

Office of the Secretary of State  
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Secretary of State

Jean Straight  
Deputy Secretary of State



Audits Division  
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February 6, 2007

Matthew Garrett, Director  
Oregon Department of Transportation  
355 Capitol St. NE, Rm. 135  
Salem, Oregon 97301-3871

Dear Mr. Garrett:

The statewide single audit that included selected financial accounts and federal awards at the Oregon Department of Transportation (department) for the year ended June 30, 2006, has been completed.

This statewide single audit work is not a comprehensive audit of the department. Instead, this audit permits us to give an opinion on the statewide financial statements contained in the State of Oregon's Comprehensive Annual Financial Report and to report on internal control and the state's compliance with laws and regulations. Regular audits of the department will continue on a periodic basis.

The following department accounts and transactions were audited to determine their fair presentation in accordance with generally accepted accounting principles in relation to the statewide financial statements.

<u>SFMA Account</u>	<u>Description</u>	<u>Audit Amount</u>
<u>Government-Wide Reporting Fund (8500)</u>		
0815	Equipment and Machinery	\$ 217,488,743
0840	State Highways	10,392,873,319
0842	Tunnels and Bridges	2,660,782,915
0850	Land	1,502,330,237
0852	Buildings and Building Improvements	131,296,802
0856	Land Improvements	51,016,327
0861	Construction in Progress	1,525,924,444
0880	Accumulated Depreciation – State Highways	6,897,578,370
0881	Accumulated Depreciation – Tunnels and Bridges	997,266,731
1276	Bonds Payable – Current	23,578,303
1505	Proceeds from Refunding Bond/COP Debt	391,775,000
1714	Bonds Payable – Noncurrent	939,491,080
3018	Invested in Capital Assets	8,074,958,841
4975	Agency Program Related Services	403,069,215
7476	Depreciation Expense	573,180,033

<u>SFMA Account</u>	<u>Description</u>	<u>Audit Amount</u>
Special Revenue Fund—		
<u>Public Transportation Fund (1111)</u>		
0065	Unreconciled Deposit	\$53,481,883
0070	Cash on Deposit with Treasurer	505,705,861
0122	Motor Fuels Tax	417,832,605
0123	Weight Mile Tax	265,109,576
0126	Vehicle Registration Taxes	207,580,964
0300	Federal Revenue	350,187,902
1215	Accounts Payable	77,416,705
1401	Transfer Out to Other Fund	55,488,142
1405	Transfer to Counties	174,302,576
1503	Revenue Bonds	391,775,000
3111	Regular Employees	181,914,053
3210	Public Employees Retirement Contribution	27,564,439
3221	Social Security Taxes	15,270,186
3263	Medical, Dental, Life Insurance	37,112,188
3264	Medical, Dental, Life Insurance-Agency Subsidy	8,320,538
4500	Professional Services Non-IT	127,111,971
4975	Agency Program Related Services	502,289,210

We also determined whether the department substantially complied with the federal requirements relevant to the following federal programs.

<u>CFDA Number</u>	<u>Program Name</u>	<u>Audit Amount</u>
20.205	Highway Planning and Construction Program	\$335,903,925
20.513	Capital Assistance for Elderly and Persons with Disabilities	5,908,400

Based on our audit, we identified one reportable condition needing corrective action. Our findings and recommendations are presented in the enclosed Audit Findings and Recommendations Summary accompanying this letter. The reportable condition, along with your response, will be included in our statewide audit report. Including your response with responses from other state agencies satisfies the federal requirement that management prepare a Corrective Action Plan (CAP) covering all reported audit findings. Satisfying the federal requirement in this manner, however, can only be accomplished if the response to the reportable finding includes the information specified by the federal requirement, and only if the response is received in time to be included in the audit report. The following information is required for the response.

- 1 Your agreement or disagreement with the finding. If you do not agree with the audit finding or believe corrective action is not required, include in your response an explanation and specific reasons for your position.
- 2 The corrective action planned.
- 3 The anticipated completion date.
- 4 The name of the contact person responsible for corrective action.

For the reportable condition, please respond by February 15, 2007.

Should you have any questions, please contact Margaret Wert or me at (503) 986-2255.

Sincerely,  
OREGON AUDITS DIVISION

Kelly L. Olson, CPA  
Audit Manager

KLO:MW:brk

cc: Deb Tennant, Interim Chief Financial Officer  
Marlene Hartinger, Chief Internal Audit Manager  
Lindsay Ball, Director, Department of Administrative Services

**Audit Findings and Recommendations Summary**  
**Oregon Department of Transportation**  
**State Fiscal Year 2006**

**REPORTABLE CONDITION**

**Infrastructure Accounting**

The department has had a reportable condition surrounding the department's infrastructure accounts since fiscal year 2004. During that time, and especially in the last year, the department has taken corrective action on several issues; however, there are still some areas needing attention.

The department does not have a methodology that is in compliance with governmental accounting standards specifically to:

- remove the cost of replaced roadway surfaces and associated accumulated depreciation for all types of projects capitalized (e.g., resurfacing)
- update the useful life of the state highway system

The department appropriately capitalizes the costs of all project types that extend the life of the highway system or increase the serviceability. However, the department only removes the cost of the replaced roadway surface and its associated accumulated depreciation for project types classified as Reconstruction. The department does not have a methodology in place to remove the value of the replaced roadway surface for other project types (e.g. resurfacing). Governmental accounting standards guidance state if a project increases the serviceability or extends the original useful life of the road, the project should be capitalized and the cost of the replaced roadway surface and its associated accumulated depreciation should be removed.

Governmental accounting standards state the average useful lives of assets may change as assets are capitalized or taken out of service. Currently, the department has not determined how to extend the useful life of the highway system as a result of all types of construction that occur that extend the useful life of the roads. We noted at the current rate, the state's highway system could be fully depreciated by 2014. When the department first reported the highway system in fiscal year 2002, they estimated the system was 42 percent depreciated and only had a remaining useful life of approximately 12 years. In fiscal year 2006, the state accounting system showed the cost of the highway system to be \$10.7 billion and the related accumulated depreciation to be \$6.9 billion. As a result, the accounting records currently report the department's highway system as 64 percent depreciated. Governmental accounting standards state the depreciation rate should be recalculated if the composition of the assets or the estimate of average useful lives changes significantly. Governmental accounting standards guidance state the estimated useful lives assigned to capital assets should be reconsidered if the assets are significant. Assets still in use should not be reported as fully depreciated.

**We recommend** the department develop a methodology to remove the cost and associated mileage of the replaced roadway surface and its associated accumulated depreciation for all project types.

**We recommend** the department develop a methodology to update the useful life of the highway system as a result of ongoing road construction.

**We recommend** the department re-evaluate the appropriateness of the depreciation percentage originally recorded for infrastructure in 2002 and determine if a prior period adjustment is appropriate.

**We recommend** the department develop a methodology to monitor the depreciation rate of the highway system to ensure it does not become fully depreciated and more appropriately reflects the value of the asset.