



# Oklahoma State Auditor & Inspector

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December 22, 2011

Gary Ridley, Director  
Oklahoma Department of Transportation  
200 NE 21<sup>st</sup> Street  
Oklahoma City Oklahoma 73105

Dear Mr. Ridley:

This communication is provided pursuant to the parameters of the 2011 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, 2011, 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, 2011, of the ARRA-Formula Grants for Other Than Urbanized Areas program, CFDA 20.509, and the ARRA- Highway Planning and Construction, CFDA 20.205 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, 2011. 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 ARRA-Formula Grants for Other Than Urbanized Areas program and the ARRA- Highway Planning and Construction 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, 2011, we identified deficiencies in internal control over compliance that we consider to be a significant deficiency.

A *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 findings 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,

A handwritten signature in blue ink, appearing to read "Gary A. Jones". The signature is fluid and cursive, with a long horizontal stroke at the end.

GARY A. JONES, CPA, CFE  
OKLAHOMA STATE AUDITOR AND INSPECTOR

## Schedule of Findings

**STATE AGENCY:** Oklahoma Department of Transportation (the Department)

**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-18-X024-00, OK-18-X027-00, OK-18-X035-00, OK-18-X044-00, OK-18-X057-00 (Regular funds), and OK-86-X002-00 (American Recovery and Reinvestment Act (ARRA) Federal funds)

**FEDERAL AWARD YEAR:** 2007, 2008, 2009, 2010 and 2011

**CONTROL CATEGORY:** Activities Allowed or Unallowed; Allowable Costs/Cost Principles; Cash Management; Davis-Bacon Act; Eligibility; Matching and Earmarking; Procurement and Suspension and Debarment; Reporting; Subrecipient Monitoring; Special Tests & Provisions (regular and ARRA Federal funds)

**Criteria:** The five components of internal controls consist of control environment, risk assessment, control activities, information and communication, and monitoring. The Department 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 Department should also periodically assess the quality and effectiveness of the organization's internal control processes and implement appropriate actions when necessary.

**Condition:** Current formal risk assessments of the Department's State and Federal program objectives and related internal controls have not been performed by the Transportation Commission, the Department's management, or the Department's Operations Review and Evaluation (OR&E) Division. Instead, changes to internal controls appear to be based on control deficiencies noted in audit findings by the State Auditor and Inspector's office.

During discussions with Department personnel, communication barriers appeared to exist between the Department's management and operation personnel.

**Cause:** The Department reactively addresses internal control issues based on audit findings issued rather than proactively assessing internal controls through risk assessment procedures to ensure risks are mitigated.

The Department's management does not ensure information is properly communicated to operation personnel.

**Effect:** Unidentified internal control deficiencies and communication barriers may place the Department at a higher risk for errors, fraud, waste and abuse.

**Recommendation:** We recommend the Transportation Commission, the Department's management, and/or the Department's OR&E Division periodically perform risk assessments to evaluate and assess the adequacy and effectiveness of internal controls over the Federal programs and State funds administered by the Department.

We recommend the Department implement procedures to ensure pertinent and important information is properly communicated from the Department's management to operations personnel.

**Views of Responsible Official(s):** The Department concurs in part.

**Contact Person:** John K. Parker, Audit Director

**Anticipated Completion Date:** June 30, 2012

**Corrective Action Planned:** Operations Review and Evaluation Division does consider both State and Federal programs along with all other areas of ODOT's operations during their annual risk assessment. This assessment is the basis for development of our annual audit work plan. However, our evaluation also incorporates the fact that the Federal programs are required to be audited by the State Auditor and Inspectors Office along with constant monitoring by the local FHWA office and periodic audit by FHWA National Review Teams. Based on these reviews, these areas have not been assessed sufficiently high risk rating to rank them within the range of audit areas for the year with the exceptions noted below. Naturally if we find or are notified that significant risk have not been addressed and mitigated then our assessment is adjusted and changes in the audit work plan are considered. Prior to this Finding, we have never received any indication that issues existed which would impact our assessments.

Our audit coverage within the last two years has included compliance with the Davis-Bacon Act both from ODOT's monitoring processes through required data provided by contractors and subcontractors along with verification of this data with contractor's records. These audits have also confirmed posting of required Federal and State notices at job sites. Additionally, we have also audited DBE subcontractor payment compliance by contractors and an audit of the Regulatory Services branch, which oversees the DBE program, has been previously conducted.

Although the findings of the State Auditor and Inspectors Office are generally not available until late in the second quarter or early third quarter there is very a very short time frame for ODOT to implement corrective

action and for OR&E to verify resolution of the issue. However, OR&E will make this a higher priority and be more proactive in these areas.

We would consider any information or data from the State Auditor and Inspectors Office which would aid in the development of future audit work plans.

**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](mailto:mpatterson@odot.org)  
405.521.4768

**Auditor Response:** Determining significant risks and existing issues which would impact OR&E's assessments and/or aid in the development of work plans is the responsibility of the Department and its management.

**FINDING NO: 11-345-004 Repeat Finding**

**STATE AGENCY:** Oklahoma Department of Transportation (the Department)

**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-18-X024-00, OK-18-X027-00, OK-18-X035-00, OK-18-X044-00, and OK-18-X057-00 (regular Federal funds); and OK-86-X002-00 (American Recovery and Reinvestment Act (ARRA) Federal funds)

**FEDERAL AWARD YEAR:** 2007, 2008, 2009, 2010 and 2011

**CONTROL CATEGORY:** Eligibility (regular Federal funds and ARRA funds)

**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, to facilitate an efficient transition of duties when personnel changes occur, and to obtain supporting documentation for transactions and items affecting management decisions. Obtaining supporting documentation reduces the Department's risk of noncompliance.

The Office of Management and Budget (OMB) 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.”

Federal Transit Administration (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);. . . (8) certify eligibility of applicants and project activities.”

**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. Prior to June 17, 2011 the Department did not, however, have written policies and procedures in place to help ensure eligibility determinations are documented and made in accordance with the Department's State Management Plan. 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 Department's subrecipient project files.

The Department also did not have written policies and procedures for re-determination of subrecipients' eligibility. The Department's unwritten procedure was to obtain, review, and maintain an application. However, annually the subrecipient was not required to resubmit the eligibility documentation, listed above, nor did the Department perform procedures to ensure the subrecipient was still eligible.

In the prior year audit we noted that for 3 (16 percent) of the 19 subrecipients, the Department was unable to provide evidence that eligibility documentation was obtained prior to the eligibility determination. During the current year audit, we noted the Department was still unable to provide evidence that eligibility documentation was obtained prior to the eligibility determination for the 3 subrecipients noted in the prior year audit.

On June 17, 2011 the Department published written policies and procedures (with an effective date of July 1, 2011). The eligibility portion states, “Division staff will verify the legitimacy of all documents submitted by the applicant. This process of verification will be performed with each application submitted, or annually at a minimum. Each

Division employee who reviews any application for financial assistance will annually execute a “Transit Programs Division Annual Eligibility-Conflict-of-Interest Statement”.

**Cause:** Prior to July 1, 2011 the Department had not implemented proper written policies and procedures for determining or re-determining eligibility, nor did it follow its stated procedures.

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

**Recommendation:** The Department has implemented written policies and procedures to help ensure eligibility determinations are documented and made in accordance with the Department’s State Management Plan as well as program requirements. However, these policies and procedures were not effective until July 1, 2011, which means there were not written policies and procedures in place during state fiscal year 2011. We recommend the Department establish and implement effective written policies and procedures to ensure eligibility re-determinations are documented and made in accordance with the Department’s State Management Plan as well as program requirements. In addition, 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 and re-determinations of eligibility are performed annually. We also recommend the Department obtain and maintain conflict-of-interest statements for staff who determine eligibility.

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

**Contact Person:** Kenneth R. LaRue

**Anticipated Completion Date:** 07/01/2011

**Corrective Action Planned:** Each Division employee has executed a conflict of interest statement which is on file in the Division’s personnel documents.

**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](mailto:dstreb@odot.org)

405.521.6916

**FINDING NO:** 11-345-005 **Repeat Finding**

**STATE AGENCY:** Oklahoma Department of Transportation (the Department)

**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(American Recovery and Reinvestment Act (ARRA) Federal funds)

**FEDERAL AWARD YEAR:** 2009; 2010; 2011

**CONTROL CATEGORY:** Reporting (ARRA Federal funds): Section 1512 ARRA Report and SF-425 - Federal Financial Report

**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 component objective of an effective internal control system is to ensure policies and procedures for performing essential duties are adequately documented to ensure compliance requirements are met and ensure accurate and reliable information through proper review and approval.

**Condition:** We noted the Department does not have adequate internal controls in place to ensure the following reports presents accurate and reliable information: the Section 1512 ARRA Report for CFDA #20.205 – Highway Planning and Construction, the Section 1512 ARRA Report for CFDA #20.509 – Formula Grants for Other than Urbanized Areas, and the SF-425 – Federal Financial Report for CFDA #20.509 – Formula Grants for Other than Urbanized Areas.

**Cause:** The Department does not have internal controls in place to ensure the accuracy of the reports listed in the condition. The Department relies on other State and Federal entities for reconciliation of the Section 1512 ARRA Report.

**Effect:** The reports listed in the condition may contain improper expenditures. The Department may not be in compliance with the applicable reporting requirements.

**Recommendation:** We recommend the Department develop and document internal controls for the reports listed in the Condition to ensure compliance with the applicable reporting requirements. These internal controls should provide for a detailed review and approval of the reported information prior to submission to the Oklahoma Office of State Finance (Section 1512 ARRA Report) or the Federal Transit Administration (SF-425 – Federal

Financial Report). The internal controls related to the Section 1512 ARRA Report should also provide for a reconciliation of the reported information to the information posted on the Recovery.gov website.

**Views of Responsible Official(s):** We agree with the recommendation.

**Contact Person:** Chelley Hilmes, Comptroller

**Anticipated Completion Date:** June 30, 2012

**Corrective Action Planned:** The Comptroller Division will provide a reconciliation of information reported to the information posted on the Recovery.gov website.

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

Mike Patterson – Deputy Director

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405.521.4768

**FINDING NO:** 11-345-012 **Repeat Finding**

**STATE AGENCY:** Oklahoma Department of Transportation (the Department)

**FEDERAL AGENCY:** United States Department of Transportation

**CFDA NO:** 20.205

**FEDERAL PROGRAM NAME:** Highway Planning and Construction

**FEDERAL AWARD NUMBER:** Not Applicable

**FEDERAL AWARD YEAR:** 2009, 2010, and 2011

**CONTROL CATEGORY:** Reporting – Schedule of Expenditures of Federal Awards (SEFA); Special Tests and Provisions for Awards with ARRA Funding - Presentation on the Schedule of Expenditures of Federal Awards and Data Collection Form (regular and American Recovery and Reinvestment Act (ARRA) Federal funds)

**Criteria:** 2 CFR § 215.21 (b) (3) states, “Recipients’ financial management systems shall provide for the following: Accurate, current and complete disclosure of the financial results of each federally-sponsored project or program in accordance with the reporting requirements set forth in § 215.52.”

A basic component of adequate internal controls is the reconciliation of documentation used to prepare financial statements. The reconciliation should be performed prior to the issuance of financial statements to provide reasonable assurance of the accuracy of the financial statements.

**Condition:** ARRA revenue and expenditure amounts for CFDA #20.205 reported on the state fiscal year (SFY) 2011 SEFA were \$2,937,317 more than the Federal Highway Administration (FHWA) confirmation for Federal revenue. The same variance was noted for regular program (non-ARRA) revenue and expenditure amounts. Based on our inquiry of the variance, the Department discovered an input error in the amount of \$2,937,317 on the weekly billing spreadsheet used to prepare the SFY 2011 SEFA.

The Department utilizes a final voucher spreadsheet to track final vouchers reimbursed by FHWA. The total amount of final voucher reimbursements on this spreadsheet supports the final voucher revenue and expenditure amounts reported on the SEFA for CFDA #20.205. Based on review of the documentation supporting the SFY 2011 SEFA, \$137,141 of final vouchers billed but not received at June 30 were not included in the SFY 2011 SEFA. We also noted one final voucher receivable in the amount of \$556.99 should have been categorized as an ARRA receivable on the SEFA.

**Cause:** The Department does not have adequate internal controls in place to ensure the amount reported on the SEFA is accurate.

**Effect:** ARRA revenue and expenditures for CFDA #20.205 were overstated by \$2,937,317 on the SFY 2011 SEFA. Accounts receivable reported on the SEFA was understated by a total of \$137,141, of which \$556.99 of the total should have been reported as an ARRA receivable.

**Recommendation:** We recommend the Department perform an adequate review of the SEFA and supporting documentation prior to the issuance to ensure the accuracy of the SEFA.

**Views of Responsible Official(s):** We agree with the recommendation.

**Contact Person:** Chelley Hilmes, Comptroller

**Anticipated Completion Date:** March 31, 2012

**Corrective Action Planned:** The Comptroller Division will review our process and supporting documentation to improve reporting accuracy.

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

Mike Patterson – Deputy Director

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