

Office of the Secretary of State

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Kris Strickler, Director
Oregon Department of Transportation
355 Capitol St NE MS 11
Salem, Oregon 97301

Dear Mr. Strickler:

We have completed a risk assessment of the Oregon Department of Transportation's (ODOT) External Audits' engineering rate cognizant review process. The objectives of this assessment were to (1) review ODOT's interpretation and application of the Federal Acquisition Regulations (FAR), and (2) review Generally Accepted Government Auditing Standards (GAGAS) to identify any challenges to independence among the three entities involved in the External Audit review process. To meet these objectives, we performed the following limited procedures:

- Gained an understanding of the department's engineering rate review process;
- Reviewed applicable laws and regulations;
- Reviewed ODOT's cognizant review procedures and compared them to procedures recommended by the standard setting bodies (AASHTO and FAR);
- Reviewed a completed cognizant review by ODOT to ensure that key TeamMate procedures were addressed during the agency's review; and
- Reviewed GAGAS around independence.

Background

ODOT has an external audit program that includes auditing the rates of engineering design firms. Engineering firms set rates, including overhead rates, and another firm audits the rates. ODOT then reviews the audit firm's work and the audited rates for compliance with federal requirements and reasonableness. ODOT received questions related to these oversight reviews and any impact on the independence of ODOT and the involved audit firm. As a result, ODOT requested we conduct a risk assessment of their compliance review process.

Results

ODOT's interpretation and application of FAR

Based on FAR, ODOT is the cognizant agency for the State of Oregon. As the cognizant agency, ODOT has the responsibility to review the audits and indirect cost rates of contracting entities to determine whether ODOT agrees and will accept the audits and accept, adjust, or deny the rates. Additionally, as a state agency, ODOT has a responsibility to ensure proper management of taxpayer funds and compliance with federal requirements for itself and any recipients or subrecipients.

As recipients, Architecture and Engineering (A/E) firms have the responsibility to support all costs claimed in the creation of indirect cost rates.

It appears that ODOT's current procedures are appropriately designed to address most aspects of the FAR through their cognizant reviews, such as executive compensation, utilization rate analysis,

and quality assurance procedures. ODOT procedures included additional steps around executive compensation, in accordance with the 2009 Office of Inspector General audit that called for further review by both the auditors and the A/E firms.

However, we did identify areas for improvement. During our review, there were instances in which references to the AASHTO guide were not current, although the information in the procedure still appeared accurate. Procedures encompass FAR, AASHTO Guide, and state-specific testing. However, program steps did not clearly identify the source for each.

We recommend ODOT assess their cognizant review procedures to ensure all references are up to date and that program steps clearly detail the source requirement of the planned procedures.

Independence

We reviewed professional auditing standards and FAR guidelines in considering whether independence risks exist in ODOT performing the functions required of a cognizant agency. The oversight process for cognizant review and acceptance of audits and indirect rates is not intended to impair the independence of auditors performing work for a contracting A/E firm. Engineering firms are required to adequately support calculated indirect cost rates and ensure only allowable compensation is included in indirect cost rates. FAR requires audits, and those audits should include sufficient evidence to support compliance with indirect rate requirements. It is up to an auditor's professional judgment when determining what procedures and documentation comprise adequate support. Furthermore, as the cognizant agency, ODOT is responsible for ensuring audit work is sufficient to detect unallowed costs and support an opinion on compliance with FAR. ODOT may also question indirect cost rates and the related audits in performing its required oversight, and provide guidance and feedback to A/E firms on areas to improve. This oversight, as with other compliance reviews, does not appear to pose a threat to an audit firm's independence with respect to professional auditing standards.

The purpose of this letter is solely to describe the scope of our review and the results of the procedures performed. Because this was a limited review, we were not required to and did not follow generally accepted government auditing standards.

We appreciate the time, effort, and cooperation of department staff. The professionalism we encountered and openness to suggestions have made this a collaborative process. If you have any questions, please contact Amy Dale, Audit Manager, or Kari Mott, Principal Auditor, at (503) 986-2255.

Sincerely,

Office of the Secretary of State, Audits Division

cc: Marlene Hartinger, Chief Auditor
Margaret Cole, External Audit Manager