



# MICHIGAN

OFFICE OF THE AUDITOR GENERAL

## AUDIT REPORT



THOMAS H. McTAVISH, C.P.A.  
AUDITOR GENERAL

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**

*Performance Audit*

*Funding for Department Services Provided to  
Local Units of Government  
Michigan Department of Transportation*

Report Number:  
591-0174-12

Released:  
December 2012

*The Michigan Department of Transportation (MDOT) receives appropriated funds from the Michigan Transportation Fund (MTF) for expenditures incurred for providing services that benefit local units of government. These services range from assistance with asset management to transportation planning. MDOT uses various allocation methodologies to charge the MTF for expenditures related to services provided to local units of government.*

**Audit Objective:**

To assess the effectiveness of MDOT's efforts to allocate to the MTF the MDOT expenditures incurred for services provided to local units of government.

**Audit Conclusion:**

We concluded that MDOT's efforts to allocate to the MTF the MDOT expenditures incurred for services provided to local units of government were effective. However, we noted one reportable condition (Finding 1).

**Reportable Condition:**

MDOT had not developed formal procedures for allocating to the MTF the MDOT expenditures related to services provided to local units of government (Finding 1).

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**Audit Objective:**

To assess the effectiveness of MDOT's efforts to evaluate and monitor the appropriateness of MDOT expenditures allocated to the MTF for services provided to local units of government.

**Audit Conclusion:**

We concluded that MDOT's efforts to evaluate and monitor the appropriateness of MDOT expenditures allocated to the MTF for services provided to local units of government were effective. However, we noted one reportable condition (Finding 2).

**Reportable Condition:**

MDOT needs to request appropriations that are commensurate with the amount of expenditures incurred for the level of service efforts provided to local units of government or reduce such expenditures (Finding 2).

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**Agency Response:**

Our audit report contains 2 findings and 2 corresponding recommendations. MDOT's preliminary response indicates that it agrees with both recommendations.

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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://audgen.michigan.gov>



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December 11, 2012

Mr. Jerrold M. Jung, Chair  
State Transportation Commission  
and  
Kirk T. Steudle, P.E., Director  
Michigan Department of Transportation  
Murray Van Wagoner Transportation Building  
Lansing, Michigan

Dear Mr. Jung and Mr. Steudle:

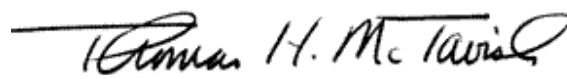
This is our report on the performance audit of Funding for Department Services Provided to Local Units of Government, Michigan Department of Transportation.

This report contains our report summary; description; audit objectives, scope, and methodology and agency responses and prior audit follow-up; comments, findings, recommendations, and agency preliminary responses; allocation methodologies, 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 agency's response subsequent to our audit fieldwork. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a plan to comply with the audit recommendations and submit it within 60 days after release of the audit report to the Office of Internal Audit Services, State Budget Office. Within 30 days of receipt, the Office of Internal Audit Services is required to review the plan and either accept the plan as final or contact the agency to take additional steps to finalize the plan.

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

Sincerely,

  
Thomas H. McTavish, C.P.A.  
Auditor General



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## Description

The mission\* of the Michigan Department of Transportation (MDOT) is to provide the highest quality integrated transportation services for economic benefit and improved quality of life. To accomplish this mission, MDOT must collaborate and sustain partnerships with both private and public entities to optimize the contributions of MDOT's efforts. Those partnerships include an involved relationship with local units of government\* in which MDOT provides assistance to these entities with their transportation projects. Such assistance includes working closely with local government and urban planning organizations to develop a Statewide Transportation Improvement Program and long-range planning goals, performing data collection and planning activities to ensure that local units of government continue to qualify for federal aid, helping local units of government with roadway project developments, developing project contract proposals, providing technical assistance and support on a wide variety of engineering and business disciplines, processing contractor payments and posting completion progress on MDOT's Web site, and conducting audits of contracts and contractor payments.

MDOT receives a significant portion of its funding from the Michigan Transportation Fund\* (MTF). The MTF is funded primarily through revenues from gasoline and diesel fuel taxes and vehicle registration taxes and fees. Money from the MTF is distributed to MDOT through the State Trunkline Fund\*, counties, and cities and villages in accordance with an allocation formula identified within Act 51, P.A. 1951, as amended. In addition, MDOT receives appropriated funds from the MTF for expenditures incurred for providing services that benefit local units of government. For the period October 1, 2009 through September 30, 2012, MDOT was appropriated \$56.5 million for eight areas that provided services to local units of government. The eight service areas include Asset Management Council; Design and Engineering Services; Economic Development and Enhancement Programs; Finance, Contracts, and Support Services; Freight and Safety Services; Information Technology Services and Projects; Passenger Transportation Services; and Transportation Planning.

Within the eight service areas, there are 15 service activities that provide services to local units of government. Each of the 15 service activities had developed a

\* See glossary at end of report for definition.



methodology for allocating expenditures to the MTF. The methodologies vary significantly among service activities. MDOT uses the various allocation methodologies to charge the MTF for expenditures related to services provided to local units of government. The allocation methodologies are presented as supplemental information.

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

### Audit Objectives

Our performance audit\* of Funding for Department Services Provided to Local Units of Government, Michigan Department of Transportation (MDOT), had the following objectives:

1. To assess the effectiveness\* of MDOT's efforts to allocate to the Michigan Transportation Fund (MTF) the MDOT expenditures incurred for services provided to local units of government.
2. To assess the effectiveness of MDOT's efforts to evaluate and monitor the appropriateness of MDOT expenditures allocated to the MTF for services provided to local units of government.

### Audit Scope

Our audit scope was to examine the processes used by the Michigan Department of Transportation to allocate, evaluate, and monitor expenditures for services provided to local units of government. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Our preliminary review and audit procedures, primarily conducted from June through September 2012, generally covered the period October 1, 2009 through August 31, 2012.

As part of the audit, we compiled and reported MDOT's allocation methodologies that relate to our audit objectives and findings (see supplemental information). Our audit was not directed toward expressing a conclusion on this information and, accordingly, we express no conclusion on it.

\* See glossary at end of report for definition.

### Audit Methodology

We conducted a preliminary review of MDOT's processes to allocate funds to the MTF to formulate a basis for defining our audit objectives and scope. Our preliminary review included interviewing various MDOT staff, reviewing applicable statutes, analyzing available data, reviewing MDOT policies and procedures, and reviewing internal control\* to obtain an understanding of MDOT's allocation processes.

To accomplish our first objective, we interviewed MDOT staff to identify the individual methodologies used by MDOT for allocating expenditures to the MTF for services provided to local units of government. For each allocation methodology, we reviewed the steps that MDOT used to develop the methodology and determined whether MDOT considered all costs of services provided to local units of government. Also, we tested MDOT's calculated allocation percentages assigned to specific staff.

To accomplish our second objective, we interviewed MDOT staff and reviewed MDOT's process to evaluate and monitor the appropriateness of expenditures allocated to the MTF. We compared MDOT expenditures for services provided to local units of government with amounts appropriated from the MTF and reconciled MDOT expenditures with those recorded in the State's accounting system. Also, we extracted labor expenditures coded as services provided to local units of government from the State's payroll system and compared them with labor expenditures that MDOT charged to the MTF. In addition, we examined a sample of transactions to determine if MDOT charged expenditures to the MTF correctly. Further, we compared total expenditure amounts that MDOT charged to the MTF with expenditure amounts incurred for services provided to local units of government.

### Agency Responses and Prior Audit Follow-Up

Our audit report contains 2 findings and 2 corresponding recommendations. MDOT's preliminary response indicates that it agrees with both recommendations.

The agency preliminary response that follows each recommendation in our report was taken from the agency's written comments and oral discussion subsequent to our audit fieldwork. Section 18.1462 of the *Michigan Compiled Laws* and the State of Michigan Financial Management Guide (Part VII, Chapter 4, Section 100) require MDOT to develop a plan to comply with the audit recommendations and submit it within 60 days

\* See glossary at end of report for definition.

after release of the audit report to the Office of Internal Audit Services, State Budget Office. Within 30 days of receipt, the Office of Internal Audit Services is required to review the plan and either accept the plan as final or contact the agency to take additional steps to finalize the plan.

We released our prior performance audit of Services Provided to Local Road Agencies, Michigan Department of Transportation (59-132-01), in November 2001. Within the scope of this audit, we followed up the 1 prior audit recommendation. We rewrote the prior audit recommendation for inclusion in Finding 2 of this audit report.

COMMENTS, FINDINGS, RECOMMENDATIONS,  
AND AGENCY PRELIMINARY RESPONSES

## EFFORTS TO ALLOCATE MDOT EXPENDITURES INCURRED FOR SERVICES PROVIDED TO LOCAL UNITS OF GOVERNMENT

### COMMENT

**Audit Objective:** To assess the effectiveness of the Michigan Department of Transportation's (MDOT's) efforts to allocate to the Michigan Transportation Fund (MTF) the MDOT expenditures incurred for services provided to local units of government.

**Audit Conclusion:** We concluded that MDOT's efforts to allocate to the MTF the MDOT expenditures incurred for services provided to local units of government were effective. However, our assessment disclosed one reportable condition\* related to allocation procedures (Finding 1).

### FINDING

#### 1. Allocation Procedures

MDOT had not developed formal procedures for allocating to the MTF the MDOT expenditures related to services provided to local units of government. As a result, MDOT could not document that its allocation methodologies properly included all eligible expenditures from across all areas within MDOT that provide services to local units of government.

MDOT received appropriated funds from the MTF for expenditures incurred for MDOT services that benefited local government units. MDOT incurred these expenditures while providing services to local units of government within 8 separate service areas involving 15 service activities. Each service activity within MDOT developed its own allocation methodology to estimate the cost of services provided to the local units.

We reviewed MDOT's various methodologies for allocating MDOT expenditures related to services provided to local units of government for the 15 service activities. Our review disclosed:

- a. MDOT had not developed written procedures for 14 (93%) of the 15 expenditure allocation methodologies.

\* See glossary at end of report for definition.

- b. MDOT did not document the internal control used to ensure that the 6 MTF allocation methodologies based on the professional judgment of management were effective.
- c. MDOT did not document how it determined that the 15% allocation of MDOT supervisory and/or secretarial costs totaling \$70,068 in fiscal year 2010-11 was for activities related to the MTF in 2 service areas within MDOT. The 15% was based on the professional judgment of the managers in the 2 service areas.

### **RECOMMENDATION**

We recommend that MDOT develop formal procedures for allocating to the MTF the MDOT expenditures related to services provided to local units of government.

### **AGENCY PRELIMINARY RESPONSE**

MDOT agrees with the recommendation and will develop formal procedures for allocating expenditures related to services provided to local units of government to the MTF. The written procedures will be completed by March 31, 2013.

## **EFFORTS TO EVALUATE AND MONITOR THE APPROPRIATENESS OF MDOT EXPENDITURES ALLOCATED**

### **COMMENT**

**Audit Objective:** To assess the effectiveness of MDOT's efforts to evaluate and monitor the appropriateness of MDOT expenditures allocated to the MTF for services provided to local units of government.

**Audit Conclusion:** We concluded that MDOT's efforts to evaluate and monitor the appropriateness of MDOT expenditures allocated to the MTF for services provided to local units of government were effective. However, our assessment disclosed one reportable condition related to request for appropriations (Finding 2).

## FINDING

### 2. Request for Appropriations

MDOT needs to request appropriations that are commensurate with the amount of expenditures incurred for the level of service efforts provided to local units of government or reduce such expenditures. As a result, MDOT had to utilize other funding sources for the amount of expenditures that exceeded appropriations for its services provided to local units of government.

MDOT annually receives appropriated funding from the MTF. MTF funding is appropriated by line item to 8 areas in MDOT that provide services to local units of government. These 8 service areas, their allocated appropriated amounts, and our estimate of expenditures incurred by area for fiscal years 2009-10 and 2010-11 are as follows:

Service Area Within MDOT	Fiscal Year 2009-10		Fiscal Year 2010-11	
	Allocated Appropriated Amount	Estimated Expenditures Incurred	Allocated Appropriated Amount	Estimated Expenditures Incurred
Asset Management Council	\$ 1,626,400	\$ 1,441,564	\$ 1,626,400	\$ 1,654,096
Design and Engineering Services	5,835,200	4,845,006	6,355,300	4,527,135
Economic Development and Enhancement Programs	185,000	481,147	201,700	496,523
Finance, Contracts, and Support Services	1,625,200	1,654,931	1,792,700	1,683,828
Freight and Safety Services	1,996,900	1,609,814	2,104,400	1,427,869
Information Technology Services and Projects	249,400	174,246	254,200	79,399
Passenger Transportation Services	201,400	166,599	214,800	171,323
Transportation Planning	6,304,500	9,716,411	6,304,500	9,836,815
Total	<u>\$18,024,000</u>	<u>\$20,089,718</u>	<u>\$18,854,000</u>	<u>\$19,876,988</u>

Our review of the allocated appropriations and MDOT expenditures for the 8 service areas disclosed that MDOT's costs for providing services to local units exceeded its allocated appropriations in 2 areas:

- a. The Bureau of Transportation Planning expended \$3.4 million and \$3.5 million more than its allocated MTF appropriations in fiscal years 2009-10 and 2010-11, respectively. As a result, MDOT used federal funding to satisfy these expenditures. The Bureau of Transportation Planning provides services to local units of government for transportation planning and data collection services.



- b. The Office of Economic Development expended \$0.3 million more than its allocated MTF appropriations for both fiscal years 2009-10 and 2010-11. As a result, MDOT used State Trunkline Fund funding to satisfy these expenditures. The Office of Economic Development provides services to local units of government for various grants to assist local units with the funding of projects that are aimed at supporting economic growth.

### **RECOMMENDATION**

We recommend that MDOT request appropriations that are commensurate with the amount of expenditures incurred for the level of service efforts provided to local units of government or reduce such expenditures.

### **AGENCY PRELIMINARY RESPONSE**

MDOT agrees that additional appropriations from the MTF would provide more funding for the State Trunkline Fund. However, MDOT stated that, based on the current statute and appropriations bills, MDOT has only been able to recover these costs through charges to the MTF before the formula distributions. MDOT also stated that legislation currently does not allow MDOT to charge the individual funds, which would provide for a more equitable distribution of the charges. MDOT will utilize the results of the finding to seek legislative changes to provide for charges to the individual funds as deemed appropriate.



# SUPPLEMENTAL INFORMATION

FUNDING FOR DEPARTMENT SERVICES PROVIDED TO LOCAL UNITS OF GOVERNMENT

Michigan Department of Transportation

Allocation Methodologies

As of August 31, 2012

<u>Service Area/Service Activity</u>	<u>Allocation Methodology</u>
Asset Management Council	Direct charges for contracted services or training fees (contracts with regional planning organizations, local planning agencies, Michigan Technological University, and Michigan's Center for Shared Solutions and Technology Partnerships).
Design and Engineering Services:	
Engineering Services	Direct labor charges for research projects and providing assistance to local units of government.
Local Program Services	100% of staff labor and related costs
Economic Development and Enhancement Programs	Professional judgment of the Transportation Economic Development Fund management.
Finance, Contracts, and Support Services:	
Accounting Outreach	Professional judgment of management from staff feedback provided on work load.
Accounts Receivable and Accounts Payable	The number of transactions processed for local projects compared to the total number of transactions processed.
Budgeting	The amount of budgeted dollars for local projects compared to total dollars budgeted.
Construction Contracts	The number of contracts processed for local projects compared to the total number of contracts processed.
Consulting Contracts	Professional judgment of management from staff feedback provided on work load.
Information Technology	Professional judgment of management from staff feedback provided on work load.
Project Accounting	The number of local projects worked on compared to the total number of projects worked on.

*Continued on next page.*

FUNDING FOR DEPARTMENT SERVICES PROVIDED TO LOCAL UNITS OF GOVERNMENT

Michigan Department of Transportation

Allocation Methodologies

As of August 31, 2012

*(Continued)*

<u>Service Area/Service Activity</u>	<u>Allocation Methodology</u>
Freight and Safety Services	Professional judgment of management from staff feedback provided on work load.
Information Technology Services and Projects	Direct, monthly charges to the Michigan Transportation Fund from the Department of Technology, Management, and Budget for technology services provided to the Michigan Department of Transportation that benefit local units of government.
Passenger Transportation Services	Professional judgment of management from staff feedback provided on work load.
Transportation Planning	Direct labor charges for research projects benefiting local units of government coded on time sheets and matching contributions (labor and research payments) provided for federally funded research projects.

Source: Compiled by the Office of the Auditor General from information provided by Michigan Department of Transportation staff.

# GLOSSARY

## Glossary of Acronyms and Terms

effectiveness	Success in achieving mission and goals.
internal control	The plan, policies, methods, and procedures adopted by management to meet its mission, goals, and objectives. Internal control includes the processes for planning, organizing, directing, and controlling program operations. It includes the systems for measuring, reporting, and monitoring program performance. Internal control serves as a defense in safeguarding assets and in preventing and detecting error; fraud; violations of laws, regulations, and provisions of contracts and grant agreements; or abuse.
local units of government	County, city, and village governmental components.
MDOT	Michigan Department of Transportation.
Michigan Transportation Fund (MTF)	A fund established in the Department of Treasury to receive money collected under the Motor Fuel Tax Act and taxes, fees, licenses, and other money received and collected under sections of the Michigan Vehicle Code.
mission	The main purpose of a program or an entity or the reason that the program or the entity was established.
performance audit	An audit that provides findings or conclusions based on an evaluation of sufficient, appropriate evidence against criteria. Performance audits provide objective analysis to assist management and those charged with governance and oversight in using the information to improve program performance and operations, reduce costs, facilitate decision making by parties with responsibility to oversee or initiate corrective action, and contribute to public accountability.

reportable condition

A matter that, in the auditor's judgment, is less severe than a material condition and falls within any of the following categories: an opportunity for improvement within the context of the audit objectives; a deficiency in internal control that is significant within the context of the audit objectives; all instances of fraud; illegal acts unless they are inconsequential within the context of the audit objectives; significant violations of provisions of contracts or grant agreements; and significant abuse that has occurred or is likely to have occurred.

State Trunkline Fund

A fund established in the Department of Treasury to appropriate funds to MDOT for the payment of bonds or obligations; for the preservation of the State trunkline highways and bridges; and for the opening, widening, improving, construction, and reconstruction of State trunkline highways and bridges.









