



STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
STACEY E. PICKERING
STATE AUDITOR

March 10, 2016

Financial Audit Management Report

Melinda McGrath, Executive Director
Mississippi Department of Transportation
P.O. Box 1850
Jackson, Mississippi 39215

Dear Ms. McGrath:

Enclosed for your review is the financial audit finding for the Mississippi Department of Transportation for the Fiscal Year 2015. In this finding, the Auditor's Office recommends the Mississippi Department of Transportation:

I. Strengthen Controls to Ensure Capital Assets are Reported Timely and Accurately

Please review the recommendation and submit a plan to implement it by March 21, 2016. The enclosed finding contains more information about our recommendation.

During future engagements, we may review the finding in this management report to ensure procedures have been initiated to address this finding.

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the Mississippi Department of Transportation's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Mississippi Department of Transportation's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, this report is a matter of public record and its distribution is not limited.

I hope you find our recommendation enables the Mississippi Department of Transportation to carry out its mission more efficiently. If you have any questions or need more information, please contact me.

Sincerely,

A handwritten signature in cursive script that reads "Sallie Dier".

Sallie Dier, CPA
Director, Financial Audit and Compliance Division
Enclosures

FINANCIAL AUDIT MANAGEMENT REPORT

The Office of the State Auditor has completed its audit of selected accounts included on the financial statements of the Mississippi Department of Transportation for the year ended June 30, 2015. These financial statements are consolidated into the State of Mississippi's *Comprehensive Annual Financial Report*. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The Office of the State Auditor's staff members participating in this engagement included Donna Parmegiani, CPA, Kevin Cribs, John Newell, Justin Reulet, Alan Jarrett, Jeremy Miller, CPA, and Haley Hesdorffer.

Our procedures and tests cannot and do not provide absolute assurance that all state legal requirements have been met. In accordance with Section 7-7-211, Miss. Code Ann. (1972), the Office of the State Auditor, when deemed necessary, may conduct additional procedures and tests of transactions for this or other fiscal years to ensure compliance with legal requirements.

Internal Control over Financial Reporting

In planning and performing our audit of selected accounts included on the financial statements, we considered the Mississippi Department of Transportation's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on these accounts, but not for the purpose of expressing an opinion on the effectiveness of internal control. Accordingly, we do not express an opinion on the effectiveness of the Mississippi Department of Transportation's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, we identified certain deficiencies in internal controls that we consider to be material weaknesses.

A *deficiency in internal control* 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 and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency identified in this letter as item 15-01 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether selected accounts included on the financial statements of the Mississippi Department of Transportation are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

MATERIAL WEAKNESS

Finding Number

2015-015

Finding and Recommendation

Controls Should be Strengthened to Ensure Capital Assets are Reported Timely and Accurately

Finding:

During our review of financial reporting at the Mississippi Department of Transportation, we noted agency personnel did not prepare their GAAP packet for Capital Assets in a timely manner. The deadline for turning in GAAP packets established by the Department of Finance and Administration – Office of Financial Reporting (DFA-OFR) was November 3, 2015. However, the GAAP packet for Capital Assets was not submitted until January 12, 2016. Additional changes were made to the Capital Assets GAAP Packet by the agency as late as March 9, 2016.

Section 27-104-4, Miss. Code Ann. (1972) requires each state agency to prepare annual financial statements at such times as determined by the State Fiscal Officer. The State Fiscal Officer is required to combine the financial statements into a comprehensive annual financial report (CAFR) and provide it to the State Auditor for postauditing. The law further requires the CAFR be published within six months after the June 30 close of the fiscal year. In addition, the Government Finance Officers Association (GFOA) requires CAFRs to be submitted within six months of the government's fiscal year end. It should be noted that DFA-OFR obtained an extension for the CAFR from GFOA this year due to the implementation of the Mississippi Accountability System for Government Information and Collaboration, or MAGIC, the new accounting system used by the State.

The failure of agency personnel to prepare their GAAP packets in a timely manner resulted in the CAFR not being published in accordance with state law and hindered the efficiency of the audit of the State of Mississippi's financial statements. In addition, these delays could result in the state not being awarded a Certificate of Achievement for Excellence in Financial Reporting by GFOA. Receiving GFOA's certificate increases the likelihood the credit agencies or other stakeholders may consider the state's financial statements in a positive manner. The timeliness of the CAFR being published impacts its relevance to the various users of the CAFR.

In addition, the Single Audit Act requires the State to issue the Single Audit Report within nine months of fiscal year end, and no extensions are granted. The independent auditor's report on internal control over financial reporting and the schedule of expenditures of federal awards (SEFA) are both required to be included in the Single Audit Report and both an integral part of the financial audit of the State. The failure to timely complete the CAFR could also hinder the

timely submission of the Single Audit Report which could result in federal discretionary drawdowns being suspended.

Annually, MDOT submits the information, known as their Capital Assets GAAP Packet, along with supporting schedules to DFA-OFR. MDOT is responsible for recording and reporting all information related to their capital assets. During our review of the Capital Asset GAAP Packet at MDOT, we noted the following errors that required correction:

- Depreciation expense for infrastructure assets was not booked in the current year in the amount of \$325,161,575.
- Building and land improvement assets were incorrectly reported as infrastructure assets in the amount of \$64,652,868.
- Of the \$64,652,868 amount listed above, \$48,847,439 was reported as building and land improvements at the same time it was improperly included as infrastructure resulting in an overstatement in MDOT's capital assets.

Failure to record current year infrastructure depreciation and properly reflect capital asset additions could result in a material misstatement in Mississippi's CAFR that is reported in accordance with GAAP.

Recommendation:

We recommend the Mississippi Department of Transportation strengthen internal controls to ensure their capital assets are reported timely, accurately, and in accordance with federal and state law. Additionally, we recommend the Mississippi Department of Transportation ensure the individuals responsible for preparing and approving GAAP packets have adequate knowledge to ensure the capital asset GAAP packet is properly completed.

End of Report

Melinda L. McGrath
Executive Director

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FINANCIAL AUDIT FINDING

March 21, 2016

Stacey E. Pickering, State Auditor
Office of the State Auditor
State of Mississippi
P.O. Box 956
Jackson, MS 39205-0956

Dear Mr. Pickering:

We received the Financial Audit Management Report and the following details our response to the Audit Finding for FY 2015:

<u>Finding Number</u>	<u>Finding and Recommendation</u>
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MATERIAL WEAKNESS

2015-015	<u>Controls Should Be Strengthened to Ensure Capital Assets are Reported Timely and Accurately</u>
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- Of the \$64,652,868 amount listed above, \$48,847,439 was reported as building and land improvements at the same time it was improperly included as infrastructure resulting in an overstatement in MDOT's capital assets.

Response:

1. *MDOT did not prepare the GAAP Package for Capital Assets in a timely manner.*

MDOT does not concur with this finding. The department received all required information and MAGIC functionality from DFA on January 7, 2016 and submitted the Capital Assets GAAP packet on January 12, 2016.

In order for MDOT to timely prepare the capital assets GAAP packet, we need directives from DFA to be complete and timely. MS Code Section 27-104-4(1) sets forth not only the agency's responsibilities in GAAP preparation but also the responsibility of DFA to provide procedures and accounting systems necessary for the agency's to fulfill their responsibility:

“Each state agency shall prepare annual financial statements at such times as required by the State Fiscal Officer. The statements shall be in accordance with generally accepted accounting principles. *The State Fiscal Officer, in consultation with the State Auditor, shall prescribe rules and regulations to implement and specify the records, procedures and accounting systems necessary to carry out the provisions of this section* [emphasis added].”

Section 27 of the Mississippi Agency Accounting Policies and Procedures (MAAPP) Manual contains the regulations, procedures, and templates for GAAP reporting but has not been updated since MAGIC was implemented. DFA did not provide agencies with the new procedures and templates until the GAAP packets were delivered so there was no way for agencies to prepare or obtain training.

DFA did not provide the agencies with a complete FY 2015 GAAP packet timely. Prior to MAGIC, DFA would submit a GAAP packet to the agencies around the first of July with the trial balances for each fund, schedules and which funds and notes were

required. This year, the GAAP packet was pieced to us with minimal training until October 13, 2015, three months later than normal. Agencies were then given a two week period to complete. Due to the complexity of our GAAP packet, MDOT has always received a time extension in the past. It was unreasonable to expect MDOT to meet a November 3rd deadline.

Entering capital assets GAAP entries into MAGIC was a new process. Prior to MAGIC, DFA had always made the necessary classifications as part of their GAAP preparation. DFA did not inform MDOT of this new process until mid-October 2015 and they did not provide nor develop the accounting structure that would allow us to make our infrastructure entries until December 2015.

MDOT has been attempting to work with DFA for over two years to bring proper attention to capital assets. MDOT initiated a meeting with DFA-OFR, an MMRS MAGIC representative, and an SAP representative on March 26, 2014 to proactively develop procedures for capturing capital assets such as buildings, land, and land improvements in MAGIC. MDOT repeatedly sought guidance from DFA throughout the last two years, as we were not able to post our buildings, land, or land improvements into MAGIC. Processes regarding capital assets continued to be undefined with no engagement from DFA until entries were required for GAAP purposes. DFA finally began working with MDOT in October 2015 to determine how these assets were to be entered into MAGIC for GAAP purposes. We emailed DFA several times in November about CIP adjustments and conversions to be posted in MAGIC. At this point, DFA required us to prepare GAAP entries for capital assets in MAGIC without providing a process or training. We met with DFA twice in December regarding the posting of our FY 2014 and FY 2015 assets in MAGIC. It wasn't until December 23, 2015 that we were able to post our outstanding CIP assets in MAGIC. As of January 7, 2016, the beginning balances for capital assets were not entered in MAGIC. We were provided a paper copy of FY 2014 verified ending balances by DFA on January 6, 2016. Two new accounts for capital assets (1) OFR Capital Assets Infrastructure Under Const (Reporting) and (2) OFR Capital Assets Right of Way (Reporting) needed to be set up in MAGIC in order for us to properly make the GAAP entries.

We were not notified that the two new accounts were set up until January 7, 2016.

2. *Depreciation expense for infrastructure assets was not booked in the current year in the amount of \$325,161,575.*

Preparing entries for Capital Assets in MAGIC was a new process for both DFA and MDOT. Prior to MAGIC, DFA had always made the necessary classifications as part of their GAAP preparation. Since MDOT did not have any prior knowledge of how DFA treated capital assets after the GAAP packet was submitted, DFA provided MDOT with the entries to prepare for FY 2015. However, neither DFA nor MDOT realized depreciation expense for infrastructure assets needed a journal entry in MAGIC.

3. *Building and land improvements assets were incorrectly reported as infrastructure assets in the amount of \$64,652,868.*
4. *Of the \$64,652,868 amount listed above, \$48,847,439 was reported as building and land improvements at the same time it was improperly included as infrastructure resulting in an overstatement in MDOT's capital assets.*

The misclassification of buildings was our oversight due to certain buildings being constructed with federal dollars. In the future, the Financial Reporting Section will be working with the Asset Management Division to reconcile building additions and deletions monthly. It should be noted the error was not detected by the Office of the State Auditor's staff during their review but by MDOT management, who then reported the error to DFA and OSA.

In summary, MDOT did timely submit the Capital Assets GAAP packet once the proper accounting structure was setup in MAGIC by DFA. We are always looking for opportunities to strengthen our internal controls and will begin a monthly reconciliation of capital assets to minimize errors like the one we self-reported this year.

Corrective Action Plan:

- A. While we had many controls in place, we believe performing a monthly reconciliation of capital assets will enhance our process.

- B. The Financial Management Director, Alison Brown and her staff as well as Asset Management Director, Julie Ethridge and her staff are responsible for this corrective action plan.
- C. This corrective action plan was implemented immediately.

Should you have any questions or need additional information, contact our Financial Management Division at (601) 359-7400.

Sincerely,



Melinda L. McGrath, PE
Executive Director

MLM:kyo

cc: Lisa Hancock, Deputy Executive Director/Administration
Alison Brown, Financial Management Director
Julie Ethridge, Asset Management Director



**STATE OF MISSISSIPPI
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Auditor's note to the Response from Management

MISSISSIPPI DEPARTMENT OF TRANSPORTATION

MATERIAL WEAKNESS

Finding Number

Finding Heading

2014-015

Controls Should Be Strengthened to Ensure Capital Assets are Reported Timely and Accurately

Rebuttal to Agency Response:

We have reviewed the comments made by the agency in response to the above noted finding. The Mississippi Department of Transportation (MDOT) provided the Department of Finance and Administration (DFA) with a GAAP Management Representation letter, dated November 3, 2015, in which Management represented that the agency's financial statements were presented fairly in all material aspects and that all material transactions had been recorded in the accounting records. This letter included representations regarding any capital asset accounts. While the Office of the State Auditor (OSA) disagrees with the above detailed timeline of events, implications that DFA did not provide adequate assistance, and that OSA did not alert management of MDOT to material misstatements noted in the finding, the final responsibility of providing accurate and timely financial information for the ongoing operations of MDOT lies with the management of MDOT.

Deficiencies in this reporting were noted for Fiscal Year 2015, and require appropriate disclosure to the users of the Consolidated Annual Financial Report and to the federal grantor agency.

We also wish to place emphasis on finding number **2015-030** in which weaknesses regarding the filing of the Consolidated Annual Financial Report are addressed and Corrective Action Plans were submitted by the Department of Finance and Administration.