



# Department of Transportation

## State Infrastructure Bank Audit

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**Audit Period: June 30, 2009 through March 30, 2011**



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## Contents

Executive Summary .....	3
Background .....	3
Scope and Objectives.....	4
Summary of Observations .....	5
Detailed Observation and Recommendation .....	6
Observation 1 – Standardized Review Protocols .....	6
Appendix A – Classification of Audit Objective Conclusions and Audit Observations .....	7
Classification of Audit Objective Conclusions .....	7
Classification of Audit Observations .....	7
Appendix B – Audit Follow-up Procedures .....	8



## Executive Summary

### Background

Ohio's State Infrastructure Bank (SIB) is a program that provides direct loans and financing of local government bonds. The SIB is used as a method of funding highway, rail, transit, intermodal, and other transportation projects, which produce revenue to amortize debt while enhancing Ohio's transportation system. This program is authorized under the Ohio Revised Code, Chapter 5531, for the purpose of developing transportation facilities throughout Ohio.

With the assistance of the Office of the Treasurer of State, the Department of Transportation (DOT) established two investment grade bond funds to leverage the SIB funds available to local entities. The general revenue bond program was established in September 2006 and the Federal Title 23 bond program was established in July 2008. Both funds are structured with an open indenture, which allows bonds to be issued as needed, on a project-by-project basis.

With each bond fund, all repayments from the existing General Revenue and Title XXIII loan portfolio accounts are pledged to support any borrower repayment shortfall. This pledge is followed by all cash in each respective account and is additionally supported by a bond reserve fund that can also be accessed in the event of a borrower defaulting or having a shortfall in payment. Each bond program can issue approximately \$50 million in bonds.

Since the beginning of the program, the SIB has issued 131 loans and two bond issuances totaling over \$404 million. As of October 31, 2010, there are 72 loans outstanding with a principle balance totaling over \$113 million. As of March 31, 2011 there are two bonds with an original amount totaling \$29 million and an outstanding principle balance totaling \$25 million. These bonds are handled through the state treasury and not through DOT.

During the audit, OIA identified opportunities for DOT to strengthen internal controls and improve business operations. A summary, along with detailed observations, have been provided. OIA would like to thank DOT staff and management for their cooperation and time in support of this audit.

This report is solely intended for the information and use of agency management and the State Audit Committee. It is not intended for anyone other than these specified parties.



## Scope and Objectives

OIA staff was engaged to perform assurance work related to the DOT State Infrastructure Bank. This work was completed between January 2011 and May 2011. The scope of the audit included the following areas:

- State Infrastructure Bank
  - Awarding Process
  - Collection of Payments from Outstanding Loans Process
  - Reporting Process
  - Program Oversight and Monitoring Process

The following summarizes the objectives of the review along with a conclusion on the effectiveness of management’s internal controls.

Objective	Conclusion <sup>1</sup>
Evaluate the design and effectiveness of the awarding process of State Infrastructure Bank program.	Improvements Needed See Observation 1
Evaluate the design and effectiveness of the State Infrastructure Bank collection process.	Well Controlled
Evaluate the effectiveness of reporting program activities.	Well Controlled with Improvement Needed
Evaluate the effectiveness of DOT’s monitoring efforts performed on the State Infrastructure Bank.	Well Controlled

<sup>1</sup> Refer to Appendix A for classification of audit objective conclusions.



## Summary of Observations

The Summary of Observations includes only those risks which were deemed high or moderate. Low risk observations were discussed with individual agency management and are not part of this report. However, the low risk observations were considered as part of the audit objective conclusions on the previous page.

No.	Observation	Risk <sup>2</sup>
1.	<b>Standardized Review Protocols</b> – State Infrastructure Bank (SIB) management utilizes an informal review process to evaluate project applications and does not include a standard review protocol to detail whether eligibility requirements were met.	<b>Moderate</b>

Due to the limited nature of our audit, we have not fully assessed the cost-benefit relationship of implementing the observation and recommendation suggested above. However, this observation reflects our continuing desire to assist your department in achieving improvement in internal controls, compliance, and operational efficiencies.

<sup>2</sup> Refer to Appendix A for classification of audit observations.



## Detailed Observation and Recommendation

### Observation 1 – Standardized Review Protocols

A sound internal control framework has established policies and procedures to help ensure the actions initiated by management address risks and achieve the entity’s objectives. Ohio Administrative Code Section 5501:6-1-06 lists eligibility criteria for evaluating projects to determine if the application qualifies for a State Infrastructure Bank (SIB) loan. 23 US Code, Section 602 and 49 US Code, Section 5305 include the requirements a project must meet in order to be eligible for federal funding of the SIB loan.

The State Infrastructure Bank (SIB) program has an informal review process that is used to evaluate each project application received; however, standardized review protocols to document the evaluation process of loan applications is not utilized. In addition, the State Infrastructure Bank Loan Committee has not documented the evaluation methodology that directs how their reviews of the loan applications are to be accomplished and documented, including if all eligibility requirements have been met in order to be funded using both federal and state funding.

The risk of undocumented review protocols could create an incomplete or inconsistent review of projects to determine if the borrower is to be awarded the loan. Not documenting the evaluation methodology process of the eligibility criteria could result in an inadequate evaluation of loan applications where criteria is missed or not evaluated and could result in awarding SIB loans to ineligible borrowers. Also, the Committee may be unable to support conclusions reached.

#### Recommendation

In order to ensure consistent loan application review and business continuity, the Division of Finance and Forecasting, Office of Budget and Forecasting should develop formalized policies and procedures and review protocols for evaluating SIB loan applications.

The State Infrastructure Bank Loan Committee should develop and document their review methodology. The methodology should include all eligibility criteria outlined in state and federal law. All decisions made by the Committee should be documented as part of the process. This will help to ensure compliance with applicable laws and can be used as support for decisions.

#### Management Response

ODOT agrees with this recommendation. A checklist will be developed to incorporate with the SIB loan committee approval sheet. Items to be included on the list will be researched with other state DOT’s and the Federal Highway Administration. Review items for the checklist may include eligibility of funding source, recommended funding account, and the applicant’s financial stability.

Risk	Remediation Owner	Estimated Completion Date
Moderate	SIB Program Administrator Projects	September 2011



## Appendix A – Classification of Audit Objective Conclusions and Observations

### Classification of Audit Objective Conclusions

Conclusion	Description of Factors
<b>Major Improvements Needed</b>	Weaknesses are present that could potentially compromise achievement of its overall purpose. The impact of weaknesses on management of risks is widespread due to the number or nature of the weaknesses.
<b>Improvements Needed</b>	Weaknesses are present that compromise achievement of one or more control objectives but do not prevent the process from achieving its overall purpose. While important weaknesses exist, their impact is not widespread.
<b>Well-controlled with Improvements Needed</b>	The processes have design or operating effectiveness deficiencies but do not compromise achievement of important control objectives.
<b>Well-Controlled</b>	The processes are appropriately designed and/or are operating effectively to manage risks. Control issues may exist, but are minor.

### Classification of Audit Observations

Rating	Description of Factors	Reporting Level
<b>High</b>	Observation has broad (state or agency wide) impact and possible or existing material exposure requiring immediate agency attention and remediation.	State Audit Committee, Senior Management, Department Management
<b>Moderate</b>	Observation has moderate impact to the agency. Exposure may be significant to unit within an agency, but not to the agency as a whole. Compensating controls may exist but are not operating as designed. Requires near-term agency attention.	State Audit Committee, Senior Management, Department Management
<b>Low</b>	Observation poses relatively minor exposure to an agency under review. Represents a process improvement opportunity.	Department Management, Senior Management (Optional), State Audit Committee (Not reported)



## Appendix B – Audit Follow-up Procedures

OIA will periodically follow-up on management's plans to remediate high and moderate risk audit observations. Follow-up activities may generally be broken down into three categories:

- Detailed** Detailed follow-up is usually more time-consuming and can include substantial audit customer involvement. Verifying and testing procedures implemented as well as substantiating records are examples. The more critical audit observations usually require detailed follow-up.
- Limited** Limited follow-up typically involves more audit customer interaction. This may include actually verifying procedures or transactions and, in most cases, cannot be accomplished through memos or telephone conversations with the audit customer but requires onsite observation or testing.
- Informal** This is the most basic form of follow-up and may be satisfied by review of the audit customer's procedures or an informal telephone conversation. Memo correspondence may also be used. This is usually applicable to the less critical observations.

Low risk audit observations will not result in an OIA audit follow-up, although these observations will be factored into the continuous risk assessment process for future OIA engagements.