

FINANCIAL RELATED AUDIT
OF THE
USE OF TRANSPORTATION-RELATED FUNDING

October 1, 2001 through September 30, 2002

“...The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.”

– Article IV, Section 53 of the Michigan Constitution

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Michigan
Office of the Auditor General
REPORT SUMMARY

Financial Related Audit

Use of Transportation-Related Funding

Report Number:
 07-629-04

Released:
 March 2004

Act 59, P.A. 2001, requires State agencies that receive transportation-related funding for providing tax and fee collection and other services for transportation funds to contract with the Michigan Department of Transportation (MDOT). These agencies are also required to annually report the amount of funding contracted for, expended from, and returned to the transportation funds. The Office of the Auditor General is required to report to the Legislature on the charges to transportation funds by State agencies.

Background:

In fiscal year 2001-02, transportation-related funding was provided to the following State agencies: the Departments of State, Management and Budget (DMB), Treasury, State Police, Civil Service, Attorney General, Environmental Quality, and Transportation; the Michigan Economic Development Corporation; the Office of the Auditor General; and the Mackinac Island State Park Commission.

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Audit Objective:

To determine the adequacy of the cost allocation methodologies used to identify transportation-related costs and the appropriateness of charges to transportation funds.

Audit Conclusion:

We determined that 10 of the 11 State agencies that received transportation funding had adequate cost allocation methodologies to identify transportation related costs. We also determined that 10 of the 11 State agencies made appropriate charges to transportation funds. Our audit

disclosed a reportable condition regarding MDOT's cost allocation methodology and the Department of Treasury's incorrect calculation of transportation-related charges (Finding 1).

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Audit Objective:

To determine whether unused transportation funds' appropriations were returned to the appropriate transportation fund.

Audit Conclusion:

We determined that all the State agencies had returned their unused transportation fund appropriations for fiscal year 2001-02 to the appropriate transportation fund.

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Audit Objective:

To determine compliance with contractual and reporting requirements for transportation-related funding as prescribed by the appropriations acts.

Audit Conclusion:

We determined that all 10 State agencies had executed the required contracts with MDOT for fiscal year 2001-02. However, only 8 of the 10 State agencies submitted an annual report as required by the appropriations act. Our audit disclosed a reportable condition regarding DMB's reporting procedures (Finding 2).

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Agency Response:

MDOT and the Department of Treasury responded that they agree with the recommendations directed to them. DMB responded that it would consider the recommendation.

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A copy of the full report can be obtained by calling 517.334.8050 or by visiting our Web site at: <http://www.audgen.michigan.gov>



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AUDITOR GENERAL

March 1, 2004

The Honorable Shirley Johnson, Chairperson
Senate Appropriations Committee
Michigan Senate
and
The Honorable Marc Shulman, Chairperson
House Appropriations Committee
Michigan House of Representatives
State Capitol
Lansing, Michigan

Dear Senator Johnson and Representative Shulman:

This is the financial related audit of the Use of Transportation-Related Funding by the Departments of State, Management and Budget, Treasury, State Police, Civil Service, Attorney General, Environmental Quality, and Transportation; the Michigan Economic Development Corporation; the Office of the Auditor General; and the Mackinac Island State Park Commission for the period October 1, 2001 through September 30, 2002, as required by Section 306, Act 59, P.A. 2001.

This report contains our report summary; description of funding requirements; audit objectives, audit scope, and agency responses and prior audit follow-up; comments, findings, recommendations, and agency preliminary responses; detailed review comments by agency, a summary of annual reports of transportation-related funding used, and a summary of charges and transfers among transportation funds, presented as supplemental information; and a glossary of acronyms and terms.

Our comments, findings, and recommendations are organized by audit objective. The agency preliminary responses were taken from the agencies' responses subsequent to our audit fieldwork. The *Michigan Compiled Laws* and administrative procedures require that the audited agencies develop a formal response within 60 days after release of the audit report.

We appreciate the courtesy and cooperation extended to us by the agencies reviewed during this audit.

AUDITOR GENERAL

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Description of Funding Requirements

Act 59, P.A. 2001, requires State agencies that receive transportation-related funding for providing tax and fee collection and other services for transportation funds to contract with the Michigan Department of Transportation. The contracts must include estimated costs to be recovered from transportation funds, a description of the services financed by transportation funds, and cost allocation methods and rationale for the portion of costs allocated to transportation funds. These agencies are also required to annually report the amount of funding contracted for, expended from, and returned to the transportation funds.

In fiscal year 2001-02, transportation-related funding of \$118,116,732 was provided to the following 10 State agencies: the Departments of State, Management and Budget, Treasury, State Police, Civil Service, Attorney General, and Environmental Quality; the Michigan Economic Development Corporation; the Office of the Auditor General; and the Mackinac Island State Park Commission. Information regarding the charges and transfers among the transportation funds is presented as supplemental information.

Audit Objectives, Audit Scope, and Agency Responses and Prior Audit Follow-Up

Audit Objectives

Our financial related audit* of the Use of Transportation-Related Funding had the following objectives:

1. To determine the adequacy of the cost allocation methodologies used to identify transportation-related costs and the appropriateness of charges to transportation funds.
2. To determine whether unused transportation funds' appropriations were returned to the appropriate transportation fund.
3. To determine compliance with contractual and reporting requirements for transportation-related funding as prescribed by the appropriations acts.

Audit Scope

Our audit was required by Section 306, Act 59, P.A. 2001. Our audit scope was to examine the financial and other records supporting transportation-related costs and charges to transportation funds for the period October 1, 2001 through September 30, 2002. Our audit was conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances, except that we were not independent in regards to the Office of the Auditor General.

In connection with our audit, we compiled supplemental information about the agencies' use of transportation-related funding based on information provided by the agencies and the Michigan Department of Transportation (MDOT). Our audit was not directed toward expressing an opinion on the supplemental information and, accordingly, we express no opinion on it.

* See glossary at end of report for definition.

Agency Responses and Prior Audit Follow-Up

Our audit report includes 2 findings and 3 corresponding recommendations. MDOT and the Department of Treasury responded that they agree with the recommendations directed to them. The Department of Management and Budget responded that it would consider the recommendation.

The agency preliminary response that follows each recommendation in our report was taken from the agencies' written comments and oral discussion subsequent to our audit fieldwork. Section 18.1462 of the *Michigan Compiled Laws* and Department of Management and Budget Administrative Guide procedure 1280.02 require the audited agencies to develop a formal response to our audit findings and recommendations within 60 days after release of the audit report.

We released our prior financial related audit of the Use of Transportation-Related Funding in April 2003. Various agencies that received transportation-related funding complied with 2 of the 4 prior audit recommendations. One prior audit recommendation was repeated, and the other was rewritten for inclusion in this report.

COMMENTS, FINDINGS, RECOMMENDATIONS, AND AGENCY PRELIMINARY RESPONSES

COST ALLOCATION METHODOLOGIES AND TRANSPORTATION FUNDS' CHARGES

COMMENT

Audit Objective: To determine the adequacy of the cost allocation methodologies used to identify transportation-related costs and the appropriateness of charges to transportation funds.

Conclusion: We determined that 10 of the 11 State agencies that received transportation funding had adequate cost allocation methodologies to identify transportation related costs. We also determined that 10 of the 11 State agencies made appropriate charges to transportation funds. Our audit disclosed a reportable condition* regarding the Michigan Department of Transportation's (MDOT's) cost allocation methodology and the Department of Treasury's incorrect calculation of transportation-related charges (Finding 1).

FINDING

1. Cost Allocation Methodologies

MDOT had not implemented detailed cost allocation methodologies to identify and equitably allocate departmental costs related to local units of government. In addition, the Department of Treasury did not properly calculate transportation-related charges based on its approved cost allocation methodology.

Section 504, Act 59, P.A. 2001, requires annual contracts between MDOT and other State agencies providing services applicable to transportation funds. The contracts shall include the estimated costs, description of services provided, and detailed cost allocation methods that are appropriate to the type of services provided and supporting rationale for the portion of costs allocated to transportation funds.

* See glossary at end of report for definition.

We reviewed the adequacy of the cost allocation methodologies used and the appropriateness of the charges to the transportation funds for 10 State agencies and within MDOT (see the detailed review comments by agency and MDOT's allocation of transportation costs within its own department, presented as supplemental information). Our review noted:

- a. During our audit period, MDOT completed a cost allocation study that identifies all costs associated with activities directed at local units of government and identifies methods for the equitable allocation of all costs to the local units of government and the State Trunkline Fund. However, MDOT indicated that it does not plan to implement changes to the cost allocation methodology until fiscal year 2004-05.
- b. The Department of Treasury did not properly calculate transportation-related charges based on its approved methodology. The contract with MDOT specified a cost allocation methodology based on expenditures related to the collection of transportation taxes. However, the Department of Treasury included costs related to non-tax collection activity in its calculation. Consequently, the Department of Treasury overbilled the State Aeronautics Fund and the Michigan Transportation Fund by \$25,175 and \$7,844, respectively.

RECOMMENDATIONS

We recommend that MDOT implement detailed cost allocation methodologies to identify and equitably allocate departmental costs related to local units of government.

We also recommend that the Department of Treasury properly calculate transportation-related charges based on its approved cost allocation methodology.

AGENCY PRELIMINARY RESPONSE

MDOT agrees with the recommendation directed to it and concurs that it needs to implement a detailed cost methodology for those areas within MDOT that do not equitably allocate costs related to local units of government. MDOT informed us that its completed cost allocation study concluded that most areas within MDOT are currently using a methodology that identifies and equitably allocates charges reasonably. For those areas where changes to the current methodology are

recommended, MDOT is initiating changes that will identify and equitably allocate charges related to local units of government. Some changes were made in the closing of the fiscal year 2002-03 books and other changes were made in the fiscal year 2004-05 budget request, but all changes will not likely be able to be completed until the fiscal year 2005-06 budget cycle.

The Department of Treasury agrees with the recommendation directed to it and will restrict its calculation to tax collection related activity.

UNUSED TRANSPORTATION FUNDS' APPROPRIATIONS

COMMENT

Audit Objective: To determine whether unused transportation funds' appropriations were returned to the appropriate transportation fund.

Conclusion: We determined that all the State agencies had returned their unused transportation fund appropriations for fiscal year 2001-02 to the appropriate transportation fund.

CONTRACTUAL AND REPORTING REQUIREMENTS

COMMENT

Audit Objective: To determine compliance with contractual and reporting requirements for transportation-related funding as prescribed by the appropriations acts.

Conclusion: We determined that all 10 State agencies had executed the required contracts with MDOT for fiscal year 2001-02. However, only 8 of the 10 State agencies submitted an annual report as required by the appropriations act. Our audit disclosed a reportable condition regarding proper reporting (Finding 2).

FINDING

2. Proper Reporting

The Department of Management and Budget (DMB) had not developed procedures for State agencies to ensure proper and consistent annual reporting of charges to transportation funds.

Detailed reporting procedures would assist State agencies in defining which expenditures and services should be reflected in the annual reports and in determining if an annual report should be filed.

Section 504, Act 59, P.A. 2001, requires that each agency submit a written report to the State Budget Director and the Auditor General stating, by spending authorization account, the amount of estimated funds contracted with MDOT, the amount of funds expended, and the amount of funds returned to the transportation funds.

In our review of transportation-related expenditures and the annual reports submitted by the agencies, we noted:

- a. Two agencies did not include miscellaneous charges of \$40,933 on their annual reports. These charges were reimbursed via expenditure credit or revenue debit. The other agencies generally included these types of charges in their annual reports.
- b. Agencies did not utilize consistent methodologies for reporting the "amount of funds expended." Some agencies reported transportation-related expenditures as the amount of funding received from MDOT, some reported the amount of expenditures incurred in providing the service, and others included encumbrances. Although DMB Administrative Guide procedure 1210.27, Attachment A, allows for encumbrances to be included, most agencies generally did not include encumbrances in the amounts expended.
- c. Two agencies did not submit their annual reports because of executive reorganizations and changes in personnel that resulted in the agencies being unaware of the reporting requirements. We assisted one agency, with transportation-related expenditures of about \$1.9 million, in preparing its table for inclusion as supplemental information in this report. The other agency's

charges of \$35,000 were not material; consequently, we did not prepare a separate table but did include its charges in the summary of annual reports of transportation-related funding used.

In our prior audit, we recommended that DMB develop procedures for State agencies to ensure proper and consistent annual reporting of charges to transportation funds. DMB agreed to consider our recommendation; however, it did not pursue issuing procedures. As a result, we noted similar missing items and inconsistencies in reporting again this year.

DMB, with its oversight responsibility for the State's financial activity, financial reporting, and internal control, should take the lead in establishing procedures to ensure proper and consistent reporting of this financial activity. Furthermore, DMB's Office of the State Budget is one of the primary users of the annual reports and should ensure the proper and consistent reporting necessary for the budget process.

RECOMMENDATION

WE AGAIN RECOMMEND THAT DMB DEVELOP PROCEDURES FOR STATE AGENCIES TO ENSURE PROPER AND CONSISTENT ANNUAL REPORTING OF CHARGES TO TRANSPORTATION FUNDS.

AGENCY PRELIMINARY RESPONSE

DMB responded that it would consider the recommendation.

SUPPLEMENTAL INFORMATION

Description of Supplemental Information

The tables in the detailed review comments by agency on pages 17 through 36 were compiled from information contained in the 9 agencies' fiscal year 2001-02 annual reports and the Michigan Department of Transportation's (MDOT's) records related to State agencies' use of transportation-related funding. These tables include the following information:

- a. Contract amount: This column includes the annually reported interagency contract amount between MDOT and the State agency. The contract amount includes amounts funded through interdepartmental grants, transfers, routine expenditure transactions, or expenditure credits.
- b. Expended/Encumbered: This column includes amounts reported by the State agency as expended. If the agency included encumbrances in its annual report, these amounts are also included in this column.
- c. Authorized but not used: This column includes contract amounts that were not used because the agency's expenditures were less than anticipated. If the excess was provided to the agency in the form of funding, the funding was returned to MDOT. If the amount was authorized, but no funding was transferred to the State agency, the amount in the schedules represents the unused authorization.

The supplemental information on pages 37 and 38 identifies transportation-related spending by State agencies and the charges and transfers among transportation funds.

DEPARTMENT OF STATE
 Use of Transportation-Related Funding
Fiscal Year Ended September 30, 2002

<u>Services and Other Charges to the Transportation Funds</u>	<u>Contract Amount</u>	<u>Expended/ Encumbered *</u>	<u>Authorized But Not Used</u>
Michigan Transportation Fund			
Collection of taxes, fees, and other services			
Executive direction - Operations	\$ 869,800	\$ 802,152	\$ 67,648
Department services	26,061,200	24,234,877	1,826,323
Regulatory services	7,500,600	6,891,698	608,902
Customer delivery services	56,615,500	51,519,779	5,095,721
Departmentwide	<u>4,767,000</u>	<u>4,411,231</u>	<u>355,769</u>
Total	<u>\$ 95,814,100**</u>	<u>\$ 87,859,737</u>	<u>\$ 7,954,363</u>

* The Department of State included encumbrances in its annual report in accordance with Department of Management and Budget Administrative Guide procedure 1210.27, Attachment A.

** Act 59, P.A. 2001, granted the Department of State \$55.8 million of funding from the Michigan Transportation Fund. Executive Order No. 2001-9 provided the Department of State with an additional \$40 million of funding from the Michigan Transportation Fund.

Appropriateness of Charges and Cost Allocation Methodology

The preceding table represents amounts reported by the Department of State pursuant to Section 504, Act 59, P.A. 2001. The Department of State's charges to the Michigan Transportation Fund (MTF) were used to finance the collection of transportation taxes, fees, and other transportation-related services.

The Department of State's charges against MTF were based on MTF's share of funding (funding ratio) of the appropriated expenditures. The Department calculated the amount expended consistent with prior years. Each year the Department retains an independent consulting firm to conduct time-and-effort cost studies. These studies serve as an after-the-fact analysis to determine the full cost of services provided by the Department and the appropriateness of MTF funding. For fiscal year 2001-02, the firm determined that the Department should have charged MTF \$96,604,985 for the services provided in fiscal year 2001-02. We reviewed the firm's documentation and concluded that it supports the firm's position for fiscal year 2001-02.

Status of Pending Lawsuit

County Road Association of Michigan et al v John M. Engler et al: On March 6, 2002, the County Road Association of Michigan and the Chippewa County Road Commission filed a complaint in Ingham County Circuit Court challenging various provisions of Executive Order No. 2001-9. The complaint consisted of five counts, one of which alleges that the State violated Article IX, Section 9 of the State Constitution by unlawfully allowing the Department of State to bill the Michigan Department of Transportation for expenses in excess of those necessary to collect motor vehicle taxes and fees.

On December 23, 2002, the trial court determined that \$20 million of the disputed costs were not necessary collection expenses, and the court issued a preliminary injunction enjoining the transfer of that amount of the funds. On appeal, defendants challenged whether the trial court had abused its discretion when determining that the plaintiffs were likely to prevail on the merits and, thus, inappropriately issued the injunction. On December 10, 2003, the parties gave oral arguments in the Court of Appeals on the injunctions.

On January 13, 2004, the Court of Appeals directed the trial court on remand to modify the preliminary injunction at issue so that it applies to only the amount of \$7.3 million. This amount relates to costs associated with processing automobile dealer licenses and drivers' license appeals and operating driver improvement programs. The Court of Appeals concluded that the trial court properly determined that the plaintiffs were likely to prevail on the merits with respect to only the \$7.3 million of the \$20 million and, therefore, had a basis for issuing the injunction.

Based on information provided by the Department of Attorney General, this is only a preliminary injunction that provides temporary relief to the plaintiff while the case is tried on its merits. At this time, the State is evaluating its legal options and anticipates that there will be additional legal proceedings in regard to the \$7.3 million. Therefore, we cannot conclude as to the reasonableness of these charges until a legal determination is made as to whether the disputed costs are a necessary collection expense and, thus, an appropriate charge to the transportation funds.

DEPARTMENT OF MANAGEMENT AND BUDGET
Use of Transportation-Related Funding
Fiscal Year Ended September 30, 2002

<u>Services and Other Charges to the Transportation Funds</u>	<u>Contract Amount</u>	<u>Expended/ Encumbered</u>	<u>Authorized But Not Used</u>
Comprehensive Transportation Fund			
Central services	\$ 57,000	\$ 57,000	\$ 0
MAIN user charges	91,100	91,100	0
Michigan Transportation Fund			
MAIN user charges	245,700	245,700	0
State Aeronautics Fund			
Central services	30,500	30,500	0
MAIN user charges	49,000	49,000	0
State Trunkline Fund			
Central services	1,057,000	1,057,000	0
MAIN user charges	1,687,500	1,687,500	0
Building occupancy charges	4,625,879	4,625,879	0
Total	<u>\$ 7,843,679</u>	<u>\$ 7,843,679</u>	<u>\$ 0</u>

Appropriateness of Charges and Cost Allocation Methodology

The preceding table represents amounts reported by the Department of Management and Budget (DMB) pursuant to Section 504, Act 59, P.A. 2001. DMB charged the transportation funds for central services, such as payroll, central audit, fixed assets accounting, space leasing services, mail and freight, purchasing, employer services, budgeting, and contract management; the Michigan Administrative Information Network's (MAIN's) development and operation costs; and operating costs of buildings used by transportation programs.

For these charges, DMB uses the Statewide Cost Allocation Plan* (SWCAP) to allocate expenditures to the transportation funds. This method allocates costs based on estimated expenditures and adjusts future allocations for the differences between estimates and actual expenditures. We conclude that the types of charges and the cost allocation methodology were reasonable.

* See glossary at end of report for definition.

DMB has an additional contract with the Michigan Department of Transportation (MDOT) for MAIN user charges. These charges are limited by the contract and are not included as part of the SWCAP calculation. We concluded that the charges and the cost allocation methodology were reasonable.

DMB reported additional charges to the transportation funds for routine costs incurred by MDOT for State Employees' Retirement Services and services provided by DMB's internal service funds (State Sponsored Group Insurance Fund, Office Services Revolving Fund, Information Technology and Energy Fund, and Motor Transport Fund). These charges are not included in the table and are similar to costs incurred by all State agencies and funds.

DMB also incurred an additional \$1,656,099 in SWCAP charges that were not billed to MDOT because DMB did not seek reimbursement in excess of appropriations.

DEPARTMENT OF TREASURY
 Use of Transportation-Related Funding
Fiscal Year Ended September 30, 2002

<u>Services and Other Charges to the Transportation Funds</u>	<u>Contract Amount</u>	<u>Expended/ Encumbered *</u>	<u>Authorized But Not Used</u>
Comprehensive Transportation Fund			
Investment services	\$ 5,300	\$ 5,300	\$
Michigan Transportation Fund			
Collection of fuel taxes	8,000,000	6,670,498	1,329,502
State Aeronautics Fund			
Investment services		2,400	
Collection of aviation fuel taxes	64,100	61,700	
State Trunkline Fund			
Investment services	29,100	29,100	
Warrant processing and miscellaneous		5,170	
 Total	 <u>\$ 8,098,500</u>	 <u>\$ 6,774,168</u>	 <u>\$ 1,329,502</u>

* The Department of Treasury included encumbrances in its annual report in accordance with Department of Management and Budget Administrative Guide procedure 1210.27, Attachment A.

Appropriateness of Charges and Cost Allocation Methodology

The preceding table represents amounts reported by the Department of Treasury pursuant to Section 504, Act 59, P.A. 2001. The Department of Treasury charged the transportation funds \$61,700 for collecting aviation fuel tax revenues on behalf of the State Aeronautics Fund, \$6,670,498 for collecting fuel taxes on behalf of the Michigan Transportation Fund, and \$36,800 for investment services conducted on behalf of the transportation funds.

The Department of Treasury collected \$6,699,000 of revenue on behalf of the State Aeronautics Fund for fiscal year 2001-02. The Department of Treasury's charges of \$61,700 were based on the proportionate share of collection costs of the State Aeronautics Fund revenue to total tax revenue. The Department of Treasury's charges of \$6,670,498 to the Michigan Transportation Fund were based on the proportionate share of costs of administering transportation taxes to the total cost of administering all taxes. The Department of Treasury's charge of \$36,800 for investment services was

based on the transportation funds' proportionate share of the Department of Treasury's cost of investing activities. The Department of Treasury conducts similar services for other State special revenue funds and the charge method used for the transportation funds was consistent with the method used for State special revenue funds.

Miscellaneous Charges

The Michigan Department of Transportation used funding from the State Trunkline Fund to reimburse the Department of Treasury for miscellaneous expenses of \$5,170 that were for services not anticipated or covered in the contract. These charges were included in the Department of Treasury's annual report for items such as manual warrants and subscriptions. We concluded that these costs were reasonable.

During our review, we also noted that the Department of Treasury included costs that were not covered by the contract and were not related to tax collections, therefore, we conclude that the Department of Treasury overbilled the State Aeronautics Fund and the Michigan Transportation Fund by \$25,175 and \$7,844, respectively (see Finding 1).

MICHIGAN DEPARTMENT OF STATE POLICE
Use of Transportation-Related Funding
Fiscal Year Ended September 30, 2002

<u>Services and Other Charges to the Transportation Funds</u>	<u>Contract Amount</u>	<u>Expended/ Encumbered*</u>	<u>Authorized But Not Used</u>
State Trunkline Fund			
Motor Carrier Division	\$ 7,872,200	\$ 5,945,710	\$ 1,926,490
Criminal Justice Information Center	338,500	328,311	10,189
Uniform Services	198,520	198,520	
State Aeronautics Fund			
Special Operations	70,819	70,819	
 Total	 <u>\$ 8,480,039</u>	 <u>\$ 6,543,360</u>	 <u>\$ 1,936,679</u>

* The Michigan Department of State Police included encumbrances in its annual report in accordance with Department of Management and Budget Administrative Guide procedure 1210.27, Attachment A.

Appropriateness of Charges and Cost Allocation Methodology

The preceding table represents amounts reported by the Michigan Department of State Police (MSP) pursuant to Section 504, Act 59, P.A. 2001. MSP charged the transportation funds for the cost of services provided to the Michigan Department of Transportation (MDOT) by MSP's Motor Carrier Division, MSP's Criminal Justice Information Center (CJIC), MSP's Uniform Services, and MSP's Special Operations.

The Motor Carrier Division charged \$5,945,710 for enforcing State Trunkline Fund related regulations as well as other motor carrier regulations financed with motor carrier fees. These transportation funds were used to support 123 full-time equated employees who administered and enforced the Motor Carrier Division's programs and regulations. The Motor Carrier Division performed enforcement activities related to traffic safety, commercial vehicle regulations, and other activities performed through weigh stations and road patrol. The Motor Carrier Division used a random moment sampling system for cost allocation. We conclude that the cost allocation methodology for the Motor Carrier Division was reasonable.

CJIC charged \$328,311 for the salary and wage, retirement, insurance, and other related costs of personnel who directly supported the processing of traffic accident reporting. CJIC also provided software, mainframe processing, data keying equipment,

and related services to maintain the traffic accident records database. MSP's contract with MDOT states that costs of the traffic accident records function will be allocated between the three State departments (Department of State, MDOT, and MSP) that received and used data that it produced. However, we noted that the costs were not allocated correctly, and therefore, MSP underbilled the State Trunkline Fund by \$10,189. We conclude that, although the charges for CJIC were reasonable, the cost allocation methodology was not followed appropriately.

The MSP annual report included charges to the State Trunkline Fund for Uniform Services in the amount of \$198,520 and charges to the State Aeronautics Fund for Special Operations in the amount of \$70,819. Uniform Services is reimbursed by MDOT for patrols of construction zone areas and Special Operations is reimbursed by MDOT for use of aviation fuel. These services and costs appeared to be reasonable and were included in the contract.

DEPARTMENT OF CIVIL SERVICE
 Use of Transportation-Related Funding
 Fiscal Year Ended September 30, 2002

<u>Services and Other Charges to the Transportation Funds</u>	<u>Contract Amount</u>	<u>Expended/ Encumbered</u>	<u>Authorized But Not Used</u>
Comprehensive Transportation Fund			
Constitutionally required 1% funding	\$ 115,000	\$ 87,325	\$ 27,675*
State Aeronautics Fund			
Constitutionally required 1% funding	75,000	50,129	24,871*
State Trunkline Fund			
Constitutionally required 1% funding	<u>1,430,000*</u>	<u>1,967,602</u>	
Total	<u>\$ 1,620,000</u>	<u>\$ 2,105,056</u>	<u>\$ (52,546)</u>

* The amounts granted to the Department of Civil Service for the constitutionally required 1% program are estimates and are reviewed and made current during year-end closing.

Appropriateness of Charges and Cost Allocation Methodology

The preceding table represents amounts reported by the Department of Civil Service (DCS) pursuant to Section 504, Act 59, P.A. 2001. DCS charged the transportation funds \$2,105,056 for the constitutionally required 1% of the aggregate payroll associated with the transportation funds.

The primary funding for the operations of DCS is provided under Article XI of the State Constitution. Article XI, Section 5 of the State Constitution states: ". . . the legislature shall appropriate to the [civil service] commission for the ensuing fiscal year a sum not less than one percent of the aggregate payroll of the classified services for the preceding fiscal year"

Transportation funds were appropriated to DCS based on the executive budget request prepared by the Office of Budget Development and General Government, Department of Management and Budget, in conjunction with DCS's Budget and Financial Services.

For fiscal year 2001-02, DCS charges to transportation funds for the constitutionally required 1% were based on actual fiscal year 2000-01 salary and fringe benefit

expenditures charged to the transportation funds. We conclude that the charges and the cost allocation methodology were reasonable.

Miscellaneous Charges

The Michigan Department of Transportation (MDOT) incurred approximately \$386,895 for training expenses provided by DCS. DCS offers various training sessions available to all State departments. DCS does not contract with State agencies for these types of services; instead, they are handled through a reservation process. Therefore, these services and related charges are not covered in the contract between MDOT and DCS and were not reported in the annual report. We reviewed these charges and concluded that they were reasonable.

DEPARTMENT OF ATTORNEY GENERAL
 Use of Transportation-Related Funding
Fiscal Year Ended September 30, 2002

<u>Services and Other Charges to the Transportation Funds</u>	<u>Contract Amount</u>	<u>Expended/ Encumbered</u>	<u>Authorized But Not Used</u>
Comprehensive Transportation Fund			
Legal services	\$ 129,400	\$ 97,932	\$ 31,468
State Aeronautics Fund			
Legal services	123,600	68,967	54,633
State Trunkline Fund			
Legal services	2,524,300	1,714,825	809,475
Travel	7,362	7,362	
Rent	17,927	17,927	
 Total	 <u>\$ 2,802,589</u>	 <u>\$ 1,907,013</u>	 <u>\$ 895,576</u>

Appropriateness of Charges and Cost Allocation Methodology

The preceding table represents amounts that should have been reported by the Department of Attorney General pursuant to Section 504, Act 59, P.A. 2001. However, because of changes in personnel that resulted in the agency being unaware of the reporting requirements, the Department of Attorney General did not submit the required annual report.

The Department of Attorney General's appropriated charges of \$1,881,723 consisted of salary, insurance, and retirement costs of attorneys and staff assigned to work on legal issues relating to the transportation funds. These positions provided legal services exclusively to transportation programs and were assigned to the Highway Negligence Division and the Transportation Division.

The charges shown in the table were allocated according to the percentage of time that the attorney or staff position worked on legal issues relating to that fund.

The Michigan Department of Transportation (MDOT) also reimbursed the Department of Attorney General for miscellaneous charges of \$17,927 for State building occupancy costs and \$7,362 for travel costs. These costs were reasonable and were authorized by the contract between MDOT and the Department of Attorney General.

DEPARTMENT OF ENVIRONMENTAL QUALITY
 Use of Transportation-Related Funding
Fiscal Year Ended September 30, 2002

<u>Services and Other Charges to the Transportation Funds</u>	<u>Contract Amount</u>	<u>Expended/ Encumbered</u>	<u>Authorized But Not Used</u>
Michigan Transportation Fund			
Permits for transportation projects	\$ 885,300	\$ 823,532	\$ 61,768
State Aeronautics Fund			
Permits for transportation projects	40,000	5,631	34,369
State Trunkline Fund			
Membership dues	<u>15,125</u>	<u>15,125</u>	
Total	<u>\$ 940,425</u>	<u>\$ 844,288</u>	<u>\$ 96,137</u>

Appropriateness of Charges and Cost Allocation Methodology

The preceding table represents amounts reported by the Department of Environmental Quality (DEQ) pursuant to Section 504, Act 59, P.A. 2001.

DEQ's Geological and Land Management Division charged and received \$823,532 from the Michigan Transportation Fund to pay for the salaries, fringe benefits, and other associated expenses of employees who reviewed environmental permits for transportation projects.

The Division was also reimbursed \$5,631 by the State Aeronautics Fund for salaries, fringe benefits, and other associated expenses of employees who worked on reviewing environmental permits for State Aeronautics Fund projects. These charges were reasonable and were included in the contract with the Michigan Department of Transportation (MDOT).

For the charges shown in the table, DEQ used a time-and-effort system for allocating the payroll costs to the Michigan Transportation Fund and the State Aeronautics Fund. We conclude that the charges and cost allocation methodology used were reasonable.

Miscellaneous Charges

Additionally, MDOT reimbursed DEQ with \$15,125 from the State Trunkline Fund for charges that were not included in the annual report. These expenditures were made by

DEQ on behalf of MDOT primarily for membership dues in the Great Lakes Commission. We concluded that these charges were reasonable.

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION
 Use of Transportation-Related Funding
Fiscal Year Ended September 30, 2002

<u>Services and Other Charges to the Transportation Funds</u>	<u>Contract Amount</u>	<u>Expended/ Encumbered</u>	<u>Authorized But Not Used</u>
State Trunkline Fund			
Welcome Center operations	\$ 3,725,800	\$ 3,709,431	\$ 16,368
Miscellaneous charges		8,400	
Total	<u>\$ 3,725,800</u>	<u>\$ 3,717,831</u>	<u>\$ 16,368</u>

Appropriateness of Charges and Cost Allocation Methodology

The preceding table represents costs incurred by the Michigan Economic Development Corporation (MEDC) pursuant to Section 504(4), Act 59, P.A. 2001. MEDC's 2001-02 contract with the Michigan Department of Transportation (MDOT) for \$3,725,800 provides for the cost of daily operations of the Michigan Welcome Centers.

Miscellaneous Charges

MEDC reported costs of \$3,683,624 in its annual report. In addition, MDOT reimbursed MEDC for routine contracted amounts of approximately \$25,808 that were not reported in the annual report. These reimbursements were for snow removal at Welcome Centers around Michigan. MDOT also reimbursed MEDC for nonroutine miscellaneous maintenance-related expenses of approximately \$8,400 that were for services not anticipated or covered in the contract. We reviewed these charges to the transportation funds and determined they were reasonable and appropriate.

OFFICE OF THE AUDITOR GENERAL
Use of Transportation-Related Funding
Fiscal Year Ended September 30, 2002

<u>Services and Other Charges to the Transportation Funds</u>	<u>Contract Amount</u>	<u>Expended/ Encumbered</u>	<u>Authorized But Not Used</u>
Comprehensive Transportation Fund			
Audit services	\$ 47,600	\$ 47,600	\$ 0
Michigan Transportation Fund			
Audit services	108,900	108,900	0
State Aeronautics Fund			
Audit services	31,100	15,900	15,200
State Trunkline Fund			
Audit services	<u>314,200</u>	<u>314,200</u>	<u>0</u>
Total	<u>\$ 501,800</u>	<u>\$ 486,600</u>	<u>\$ 15,200</u>

Appropriateness of Charges and Cost Allocation Methodology

The preceding table represents amounts reported by the Office of the Auditor General (OAG) pursuant to Section 504, Act 59, P.A. 2001. The OAG's charges of \$486,600 to the transportation funds consisted of salaries, fringe benefits, supplies, materials, and travel costs for conducting audits of transportation programs and funds.

The OAG maintains a time-and-effort reporting system to account for audits conducted. The time-and-effort reporting system is the basis for allocating costs by audit, program, and fund. Most audit charges are based on average actual audit hours and hourly audit costs. Programs and funds audited annually are charged by the average audit hours; programs and funds not audited annually are charged proportionally. Changes in the average actual audit hours and the hourly audit costs are used to adjust future requests for transportation-related funding. In fiscal year 2001-02, the OAG methodology calculated a rate of approximately \$70 per hour. We conclude that the charges and the cost allocation methodology were reasonable. However, the OAG did not bill the Michigan Department of Transportation an estimated \$58,739 in transportation-related audit costs for fiscal year 2001-02 because the OAG did not seek reimbursement in excess of the appropriated amounts.

MICHIGAN DEPARTMENT OF TRANSPORTATION

Michigan Transportation Fund Expenditures and Transfers Out to Other Transportation Funds

Michigan Department of Transportation (MDOT) expenditures and transfers to other transportation funds from the Michigan Transportation Fund (MTF) for fiscal year 2001-02 were:

Receiving Fund	Appropriations and Authorizations	Transfers Out	Returned	Lapsed	Agency Total
Department of Transportation:					
Comprehensive Transportation Fund:					
10% Comprehensive Transportation Purposes	\$ 162,788,000	\$ 160,530,656		\$ 2,257,344	\$ 162,788,000
Railroad Safety and Tariffs Program	1,814,900	1,229,625	\$ 585,275		1,814,900
State Trunkline Fund:					
39.1% State Trunkline Purposes	649,751,700	641,072,857		8,678,843	649,751,700
Critical Bridge Program	5,000,000	5,000,000			5,000,000
Critical Bridge Debt Service	3,000,000	2,383,948	616,052		3,000,000
Economic Development Fund (EDF)	36,775,000	36,775,000			36,775,000
Targeted Industries (EDF)	3,500,000	3,500,000			3,500,000
Debt Service	43,000,000	43,000,000			43,000,000
Local Road Program	33,000,000	33,000,000			33,000,000
Rail Grade Crossing Program	3,000,000	3,000,000			3,000,000
Executive Direction	35,900	35,900			35,900
Bureau of Transportation Planning	5,840,700	5,840,700			5,840,700
Highways for Engineering	4,089,500	2,543,489	1,546,012		4,089,500
Bureau of Finance and Administration	1,115,300	999,980	115,321		1,115,300
Office of Information Management	34,900	24,230	10,670		34,900
Total	<u>\$ 952,745,900</u>	<u>\$ 938,936,384</u>	<u>\$ 2,873,328</u>	<u>\$ 10,936,188</u>	<u>\$ 952,745,900</u>

Lapses in appropriations occurred because actual MTF revenues were less than expected, resulting in smaller distributions based on the MTF formula provided for in Section 247.660 of the *Michigan Compiled Laws* (Act 51, P.A. 1951, as amended). At the end of the year, programs returned unused MTF funds, which are subsequently redistributed through the MTF formula to the Comprehensive Transportation Fund, State Trunkline Fund, counties, cities, and villages.

Cost Allocation Methodology and Transportation Fund Charges

Comprehensive Transportation Fund:

10% Comprehensive Transportation Purposes

Section 247.660 of the *Michigan Compiled Laws* (Act 51, P.A. 1951, as amended) requires that up to 10% of the revenues deposited in the Department of Treasury to the credit of MTF be transferred to the Comprehensive Transportation Fund. The use of the funds is prioritized by statute. In fiscal year 2001-02, \$160,530,656 was paid to the Comprehensive Transportation Fund consistent with the statute.

Railroad Safety and Tariffs Program

To reimburse the Comprehensive Transportation Fund for MTF's share in the costs of the administration of the Transportation Safety and Tariffs Program, Bureau of Urban and Public Transportation, \$1,229,625 was paid.

State Trunkline Fund:

39.1% State Trunkline Purposes

Section 247.660 of the *Michigan Compiled Laws* (Act 51, P.A. 1951, as amended) requires that, after up to 10% of MTF revenues have been credited to the Comprehensive Transportation Fund and several other statutorily required distributions, 39.1% of the remaining funds must be distributed to the State Trunkline Fund for State trunkline purposes.

Critical Bridge Program

Section 247.661b of the *Michigan Compiled Laws* (Act 51, P.A. 1951, as amended) requires the annual transfer of \$5,000,000 to the Critical Bridge Program from MTF. The money appropriated and interest accruing to MTF is administered by MDOT according to promulgated rules. The Program provides financial assistance to local and county road commissions for the improvement or reconstruction of existing bridges or for the construction of replacement bridges. In fiscal year 2001-02, \$5,000,000 was appropriated to the Critical Bridge Program and \$5,000,000 was expended.

Critical Bridge Debt Service

Section 247.660(b) of the *Michigan Compiled Laws* (Act 51, P.A. 1951, as amended) requires the annual transfer from MTF of not less than \$3,000,000 to the Critical Bridge Fund for the payment of principal, interest, and redemption on

any notes or bonds issued by the State Transportation Commission under Section 247.661b. In fiscal year 2001-02, \$3,000,000 was appropriated, but MDOT paid the debt service requirement of \$2,383,948 and returned \$616,052.

Economic Development Fund and Targeted Industries

Section 247.660 of the *Michigan Compiled Laws* (Act 51, P.A. 1951, as amended) requires the payment of \$36,775,000 to the State Trunkline Fund for subsequent deposit in MDOT's Economic Development Fund. In fiscal year 2001-02, the full amount was paid consistent with the statute.

In addition, this Section requires, beginning October 1, 1997, that \$3,500,000 be appropriated from MTF to the State Trunkline Fund for subsequent deposit in MDOT's Economic Development Fund to be used for economic development road projects in any of the following targeted industries: agriculture or food processing, tourism, forestry, high technology research, manufacturing, mining, and office centers of not less than 50,000 square feet. In fiscal year 2001-02, the full amount was paid consistent with the statute.

Debt Service

Section 247.660 of the *Michigan Compiled Laws* (Act 51, P.A. 1951, as amended) requires the payment of \$43,000,000 to the State Trunkline Fund for debt service costs on State of Michigan projects. In fiscal year 2001-02, the full amount was paid consistent with the statute.

Local Road Program

Section 247.660 of the *Michigan Compiled Laws* (Act 51, P.A. 1951, as amended) requires that, beginning October 1, 1995, a grant of not less than \$33,000,000 be made to the State Trunkline Fund, which shall then be made to the Local Road Program. These funds received shall then be distributed 64.2% to county road commissions and 35.8% to cities and villages. In fiscal year 2001-02, the full amount was paid consistent with the statute.

Rail Grade Crossing Program

Section 247.660 of the *Michigan Compiled Laws* (Act 51, P.A. 1951, as amended) provides that not more than \$3,000,000 shall be appropriated for improvements in rail grade crossings. Accordingly, \$3,000,000 was appropriated from MTF and paid to the State Trunkline Fund.

Executive Direction

To cover MTF's share of workers' compensation costs, \$35,900 was appropriated and paid to the State Trunkline Fund.

Bureau of Transportation Planning

To reimburse the State Trunkline Fund for MTF's share in the costs of the Bureau of Transportation Planning, \$5,840,700 was appropriated and paid.

Highways for Engineering

To reimburse the State Trunkline Fund for the full cost of local contracts and project management of the Engineering Services Division, Bureau of Highways, \$4,089,500 was appropriated and \$2,543,489 was paid.

Bureau of Finance and Administration

To reimburse the State Trunkline Fund for MTF's share in the costs of the Bureau of Finance and Administration, \$1,115,300 was appropriated and \$999,980 was paid.

Office of Information Management

To cover MTF's share of computer equipment/software costs, \$34,900 was appropriated and \$24,230 was paid to the State Trunkline Fund.

State Trunkline Fund Charges to the Comprehensive Transportation and State Aeronautics Funds

State Trunkline Fund charges to the Comprehensive Transportation Fund were as follows:

<u>Fund/Purpose</u>	<u>Appropriated Funding</u>	<u>Allocated Charges</u>	<u>Returned Appropriations</u>	<u>Overallocated (Underallocated) Charges</u>
Comprehensive Transportation Fund:				
Administration and Data Center	\$ 1,182,700	\$ 1,174,395*	\$ 7,191	\$ 0
Planning	<u>2,024,900</u>	<u>1,033,291</u>	<u>991,609</u>	<u>0</u>
Total	<u>\$ 3,207,600</u>	<u>\$ 2,207,686</u>	<u>\$ 998,800</u>	<u>\$ 0</u>

* Amount does not include recorded encumbrances of \$1,114 that were expended in a subsequent fiscal year.

State Trunkline Fund charges to the State Aeronautics Fund were as follows:

Fund/Purpose	Appropriated Funding	Allocated Charges	Returned Appropriations	Overallocated (Underallocated) Charges
State Aeronautics Fund:				
Administration and Data Center	\$ 687,100	\$595,329*	\$ 91,079	\$ 0
Planning	<u>321,900</u>	<u>195,683</u>	<u>126,217</u>	<u>0</u>
 Total	 <u>\$1,009,000</u>	 <u>\$791,012</u>	 <u>\$ 217,296</u>	 <u>\$ 0</u>

* Amount does not include recorded encumbrances of \$692 that were expended in a subsequent fiscal year.

Cost Allocation Methodology and Transportation Fund Charges

The administration and data center charges and the planning charges consisted of the Comprehensive Transportation and State Aeronautics Funds' allocated portion of these costs to the State Trunkline Fund. We determined that these costs were appropriate.

MDOT has completed a cost allocation study that identifies all costs associated with activities directed at counties, cities, and villages (local units of government) and identifies methods for the equitable allocation of all costs to the local units of government and the State Trunkline Fund. MDOT plans to implement changes as a result of this study beginning in fiscal year 2004-05.

TRANSPORTATION FUNDS
 Summary of Annual Reports of Transportation-Related Funding Used
 Fiscal Year Ended September 30, 2002

Receiving Agency	Charges Paid By					Agency Total
	Comprehensive Transportation Fund	Michigan Transportation Fund	State Aeronautics Fund	State Trunkline Fund	Transportation Related Trust Funds	
Department of State	\$	\$ 87,859,737	\$	\$	\$	\$ 87,859,737
Department of Management and Budget	148,100	245,700	79,500	7,370,379		7,843,679
Department of Treasury	5,300	6,670,498	64,100	34,270		6,774,168
Michigan Department of State Police			70,819	6,472,541		6,543,360
Department of Civil Service	87,325		50,129	1,967,602		2,105,056
Department of Attorney General	97,932		68,967	1,740,114		1,907,013
Department of Environmental Quality		823,532	5,631	15,125		844,288
Michigan Economic Development Corporation				3,717,831		3,717,831
Office of the Auditor General	47,600	108,900	15,900	314,200		486,600
Mackinac Island State Park Commission*			35,000			35,000
Total for Nontransportation Agencies	<u>\$ 386,257</u>	<u>\$ 95,708,367</u>	<u>\$ 390,046</u>	<u>\$ 21,632,062</u>	<u>\$ 0</u>	<u>\$ 118,116,732</u>

* Per Section 324.76503(6) of the *Michigan Compiled Laws*, the Mackinac Island State Park Commission was moved from the Department of Natural Resources to the Department of History, Arts and Libraries. Because of this change, the new department was not aware of the annual reporting requirement. We included the amounts contracted and expended as part of this summary but did not prepare detailed review comments.

TRANSPORTATION FUNDS
 Summary of Charges and Transfers Among Transportation Funds
Fiscal Year Ended September 30, 2002

Receiving Agency	Transfers From				Agency Total
	Comprehensive Transportation Fund	Michigan Transportation Fund	State Aeronautics Fund	State Trunkline Fund	
Michigan Department of Transportation:					
Comprehensive Transportation Fund:					
10% Comprehensive Transportation Purposes	\$	\$ 160,530,656	\$	\$	\$ 160,530,656
Railroad Safety and Tariffs Program		1,229,625			1,229,625
State Trunkline Fund:					
39.1% State Trunkline Purposes		641,072,857			641,072,857
Critical Bridge Program		5,000,000			5,000,000
Critical Bridge Debt Service		2,383,948			2,383,948
Economic Development Fund (EDF)		36,775,000			36,775,000
Targeted Industries (EDF)		3,500,000			3,500,000
Debt Service		43,000,000			43,000,000
Local Road Program		33,000,000			33,000,000
Rail Grade Crossing Program		3,000,000			3,000,000
Executive Direction		35,900			35,900
Bureau of Transportation Planning		5,840,700			5,840,700
Highways for Engineering		2,543,489			2,543,489
Bureau of Finance and Administration		999,980			999,980
Office of Information Management		24,230			24,230
Administration and Data Center	1,174,395		595,329		1,769,724
Planning	1,033,291		195,683		1,228,974
Total	<u>\$ 2,207,686</u>	<u>\$ 938,936,384</u>	<u>\$ 791,012</u>	<u>\$ 0</u>	<u>\$ 941,935,082</u>

Glossary of Acronyms and Terms

CJIC	Criminal Justice Information Center.
DCS	Department of Civil Service.
DEQ	Department of Environmental Quality.
DMB	Department of Management and Budget.
financial related audit	An audit that is designed to provide reasonable assurance that (1) financial information is presented in accordance with established or stated criteria, (2) the entity has adhered to specific financial compliance requirements, or (3) the entity's internal control over financial reporting is suitably designed and implemented to achieve the control objectives.
MAIN	Michigan Administrative Information Network.
MDOT	Michigan Department of Transportation.
MEDC	Michigan Economic Development Corporation.
MSP	Michigan Department of State Police.
MTF	Michigan Transportation Fund.
OAG	Office of the Auditor General.
reportable condition	A matter coming to the auditor's attention relating to a significant deficiency in the design or operation of internal control that, in the auditor's judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial schedules and/or financial statements.

**Statewide Cost
Allocation Plan
(SWCAP)**

The official cost allocation methodology accepted by federal grantor agencies for the State's negotiated indirect cost rate.