
Secretary of State

State of Oregon

OREGON DEPARTMENT OF TRANSPORTATION

Overhead Costs



Audits Division

Contract Auditors: Talbot, Korvola and Warwick, L.L.P.

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Auditing for a Better Oregon

Senator Gene Timms and
Representative Jim Welsh, Co-Chairs
Legislative Audit Committee

Dear Committee Members:

At the September 1997 and November 1997 meetings of the Legislative Audit Committee, the Oregon Audits Division presented the results of its audit survey at the Oregon Department of Transportation (ODOT). The survey summarized the views and concerns of ODOT stakeholders and identified potential audit issues. Based on input from committee members, the Audits Division began work on five of the proposed projects.

This audit report, one of the five projects, responds to requests for information about ODOT administrative and indirect (overhead) expenditures. The audit was conducted by the accounting firm of Talbot, Korvola and Warwick, L.L.P., under contract to the Audits Division.

The audit found that the portion of expenditures for administrative and indirect (overhead) services (9.8 percent) within ODOT's highway construction and maintenance branch compared favorably to transportation program expenditures by 25 Oregon local governments. Due to a lack of formal or comparative criteria, the auditors concluded that detailed cost analysis, outside the scope of this audit engagement, is needed to conclude on the reasonableness and economy of expenditures within ODOT's Central Administration area, Driver and Motor Vehicle Services Branch, Transportation Development Branch, and in other areas.

We appreciate the cooperation of ODOT management and staff during this review.

OREGON AUDITS DIVISION

John N. Lattimer
Director

FAX (503) 452-7174
E-Mail: tkw@tkw.com

Oregon Department of Transportation



Audit of Administrative and Overhead Costs

August 1998



6420 SW Macadam, Suite 500
Portland, Oregon 97201
(503) 452-7172

August, 1998

Mr. John Lattimer, Director
Secretary of State Audit Division
255 Capitol Street NE, Suite 500
Salem, Oregon 97310

Dear Mr. Lattimer:

We have completed our audit of the Oregon Department of Transportation (ODOT) Administrative and Overhead Costs. This report contains our detailed analysis and conclusions based on our review.

We wish to express our appreciation to ODOT staff, Secretary of State Audits Division personnel assigned to this project and those persons from other organizations we spoke with, for their cooperation and assistance during this audit.

Talbot, Korvola & Warwick, LLP

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REPORT SUMMARY

This report is the result of our audit of the Oregon Department of Transportation's (ODOT) administrative and overhead costs. Our primary objectives were to:

1. Develop working definitions for administrative and overhead costs.
2. Determine and evaluate the reasonableness of ODOT administrative and overhead costs.
3. Determine and evaluate costs pertaining to office supplies and equipment, facilities, and training and travel.

To achieve our audit objectives, we assembled reasonable, practical definitions for administrative and overhead costs, developed a reliable and straightforward methodology for use in audits of other state agencies and we applied the definitions and methodology in describing and evaluating ODOT expenditures.

Because no standard definitions of administrative and overhead costs exist, a major task was to develop working definitions. We chose to use Title 23 of the Code of Federal Regulations in conjunction with the US Office of Management and Budget Circular A-87 as a basis. Title 23, which has been applied to ODOT's construction and maintenance activities and Circular A-87 define administrative, indirect, and direct costs.

We found that those activities characterized as indirect costs were similar to those currently referred to as "overhead costs." In conjunction with the Secretary of State's Audits Division, we agreed to the following convention:

Indirect Costs = Overhead Costs

Indirect (overhead costs) are not the same as administrative costs. Costs are classified as administrative if they are considered necessary for the management, supervision and administrative control of a suitably equipped, staffed and operational state highway

agency. Indirect costs are generally considered as operating costs incurred for joint purposes within an organization and are not necessarily assignable to specific projects.

This working definition distinguishes administrative and indirect (overhead) from direct costs, as defined. Applying these definitions to ODOT expenditures for the 1995-97 biennium resulted in the following amounts:

**ODOT Total Expenditures by Branch
1995-97 Biennium**

	Admin. \$	%	Indirect (Overhead) \$	%	Subtotal \$	%	Direct \$	%	Total \$	% of Total
Central Admin.	47,955,837	37.14	74,037,041	57.33	121,992,878	94.47	7,141,894	5.53	129,134,772	9.52
TSO	14,962,981	1.44	86,746,805	8.36	101,709,786	9.80	936,145,408	90.20	1,037,855,194	76.53
DMV	5,934,641	5.19	30,786,952	26.92	36,721,593	32.11	77,630,267	67.89	114,351,860	8.43
MCTB	2,516,714	6.32	4,984,501	12.52	7,501,215	18.84	32,311,652	81.16	39,812,867	2.94
TDB	4,662,282	13.33	18,121,561	51.82	22,783,843	65.15	12,189,494	34.85	34,973,337	2.58
Total	76,032,455	5.61	214,676,860	15.83	290,709,315	21.44	1,065,418,715	78.56	1,356,128,030	100

TSO = Transportation System Operations Branch
DMV = Driver and Motor Vehicle Services Branch
MCTB = Motor Carrier Transportation Branch
TDB = Transportation Development Branch

Source: Compiled by TKW

Illustration 1

We identified no formally established criteria to evaluate the reasonableness and economy of ODOT’s overall administrative and indirect (overhead) costs. However, administrative and indirect (overhead) costs within ODOT’s largest branch, Transportation System Operations, appear reasonable when compared to Oregon city and county expenditures shown in our companion report - *Local Agencies Use of Highway Funds*. In that report the ten Oregon counties and fifteen cities reviewed

used, on the average, 6% of transportation funds for administration and another 9% for indirect (overhead) services.

Due to a lack of formal or comparable criteria we concluded that detailed cost analysis, outside the scope of this engagement, is needed to determine the reasonableness and economy of ODOT expenditures incurred by Central Administration, the Driver and Motor Vehicle Services Branch, the Transportation Development Branch, and the Non-Limited Program area. We also noted opportunities for modifications in ODOT's use of its automated financial system. The following chapters detail our approach and the results of our review

INTRODUCTION

Talbot, Korvola & Warwick, LLP, under contract to the Oregon Secretary of State Audits Division, conducted an audit of the Oregon Department of Transportation (ODOT) Administrative and Overhead Costs. This report outlines the analysis and conclusions based on our work.

AUDIT OBJECTIVES

The objectives of this audit were to:

1. Develop working definitions for administrative and overhead costs.
2. Determine and evaluate the reasonableness of ODOT administrative and overhead costs.
3. Develop a practical methodology to calculate administrative and overhead costs suitable for use in future studies by the Audits Division or other state agencies.
4. Determine and evaluate costs pertaining to office supplies and equipment, facilities, and training and related travel.

AUDIT SCOPE

Once our working definitions of administrative and indirect (overhead) costs were established, they were used as the foundation for classifying actual expenditures incurred by ODOT. The audit analyzed expenditures reported in 1995-97 biennium - the most recent biennium with complete financial information.

STANDARDS

This audit was conducted in accordance with generally accepted governmental performance audit standards.

COMPLIANCE

Because of the nature of this audit, we did not examine compliance with any federal or state statutes pertaining to administrative and overhead costs. However, for those items we did not specifically test for compliance, nothing came to our attention that would indicate significant instances of non-compliance.

AUDIT METHODOLOGY

In developing working definitions for administrative and overhead costs and establishing an implementable methodology for future calculations, we focused on three specific tasks: understanding the ODOT organization, determining what criteria existed, and formulating an approach.

THE APPROACH

To gain an understanding of ODOT activities and expenditures, we interviewed approximately 50 employees throughout the agency. In addition, we analyzed ODOT financial documents and reports. Included in this review were organizational charts, budget documents, applicable federal regulations, and internal reporting systems.

Other States

Officials within ODOT and transportation officials in the states of Colorado, Idaho, Nevada and Washington were contacted to determine how administrative and overhead costs were calculated and reported.. We found very dissimilar practices. No standard or explicit definition of these costs was available, nor were consistent methodologies being used. We concluded that any comparison among these state transportation agencies would result in unreliable and possibly invalid conclusions.

Financial Information

To accurately categorize ODOT expenditures, we requested financial information through the agency's "TEAMS"¹ accounting system. Although an analysis of the propriety of individual transactions was outside the scope of this

¹ Transportation Environment Accounting and Management System

project, we used several methods to determine the accuracy and the validity of the information received from the system.

First, we gained an understanding of the system's reporting ability through interviews with ODOT employees and a review of the TEAMS transaction coding manual. Second, reports of total expenditures were obtained and compared against:

- the agency's *Comprehensive Annual Financial Report*;
- expenditures as reported to the Department of Administrative Services; and
- reports created by the Secretary of State Audits Division using audit software and the ODOT database.

In each of the comparisons, minimal differences were identified. These results suggested that reports obtained through the TEAMS database accurately capture individual transaction amounts and could be relied upon.

Budget Limitation vs. Branch Expenditures

ODOT's methods of monitoring expenditures does not provide a ready depiction of how funds are being used. As a state agency, ODOT prepares its biennial budget according to the *State of Oregon Budget and Legislative Concept* instructions. Once approved, the budget is entered into the TEAMS accounting system by legislative appropriation or "limitation". Budget limitations provide for certain types of spending. For example, ODOT has a limitation for highway construction, one for maintenance, etc. As expenditures are incurred, they are charged against a limitation. ODOT financial specialists compare expenditures to the budget limitation throughout the biennium to ensure that spending does not exceed budget.

We found that although tracking costs by limitation is necessary to stay within budget, it is not an effective way to evaluate expenditures by organizational activity. The limitations are not intended to prescribe the ODOT organizational branch in which funds will actually be spent.

Classification of Costs

We chose to classify costs as administrative, indirect (overhead), and direct by examining the nature of the work performed by each of the organizational units within ODOT. In most cases, ODOT organizational charts accurately differentiated the work performed, and expenditure classifications were made along organizational lines. The TEAMS accounting system could be used to classify expenditures whenever they were coded to the appropriate organizational unit. Most, but not all, ODOT branches assigned their transactions to a “responsible unit” code that corresponded to an organization chart.

RECOMMENDATION #1

To help simplify the classification, recording, and evaluation of costs, we recommend that ODOT:

- Assign TEAMS “responsible unit” codes based on the branch organization chart.
 - Assign to responsible units a cost classification (administrative, direct, indirect) that most accurately describes the work.
 - Consistently record time and costs to the correct responsible unit.
 - Update TEAMS coding when organizational changes are made.
-

EVALUATION OF EXPENDITURES

Once expenditures for the 1995-97 biennium were identified and categorized based on the working definitions, an evaluation of the reasonableness of the expenditures was attempted. This task proved to be extremely difficult. We identified no reliable basis for comparison among state transportation agencies to determine whether expenditures by branch, function, limitation, etc. were appropriate and reasonable. However, our firm's audit work in a companion report, *Local Agencies Use of Highway Funds*, performed under contract to the Audits Division, did provide criteria for assessing expenditures by ODOT's Transportation System Operations Branch. The companion audit shows administrative and indirect (overhead) charges against transportation funds by ten Oregon counties and fifteen cities. However, because of differences between ODOT and local government responsibilities, structures, and funding, it was not possible to use the results of that audit to arrive at a definitive conclusion on the reasonableness of expenditures in all ODOT branches. In addition, the amount of some ODOT expenditures did raise questions. These issues are presented in the sections that follow.

THE DEFINITIONS

To arrive at working definitions of administrative and overhead costs, we chose to use as our basis Title 23 of the Code of Federal Regulations in conjunction with the US Office of Management and Budget Circular A-87. Title 23, which has been applied to ODOT's construction and maintenance activities, and Circular A-87, define administrative, indirect and direct costs. Using these, we compiled the following definitions:

Direct Costs

Actual costs - salaries, wages, payroll expenses, transportation, supplies, materials, etc. of key project and service-related activities.

Administrative Costs

General administration, supervision and other support services necessary for the management, supervision and administrative control of the agency. ODOT administrative costs include all costs associated with the following organizational units:

- the ODOT director, deputy directors and related support staff, and
- the first and second levels of branch and region management and all related support staff.

Administrative costs are also incurred by ODOT branches involved in financial services, information technology, human resources, and communications, among others.

Indirect Costs

Operating costs incurred for common or joint purposes that benefit more than one organizational objective or unit. This includes costs which are not easily adaptable to charging directly to individual projects or services. Examples of indirect costs include:

- office supplies and equipment

- building rent or lease expenses
- building and grounds maintenance
- utilities and communications
- training
- records management
- general clerical support
- general analytical and/or coordinating support

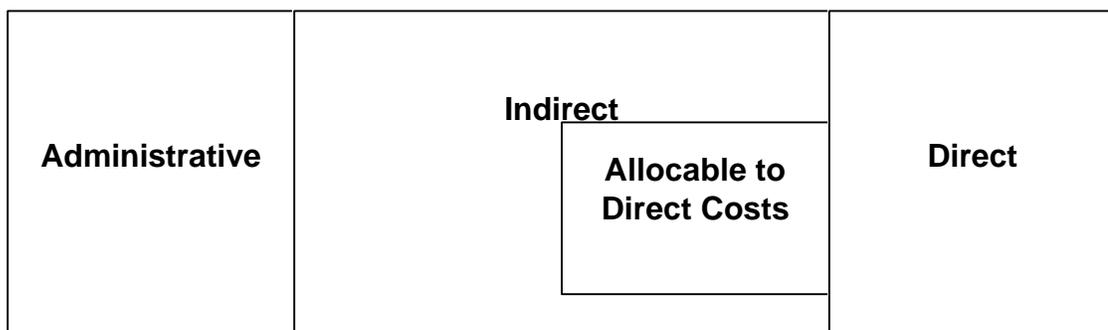
Some indirect costs are incurred by ODOT branches involved in financial services, information technology, human resources, and communications, among others.

Certain costs can, at times, be classified as direct or indirect depending on how they are applied. For example, engineering costs specifically attributable to a highway construction project are considered direct whereas engineering costs related to highway maintenance are classified as indirect.

Our review found that those activities generally classified as indirect costs were similar to those commonly referred to as overhead costs. Therefore, in conjunction with the Secretary of State's Audits Division, we agreed to the following convention:

Indirect Costs = Overhead Costs

This working definition distinguished administrative and indirect (overhead) from direct costs as defined. The following illustration depicts our classification of costs.

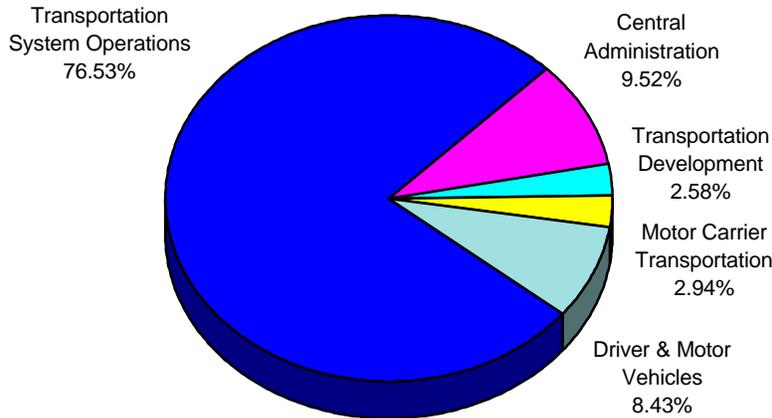


Source: Developed by TKW

Illustration 2

COSTS

ODOT - TOTALS (1995-97 Biennium)



This section identifies the administrative and indirect (overhead) expenditures incurred by ODOT in the 1995-97 biennium, as classified by the working definitions.

Certain expenditures have been excluded in the detailed breakdowns. These include:

- **Capital Outlay**

Capital outlay expenditures are the basis for reporting the costs of assets. However, because ODOT has not consistently calculated depreciation for all assets, that expense has not been included in the detailed breakdowns.

- **Special Payments and Debt Service**

The special payments and debt service categories have not been included in the calculation of administrative and indirect (overhead) costs. These expenditures are not related to the usual activity of the organization and their inclusion in the total expenditures was determined

to be misleading. These expenditures are shown separately in the following tables:

Debt Service Expenditures
1995-97 Biennium

	Debt Service \$
Central Administration	46,155,065
Transportation Sys. Operations	0
Driver & Motor Vehicle	6,385,819
Motor Carrier Transportation	0
Transportation Development	0
Total	52,540,884

Source: Compiled by TKW

Illustration 3

Special Payments
1995-97 Biennium

	Central Admin. \$	Transportation System Operations \$	Driver & Motor Vehicle \$	Motor Carrier Transport. \$	Transportation Development \$	Total Payments from ODOT \$
Distribution To:						
State Agencies	-	2,314,031	51,334	463,832	2,457,664	5,286,861
Cities	1,994,410	17,148,445	-	72,606	1,984,811	2,057,417
Counties	498,481	28,702,446	-	312,231	2,470,984	2,783,215
Other Govts	112,500	20,913,239	-	208,407	3,938,569	4,146,976
Non Govts	90,250	804,095	-	-	4,774,956	4,774,956
Individuals	-	-	-	-	6,755	6,755
Total	2,695,641	69,882,256	51,334	1,057,076	15,633,739	\$89,320,046.00

Source: Compiled by TKW

Illustration 4

Total ODOT expenditures have been calculated as follows:

**ODOT Total Expenditures by Branch
1995-97 Biennium**

	Admin. \$	%	Indirect (Overhead) \$	%	Subtotal \$	%	Direct \$	%	Total \$	% of Total
Central Admin.	47,955,837	37.14	74,037,041	57.33	121,992,878	94.47	7,141,894	5.53	129,134,772	9.52
TSO	14,962,981	1.44	86,746,805	8.36	101,709,786	9.80	936,145,408	90.20	1,037,855,194	76.53
DMV	5,934,641	5.19	30,786,952	26.92	36,721,593	32.11	77,630,267	67.89	114,351,860	8.43
MCTB	2,516,714	6.32	4,984,501	12.52	7,501,215	18.84	32,311,652	81.16	39,812,867	2.94
TDB	4,662,282	13.33	18,121,561	51.82	22,783,843	65.15	12,189,494	34.85	34,973,337	2.58
Total	76,032,455	5.61	214,676,860	15.83	290,709,315	21.44	1,065,418,715	78.56	1,356,128,030	100

TSO = Transportation System Operations Branch
DMV = Driver and Motor Vehicle Services Branch
MCTB = Motor Carrier Transportation Branch
TDB = Transportation Development Branch

Source: Compiled by TKW

Illustration 5

OTHER EXPENDITURES

As part of our audit work, the Audits Division requested a breakdown of the following ODOT indirect (overhead) expenditures: office supplies, equipment, facilities, training and travel. These were calculated as follows:

Other Expenditures - Office Supplies, Facilities & Training

1995-97 Biennium

	Expenditures \$	% of Total
Office Supplies	16,224,691	38.73
Facilities Rent and Utilities	21,817,290	52.09
Training and Related Travel	3,844,961	9.18
Total	41,886,942	100

Source: Compiled by TKW

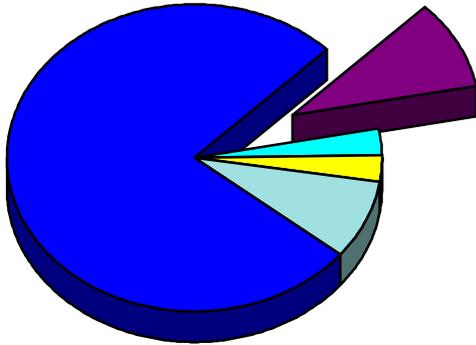
Illustration 6

Although we did not perform a detailed analysis of these expenditures, we did note the following office supply expenditures that merit additional examination:

- Postage \$4,188,595
- Forms \$1,957,363

The Audits Division also requested an analysis of ODOT's compliance with state rules concerning travel awards (frequent flyer miles). The rules require state employees to return travel awards, earned while on state business, to the state. We found no indication that ODOT was out of compliance with these requirements.

CENTRAL ADMINISTRATION



OVERVIEW

ODOT maintains a core group of administrative and indirect (overhead) services collectively referred to as Central Administration. In the 1995-97 biennium, ODOT's Central Administration area was comprised five distinct functions and approximately 600 FTE. These included:

- Communications
- Financial Services
- Information Systems
- Support Services Section
- Human Resources Section

COMMUNICATIONS

The Communications function is responsible for coordinating all interactions between the public and ODOT. Staff within this function assist each of the ODOT's five regional offices in responding to the public's concerns, coordinating legislative matters, providing information about ODOT to the public, and preparing media releases.

The majority of the function is centralized in Salem with the exception of 10 FTE located in region offices and at other ODOT branches.

FINANCIAL SERVICES

The Financial Services function is responsible for performing accounting, budgeting, and financial reporting-related tasks for all ODOT branches and regions. These include the following:

- Accounts payable
- Payroll
- Accounts receivable and receipting
- Budget development and analysis
- Statewide financial reporting
- Internal audit
- Fuel tax audit & collection
- Cost allocation
- Financial analysis and reporting

INFORMATION SYSTEMS

The Information Systems function provides agency-wide data processing, data management, application development, technology support, information management, voice and data communications, and consultation. These services are also provided to other governmental agencies and organizations including the Forestry Department, Department of Parks and Recreation, Oregon State Police, and several city and county programs.

Much of the function is decentralized to the five regions and to ODOT branches.

SUPPORT SERVICES

The Support Services function includes a variety of indirect (overhead) services. These include the following:

Records Retention

This section develops records retention and disposition schedules; coordinates off-site records storage; designs, develops and revises forms; assures standard filing systems and coordinates and distributes ODOT policies and procedures. In addition, the section operates reprographics services, photo and video services, a storeroom, and a sign shop. It also transports fleet equipment and supplies to and from various locations within Oregon.

Purchasing

The Purchasing section is responsible for processing public works and personal services contracts. Purchasing staff develop contracts and price agreements used to purchase the tools, materials, goods and services necessary for ODOT to develop, manage, and maintain a statewide transportation network.

Facilities Management

This section is divided into two functions; facilities construction and facilities maintenance. The construction portion manages all building construction for ODOT-owned structures. The maintenance portion provides for lease negotiations, office space planning, building maintenance, and minor building improvements.

Fleet Services

The Fleet Services section is responsible for acquisition and management of ODOT's motor vehicle equipment. Included are; three repair and parts shops in Bend, LaGrande, and Salem. In addition, field mechanics are located throughout the state for on-site support.

For the 1997-99 biennium, Support Services was reorganized as two separate sections: Business Services and Purchasing.

HUMAN RESOURCES

The Human Resources function is responsible for recruiting competent employees, providing for a safe work environment, and maintaining and enhancing employee skills. This function is organized into three sections: Human Resources Program Services, Personnel Services and Safety, and Human Resource Development. These sections provide technical advice on personnel, safety, and training issues; provide for employee recruitment and selection; collect and analyze data; and produce reports to help management identify employment related issues and trends.

For the 1997-99 biennium, Human Resources was renamed Human Resource Management and Organizational Development.

CENTRAL ADMINISTRATION COSTS

As previously mentioned, ODOT maintains a core group of administrative and indirect (overhead) services known as Central Administration. Each function within Central Administration provides support and services to other ODOT branches; the costs of these services are charged against other ODOT branches as direct charges and assessments.

Each Central Administration function provides support to other ODOT branches by assigning employees (FTE) to work on-site at the branch or region offices. For example, Information Systems, Human Resources and Support Services all have staff working on-site for DMV. Most costs associated with these FTE are charged to the

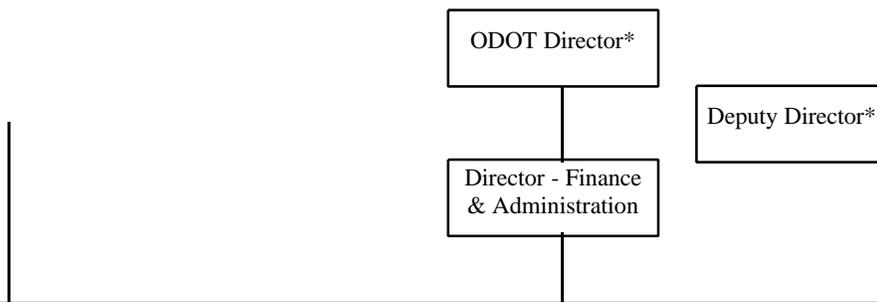
Central Administration limitation. The same applies to other Central Administration FTE assigned to other branches.

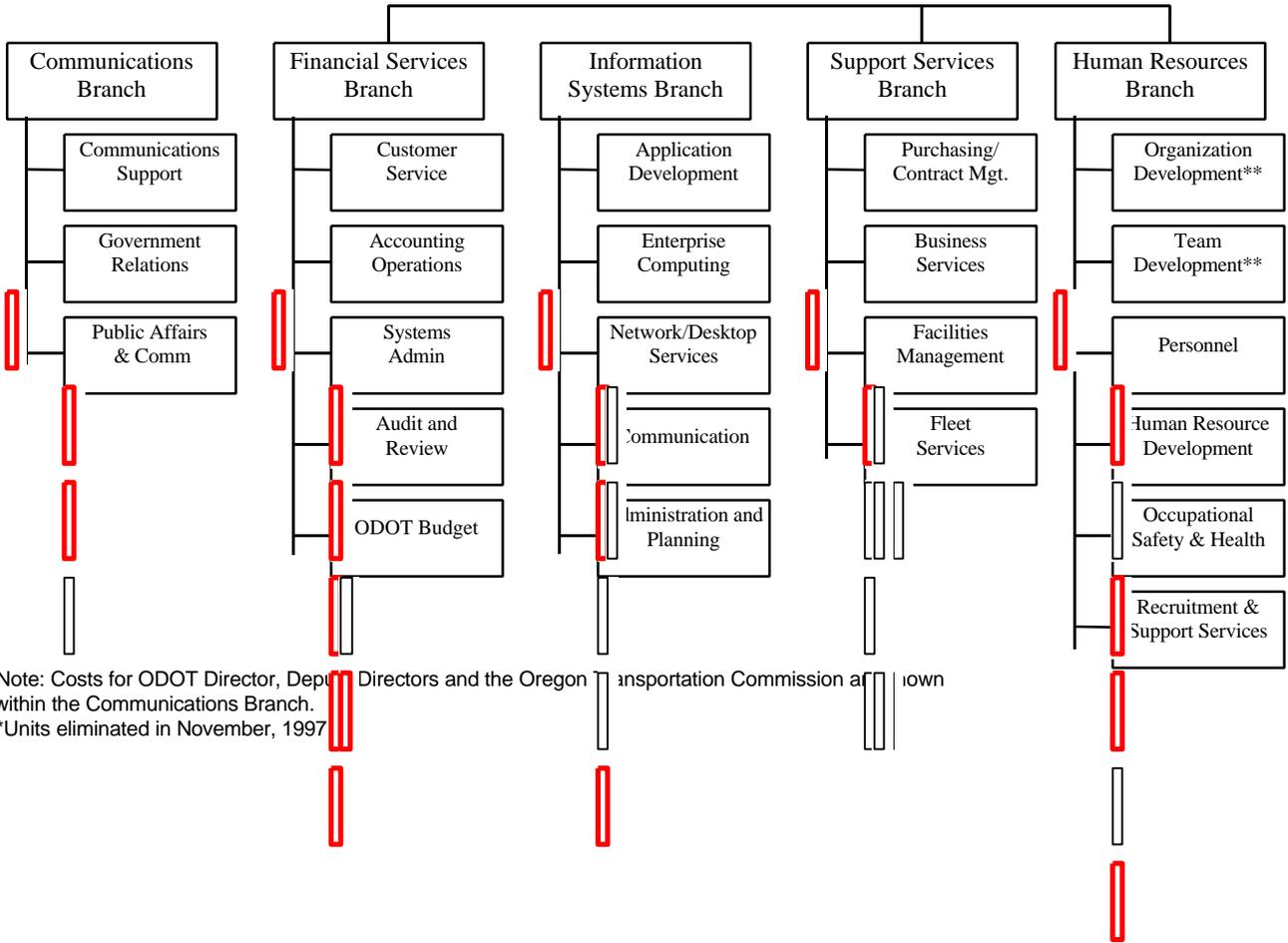
Two of the five functions within Central Administration charge for the direct services they provide; Support Services and Information Services. For example, when an outside branch (“user”) requests photo and/or video services, the Support Services function will provide the services and directly charge the “user” for all time and expenditures incurred. The same applies for other services such as design, reprographics, fleet parts, and repair.

All other expenditures incurred by Central Administration and charged against the central administration limitation are “assessed” to other ODOT branches. At the end of each quarter, all Central Administration expenditures not previously charged to other ODOT branch limitations are compiled. Each of the branches pay for a portion of these compiled charges based on the number of FTE within each branch.

ALLOCATING CENTRAL ADMINISTRATION COSTS

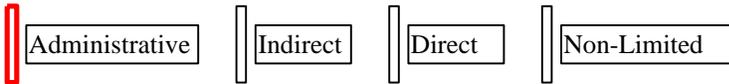
Applying the working definition of administrative and overhead costs to Central Administration resulted in the following categorization of administrative, indirect and direct costs:





*Note: Costs for ODOT Director, Deputy Directors and the Oregon Transportation Commission are shown within the Communications Branch.
**Units eliminated in November, 1997

Central administration costs by category for 1995-97 biennium are shown as follows:



Central Administration Expenditures 1995-97 Biennium

	Admin. \$	%	Indirect (Overhead) \$	%	Subtotal \$	%	Direct \$	%	Total \$	% of Total
Communicat.	6,186,476	93.24	448,556	6.76	6,635,032	100	0	0.00	6,635,032	5.14
Financial Services	20,331,646	73.47	2,174,565	7.86	22,506,211	81.33	5,167,685	18.67	27,673,896	21.43
Information										

Services	6,582,310	16.84	32,494,054	83.16	39,076,364	100	0	0.00	39,076,364	30.26
Support Services	5,730,237	13.36	35,196,551	82.04	40,926,788	95.40	1,974,209	4.60	42,900,997	33.22
Human Resources	9,125,168	71.02	3,723,315	28.98	12,848,483	100	0	0.00	12,848,483	9.95
Central Admin. Expenditures	47,955,837	37.14	74,037,041	57.33	121,992,878	94.47	7,141,894	5.53	129,134,772	100
Less Central Admin. Assessment/Appropriation										
TSO	(31,774,198)	91.23	(3,055,027)	8.77	(34,829,225)	100	-	0.00	(34,829,225)	55.55
DMV	(7,940,603)	70.50	(3,322,971)	29.50	(11,263,574)	100	-	0.00	(11,263,574)	17.96
MCTB	(8,957,285)	90.25	(968,219)	9.75	(9,925,504)	100	-	0.00	(9,925,504)	15.83
TDB	(350,742)	100	-	0	(350,742)	100	-	0.00	(350,742)	.56
Non-limited	(1,471,019)	23.23	(2,915,397)	46.03	(4,386,416)	69.26	(1,947,226)	30.74	(6,333,642)	10.10
Total	(50,493,847)	80.53	(10,261,614)	16.37	(60,755,461)	96.90	(1,947,226)	3.11	(62,702,687)	100

TSO = Transportation System Operations Branch
 DMV = Driver and Motor Vehicle Services Branch
 MCTB = Motor Carrier Transportation Branch
 TDB = Transportation Development Branch
 Non-limited = Non-limited program area

Note: Costs for the Director's and Deputy Directors' Office are included in the Communications Branch.

Source: Compiled by TKW

Illustration 7

As would be expected, Central Administration primarily consists of administrative and indirect expenditures. The above expenses may be reasonable given ODOT's size and diversity of operations. However, we are unable to conclude on this matter due to the lack of comparable information from other state transportation agencies. Additional cost analysis beyond the scope of this audit is required to determine the extent to which ODOT's Central Administration activities and resulting expenditures are reasonable and economical.

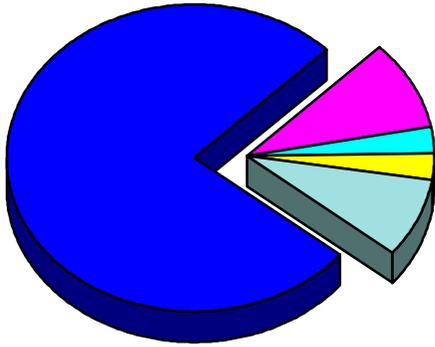
While identifying the support services allocation of administrative and indirect (overhead) costs, we found that manager, project coordinator and administrative support salaries were being charged to the fleet services portion of ODOT's non-limited limitation. Because these positions oversee all aspects of support

services operations, their costs should be allocated to the support services branch.

RECOMMENDATION #2

To improve accuracy in applying costs, we recommend ODOT allocate costs for support services manager, project coordinator, and administrative support salaries to the support service branch.

TRANSPORTATION SYSTEM OPERATIONS (Highway Construction and Maintenance)



OVERVIEW

The Transportation System Operations branch is the largest organizational unit within ODOT accounting for over 76% of ODOT expenditures in the 1995-97 biennium. It includes highway construction, maintenance and technical service activities (such as engineering and inspections) throughout the state.

CONSTRUCTION PROGRAM

The construction program's 1,300 FTE provide for major highway and bridge construction projects as identified through the State Transportation Improvement Program. Major highway projects are contracted to the private sector. Designing, contracting and inspecting projects performed by the private contractors are major activities of the program.

MAINTENANCE PROGRAM

The maintenance program provides routine and preventive maintenance to assure the state's highway system is safe and operable. Its 1,400 FTE perform a variety of tasks including: snow and ice removal, emergency repairs,

installation and replacement of signs, control of roadside vegetation, repair of potholes, and bridge maintenance.

The five ODOT regions are organized geographically; they are further subdivided into maintenance districts that align somewhat with counties. Each region is organized and staffed based on specific factors such as geography, weather patterns, and traffic density. A region manager is responsible for activities within the region and is assisted by district managers, a construction manager, a traffic engineer, a business manager, a planning and development manager, and various other personnel. Regional personnel are largely “hands-on” and spend most of their time executing and monitoring programs and projects.

TRANSPORTATION SYSTEM OPERATIONS COSTS

The majority of Transportation System Operations branch expenditures are charged to the construction, maintenance and reimbursable limitations. Other ODOT branches also spend against these limitations.

ALLOCATING COSTS

Transportation System Operations administrative and indirect (overhead) costs were generally allocated based on Title 23 definitions. However, certain inconsistencies were encountered in the methods used by ODOT to code its expenditures. To improve the accuracy of our report, we re-classified some expenditures. Because the Transportation System Operations branch has a complex organizational structure, and because direct expenditures predominate, we did not believe an organizational diagram would be helpful in showing the cost structure. The following illustration shows branch costs by category for the 1995-97 biennium:

Transportation System Operations Expenditures 1995-97 Biennium

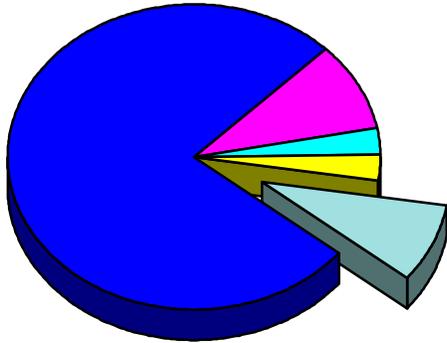
	Admin. \$.	%	Indirect (Overhead) \$	%	Subtotal \$	%	Direct \$	%	Total \$	% of Total
Branch Expenditures	14,962,981	1.44	86,746,805	8.36	101,709,786	9.80	936,145,408	90.20	1,037,855,194	96.75
Central Admin. Assessment	31,774,198	91.23	3,055,027	8.77	34,829,225	100	-	0	34,829,225	3.25
Total	46,737,179	4.36	89,801,832	8.37	136,539,011	12.73	936,145,408	87.27	1,072,684,419	100

Source: Compiled by TKW

Illustration 8

Administrative expenditures (approximately 1%) and indirect (overhead) expenditures (approximately 8%) within the Transportation System Operations branch appear to be reasonable. These numbers reflect a small percentage of total allocations for the branch and indicate that a large dollar amount was spent on project related activities. They compare favorably to Oregon city and county administrative and indirect (overhead) costs as reported in our companion report: *Local Agencies Use of Highway Funds*. In that report the ten counties and fifteen cities reviewed used, on the average, 6% of transportation funds for administration and another 9% for indirect (overhead) services.

DRIVER AND MOTOR VEHICLES



OVERVIEW

In the 1995-97 biennium, the Driver and Motor Vehicles Branch (DMV) was comprised of three major program areas and approximately 900 FTE. These programs identify, license, and regulate users and the use of the state's transportation system.

DRIVER PROGRAMS

Driver programs provide for driver licensing, identification, driver improvement, and related services.

VEHICLE PROGRAMS

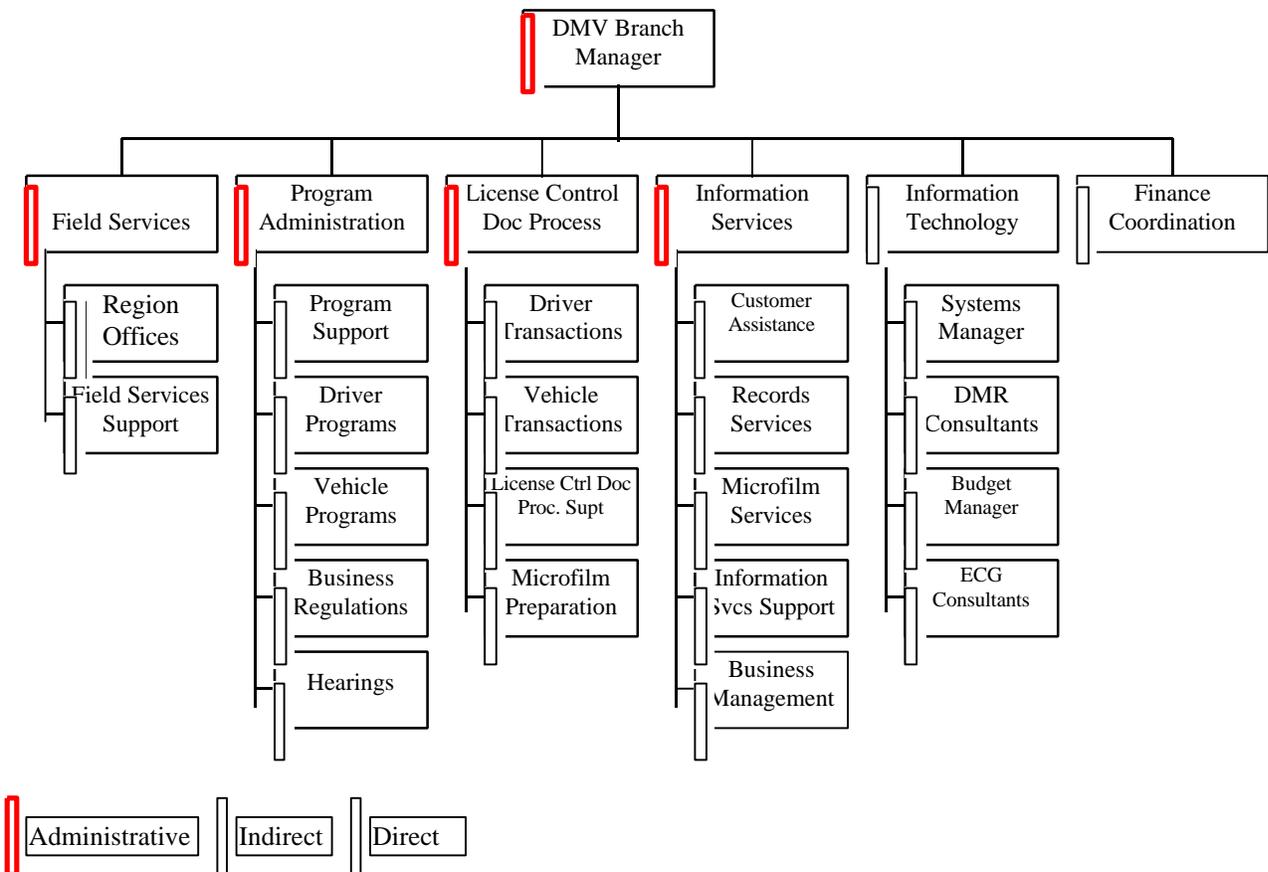
Vehicle programs provide for vehicle registrations, the issuance of license plates and renewal stickers, vehicle titles, trip permits, and related services.

BUSINESS REGULATION PROGRAMS

Business regulation programs provide for the licensing and inspection of vehicle dealers, wreckers, driving instructors, and other providers.

DRIVER AND MOTOR VEHICLE COSTS

Administrative, indirect (overhead), and direct expenditures are most readily calculated if they can be defined by organizational entity. Because DMV has not identified its expenditures in this manner, our working definitions were applied by reviewing the functions performed by organizational units. We then classified DMV expenses as direct if the work involved license or title processing or production, face-to face or telephone customer service, or regulatory services.



Indirect organizational areas in DMV were generally identified as those that do not have direct contact with customers, but provide the support (personnel and systems) necessary to provide direct services. The indirect areas include information systems; support staff; and microfilm services. Administrative costs

were incurred by field services managers, in the program administration area, in the license control/document processing area, and the information services area.

Expenditures incurred within the DMV Branch are identified and categorized in the chart that follows:

Driver & Motor Vehicle Expenditures 1995-97 Biennium

	Admin.	%	Indirect (Overhead)	%	Subtotal	%	Direct	%	Total	% of Total
Branch Manager	3,509,135	100	-	0.00	3,509,135	100	-	0.00	3,509,135	2.79
Program Admin.	245,397	1.12	9,374,217	42.87	9,619,614	43.99	12,245,619	56.00	21,865,233	17.41
Field Services	1,433,074	3.29	2,355,009	5.39	3,788,083	8.68	39,831,790	91.32	43,619,873	34.72
License Ctrl/ Document Processing	517,583	2.92	556,991	3.14	1,074,574	6.06	16,650,004	93.94	17,724,578	14.11
Information Services	229,452	3.58	1,263,908	19.73	1,493,360	23.31	4,913,826	76.69	6,407,186	5.10
Information Technology	-	0.00	17,236,827	81.21	17,236,827	81.21	3,989,028	18.79	21,225,855	16.90
Branch Expenditures	5,934,641	5.19	30,786,952	26.92	36,721,593	32.11	77,630,267	67.89	114,351,860	91.03
Central Admin. Assessment	7,940,603	70.50	3,322,971	29.50	11,263,574	100	-	0	11,263,574	8.97
Total	13,875,244	11.05	34,109,923	27.15	47,985,167	38.20	77,630,267	61.80	125,615,434	100

Note: Costs for the Finance Coordinator are included in the information technology area.

Source: Compiled by TKW

Illustration 9

As the above data indicates, administrative and indirect (overhead) costs are almost one-third of total DMV expenditures. We identified no standards or valid comparative criteria for evaluating these costs. Still, indirect (overhead) expenditures in the program administration and information technologies areas appear to be high. According to ODOT management, the high information technology expenditures were incurred as part of the deployment of a new

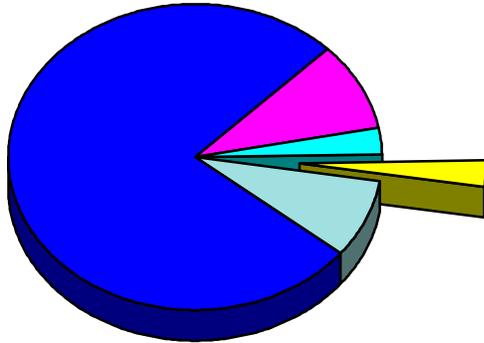
information processing system during the 1995-97 biennium. We noted that because DMV provides face-to-face customer service at 65 locations throughout the state, its indirect (overhead) costs, especially facility-related costs, would be expected to be greater than in more centralized organizations. However, due to the lack of a basis for comparison, a detailed analysis of costs, beyond the scope of this audit, is needed to assess the reasonableness and economy of DMV expenditures.

DMV has been considering three major cost components either as administrative or indirect (overhead) costs: license plates, photo identification and postage. We considered these to be direct costs. DMV should include these amounts in a unit that is classified as providing direct services.

RECOMMENDATION #3

We recommend the Driver and Motor Vehicles Branch include costs applicable to license plates, photo identification, and postage in a unit classified as providing direct services.

MOTOR CARRIER TRANSPORTATION



OVERVIEW

The mission of the Motor Carrier Transportation Branch (MCTB) is to promote a safe, efficient, and responsible commercial transportation industry. MCTB was part of the Oregon Public Utility Commission until its transfer to ODOT in early 1996². Its staff and remaining 1997 biennium budget appropriations were spread among ODOT branches and sections during the 1997 biennium. MCTB was granted its own appropriation for the 1999 biennium.

In the 1995-97 biennium, MCTB was structured into three branches: Salem Motor Carrier Services; Field Motor Carrier Services; and Investigations, Safety, and Federal Programs. Its 315 FTE register commercial vehicles, collect the commercial vehicle weight-mile tax, issue over-dimension trip permits, enforce size and weight regulations, regulate rates for the transportation of passengers and household goods in Oregon, operate a commercial motor carrier safety program, and provide information to commercial carriers.

SALEM MOTOR CARRIER SERVICES

Salem Motor Carrier Services registers carriers, collects tax payments, responds to compliance and paperwork questions, and issues permits to over-dimension carriers.

FIELD MOTOR CARRIER SERVICES

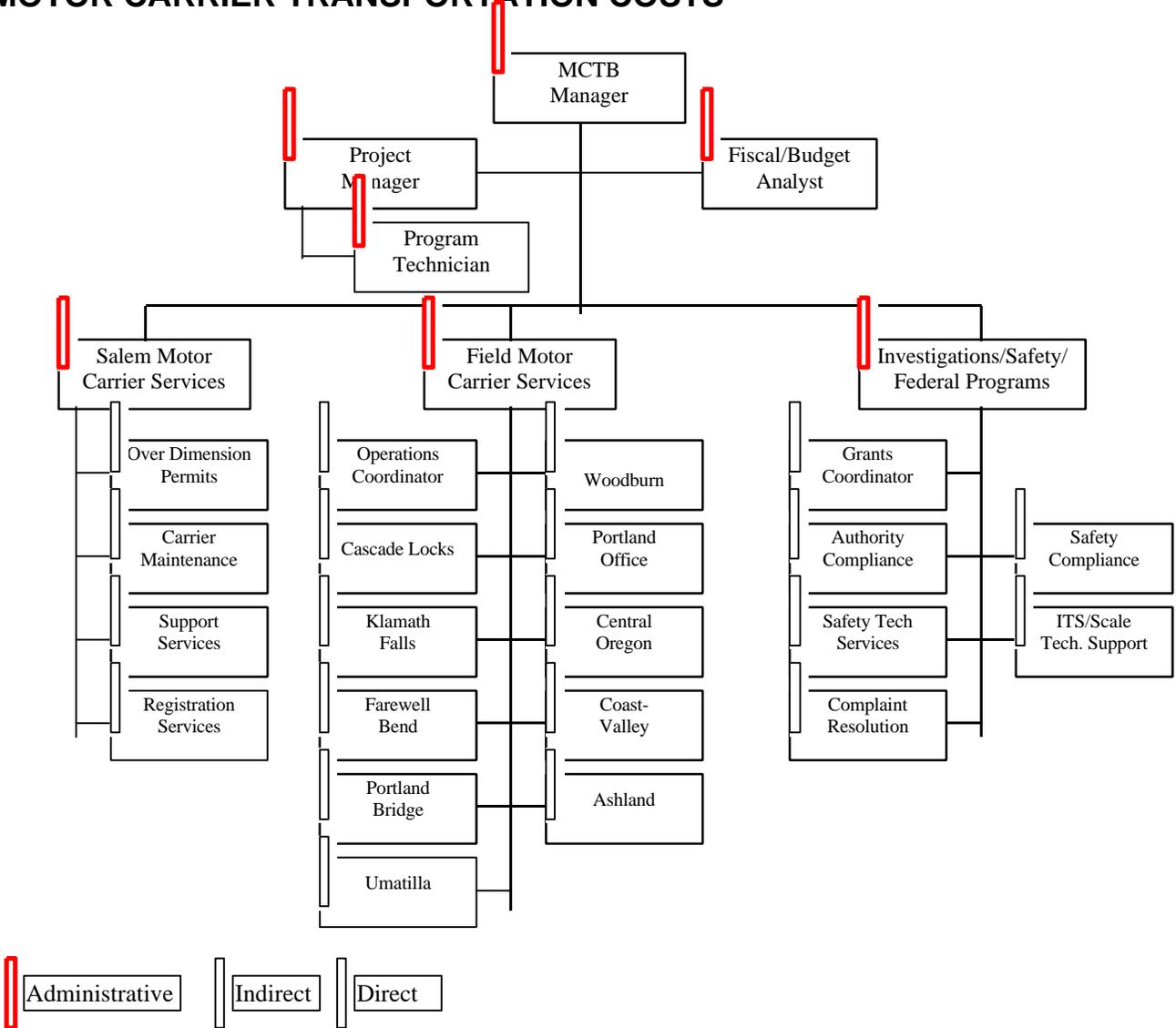
Field Motor Carrier Services is composed of fourteen field offices and six ports-of-entry throughout Oregon and performs similar functions as Salem Motor Carrier Services.

INVESTIGATIONS, SAFETY, AND FEDERAL PROGRAMS

The Investigations, Safety, and Federal Programs area investigates carriers that fail to register or pay taxes, enforces federal and state carrier safety regulations, trains department and law enforcement personnel how to perform carrier inspections, and processes data obtained from carrier inspections.

² Senate Bill 1149 (Chapter 733 of the 1995 Oregon Laws) provided for the transfer.

MOTOR CARRIER TRANSPORTATION COSTS



Expenditures incurred within the Motor Carrier Transportation Branch are identified and categorized in the table that follows:

**Motor Carrier Transportation Expenditures
1995-97 Biennium**

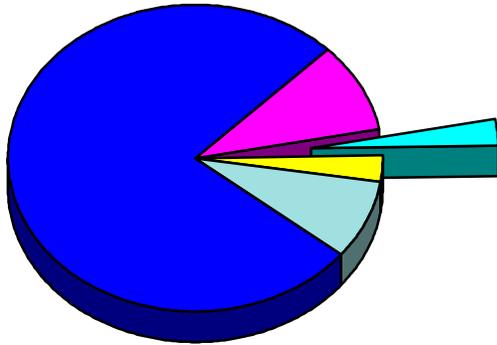
	Admin. \$	%	Indirect (Overhead) \$	%	Subtotal \$	%	Direct \$	%	Total \$	% of Total
Branch Manager	1,950,226	100	-	0.00	1,950,226	100	-	0.0	1,950,226	3.92
Salem Motor Carrier	-	0.0	1,232,128	17.30	1,232,128	17.30	5,888,830	82.70	7,120,958	14.32
Field Motor Carrier	566,488	3.49	1,229,174	7.57	1,795,662	11.06	14,447,340	88.95	16,243,002	32.66
Investigation, S afety, & Fed. Programs	-	0.0	2,523,199	17.40	2,523,199	17.40	11,975,482	82.60	14,498,681	29.15
Branch Expenditures	2,516,714	6.32	4,984,501	12.52	7,501,215	18.84	32,311,652	81.16	39,812,867	80.04
Central Admin. Assessment	8,957,285	90.25	968,219	9.75	9,925,504	100	-	0	9,925,504	19.96
Total	11,473,999	23.07	5,952,720	11.97	17,426,719	35.04	32,311,652	64.96	49,738,371	100

Source: Compiled by TKW

Illustration 10

We identified no standards or formal criteria against which to compare these administrative and indirect (overhead) costs. However, compared to other ODOT branches and organizational units, these numbers appear reasonable.

TRANSPORTATION DEVELOPMENT



OVERVIEW

The Transportation Development Branch (TDB) is responsible for developing many of the state's long-range plans, policies, and implementation activities in support of a balanced, interconnected transportation system. This branch also provides transportation information to state and local decision makers.

In the 1995-97 biennium, the TDB was made up of nine program areas:

ADMINISTRATIVE SUPPORT SERVICES SECTION

The Administrative Support Services Section was headed by one manager who supervises nine key contacts and three assistants. Each key contact was assigned one program area within TDB to provide assistance as needed.

AERONAUTICS SECTION

Aeronautics owns and operates 32 state-owned airports throughout Oregon. These airports are primarily used by small airplane operators and allow emergency crew (e.g.: firefighters) landings in remote areas. Staff members inspect and license approximately 100 public and 300 private airports. The

section also registers pilots, aircraft and aircraft dealers, and performs a variety of planning and coordinating services concerning air transportation.

The section receives its revenue from aviation fuel taxes and user fees.

PLANNING SECTION

The Planning section guides short and long-range planning for Oregon's transportation system. Projects include the Oregon Transportation Plan and the Statewide Transportation Improvement Program.

POLICY AND RESEARCH SECTION

The Policy and Research Section consists of two units:

- A Policy Unit assists in the development of policies that are requested by the Oregon Public Utilities Commission and the Governor.
- A Research Unit studies materials used by ODOT and conducts surveys that affect the public regarding transportation. This group often contracts to state universities to collect information and, once received, analyzes the data and reports findings.

PUBLIC TRANSIT SECTION

The Public Transit Section focuses on how the elderly and disabled are transported. This group distributes various grant money for Public Transit.

QUALITY COMMUNITIES/TRANSPORTATION GROWTH MANAGEMENT PROGRAM

Created by the Governor, the Quality Communities/Transportation Growth Management Program assures state agencies and local governments work together to create quality communities.

RAIL SECTION

The newest area within the TDB, the Rail Section joined ODOT in 1997. This section is responsible for inspections of railroad tracks, crossings, and railroad stations in regard to passenger and railroad employee safety. In addition, it evaluates with policy issues involving the railroad industry.

TRANSPORTATION DATA SECTION

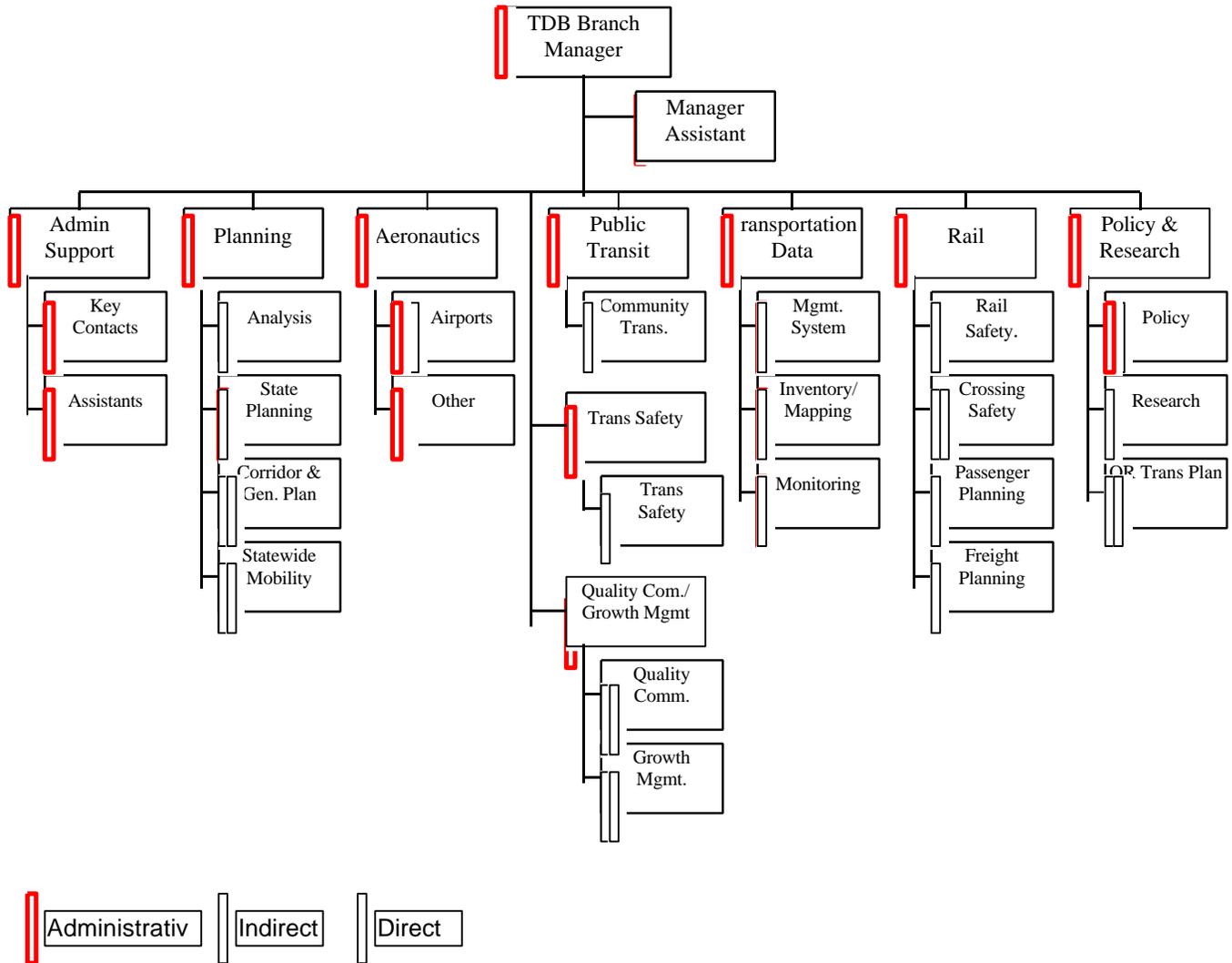
The Transportation Data Section creates all maps used by ODOT. The section also maintains video records of the condition of all state highways in Oregon, collects data and statistics regarding transportation issues, compiles data on airport use, and analyzes information obtained from accident report forms.

TRANSPORTATION SAFETY SECTION

Transportation Safety is responsible for motorist behavioral safety issues throughout Oregon. The section addresses issues such as drinking and driving, child safety belts, bicycle safety, driver education, and motorcycle safety.

TRANSPORTATION DEVELOPMENT COSTS

The majority of funding for the Transportation Development branch comes from federal grant money and state matching funds. The only two sections that do not rely heavily on these sources are the Rail and Aeronautics sections. The Rail section also receives money from railroad companies, and inspection contracts.



The TDB's varied responsibilities, and the nature of the work being performed, did not allow for a straightforward allocation of costs into direct and indirect (overhead) classifications. Nor was it always possible to classify of costs along organizational lines. In addition, ODOT's financial accounting system was not used in such a manner as to provide consistent information on how time was being used. We considered direct services provided by the TDB to include activities to develop planning documents that are used for decision making by ODOT and Oregon local governments. Most other aspects of TDB operations such as information processing, traffic monitoring, mapping, and general analysis, were considered to be indirect (overhead) in nature.

Transportation Development Expenditures 1995-97 Biennium

	Admin. \$	%	Indirect (Overhead) \$	%	Subtotal \$	%	Direct \$	%	Total \$	% of Total
Branch Manager	820,423	100	-	0.0	820,423	100	-	0.0	820,423	2.32
Admin. Support	415,892	100	-	0.0	415,892	100	-	0.0	415,892	1.18
Aeronautics	487,852	6.66	5,175,482	70.60	5,663,334	77.26	1,667,057	22.74	7,330,391	20.75
Transportation Data	1,374,973	23.59	4,454,864	76.41	5,829,837	100	-	0.0	5,829,837	16.50
Public Transit	466,072	34.27	894,036	65.73	1,360,108	100	-	0.0	1,360,108	3.85
Planning Section	504,054	7.58	1,425,329	21.42	1,929,383	29.00	4,723,357	71.00	6,652,740	18.83
Policy & Research	257,143	7.37	1,605,678	46.01	1,862,821	53.37	1,627,259	46.63	3,490,080	9.88
Quality Com./ Trans. Growth Management	-	0.00	1,331,972	33.02	1,331,972	33.02	2,702,174	66.98	4,034,146	11.42
Transportation Safety	335,873	13.13	2,222,268	86.87	2,558,141	100	-	0.0	2,558,141	7.24
Rail Section	-	0.00	1,011,932	40.78	1,011,932	40.78	1,469,647	59.22	2,481,579	7.03
Branch Expenditures	4,662,282	13.33	18,121,561	51.82	22,783,843	65.15	12,189,494	34.85	34,973,337	99.01
Central Admin. Assessment	350,742	100	-	0	350,742	100	-	0	350,742	.99
Total	5,013,024	14.19	18,121,561	51.30	23,134,585	65.49	12,189,494	34.51	35,324,079	100

Source: Compiled by TKW

Illustration 11

We identified no standards or valid comparative criteria to assess TDB expenses. Therefore, we concluded that detailed cost analysis, beyond the scope of this audit, is needed to draw conclusions on the reasonableness and economy of TDB operations.

The TDB is currently undergoing reorganization. The Administrative Support Services section will soon “charge out” its key employees to each of the program areas. These employees will continue to report to the Administrative Support Services Supervisor but will be organizationally located in each section.

RECOMMENDATION #4

To improve information on TDB operations, we recommend the Transportation Development Branch:

- Assign administrative classifications to appropriate units within the branch.
- Assign specific responsible unit codes to each organizational unit to facilitate the classification of administrative and indirect (overhead) costs.
- Identify direct services and products and separately record expenditures for those activities.

NON-LIMITED PROGRAMS

OVERVIEW

During the 1997 biennium, ODOT recorded expenditures totaling \$41,497,173 to the non-limited appropriation. The non-limited appropriation provides for certain service and supply expenditures for services performed for other ODOT units or externally for entities such as cities, counties, and construction contractors. Examples of non-limited program services include the inspection and testing of project construction materials, storeroom services, testing of traffic signals, the manufacture of traffic signs, and fleet-related services (acquiring, maintaining and disposing of ODOT's fleet vehicles, and purchasing fuel).

NON-LIMITED COSTS

Based on our understanding of non-limited unit activities and functions, we categorized expenditures among administrative, indirect (overhead), and direct categories, as follows:

Admin. \$	%	Indirect (Overhead) \$	%	Subtotal \$	%	Direct \$	%	Total \$
1,141,205	2.75	12,766,750	30.77	13,907,955	33.52	27,589,218	66.48	\$41,497,173

Source: Compiled by TKW

Illustration 12

Non-limited units charge other ODOT units and external entities for services rendered using hourly or per task charge rates. Charge rates are pre-calculated to combine direct personnel and materials costs as well as administrative and indirect (overhead) costs. The intent is for non-limited units to bill out their services using charge rates that recover the entire cost of providing the service. In theory, non-limited unit expenditures should exactly match billings for a period. However, due to the use of pre-calculated

charge rates, variances do exist and are taken into account when calculating future charge rates. Per ODOT reports, non-limited unit billings for services provided internally to other ODOT units totaled \$36,186,775 during the 1995-1997 biennium.

**Non-Limited Unit Services to Other ODOT Branches
1995-97 Biennium**

	Admin. \$	%	Indirect (Overhead) \$	%	Subtotal \$	%	Direct \$	%	Total \$	% of Total
Central Admin.	127,436	2.67	1,436,561	30.08	1,563,997	32.75	3,212,475	67.26	4,776,472	13.20
TSO	814,461	2.77	9,093,409	30.95	9,907,870	33.72	19,472,684	66.28	29,380,554	81.19
TSO/Tech. Services	35,591	2.76	397,827	30.84	433,418	33.60	856,423	66.40	1,289,841	3.56
DMV	4,965	2.71	55,730	30.45	60,695	33.16	122,308	66.83	183,003	.51
MCTB	12,325	2.78	137,450	31.06	149,775	33.84	292,820	66.16	442,595	1.22
TDB	2,967	2.60	33,683	29.47	36,650	32.07	77,660	67.94	114,310	.32
Total	997,745	2.76	11,154,660	30.82	12,152,405	33.58	24,034,370	66.42	36,186,775	100

TSO = Transportation System Operations Branch (Technical Services is part of TSO)
DMV = Driver and Motor Vehicle Services Branch
MCTB = Motor Carrier Transportation Branch
TDB = Transportation Development Branch

Source: Compiled by TKW

Illustration 13

ODOT units that purchase services from non-limited units account for billings as direct expenditures. This method is consistent with the method used by ODOT to record purchases from external entities, such as suppliers and contractors. However, it does not accurately depict ODOT's own costs. Because of ODOT's subsequent recording of non-limited services as direct costs, administrative and indirect (overhead) costs within billings are converted to direct costs. We determined that non-limited unit administrative and indirect (overhead) costs of \$997,745 and \$11,154,660, respectively, were recorded as direct costs for internal non-limited transactions during the 1997 biennium.

We were unable to identify any standards or valid comparative criteria to assess the reasonableness of non-limited unit expenses. Detailed cost analysis, beyond the scope of this audit, is necessary to draw conclusions regarding the economy of these operations.

AUDIT RESPONSE



Oregon

John A. Kitzhaber, M.D., Governor

Department of Transportation
Office of the Director
135 Transportation Bldg.
Salem, OR 97310
(503) 986-3200

August 27, 1998

File Code:

Mr. John Lattimer
State Auditor
Secretary of State Audit Division
255 Capitol Street NE, Suite 500
Salem, Oregon 97310

Dear Mr. Lattimer:

Thank you for this examination of ODOT's Administrative and Indirect Costs. It is significant that your calculation of our administrative costs at 5.6% is very close to the percentage that we calculated for the 1995-97 biennium. I am pleased that you have concluded this rate is reasonable when compared with other jurisdictions you have recently examined.

I concur with your implied suggestion that we use the indirect rate of 15.8% (those direct costs not allocated to specific projects) as a management tool to improve cost consciousness and accountability throughout ODOT. The audit results validate the direction the department is taking to account for the full cost of ODOT's products and services.

I have reviewed the recommendations in the report and my responses are as follows:

Recommendation #1:

To help simplify the classification, recording, and evaluation of costs, we recommend that ODOT:

- Assign TEAMS "Responsible Unit" codes based on the branch organization chart;
- Assign to responsible units a cost classification (administrative, direct, and indirect) that most accurately describes the work.
- Consistently record time and costs to the correct responsible unit.
- Update TEAMS coding when organizational changes are made.

Response to recommendation #1:

ODOT agrees in concept that expenditures need to be accurately classified, as direct, indirect, or administrative. We believe that the "Responsible Unit" codes need to be used with other codes to accurately classify expenditures.

All expenditures are recorded in ODOT's accounting system at the Expenditure Account (EA) level. Each EA has many fields associated with it. Among the fields are EA type, EA status, Activity, and Responsible Unit. EA type and status are editable fields. In other words by using type and status the system can control the types of expenditures (by either object detail or activity) that can be charged to a specific EA. We feel that the use of EA type and status in conjunction with activity and responsible unit will provide more accurate classification of costs.

August 27, 1998
Mr. John Lattimer

Recommendation # 2:

To improve accuracy in applying costs, we recommend ODOT allocate costs for support services manager, project coordinator, and administrative support salaries to the support services branch.

Response to Recommendation # 2:

We agree with the recommendation. This will be accomplished as part of the ODOT True Product Cost Initiative.

Recommendation # 3:

We recommend the Driver and Motor Vehicles Branch include costs applicable to license plate photo identification, and postage in a unit classified as providing direct services.

Response to recommendation # 3:

We agree that these costs should be classified as direct. Financial Services Branch will work with DMV to identify the best use of the accounting structure to accomplish the proper classification.

Recommendation # 4:

To improve information on TDB operations, we recommend the Transportation Development Branch:

- Assign administrative costs to appropriate units within the Branch;
- Assign specific responsible unit codes to each organizational unit to facilitate the classification of administrative and indirect (overhead) costs;
- Identify direct services and products and separately record expenditures for those activities

Response to Recommendation # 4:

We agree that the expenditures must be properly classified. Our first step will be to identify the TDB products and services. We will then apply the methodology referred to in our response to recommendation #1 by changing the accounting structure to accurately account for the costs of those products and services.

We expect to move quickly on the implementation of these recommendations.

Sincerely,

Grace Crunican
Director

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Director

Deputy Director

Deputy Director

John N. Lattimer

Catherine E. Pollino, CGFM

Sharron E. Walker, CPA, CFE

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the best possible management of public resources.



Oregon Audits Division
Public Service Building
Salem, Oregon 97310
503-986-2255 Hotline: 800-336-8218
Internet: Audits.Hotline@state.or.us
<http://www.sos.state.or.us/audits/audithp.htm>

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