

Management Letter**Department of Transportation
Fiscal Year Ended June 30, 1999**

Financial Audit Division

The Office of the Legislative Auditor (OLA) is a professional, nonpartisan office in the legislative branch of Minnesota State government. Its principal responsibility is to audit and evaluate the agencies and programs of state government (the State Auditor audits local governments).

OLA's Financial Audit Division annually audits the state's financial statements and, on a rotating schedule, audits agencies in the executive and judicial branches of state government, three metropolitan agencies, and several "semi-state" organizations. The division also investigates allegations that state resources have been used inappropriately.

The division has a staff of approximately fifty auditors, most of whom are CPAs. The division conducts audits in accordance with standards established by the American Institute of Certified Public Accountants and the Comptroller General of the United States.

Consistent with OLA's mission, the Financial Audit Division works to:

- Promote Accountability,
- Strengthen Legislative Oversight, and
- Support Good Financial Management.

Through its Program Evaluation Division, OLA conducts several evaluations each year and one best practices review.

OLA is under the direction of the Legislative Auditor, who is appointed for a six-year term by the Legislative Audit Commission (LAC). The LAC is a bipartisan commission of Representatives and Senators. It annually selects topics for the Program Evaluation Division, but is generally not involved in scheduling financial audits.

All findings, conclusions, and recommendations in reports issued by the Office of the Legislative Auditor are solely the responsibility of the office and may not reflect the views of the LAC, its individual members, or other members of the Minnesota Legislature.

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If you have comments about our work, or you want to suggest an audit, investigation, evaluation, or best practices review, please contact us at 651-296-4708 or by e-mail at auditor@state.mn.us



OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

Summary

Management Letter

Department of Transportation Fiscal Year Ended June 30, 1999

Key Findings and Recommendations:

- The Department of Transportation did not enter the correct date for its state aid payments in the state's accounting system. We recommended that the department enter the date that the district engineer approves the local government's request for aid. (Finding 1, page 3)
- The department did not comply with certain federal requirements for the Highway Planning and Construction Program (CFDA 20.205). The department did not comply with selected regulations related to allowable costs, materials testing, and supplemental agreements. We recommended that the department resolve these issues. (Finding 2, page 3)

Management letters address internal control weaknesses and noncompliance issues found during our annual audit of the state's financial statements and federally-funded programs. The scope of work in individual agencies is limited. During the fiscal year 1999 audit, our work at the Department of Transportation focused on selected components of the state's financial statements, including state highway construction expenditures and grants to local governments for road construction and maintenance. The audit included three federal programs administered by the department. The department's response to our recommendations is included in the report.

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Audit Participation

The following staff of the Office of the Legislative Auditor prepared this report:

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Renee Redmer, LPA	Audit Manager
Carl Otto, CPA	Auditor-in-Charge
Fubara Dapper, CPA	Senior Auditor
Kathy Fisher	Intern

Exit Conference

The findings and recommendations in this report were discussed with the following staff of the Department of Transportation at an exit conference held on March 1, 2000:

Ed Cohoon	Chief Financial Officer
Larry Kienitz	Internal Audit Manager
Richard Swanson	Director of Financial Management
Bonnie Kollmann	Director of Financial Operations
Dennis Herzog	Financial Reporting Supervisor

Representative Dan McElroy, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Elwyn Tinklenberg, Commissioner
Department of Transportation

We have performed certain audit procedures at the Department of Transportation (MnDOT) as part of our audit of the financial statements of the State of Minnesota as of and for the year ended June 30, 1999. We also have audited certain federal financial assistance programs administered by MnDOT as part of our audit of the state's compliance with the requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement*. We emphasize that this has not been a comprehensive audit of the Department of Transportation.

Table 1 identifies the financial activities within MnDOT that were material to the state's financial statements. We performed certain audit procedures on these MnDOT programs as part of our objective to obtain reasonable assurance about whether the State of Minnesota's financial statements for the year ended June 30, 1999, were free of material misstatement.

Table 1
Expenditures Material to the State's Financial Statements
Fiscal Year 1999
(in thousands)

<u>Fund</u>	<u>Area</u>	<u>Amount</u>
Trunk Highway	Capital Outlay	\$469,831
County State-Aid Highway	Grants to Counties	\$338,567
Municipal State-Aid Street	Grants to Municipalities	\$109,372
Federal Fund	Federal/County Road and Bridge Grants	\$83,980
	Airport Improvement Grants	\$30,404

Source: State of Minnesota Comprehensive Annual Financial Report and Minnesota Accounting and Procurement System (MAPS) for fiscal year 1999.

The Departments of Revenue and Public Safety deposit fuel tax receipts and motor vehicle registration tax receipts into the Highway User Tax Distribution Fund. Funds are transferred from the Highway User Tax Distribution Fund mainly to the Trunk Highway

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Fund, the County State-Aid Highway Fund, and the Municipal State-Aid Street Fund. Distributions from the Highway User Tax Distribution Fund to MnDOT are identified in Table 2.

Table 2
Highway User Tax Fund Distributions
Fiscal Year 1999
(in thousands)

<u>Fund</u>	<u>Amount</u>
Trunk Highway	\$678,231
County State-Aid Highway	\$345,553
Municipal State-Aid Street	\$100,576

Note: MnDOT provides rail service improvement loans through the Minnesota Rail Service Assistance Act of 1976. Outstanding rail service improvement loans as of June 30, 1999, totaled \$18.5 million.

Source: State of Minnesota Comprehensive Annual Financial Report and Minnesota Accounting and Procurement System (MAPS) for fiscal year 1999.

Table 3 identifies the State of Minnesota's major federal programs administered by the Department of Transportation. We performed certain audit procedures on these Department of Transportation programs as part of our objective to obtain reasonable assurance about whether the State of Minnesota complied with the types of compliance requirements that are applicable to each of its major federal programs. We worked in conjunction with the MnDOT Internal Audit Section to perform the Single Audit work.

Table 3
Major Federal Programs Administered by the Department of Transportation
Fiscal Year 1999
(In thousands)

<u>Program Name</u>	<u>Federal Funds</u>
Highway Planning and Construction – CFDA 20.205	\$312,218
Airport Improvement Program – CFDA 20.106	\$30,404
Aviation Education – CFDA 20.100	\$5,184

Source: Minnesota Accounting and Procurement System (MAPS) for fiscal year 1999.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Conclusions

In accordance with *Government Auditing Standards*, we issued our report, dated December 1, 1999, on our consideration of the State of Minnesota's internal control over

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financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. At a later date, we will issue our report on compliance with requirements applicable to each major federal program and internal control over compliance in accordance with OMB *Circular A-133*.

As a result of our audit procedures and the result of the Federal Compliance Review performed by the MnDOT Internal Audit Section, we identified the following weaknesses in internal control at the Department of Transportation.

1. The Department of Transportation did not properly record the date of liability for state aid grants in the accounting system.

The Department of Transportation did not enter the correct date of liability in the state's accounting system for state aid grant payments to cities and counties. As a result of our audit work, we made adjustments of approximately \$5.6 million to the state's draft financial statements for the year ended June 30, 1999. The payments are initially paid through the state aid subsystem and subsequently entered in the state's accounting system with a journal voucher entry. The payable date (record date) entered in the subsystem was the date the state aid division approved the invoice. MnDOT should use the date that the liability is incurred, which is the date that the state district engineer authorizes the invoice for payment. The correct liability date is important to determine accounts payable for financial reporting purposes. The Department of Finance summarizes all payments with a record date of June 30 or prior as accounts payable in the state's annual financial statements.

Recommendation

- *The Department of Transportation should enter the date the district state aid engineer approves the request from the city or county as the record date in the state's accounting system.*

2. The Department of Transportation did not comply with certain federal requirements for the Highway Planning Construction Program.

The Department of Transportation did not have adequate controls to ensure compliance with certain regulations related to allowable costs, materials testing, and supplemental agreements. The MnDOT Internal Audit Section issued a report to MnDOT management describing reportable conditions involving internal control over compliance related to the Highway Planning and Construction Program (CFDA 20.205). The internal audit report had six findings and one observation citing concerns related to allowable costs, materials testing, and supplemental agreements. Following are the internal audit findings:

- Prior Audit Recommendation Partially Implemented: Controls established to account for and classify bridge paint residue need improvement.

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- Bituminous production controls need improvement to ensure attainment of pavement performance and life expectations.
- Prior Audit Recommendation Partially Implemented: Additional management oversight is needed to ensure existing requirements for supplemental agreement work and payments are followed.
- Prior Audit Recommendation Partially Implemented: Additional opportunities exist to improve controls over materials certification audits performed by the Office of Materials and Road Research.
- The department should develop a policy for the timely application of incentive and disincentive payments to contractors.
- The department should clarify asphalt binder property testing requirements.

In addition to the above findings, MnDOT's Internal Audit Section had the following observation:

- Opportunities exist to improve bituminous pavement performance through the use of 2350 bituminous specification.

Recommendation

- *The Department of Transportation should resolve these weaknesses in internal control and noncompliance and implement the recommendations in a timely manner.*

This report is intended for the information of the Legislative Audit Commission and the management of the Department of Transportation. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 14, 2000.

/s/ *James R. Nobles*

James R. Nobles
Legislative Auditor

/s/ *Claudia J. Gudvangen*

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: January 21, 2000

Report Signed On: March 8, 2000

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Status of Prior Audit Issues As of January 21, 2000

March 5, 1999, Legislative Audit Report 99-14 examined MnDOT's activities and programs material to the State of Minnesota's Annual Financial Report and the Single Audit for the year ended June 30, 1998. The audit covered the Highway Planning and Construction Program (CFDA 20.205), the Airport Improvement Program (CFDA 20.106), County State-Aid Highway Fund grants, Municipal State-Aid Street Fund grants, and bridge construction. This report included one finding describing various concerns related to internal control over compliance related to the Highway Planning and Construction Program. Some of these concerns were carried forward to this report. These concerns, including some new issues, are discussed in Finding 2.

State of Minnesota Audit Follow-Up Process

The Department of Finance, on behalf of the Governor, maintains a quarterly process for following up on issues cited in financial audit reports issued by the Legislative Auditor. The process consists of an exchange of written correspondence that documents the status of audit findings. The follow-up process continues until Finance is satisfied that the issues have been resolved. It covers entities headed by gubernatorial appointees, including most state agencies, boards, commissions, and Minnesota state colleges and universities. It is not applied to audits of the University of Minnesota, any quasi-state organizations, such as the metropolitan agencies or the State Agricultural Society, the state constitutional officers, or the judicial branch.



Minnesota Department of Transportation

Transportation Building

395 John Ireland Boulevard
Saint Paul, Minnesota 55155-1899

March 8, 2000

James Nobles, Legislative Auditor
1st Floor – Centennial Office Building

Dear Mr. Nobles:

Thank you for your letter of February 18, 2000 and the attached report. We certainly appreciate all of the time and effort that went into your financial audit review for Fiscal Year 1999.

Regarding Finding 1 - “The Department of Transportation did not enter the correct date for its state aid payments in the state’s accounting system,” we agree with your recommendation that the department enter the date that the district engineer approves the local government’s request for aid. In fact, that recommendation has already been implemented.

Regarding Finding 2 - “The Department of Transportation did not comply with certain federal requirements for the Highway Planning Construction Program” (which is a summation of six findings contained in our internal audit’s single audit report), our Division Directors were asked to respond to the various findings and recommendations. Our Chief Financial Officer reviews those responses and makes a determination whether any further action is required. All of the detailed responses are contained in Mn/DOT’s Internal Audit Report No. 00-800-77 dated December 21, 1999.

Progress towards implementation of specific recommendations will be monitored. The contact person for information on that follow-up activity will be Dennis Herzog. He can be reached at (651) 297-1481.

Sincerely,

/s/ Elwyn Tinklenberg

Elwyn Tinklenberg
Commissioner