

Department of Transportation

**For the Year Ended
June 30, 1996**

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July 14, 1997

The Honorable Don Sundquist, Governor
and

Members of the General Assembly
State Capitol
Nashville, Tennessee 37243

and

The Honorable J. Bruce Saltsman, Sr., Commissioner
Department of Transportation
Suite 700, James K. Polk Building
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have conducted a financial and compliance audit of selected programs and activities of the Department of Transportation for the year ended June 30, 1996.

We conducted our audit in accordance with generally accepted government auditing standards. These standards require that we obtain an understanding of management controls relevant to the audit and that we design the audit to provide reasonable assurance of the Department of Transportation's compliance with the provisions of laws, regulations, contracts, and grants significant to the audit. Management of the Department of Transportation is responsible for establishing and maintaining the internal control structure and for complying with applicable laws and regulations.

Our audit disclosed certain findings which are detailed in the Objectives, Methodologies, and Conclusions section of this report. The department's administration has responded to the audit findings; we have included the responses following each finding. We will follow up the audit to examine the application of the procedures instituted because of the audit findings.

We have reported other less significant matters involving the department's internal controls and/or instances of noncompliance to the Department of Transportation's management in a separate letter.

Very truly yours,

W. R. Snodgrass
Comptroller of the Treasury

WRS/cr
96/124

State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit
Department of Transportation
For the Year Ended June 30, 1996

AUDIT SCOPE

We have audited the Department of Transportation for the period July 1, 1995, through June 30, 1996. Our audit scope included those areas material to the Tennessee Comprehensive Annual Financial Report for the year ended June 30, 1996, and to the Tennessee Single Audit Report for the same period. In addition to those areas, our primary focus was on management's controls and compliance with policies, procedures, laws, and regulations in the area of final records. The audit was conducted in accordance with generally accepted government auditing standards.

AUDIT FINDINGS

Unsupported Payments to Contractors*

Engineers Estimates of Quantities (documents supporting payments made to construction contractors) were not adequately supported by the field books. As a result, \$424,870.13 in payments to contractors has been questioned (page 4).

Lack of Adherence to Policies Designed to Ensure Davis-Bacon Act Compliance*

The department established policies and procedures to help ensure compliance with the Davis-Bacon Act. However, department personnel do not always adhere to these policies and procedures. Interviews with laborers and mechanics to help ensure contractors' wage compliance were not always conducted (page 6).

* This finding is repeated from previous audits.

ISSUE FOR LEGISLATIVE CONSIDERATION

As noted in audits since 1983, the department coordinates and administers its own property, although *Tennessee Code Annotated* stipulates that this is the responsibility of the Department of General Services. Although both departments have agreed to work together, the Department of Transportation remains in technical violation of the law. Other than this technical violation of state law, the auditors noted no problem with the Department of Transportation's coordination and administration of its own property (page 11).

"Audit Highlights" is a summary of the audit report. To obtain the complete audit report which contains all findings, recommendations, and management comments, please contact

Comptroller of the Treasury, Division of State Audit
1500 James K. Polk Building, Nashville, TN 37243-0264
(615) 741-3697

Audit Report
Department of Transportation
For the Year Ended June 30, 1996

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Department of Transportation For the Year Ended June 30, 1996

INTRODUCTION

POST-AUDIT AUTHORITY

This is the report on the financial and compliance audit of the Department of Transportation. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes the Department of Audit to “perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller.”

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

The mission of the Department of Transportation is to plan, implement, maintain, and manage an integrated transportation system for the movement of people and products, with emphasis on quality, safety, efficiency, and the environment. In order to fulfill this mission, the department is organized into two bureaus. Planning and Development administers all phases of transportation programs from planning to the advertising of highway contracts. The Operations Bureau is responsible for awarding contracts, constructing and maintaining state highways, and administering field work.

Along with its roadway activities, other duties which fall to these two bureaus include planning and development of rail transportation, aerial photography and mapping services, maintenance and operation of state-owned aircraft, issuance of permits for overdimensional vehicles, funding and assistance for publicly owned airports, and control of outdoor advertising on state highways. The department also provides maintenance on the state’s general vehicle fleet and technical and funding assistance to over 300 public transportation agencies.

In recent years, one of the primary goals of the department has been to complete the substantial road program passed by the state legislature in 1986. The program is nearly 75% complete.

With 5,000 employees and a budget over one billion dollars, the department is one of the largest agencies in state government.

An organization chart of the department is on the following page.

AUDIT SCOPE

We have audited the Department of Transportation for the period July 1, 1995, through June 30, 1996. Our audit scope included those areas material to the Tennessee Comprehensive Annual Financial Report for the year ended June 30, 1996, and to the Tennessee Single Audit Report for the same period. In addition to those areas, our primary focus was on management's controls and compliance with policies, procedures, laws, and regulations in the area of final records. The audit was conducted in accordance with generally accepted government auditing standards.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

AREAS RELATED TO TENNESSEE'S COMPREHENSIVE ANNUAL FINANCIAL REPORT AND SINGLE AUDIT REPORT

Our audit of the Department of Transportation is an integral part of our annual audit of the Comprehensive Annual Financial Report (CAFR). The objective of the audit of the CAFR is to render an opinion on the State of Tennessee's general-purpose financial statements. As part of our audit of the CAFR, we are required to gain an understanding of the state's internal control structure and determine whether the state complied with laws and regulations that have a material effect on the state's general-purpose financial statements.

Our audit of the Department of Transportation is also an integral part of the Tennessee Single Audit which is conducted in accordance with the Single Audit Act of 1984. The Single Audit Act requires us to determine whether

- the state complied with rules and regulations that may have a material effect on each major federal financial assistance program, and
- the state has internal accounting and administrative control systems to provide reasonable assurance that it is managing federal financial assistance programs in compliance with applicable laws and regulations.

We determined that the Federal Aid Highway Program within the Department of Transportation was material to the CAFR and to the Single Audit Report.

To address the objectives of the audit of the CAFR, as they pertain to the Highway Fund, we examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessed the accounting principles used and significant estimates made by management, and evaluated the overall financial statement presentation. Our work on the Highway Fund was an integral part of the CAFR audit, and the financial statements of the special revenue funds are presented in the CAFR.

To address the objectives of the audit of the Single Audit Report, as they pertain to the Federal Aid Highway Program, we interviewed key departmental employees, reviewed applicable policies and procedures, and tested representative samples of transactions, as appropriate.

We have issued an unqualified opinion on the general-purpose financial statements of the State of Tennessee in our Independent Auditor's Report dated December 20, 1996, which is included in the CAFR for the year ended June 30, 1996. The Tennessee Single Audit Report for the year ended June 30, 1996, will include our reports on the Schedule of Federal Financial Assistance, internal control structure, and compliance with laws and regulations.

As a result of our work, we determined that the department's Engineers Estimates of Quantities were not adequately supported by the field books, as discussed in finding 1, and the department's procedures for adhering to Davis-Bacon policies are inadequate, as discussed in finding 2.

1. The department did not maintain adequate supporting documentation for all project charges

Finding

As noted in previous audits, Engineers Estimates of Quantities, documents supporting payments made to construction contractors, were not adequately supported by the field books. These estimates list the description, quantity, and cost of all items anticipated to be used on a specific construction contract and are used to monitor individual items and total contract expenditures. Each month the department's project engineer updates the Engineers Estimate of Quantities to reflect the actual quantity of items used during the month. This information is obtained from the project engineer's field book, a log kept at the construction site documenting the actual quantities used each day. Each month a progress payment is made to the contractor based on these estimates.

Field books did not adequately support one or more items for seven of the 23 estimates tested.

Testwork Results

Construction Office Visited	Contracts Tested	Contracts with Errors	Bid Items Tested	Errors Noted	Error Percentage	Amount Questioned
Nashville	3	3	43	13	30%	\$321,510.00
Cookeville	2	2	58	7	12%	19,465.90
Gallatin	3	0	28	0	0%	-
Chattanooga	1	0	8	0	0%	-
Crossville	1	0	16	0	0%	-
Knoxville	3	0	73	0	0%	-
Harriman	3	1	55	2	4%	16,560.00
Jackson	2	0	44	0	0%	-
Trenton	3	1	59	12	20%	67,334.23
Murfreesboro	2	0	15	0	0%	-
Total	<u>23</u>	<u>7</u>	<u>399</u>	<u>34</u>	9%	<u>\$424,870.13</u>

Quantities recorded on the estimates did not always agree with quantities recorded in the field books, and items were not always documented in the field books. Although management concurred with the previous finding and stated, “The Department will endeavor in the future to provide continuing education to field personnel regarding the necessity for accurate and complete recordkeeping,” the problem continues.

If quantities are not accurately recorded in the field books to support progress payments made to contractors, the department could be incorrectly charged for construction costs. Because field books did not support all payments to contractors, \$424,870.13 has been questioned.

Recommendation

Management should ensure that the engineers improve documentation of contract charges in the field books and accurately transfer that information to the Engineers Estimates of Quantities. Management should evaluate the error rates within the construction offices visited to determine explanations for the variances noted. Any inefficiencies or problems noted should be addressed and corrected department-wide. Management should then ensure that all field personnel are aware of the necessity for accurate and complete recordkeeping and are adequately trained regarding the department’s specific policies and procedures for documenting contract charges. Management should accept responsibility for the proper oversight of these activities and regularly review the field personnel’s documentation of contract charges for accuracy and completeness.

Management's Comment

We concur. Based on the detail supporting this audit finding, our Director of Construction contacted the four regional construction supervisors in an effort to receive information concerning each questioned item on the contracts. Copies of these explanations are available if needed. Proper documentation of the pay items is of the utmost importance to the department. We will continue to stress this point to our construction supervisors and field personnel. While we do know that with the volume of work we presently have an occasional problem with documentation will occur, this should be rare and not the norm. We will endeavor to see that this problem is rectified in the coming year.

2. Employees should follow departmental policies and procedures to ensure Davis-Bacon compliance

Finding

In response to prior audit recommendations, the Department of Transportation established program policies and procedures to comply with the Davis-Bacon Act. However, as noted in the past four audits, department personnel do not always adhere to these policies and procedures.

The Davis-Bacon Act requires that all laborers and mechanics employed by contractors or subcontractors to work on federally assisted construction projects be paid wages no less than those established by the Secretary of Labor for the locality of the project. To monitor compliance with this requirement, the department has established a system whereby designated personnel check contractor and subcontractor payrolls. Also, the project engineer or his representative is required to conduct a specific number of monthly interviews with laborers to verify the accuracy of the payroll records examined. A separate interview form is completed and signed by the laborer and the project engineer to document each interview. In response to the prior findings, the department issued Circular Letter 1273-03 (previously Circular Letter No. 2-89) which requires that the project engineer conduct five interviews for projects with over 25 employees, three interviews for projects with ten to 25 employees, and one interview for projects with less than ten employees.

A review of the labor interview forms indicated that the project engineers had not conducted a sufficient number of interviews for four of 23 projects tested (17%) based on the number of employees on those projects. Failure to interview a sufficient number of employees decreases the department's assurance that contractor and subcontractor payroll records reflect compliance with the act.

Recommendation

Management should re-evaluate its procedures for ensuring Davis-Bacon compliance established in Circular Letter 1273-03 to determine whether these procedures continue to be effective. If not, the department's procedures should be appropriately revised. Management should then ensure that all project engineers are aware of the department's procedures and the importance of compliance. Management should regularly monitor the project engineers' compliance with Davis-Bacon procedures and take appropriate action if the engineers fail to carry out their responsibilities.

Management's Comment

We concur. We will continue to work to bring our offices into compliance.

FINAL RECORDS

Before the final contractor payment is made on any project, the final records office of the Department of Transportation collects all documentation relating to the project. This documentation includes field books, project diaries, Engineers Estimates of Quantities, materials tickets, pay adjustments, computer printouts of excavation calculations, materials and tests certifications, utility diaries, maps and plans, test reports, inspection cards, correspondence, and tare weights. In addition, the final records office creates a final record book including an index of the documentation, history of the project, original and final estimates of quantities, over-run and under-run explanations for bid items, grading items recap sheet, test report sheets, concrete cylinder break reports, contractor's payroll summary, and an affidavit sheet signed by the construction engineer.

The final records office has established guidelines on the minimum percentage of bid items that will be recalculated, reviewed for completeness, or compared to supporting documentation. If discrepancies are noted in testing these items, the percentage of items tested is increased. The final records reviewer makes appropriate corrections and completes an error report. The final contractor payment is adjusted if necessary, and released to the contractor after the final records review is complete.

The objectives of our review of the final records office's controls and procedures focused on whether

- the department maintained proper support for bid items;
- the department complied with departmental guidelines on the minimum percentages of items to review;

- the department ensured that corrections were made and project records were documented to show the necessary corrections; and
- the regional offices, in preparing the final pay estimates, complied with procedures to preclude inaccurate submissions.

We interviewed key personnel to gain an understanding of the department's procedures and controls over the final records process. We also reviewed supporting documentation and tested a sample of construction contracts from the final records offices. No problems were noted.

OBSERVATIONS AND COMMENTS

PURCHASING—SPECIAL INVESTIGATION

On November 28, 1995, Region 1 staff received 61 invoices for emission control devices totaling \$19,582, and on December 4, 1995, Region 1 staff received an additional 70 invoices totaling \$22,562. At that point, a department supervisor responsible for the Region 1 maintenance area directed that the installation of the devices be stopped and that the purchases of the devices be reviewed. As a result, the issue of the propriety of the purchases of emission control devices was referred to the department's internal auditors for review.

According to the department's internal audit review, the vendor ultimately invoiced the department \$76,523 for the installation of devices on 256 vehicles through 205 separate invoices during the period June 22 through December 4, 1995. The department paid \$10,849 to Emissions and Stabilizers, Inc., before several department staff questioned the propriety of the purchases in December 1995.

According to the department's internal auditors, after one DOT employee had authorized the purchase of 30 devices for his DOT vehicles, various other department personnel throughout Region 1 allowed additional devices to be installed on their DOT vehicles without any written contract with the vendor or any evidence, written or verbal, of management approval of such purchases.

The department was primarily concerned that (1) employees used improper purchasing procedures to purchase the devices, and (2) employees may have received favors, promises of favors, or things of value in exchange for purchasing the devices.

Our subsequent review confirmed that nine DOT employees had used improper purchasing procedures to acquire the emission control devices. However, based on our interviews, we found no evidence of actual or promised favors or any personal gain by the DOT employees involved with the installation and purchase of these devices.

In addition to interviewing the DOT employee who initially authorized the installation of 30 emission control devices, we interviewed 12 other DOT staff responsible for vehicle maintenance who stated that they had talked with a representative of Emissions and Stabilizers, Inc. Nine stated that they “allowed” the installation of the emission control devices because they “assumed” the installation had been authorized by supervisors. They indicated that they had based their assumption on (a) their knowledge, or a company mechanic’s representation, that the devices had been installed at other DOT garages or (b) their belief that since a company representative was installing the devices, he must have already obtained appropriate prior authorization.

Two staff stated that a “company mechanic” told them that the installation of the devices had been “authorized by the Knoxville Office.” The remaining employee stated that when a representative of Emissions and Stabilizers, Inc., came to his District 16 garage (Harriman) sometime in late November or early December 1995, he questioned his authority to install the emission control devices on DOT vehicles. This employee stated that the representative told him that the devices had been installed at the Knoxville garage. This employee further stated that when he called the Region 1 supervisor over vehicle maintenance to verify the representative’s statements, he was told that the company had not obtained proper authorization to install such devices.

After central office staff reviewed the matter, the department determined that appropriate procurement procedures had not been followed. Specifically, the devices were allowed to be installed without any written contracts with the vendor and without appropriate authorization from management. Also, the devices had been, and were to be, purchased using the Delegated Purchase Authority (DPA), an authority issued by the Department of General Services that allows the Department of Transportation to directly purchase repair and replacement parts, not additional equipment, such as emission control devices.

Although our review did not disclose any evidence of personal gain by state employees from the improper purchases, the improper actions of some department personnel resulted in the inappropriate use of department funds and the inappropriate modification of department equipment.

On April 1, 1996, the department returned all of the devices that had been installed on DOT vehicles to Emissions and Stabilizers, Inc., and received a full refund from the company of the \$10,849.00 it had already paid to the company.

On May 15, 1996, the Region 1 Director met with the nine DOT employees who had used improper purchasing procedures to acquire the emission control devices. According to the Region 1 Director, at that meeting he explicitly discussed both the improper purchase of emission control devices and the proper procedures that should be followed in the future by his staff. In addition, in this meeting, he presented “letters of reprimand” to the nine employees. The letters point out the failure of these employees to communicate with each other and to determine whether the purchase of the devices was appropriate rather than assuming someone else had authorized the purchase. These letters were placed in each employee’s personnel file.

Training in purchasing procedures was provided to appropriate personnel throughout the region in April 1996.

TITLE VI OF THE CIVIL RIGHTS ACT OF 1964

Tennessee Code Annotated, Section 4-21-901, requires each state governmental entity subject to the requirements of Title VI of the Civil Rights Act of 1964 to submit an annual Title VI compliance report and implementation plan to the Department of Audit by June 30, 1994, and each June 30 thereafter. For the year ending June 30, 1996, the Department of Transportation filed its compliance report and implementation plan on May 31, 1996.

Title VI of the Civil Rights Act of 1964 is a federal law. The act requires all state agencies receiving federal money to develop and implement plans to ensure that no person shall, on the grounds of race, color, or origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving federal funds.

The State Planning Office in the Executive Department was assigned the responsibility of serving as the monitoring agency for Title VI compliance, and copies of the required reports were filed with the State Planning Office for evaluation and comment. However, the State Planning Office has been abolished. The Office of the Governor is currently evaluating which office in the Executive Branch will be the new monitoring agency.

A summary of the dates state agencies filed their annual Title VI compliance reports and implementation plans is presented in the special report, *Submission of Title VI Implementation Plans*, issued annually by the Comptroller of the Treasury.

PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The Department of Transportation filed its report with the Department of Audit on September 30, 1996. A follow-up of all prior audit findings was conducted as part of the current audit.

RESOLVED AUDIT FINDING

The current audit disclosed that the Department of Transportation has corrected a previous audit finding concerning the accounting system's lack of controls to ensure all federal projects are billed. Although this issue is not completely resolved, the DOT STARS system indicates all federal projects able to be billed are being included on the weekly federal bill.

REPEATED AUDIT FINDING

The prior audit report also contained a finding concerning compliance with policies designed to ensure Davis-Bacon Act compliance. This finding has not been resolved and is repeated in the applicable section of this report.

PAST FINDING NOT ACTED UPON BY MANAGEMENT

As noted in prior audits since 1983, the Department of Transportation coordinates and administers its own property. Section 4-3-1103 of *Tennessee Code Annotated* stipulates the following:

The department of general services shall coordinate and administer the state's purchases, personal properties, printing and motor vehicle facilities, surplus property, postal services and general public works services, and will provide for state agencies all additional support services which are not assigned by law to specific departments.

Section 4-3-1105(4), *Tennessee Code Annotated*, states that the Department of General Services has the power and shall be required to

supervise and regulate the making of an inventory of all removable equipment and other movable property belonging to the state government or any of its departments, institutions or agencies, with the exception of those institutions expressly exempted from the operation of title 12, chapter 3, and keep the same current.

Thus, in coordinating and administering its own property, the Department of Transportation is technically in violation of state law. The previous audits have recommended that the Department of Transportation work with the Department of General Services to comply with the law. Although management of both departments have always concurred, this problem still has not been resolved. Other than this technical violation of state law, the auditors noted no problems with the Department of Transportation's coordination and administration of its own property.

APPENDIX

DIVISIONS AND ALLOTMENT CODES

Department of Transportation divisions and allotment codes:

401	Transportation Headquarters
403	Bureau of Planning and Development
411	Bureau of Operations
412	Engineering Administration
414	Liability Insurance Premiums
416	Area Mass Transit
417	Waterways and Rail Transportation
418	Field Construction Operations
419	Field Maintenance Operations
430	Equipment Administration
440	Planning and Research
451	Maintenance and Marking
453	Betterments
455	State Aid
461	Rural Roads Construction
462	Federal Secondary Construction
470	State Industrial Access
471	State Construction
472	Interstate Construction
473	Primary Construction
475	Forest Highways
476	Appalachia Construction
478	Local Interstate Connectors
479	State Secondary Construction
480	State Highway Construction
481	Capital Improvements
482	Other Construction
484	Great River Road
485	Highway Beautification
487	Metropolitan - Urban Construction
488	Bridge Replacement
489	Highway Safety Construction
491	Aeronautics
494	Transportation Equity Fund

