Office of the Secretary of State

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February 5, 2009

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

Dear Mr. Garrett:

We have completed audit work of selected financial accounts at the Oregon Department of Transportation (department) for the year ended June 30, 2008.

This audit work was not a comprehensive audit of the department. Instead, the audit work performed allowed us, in part, to achieve the following objectives: (1) express an opinion on whether the financial statements contained in the State of Oregon's Comprehensive Annual Financial Report were fairly presented, in all material respects, in conformity with generally accepted accounting principles; (2) determine whether the state's internal controls provided reasonable assurance of proper accounting, financial reporting, and legal compliance of transactions; and (3) determine whether the state has complied with applicable legal requirements that may have a direct and material effect on the state's financial statements.

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

SFMA Account	Description	Audit Amount
Government-Wide Reporting Fund (8500)		
0815	Equipment and Machinery	$ 221,637,608
0840	State Highways	11,524,768,476
0842	Tunnels and Bridges	2,924,000,406
0850	Land	1,525,882,085
0852	Buildings and Building Improvements	139,129,643
0856	Land Improvements	53,148,132
0861	Construction in Progress	521,431,316
0880	Accumulated Depreciation – State Highways	7,558,379,519
0881	Accumulated Depreciation – Tunnels and Bridges	1,053,809,231
1276	Bonds Payable – Current	54,483,231
1714	Bonds Payable – Noncurrent	1,505,071,013
1503	Revenue Bonds	10,060,000
7476	Depreciation Expense	648,779,827

SFMA Account	Description	Audit Amount
Special Revenue Fund- Public Transportation Fund (1111)		
0065	Unreconciled Deposit	$ (5,836,177)
0070	Cash on Deposit with Treasurer	501,529,775
0240	Investments – Designated	113,639,000
0245	Investment Valuation Acct – Designated	(15,669)
0542	Accounts Receivable – Federal – Unbilled	82,042,402
1215	Accounts Payable	113,052,677
0122	Motor Fuels Tax	413,105,824
0123	Weight Mile Tax	238,860,075
0126	Vehicle Registration Taxes	201,245,328
0300	Federal Revenue	450,250,957
1401	Transfer Out to Other Fund	963,851,358
1405	Transfer to Counties	165,415,082
1503	Revenue Bonds	10,060,000
3111	Regular Employees	206,813,068
3210	Public Employees Retirement Contribution	26,756,292
3221	Social Security Taxes	17,335,634
3263	Medical, Dental, Life Insurance	52,282,422
4500	Professional Services Non-IT	140,973,168
4975	Agency Related Program Services	614,736,365

In planning and performing our audit of the selected financial accounts at the department as of and for the year ended June 30, 2008, in accordance with auditing standards generally accepted in the United States of America, we considered the department's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements of the State of Oregon, but not for the purpose of expressing an opinion on the effectiveness of the department's internal control. Accordingly, we do not express an opinion on the effectiveness of the department's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control. A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the following deficiencies to be significant deficiencies in internal control:

Inadequate Controls over Financial Reporting

According to the Oregon Accounting Manual, a department's internal controls must be adequate to provide reasonable assurance that transactions are accurate and properly recorded. The department did not have sufficient internal controls in place to prevent or detect the following June 30, 2008, financial reporting misstatements:

- A portion of Noncurrent Bonds Payable was not reclassified to Current Bonds Payable, resulting in each account being misstated by $9 million.
- Fiscal year 2007 accruals were not reversed in fiscal year 2008 as required by department policy, causing misstatements to Accounts Payable and Accounts Receivable in the amounts of $2.9 million and $1.1 million, respectively.

  Further, these accruals affected the Increase in the Fair Value of Investments account in fiscal year 2008 and, as a result, it was misstated by $1.7 million.
- A fiscal year 2009 transaction was inappropriately recorded in fiscal year 2008, resulting in a misstatement to Transfers to Counties of $750,000.
- A $1million investment purchase and the associated $16,260 investment discount were recorded in the opposite accounts, misstating each account by $1,016,260.

During fiscal year 2008, the department had fewer staff available for preparing year-end transactions and conducting independent reviews, which may have contributed to the number of errors we identified.

We recommend department management ensure adequate controls are in place to prevent and/or detect financial reporting errors.

Jurisdictional Transfers Not Adequately Supported

The Oregon Accounting Manual states that all transactions must be supported by appropriate documentation. We noted the department did not obtain the necessary documentation to ensure jurisdictional transfers were properly recorded.

A jurisdictional transfer occurs when the department transfers the jurisdiction[1] of a segment of the state highway system from the state to a city or county. The transfer requires a formal agreement between the state and all affected local governments. The department is then responsible for calculating the value of the transfer and removing it from the accounting records. While preparing year-end accounting transactions for jurisdictional transfers, the department did

[1] Jurisdiction refers to the territory over which authority is exercised.

not obtain adequate supporting documentation. As a result, the department removed the value for a jurisdictional transfer that was not yet complete. In another instance, a jurisdictional transfer had occurred; however, the department did not record the transfer. As a result of these two errors, the state highway system account was understated by $25 million.

We recommend department management ensure transactions relating to the state highway system are adequately supported.

Prior Audit Finding

For fiscal year 2006, we reported a significant deficiency to the department in a letter dated February 6, 2007, that related to the department's infrastructure accounting. This finding can also be found in the Statewide Single Audit Report for the fiscal year ended June 30, 2006; see Secretary of State Audit Report number 2007-06, finding number 06-7. During the current fiscal year, the department continued to make progress in correcting this finding. This finding will be reported in the Statewide Single Audit Report for the fiscal year ended June 30, 2008, with a status of partial corrective action taken.

The significant deficiencies, along with your responses, will be included in our Statewide Single Audit Report for the fiscal year ended June 30, 2008. Including your responses 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 each significant deficiency includes the information specified by the federal requirement, and only if the responses are received in time to be included in the audit report. The following information is required for each response:

(1) Your agreement or disagreement with the finding. If you do not agree with an 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(s) of the contact person(s) responsible for corrective action.

Please respond by February 23, 2009.

This communication is intended solely for the information and use of management, others within the department, and the Oregon Transportation Commission and is not intended to be and should not be used by anyone other than the specified parties.

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

Sincerely,
OREGON AUDITS DIVISION

V. Dale Bond, CPA, CISA, CFE
Audit Manager

cc: Gail Achterman, Chair, Oregon Transportation Commission
Lorna Youngs, Deputy Director, Central Services
Les Brodie, Chief Financial Officer
Marlene Hartinger, Chief Auditor
Scott Harra, Director, Department of Administrative Services