient transition of duties when personnel changes occur.

Condition: Numerous duty changes occurred in ODOT's Comptroller Division during State Fiscal Year (SFY) 2010. These changes were attributed to reassignment of staff to work on the implementation of the new CORE-PeopleSoft conversion, as well as personnel turnover. However, written policy and procedures do not reflect current operations and personnel assignments. During auditor interviews with

Comptroller Division personnel, numerous personnel, including management, were unclear in their understanding of duty assignments within the Comptroller Division.

Cause: The Comptroller Division has not updated written policy and procedures to address current operations and personnel assignments.

Effect: Appropriate controls may not be in place to ensure job duties are properly segregated to help deter, prevent and detect fraud.

Recommendation: We recommend the Comptroller Division continuously assess and monitor internal controls to ensure job duties are properly segregated. We also recommend the Comptroller Division maintain updated policies and procedures to properly reflect current operations and personnel assignments.

Views of Responsible Official(s): The Revenue Section consisted of a supervisor and three employees at year end 2010. The Revenue Section experienced turnover of three employees in a three month period. The Comptroller Division has transferred one employee in, filled one vacancy and is in the process of filling a second vacancy for the Revenue Section.

Contact Person: Chelley Hilmes, Comptroller

Anticipated Completion Date: Completed

Corrective Action Planned: The Comptroller Division is dedicated to maintaining updated policies and procedures, segregation of duties and personnel assignments.

Contact Person and contact information for high level management official who will assume overall responsibility for ensuring appropriate corrective action:

Mike Patterson – Deputy Director
mpatterson@odot.org
405.521.4768

STATE AGENCY: Oklahoma Department of Transportation

FEDERAL AGENCY: United States Department of Transportation

CFDA NO: 20.509

FEDERAL PROGRAM NAME: Formula Grants for Other than Urbanized Areas

FEDERAL AWARD NUMBER: OK-86-X002-00 (ARRA funds)

FEDERAL AWARD YEAR: 2009

CONTROL CATEGORY: Eligibility

Criteria: A basic component of adequate internal controls is to obtain supporting documentation for transactions and items affecting management decisions. Obtaining supporting documentation reduces the Department's risk of noncompliance.

FTA Circular 9040.1F, Chapter II Program Overview, part 3.a. Role of the State Agency states in part:

“The Governor designates a State agency which will have the principal authority and responsibility for administering the Section 5311 program. Specifically, the role of the State agency is to: . . . (8) certify eligibility of applicants and project activities.”

The Department defines eligible recipients in its State Management Plan for the Administration of the Section 5311 – Nonurbanized Area Formula Grant Program and Rural Transportation Assistance Program. The Department’s unwritten procedure is to obtain, review, and maintain documentation of eligibility for all subrecipients. Documentation of eligibility includes articles of incorporation for nonprofit organizations, or resolution and/or minutes from meetings approving their participation in the program for State agencies and units of local government. Eligibility documents are maintained in the Transit Program Division’s subrecipient project files.

Condition: The Department was unable to provide evidence they obtained eligibility documentation prior to the eligibility determination for three of nineteen subrecipients (15.79% of the population).

Cause: The Department did not follow their stated procedures.

Effect: Ineligible subrecipients could be approved to participate in the program and payments could be made on claims from those ineligible subrecipients.

Recommendation: We recommend the Department stress to appropriate personnel the importance of compliance with applicable policies and procedures to ensure the eligibility determination process is properly performed and documentation is properly maintained prior to payment of subrecipient claims.

Views of Responsible Official(s): We concur.

Contact Person: Kenneth R. LaRue

Anticipated Completion Date: 12/15/2010

Corrective Action Planned: Appropriate personnel have been advised to ensure that eligibility documentation is included within each application submitted.

Contact Person and contact information for high level management official who will assume overall responsibility for ensuring appropriate corrective action:

David Streb – Director of Engineering
dstreb@odot.org
405.521.6916

STATE AGENCY: Oklahoma Department of Transportation

FEDERAL AGENCY: United States Department of Transportation

CFDA NO: 20.509

FEDERAL PROGRAM NAME: Formula Grants for Other than Urbanized Areas

FEDERAL AWARD NUMBER: OK-86-X002-00 (ARRA funds)

FEDERAL AWARD YEAR: 2009

CONTROL CATEGORY: Eligibility

Criteria: Basic components of effective internal controls include ensuring written policies and procedures for performing essential duties are adequately documented to ensure compliance with laws, regulations, and grant requirements, and to facilitate an efficient transition of duties when personnel changes occur.

Circular A-133, Subpart C—Auditees § .300 Auditee responsibilities states in part: “The auditee shall: (b) Maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs.”

FTA Circular 9040.1F, Chapter II Program Overview, part 3. STATE ROLE IN PROGRAM ADMINISTRATION states in part: “Where possible, FTA defers to a State’s development of program standards, criteria, procedures and policies to provide the State with the flexibility it needs to standardize its management of FTA assistance and related State programs.”

FTA Circular 9040.1F, Chapter II Program Overview, part 3.a. Role of the State Agency states in part: “The Governor designates a State agency which will have the principal authority and responsibility for administering the Section 5311 program. Specifically, the role of the State agency is to: (1) document the State’s procedures in a State Management Plan (SMP).”

Condition: The Department defines eligible recipients in its State Management Plan for the Administration of the Section 5311 – Nonurbanized Area Formula Grant Program and Rural Transportation Assistance Program. The Department does not, however, have written policies and procedures in place to help ensure eligibility determinations are documented and made in accordance with ODOT’s State Management Plan.

Cause: Management has not established and implemented proper written policies and procedures.

Effect: Eligibility determinations may not have been documented or made in accordance with ODOT’s State Management Plan.

Recommendation: We recommend the Department establish and implement written policies and procedures to ensure eligibility determinations are documented and made in accordance with ODOT’s State Management Plan. Adequate policies and procedures should include a written process to determine eligibility, including verifying the accuracy of information used in eligibility determinations and steps to ensure periodic eligibility re-determinations are made. The Department should also obtain and maintain conflict-of-interest statements for staff who determine eligibility.

Views of Responsible Official(s): The Department does not concur with this finding. The recipient identifies its eligibility type in its annual grant application (Section A.1). Also included with the annual application is Appendix A which contains certification and assurances affirmed by the applicant. To be eligible, the recipient must be a government agency, nonprofit organization, or an Indian tribe. We do not believe a written process, other than what is currently contained in the State Management Plan, is necessary to determine or verify the accuracy. Since a recipient provides annual certification, we do not believe additional eligibility re-determination is needed. Conflict of interest and employee ethical

conduct is listed in ODOT policy B-101-2(3). We do not believe an additional conflict of interest statement for this specific duty is needed.

Contact Person: Kenneth R. LaRue

Contact Person and contact information for high level management official who will assume overall responsibility for ensuring appropriate corrective action:

David Streb – Director of Engineering

dstreb@odot.org

405.521.6916

Auditor Response: Based on substantive testwork, it does not appear eligibility documentation was properly obtained. Written policies and procedures would provide guidance to help ensure eligibility documentation is obtained, determinations are properly made, and personnel are aware of their responsibility to remain independent while making eligibility determinations.