



## Department of Transportation

# Local Public Agency Agreements Audit

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**Audit Period: July 1, 2010 through January 31, 2011**



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## Executive Summary

### Background

The Ohio Department of Transportation's (DOT) primary function is to plan, design, construct, and maintain the state's network of highways and bridges. The Department provides financial and technical assistance to the state's public transit systems, general aviation airports, and railways. Primary funding sources include state and federal motor fuel taxes and bonds, as well as funding from the State's General Revenue Fund (GRF) for non-highway programs, such as rail, transit, and aviation.

Ohio Revised Code Section 5501.03 gives the DOT authority to coordinate its activities with those of other appropriate state departments, public agencies, and authorities, and enter into contracts with such departments, agencies, and authorities as may be necessary to carry out its duties, powers, and functions. In fiscal year 2010, DOT awarded funding for 346 projects totaling approximately \$489 million to local governments. These projects are referred to as Local-Public-Agency projects or LPA-let projects (LPA).

The DOT, acting as a pass-through agency for the Federal Highway Administration (FHWA), has the responsibility for performing reviews of LPAs receiving federal funds. Through these reviews DOT validates compliance with the LPA Project Agreement, Title 23 United States Code-Section 116 and provisions of the Ohio Revised Code, and determines the degree compliance with those laws, regulations, and contractual obligations.

This audit will focus on DOT's process for monitoring the LPAs. LPAs are defined as any local political subdivision, airport authority, regional transit authority, or county transit board.

DOT's monitoring of LPAs consists of two types of reviews: Quality Assurance Reviews (QARs) and financial reviews. QARs are conducted by the DOT LPA Program Office and center around LPA compliance with applicable laws, regulations, policies, and standard operating procedures, generally QARs are performed annually. It is the responsibility of the DOT Division Deputy Directors and District Deputy Directors to ensure noncompliance items are brought into compliance in a timely manner. Financial reviews are conducted by the DOT Finance and Forecasting Department and consist of reviewing LPA financial activity.

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 Local Public Agency (LPA) Agreements audit during fiscal year 2011. This work was completed between December 2010 and January 2011. The scope of this audit included the following areas:

- Local Public Agency Monitoring
  - Program oversight and monitoring
  - Communication of monitoring efforts to applicable authorities

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

Objective	Conclusion <sup>1</sup>
Evaluate the adequacy of DOT’s risk assessment used to prioritize the sequencing, timing and extent of the monitoring efforts performed on the LPAs.	Improvements Needed See Observation 1
Evaluate the adequacy of DOT’s policies and procedures for monitoring the LPAs.	Well Controlled
Evaluate the adequacy of DOT’s audit protocols/programs to validate if protocols/programs included steps intended to review priority areas of the Local Public Agencies.	Improvements Needed See Observation 2
Evaluate the adequacy of DOT’s documentation/evidence of audits performed on LPAs including supervisory reviews of completed audits.	Well Controlled
Evaluate the adequacy of DOT’s process for communicating the results of its monitoring efforts to the LPAs, requirements for corrective action plans being submitted and follow-up to validate their remediation.	Well Controlled with Improvement Needed
Evaluate the adequacy of DOT’s process for submission of the results of its monitoring efforts to senior DOT management so that the information can be used to administer the program.	Well Controlled with Improvement Needed

<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 prior page.

No.	Observation	Risk <sup>2</sup>
1.	<b>Risk Assessment and Monitoring</b> – The Section of Local Projects does not utilize a risk-based approach to analyze the Local Public Agencies (LPA) to prioritize their monitoring efforts. The Section does not document the methodology used to determine which projects were selected to be monitored for the upcoming fiscal year. The Office of Audits, however, does have a methodology in place for selection of projects for monitoring, but has not formally documented the methodology.	Moderate
2.	<b>Maintenance Monitoring and Program Oversight</b> – For the review period of fiscal year 2011, DOT had no evidence to validate its compliance with Federal law and its own requirement, the LPA Maintenance Monitoring and Oversight Program procedure, for any LPA project inspections. The Maintenance Monitoring Policy had not been reviewed or updated since June 2008.	Moderate

Due to the limited nature of our audit, we have not fully assessed the cost-benefit relationship of implementing the observations and recommendations suggested above. However, these observations reflect our continuing desire to assist DOT in achieving improvements in internal controls, compliance, and operational efficiencies.

<sup>2</sup> Refer to [Appendix A](#) for classification of audit observations.



## Detailed Observations and Recommendations

### Observation 1 – Risk Assessment and Monitoring

The Committee Of Sponsoring Organizations' (COSO) internal control framework states that internal control systems need to be monitored through ongoing monitoring activities and/or separate evaluations. Effective monitoring processes employ a risk-based approach to identify projects that should be monitored.

The Section of Local Projects does not utilize a risk-based approach to analyze Local Public Agencies (LPA) for selection of projects to review and monitor and does not formally document the methodology used to determine which projects were selected to be monitored for the upcoming fiscal year. The Office of Audits, however, has a methodology in place for selection of projects to review and monitor, but has not formally documented the methodology.

For fiscal year 2011, DOT's Section of Local Projects did not conduct QARs (Quality Assurance Reviews) on any LPAs. QARs were conducted at the DOT district offices only. Management of the Section of Local Projects stated it was their goal to complete QARs on the LPAs for fiscal year 2012.

A risk assessment will aid the Department of Transportation (DOT) in identifying higher risk LPA projects so management can make informed decisions on the audit timing and scope for those agencies.

The lack of a risk-based monitoring process increases the risk that DOT's resources may not be effectively deployed to monitor and mitigate the LPA projects possessing the highest risks. Also, the lack of not performing reviews at the LPA level can increase the risk that LPAs are not in compliance with the LPA Project Agreement, as well as Federal and State requirements.

#### Recommendation

The Section of Local Projects should develop and document a formal risk assessment process to assist in determining which LPAs or projects represent a higher risk and should be a priority for review. The risk assessments may include:

- Developing standardized risk profiles of LPAs which should include performance issues;
- Developing weighted risk factors relating to entity attributes and significant audit areas that can be used as a basis to quantify risk;
- Developing measurable program outputs and outcomes and the tools to measure the outputs and outcomes, such as dollar amount disbursed to the subrecipient, length of time since the last review, A-133 findings noted in the Single Audit Reports, findings released in DOT financial and programmatic reports;
- An evaluation of whether the integration of all the Division of Finance and Forecasting-Office of Audits and Section of Local Projects types of reviews and audits should be combined into one cohesive risk rating and audit plan; and



- Formally document the results of the risk assessment and consider periodically evaluating its risk plan to determine whether the risks identified in previous years remain key risks or need updated to include higher risk areas.

In addition, the Division of Finance and Forecasting-Office of Audits should formally document its risk assessment approach. The DOT Section of Local Projects should implement a plan to perform QARs of LPAs for fiscal year 2012. DOT should use a risk-based approach to determine which LPAs will be included in its QAR process for the period. This will help to increase oversight and monitoring of the LPAs and ensure compliance with applicable laws and regulations.

**Management Response**

The DOT Section of Local Projects will formalize a QAR Monitoring Plan, in accordance with the ODOT QAR Policy and Standard Procedures, LPA QARs to be performed in SFY 2012. A documented risk-based approach will be developed and utilized to determine which LPAs will be included in the SFY 2012 QAR period.

The Division of Finance and Forecasting – Office of Audits will formally document its LPA risk assessment by June 30, 2011.

Risk	Remediation Owner	Estimated Completion Date
<b>Moderate</b>	LPA Coordinator, Section of Local Projects; Administrator – Office of Audits	June 2011



## Observation 2 – Maintenance Monitoring and Oversight Program

Title 23 of the United States Code, Section 116 states “It shall be the duty of the State transportation department to maintain, or cause to be maintained, any project constructed” with the use of Federal funding. The Local Public Agency (LPA ) Maintenance Monitoring and Oversight Program requires the Section of Local Projects to select a minimum of 10 completed LPA projects to ensure the LPA is providing maintenance activity to the project improvements. Department of Transportation (DOT) is required to complete maintenance inspections to help ensure the derived benefit from the project, as noted in the agreement between DOT and the LPA, is being achieved.

For the review period covering FY 2011, DOT had no evidence to validate compliance with the LPA Maintenance Monitoring and Oversight Program procedure for any LPA project inspections. The Maintenance Monitoring Policy had not been reviewed or updated since June 2008.

Regular reviews of policies and procedures help to ensure the policy is still in line with the goals and mission of the agency. The protocols and programs appeared to be complete; containing all essential information including significant laws and regulations, critical review areas, and DOT expectations.

Lack of maintenance monitoring can result in the risk that the LPA does not fulfill its responsibility to adequately maintain the project improvements which could affect awarding of future funding to the LPA.

### Recommendation

Conduct and follow the procedures in its LPA maintenance monitoring plan for the remainder of FY 2011. The Maintenance Monitoring Program policy should be reviewed periodically by the LPA Coordinator for any necessary updates or changes.

### Management Response

The DOT Section of Local Projects will complete LPA Maintenance Reviews in accordance with the procedures contained in the Ohio Department of Transportation LPA Maintenance Monitoring and Oversight Program for SFY 2011.

Risk	Remediation Owner	Estimated Completion Date
<b>Moderate</b>	LPA Coordinator, Section of Local Projects	April 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.