STATE OF ILLINOIS
OFFICE OF THE
AUDITOR GENERAL
William G. Holland, Auditor General

SUMMARY REPORT DIGEST

DEPARTMENT OF TRANSPORTATION

FINANCIAL AUDIT
For the Year Ended: June 30, 2013

Release Date: January 23, 2014

Summary of Findings:

Total this audit:	**6**
Total last audit:	**5**
Repeated from last audit:	**3**

SYNOPSIS

- The Department's year-end financial reporting process contained numerous inaccuracies.
- The Department maintained inaccurate commodities inventory records for the year ended June 30, 2013.
- The Department did not accurately report capital assets to the Illinois Office of the Comptroller for fiscal year 2013.
- Weaknesses were noted in the Department's documentation of its accounts payable at June 30, 2013.

{Financial data is summarized on the reverse page.}

DEPARTMENT OF TRANSPORTATION
FINANCIAL AUDIT
For the Year Ended June 30, 2013

STATEMENT OF ACTIVITIES INFORMATION - GOVERNMENTAL ACTIVITIES (expressed in thousands)		Fiscal Year 2013	Fiscal Year 2012
PROGRAM REVENUES			
Charges for Services		$ 54,989	$ 38,033
Operating Grants		363,575	382,279
Capital Grants		1,321,437	1,530,191
Total Revenues		1,740,001	1,950,503
EXPENSES			
Total Expenses		5,207,305	4,738,662
NET (EXPENSES) REVENUES		**(3,467,304)**	**(2,788,159)**
Total General Revenues and Transfers		3,668,427	3,518,173
CHANGE IN NET POSITION		**201,123**	**730,014**
NET POSITION, July 1,	*	18,223,105	17,504,590
ENDING NET POSITION, JUNE 30		**$ 18,424,228**	**$ 18,234,604**

*as restated

STATEMENT OF NET POSITION- GOVERNMENTAL ACTIVITIES (expressed in thousands)	Fiscal Year 2013	Fiscal Year 2012
Cash Equity with State Treasurer	$ 171,212	$ 160,732
Cash and Cash Equivalents	2,519	2,418
Receivables, Net	317,315	401,091
Inventories	54,896	57,804
Capital Assets, Net	17,767,859	17,513,771
Other Assets	1,504,162	1,526,847
Total Assets	**19,817,963**	**19,662,663**
Accounts Payable	391,620	444,662
Long Term Obligations	74,962	76,003
Other Liabilities	927,153	907,394
Total Liabilities	**1,393,735**	**1,428,059**
NET POSITION		
Net Investment in capital assets	17,750,334	17,494,412
Restricted for Transporation Programs	46,586	58,258
Restricted for Debt Service	13,134	2,400
Unrestricted	614,174	679,534
Total Net Position	**$ 18,424,228**	**$ 18,234,604**

AGENCY SECRETARY
During Examination Period: Ann Schneider
Currently: Ann Schneider

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

NEED TO IMPROVE YEAR END FINANCIAL REPORTING

Financial reporting was inaccurate

The Department's year-end financial reporting in accordance with generally accepted accounting principles (GAAP) to the Illinois Office of the Comptroller (Comptroller) contained numerous inaccuracies. These problems, if not detected and corrected, could materially misstate the Department's financial statements and negatively impact the Statewide financial statements prepared by the Comptroller.

Four financial drafts were provided before final version

For instance, the draft financial statements submitted to the auditors contained several errors which required corrections. The Department provided us with 4 drafts of its financial statements, with significant modifications, before providing its final version that we utilized in the audit report on November 19, 2013.

Department management cited the lack of a general ledger system and turnover in the past as contributing factors to inaccurate financial reporting. (Finding 1, pages 51-53) **This finding was first reported in 2009.**

We recommended the Department implement procedures and cross-training measures to ensure GAAP Reporting Packages are prepared in an accurate and complete manner. This should include allocating sufficient staff resources and the implementation of formal procedures to ensure GAAP financial information is prepared and submitted to the Comptroller in an accurate manner, and all supporting documentation is maintained in a contemporaneous manner.

Department agrees with auditors

Department officials agreed with the recommendation and stated during fiscal year 2013, additional GAAP staff was added to the Fiscal Operations Unit. None of the new staff had previous experience with the Department but did have GAAP experience. The complexity of the GAAP process within the Department and the numerous systems required to produce the reporting for the Comptroller's Office produced a longer than anticipated learning curve for the new staff. Department officials further stated several new procedures and changes to existing procedures were developed and documented during this audit using the consulting firm that has assisted with GAAP for several years. In addition, Department officials stated they have completed the identification of potential changes in organizational structure, reporting relationships and technology solutions intended to ensure the development of Statewide policies and procedures. Department officials feel that policy administration changes are necessary to improve upon and/or reduce the probability of future compliance issues. During the fall of calendar year 2013, the Department started the implementation of these administrative changes. (For the previous Department response, see Digest Footnote #1)

NEED TO IMPROVE COMMODITIES INVENTORY RECORDS

The Department maintained inaccurate commodities inventory records for the year ended June 30, 2013.

Discrepancies in 35% of inventory items counted

During our physical inventory counts, we counted 267 inventory items and noted discrepancies between audit test counts and Department inventory quantities for 94 (35%) items. The errors resulted in a net understatement of the year end inventory balance of $62,898 which, when extrapolated over the entire inventory population, resulted in an estimated understatement of $408,207. Through analytical review procedures applied to the final inventory listings, we identified 12 items with unusual final inventory cost variances from fiscal year 2012 to fiscal year 2013. Our testing of these items revealed a net quantity understatement of $42,825 in addition to the extrapolated misstatement noted above.

Inventory understated by $451,032

Combined, inventory quantity errors resulted in a net understatement of inventory of $451,032 at June 30, 2013.

Pricing errors in 80% of inventory tested

In our inventory price testing, we sampled 15 inventory items, including salt at all Districts, which accounted for $25,636,645 (47%) of the reported inventory value at June 30, 2013. Of the items tested, 12 (80%) were found to have inaccurate costs resulting in a net understatement of the year end inventory balance of $147,882 which, when extrapolated over the entire inventory population, resulted in an estimated overstatement of $233,800. Through analytical review procedures applied to the final inventory listings, we identified an additional 8 items with unusual pricing variances from fiscal year 2012 to fiscal year 2013. Our testing of these items revealed a net understatement of $455,823 in addition to the extrapolated misstatement noted above. Through analytical review procedures applied to the final inventory listings, we identified 12 items with unusual final inventory cost variances from fiscal year 2012 to fiscal year 2013. Our testing of these items revealed a net pricing overstatement of $598,305 in addition to the extrapolated misstatement noted above.

Inventory overstated by $376,282

Combined, inventory pricing errors resulted in a net overstatement of inventory of $376,282 at June 30, 2013.

Sign prices were inconsistent

During our inventory observation we noted inconsistencies in the method Districts were using to value sign inventory. It appeared that sign prices were inconsistent between district inventory sheets. The net effect of any misstatement could not be determined based upon information provided by the Department.

Gas, oil, and lubricants overstated by $20,766

Through our testing of the Department's Inventory Analysis Form, we identified gasoline, oil, and lubricants had been overstated by $20,766.

In total, audit procedures applied to inventory as reported by the Department identified a likely understatement of inventory of $53,984 at June 30, 2013. The Department did not adjust its financial statements for these errors as they were considered immaterial to the Department's overall financial statements. (Finding 2, pages 54-56) **This finding was first reported in 1994.**

We recommended the Department strongly emphasize the importance of maintaining accurate inventory quantity and cost records throughout the year. Additionally, the Department should perform periodic physical inventory counts throughout the year and reconcile those to Department records. We further recommended the Department implement a more thorough review at year-end to compare costs assigned per inventory listings to the most recent inventory amounts to ensure accurate unit costs, including signs. Finally, training and ongoing education should be provided to all employees involved in the inventory process in order to accentuate the importance of their involvement in this annual exercise.

Department agrees with auditors

Department officials agreed with the recommendation and stated they will continue to make improvements to the year-end commodity inventory process to produce an accurate count and pricing of our commodity inventory. As a part of the administrative changes, the Office of Finance and Administration will be taking a leadership role in the accountability for the commodity inventory process. The Department will work to define and document a periodic monitoring process to count and price a sample of inventory items. (For the previous Department response, see Digest Footnote #2)

NEED TO IMPROVE REPORTING OF CAPITAL ASSETS

The Department did not accurately report capital assets to the Illinois Office of the Comptroller for fiscal year 2013.

Some of the errors and weaknesses we noted in the Department's capital asset process follow:

Failed to transfer three buildings from Construction in Progress

Amount duplicated totaled $1.4 million

- At June 30, 2012, the Department did not transfer three buildings from Construction in Progress to Buildings within its capital asset records. The buildings had been placed in service during fiscal year 2012. In fiscal year 2013, the buildings were added to the reported amount of Buildings according to their placed in service dates. However, the buildings were not deleted from Construction in Progress balance on the original Agency Report of State Property (Form C-15) filed in fiscal year 2013 nor from the original capital asset records provided to us during the audit fieldwork. During the audit fieldwork, the amount duplicated, $1.4 million, was corrected by the Department and depreciation expense was adjusted accordingly.

Infrastructure additions were improperly capitalized

- The Department improperly capitalized repair and maintenance type expenditures in infrastructure additions. In the prior year, the Department made similar errors resulting in capital assets being overstated due to the capitalization of these costs as infrastructure additions. Through our testing of infrastructure additions, and with the assistance of the Department, we identified $37.5 million of fiscal year 2012 and $67.5 million of fiscal year 2013 infrastructure additions were improperly capitalized as the costs related to repair and maintenance type contracts. The Department corrected the errors by reducing infrastructure additions in fiscal year 2013 and revising its capital asset records and financial statements accordingly at June 30, 2013.

Failed to capitalize $2.1 million in infrastructure

- In our testing of repair and maintenance type expenditures, we noted the Department initially failed to capitalize costs related to significant sewage system upgrades at two rest areas. The Department has stated that rest areas are considered to be part of the Statewide infrastructure network and costs should be capitalized in accordance with the policies for infrastructure. The amounts initially not capitalized were $1.4 million for fiscal year 2012 and $650 thousand for fiscal year 2013. The total amount, $2.1 million, was corrected by the Department by increasing infrastructure additions in fiscal year 2013 within its capital asset records and its financial statements for the year ended June 30, 2013.

$1.5 million in equipment errors

- During our testing of capital assets, we noted certain assets were duplicated when performing equipment reconciliations in fiscal year 2013, and other assets were omitted. The total net amount of errors discovered, $1.5 million of overstated equipment, was corrected by the Department in its capital asset records and financial statements for the year ended June 30, 2013.

Errors in allocating accounts payable from future years' appropriations to capital outlay

- In fiscal year 2012, the Department developed a methodology to allocate accounts payable from future years' appropriations to capital outlays and capitalize those amounts. In allocating these amounts in fiscal year 2013, the Department's calculations included errors that resulted in initial capital outlay being overstated. The initial capital outlay calculation was also overstated due to the infrastructure addition errors described previously. As part of the Department's correction efforts performed during the audit fieldwork, the Department corrected the errors noted related to the amounts of accounts payable from future years' appropriations allocated to capital outlays. The corrections were included in the final, revised financial statements provided to us for the year ended June 30, 2013.

- In our prior year testing of land additions, we noted the Department improperly capitalized certain costs which were not related to the acquisition of land, resulting in an overstatement of land. During our testing of land additions in fiscal year 2013, it was noted that the prior year overstatements had not yet been corrected. During the audit fieldwork, the Department corrected the errors by reducing land additions in its capital asset records and financial statements for the year ended June 30, 2013 in fiscal year 2013 by $4.8 million.

Land was overstated by $4.8 million

- During our testing of software expenditures, the Department informed us of two internally-generated software projects over $1 million that should be capitalized. The estimated amount of these project costs were $2.8 million through June 30, 2013; however, the Department was still evaluating the applicability of the technical guidance to this situation at the time of fieldwork. Costs that should be capitalized were not determinable by the Department. The total population of potential misstatements for this weakness was not considered material by the Department and was not corrected as of June 30, 2013. (Finding 3, pages 57-60) **This finding was first reported in 2009.**

Internally-generated software projects were not capitalized

We recommended the Department devote sufficient resources to its financial accounting function such that the capital asset information is properly recorded and accounted for to permit the preparation of reliable financial information and reports to the Office of the Comptroller.

Department agrees with auditors

Department officials agreed with the recommendation and stated during FY13, additional GAAP staff was added to the Fiscal Operations Unit. None of the new staff had previous experience with the Department but did have GAAP experience. The complexity of the GAAP process within the Department and the numerous systems required to produce the annual capital asset reporting for the Comptroller's Office produced a longer than anticipated learning curve for the new staff. The accuracy of capital asset reporting should improve due to the valuable experience of lessons learned from FY13. (For the previous Department response, see Digest Footnote #3)

NEED TO IMPROVE DOCUMENTATION OF ACCOUNTS PAYABLE

Weaknesses were noted in the Department's documentation of its accounts payable balance at June 30, 2013.

The Department could not specifically demonstrate conclusions reached and included within its accounts payable model. In addition, the Department could not expressly demonstrate the accounts payable methodology considered an estimate for liabilities attributable beyond June 30, 2014.

No assessment of the reasonableness of accounts payable estimates

Within the Department's accounts payable estimation model, the Department referenced management conclusions, in which it stated it discussed the expectation of upcoming fiscal year activities, anomalies, and other events. While testing the Department's accounts payable estimation, we requested the Department provide copies of various items of supporting documentation in order for us to corroborate the conclusions reached and included within the accounts payable model. In many instances, Department personnel told us such information was reviewed and meetings occurred, but no documentation of the events were made or maintained in order to provide a complete audit trail to support the Department's estimation. Examples included:

- The spreadsheet utilized to perform the estimation calculation contained sections in which to input the various steps within the process. One of the steps allowed the Department to make an adjustment to the historic data utilized in the model for known anomalies. Rather than utilize this section, the Department hard inputted the information directly into the historic data. Because the source data was changed, it was not possible for a third party to review exactly what was changed within the estimation process.

No support for estimation process

- The estimation process also allows the Department to adjust its accounts payable estimate based on whether it believes any variance between actual, current fiscal year expenditures that occurred during July and August and the forecasted amount for that period from the model will or will not be absorbed after July and August and before the end of the fiscal year. The Department was unable to provide supporting documentation for how it arrived at the decision to adjust or keep the estimated accounts payable amount.

No detailed support for Fund 554 payables

- The Department adjusted the model for the Transportation Bond Series B Fund (Fund 0554) for known payables for work performed prior to June 30, 2013. However, the management comments in the computer model spreadsheet did not contain detailed support for the adjustment.

No supporting documentation for forecast method selected

- Part of the computer model spreadsheet involves the Department selecting a forecast method in order to arrive at forecasted total future year expenditures to estimate accounts payable. The Department was unable to provide supporting documentation as to why it decided which forecast would result in the most reasonable estimate of accounts payable.

In addition, we noted the Department could not demonstrate its accounts payable model expressly accounts for liabilities extending beyond June 30, 2014. A review of historic trends indicated a liability exists beyond one year from the Statement of Net Position relating to costs incurred at the local level, but not yet presented to the Department. We were unable to determine the Department's method for accounting for this portion of its liability, although the overall accounts payable estimate appeared reasonable in all material respects. (Finding 4, pages 61-63)

We recommended the Department document, specifically, the management comments and other considerations utilized to support the conclusions reached in its determination of its accounts payable estimate. We also recommended that modifications made to the accounts payable be maintained so that auditors can review them during the audit process. Finally, we recommended the Department expressly document within its accounts payable model how it considers the estimation for liabilities attributable 12 months beyond the date of the Statement of Net Position.

Department agrees with auditors

Department officials agreed with the recommendation and stated they had made significant enhancements to its accounts payable estimating methodology during recent years and specifically made considerable enhancements during Fiscal Year 2013. The Department stated its enhancements of its accounts payable estimating process are ongoing and continuous. To the extent possible and practical, the Department will endeavor to centralize all relevant information considered in making its accounts payable estimates within the estimates, as well as, will seek an enhanced process of centralizing information not able to be included within the estimating worksheets themselves.

OTHER FINDINGS

The remaining findings are reportedly being given attention by the Department. We will review the Department's progress toward implementation of our recommendations in our next examination.

AUDITORS' OPINION

Our auditors state the basic financial statements of the Department as of and for the year ended June 30, 2013 were fairly presented in all material respects.

WILLIAM G. HOLLAND
Auditor General

WGH:PH

AUDITORS ASSIGNED

Our special assistant auditors for this audit were Sikich, LLP.

DIGEST FOOTNOTES

#1 – NEED TO IMPROVE YEAR END FINANCIAL REPORTING

2012: The Department agreed with the recommendation and stated during FY13, the Department reorganized the Fiscal Operations Unit to include additional staff to review, revise and implement reporting processes that will ensure the timely and accurate financial reporting as required by the Office of the Comptroller. This reorganization includes the implementation of monthly processes to review and reconcile capital asset reporting to ensure accurate financial reporting.

2 - INACCURATE COMMODITIES INVENTORY RECORDS

2012: The Department agreed with the recommendation and stated they would continue to make improvements to the year-end commodity inventory process to produce an accurate count and pricing of their commodity inventory. They stated they would strongly emphasize the importance of maintaining accurate inventory quantity and cost records in planning and conducting the June 30, 2013 commodity inventory count and pricing. They further stated they would conduct a more thorough review at year-end of the commodity inventory records produced by Department personnel to ensure accurate unit costs and consistent unit of measures.

3 – INACCURATE REPORTING OF CAPITAL ASSETS

2012: The Department agreed with the recommendation and stated during FY13, the Department reorganized the Fiscal Operations Unit to include additional staff to review, revise and implement reporting processes that will ensure the timely and accurate financial reporting as required by the Office of the Comptroller. This reorganization includes the implementation of monthly processes to review and reconcile capital asset reporting to ensure accurate financial reporting.