



STATE OF NORTH CAROLINA
Office of the State Auditor

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

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August 17, 2007

Mr. Lyndo Tippet, Secretary
North Carolina Department of Transportation
1 South Wilmington Street
Raleigh, North Carolina 27611-1501

Dear Secretary Tippet:

We received a complaint through the *State Auditor's Hotline* that North Carolina Department of Transportation (DOT) employees were instructed to improperly record usage of rental equipment by a contractor for road maintenance projects. Allegedly, the Warren/Vance County Maintenance Engineer told employees to overstate the time that equipment was in operation for this contractor. Pursuant to North Carolina General Statute § 147-64.6(c)(16), our review of this matter resulted in the following findings and recommendations.

Background

According to the Division of Highways Procedure Training Manual for Rental Equipment Supervision, DOT "may supplement its equipment requirements by the rental of privately-owned equipment." The rental of equipment is limited to specified situations such as emergencies, secondary road construction, spot safety, and specialized equipment needs.

Each year, contractors submit an Equipment Rental Proposal for Fully-Operated Equipment (RE-1) listing all types of equipment their company can provide along with an associated rate for each equipment type. The district engineer approves the contractors and their rates and an open-ended purchase order (Rental Equipment Agreement) is effective for one year. When the workload requires the use of rental equipment, the county maintenance engineer contacts one of the approved vendors. The contractor is paid at the approved rate for each type of machinery.

For "fully-operated rental equipment," the contractor provides both the equipment and the employees to operate the equipment. DOT road maintenance personnel oversee all operations and DOT "time supervisors" record, on the Rental Equipment Time Supervisor's Daily Report (RE-3), the actual time each piece of equipment is used. The time supervisor provides a Rental Equipment Time Sheet (RE-2) to the contractor who uses that form to prepare an invoice for payment. The contractor is paid a rate based upon the previously approved Rental Equipment Agreement after the district engineer compares the invoice to the time sheet and the daily report to verify the correctness of the invoice.

Contractor received payment for equipment not in operation

Our review of all fully-operated rental equipment usage reports from November 2003 through April 2006 for the contractor revealed DOT paid \$25,295 for “service trucks,” “mechanical tool trucks,” “crew cab work trucks,” and “low boys”¹ in violation of DOT policy.

According to the Division of Highways Procedure Training Manual, charges should be “based upon the time the equipment was in actual productive operation. The contractor will not be paid for downtime due to meals, equipment failure, unsatisfactory weather, or any other conditions.” Our review revealed 70 instances totaling \$21,620 in which time was charged for service trucks, mechanical tool trucks, and crew cab work trucks that were not in actual production throughout the day. The County Maintenance Engineer and the District Engineer said this practice was discontinued about two years ago.

In addition, the Division of Highways Procedure Training Manual states “the contractor shall be responsible for providing transportation for all equipment to and from all job sites assigned by the Department of Transportation at no cost to the Department of Transportation.” Our review found 11 instances totaling \$3,675 in which the contractor was paid for transporting equipment using a low boy to and from the job site. DOT maintenance employees serving as time supervisors said the County Maintenance Engineer instructed them to include transportation time in their daily usage reports. The County Maintenance Engineer and District Engineer agreed that transportation costs should not be included. However, they conceded there may have been instances in the past when these costs were paid by DOT.

Contractor received an overpayment due to a time discrepancy

Our analysis also revealed an overpayment regarding the contractor. On December 17, 2003, the contractor submitted an invoice that overcharged DOT by 16 hours for the use of a motor grader. DOT approved the invoice and paid the contractor for 50.5 hours although the Rental Equipment Time Sheet (RE-2) and Rental Equipment Time Supervisor’s Daily Report (RE-3) both indicated the motor grader was used only 34.5 hours during the period covered. DOT management agreed the contractor was overpaid \$2,000 for this oversight. The current District Engineer said the error should have been corrected by the prior District Engineer.

Recommendations

DOT management should ensure contractors are paid only for the time fully-operated rental equipment is in actual productive operation. To the extent practical, DOT should pursue recovery of the \$25,295 paid to the contractor in violation of DOT policy as well as the \$2,000

¹ A service truck and mechanical tool truck provide service to equipment when needing repair. These trucks hold tools, supplies, and parts, transport workers to and from job sites, and typically sit idle during the work day. A crew cab work truck transports workers to and from the job site. A low boy is a heavy equipment trailer used to transport equipment to a work site.

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overcharge from December 2003. Management should also provide periodic training to all maintenance staff to ensure compliance with DOT policies and procedures.

Please provide your written response to these findings and recommendations, including corrective actions taken or planned, by August 30, 2007. In accordance with General Statute § 147-64.6(c)(12), the Governor, the Attorney General, and other appropriate officials will receive a copy of this management letter. If you have any questions or wish to discuss this matter further, please contact us. We appreciate the cooperation received from the employees of the Department of Transportation during our review.

Sincerely,

A handwritten signature in black ink that reads "Leslie W. Merritt, Jr." in a cursive script.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

Management letters and responses receive the same distribution as audit reports.



STATE OF NORTH CAROLINA
DEPARTMENT OF TRANSPORTATION

MICHAEL F. EASLEY
GOVERNOR

1501 MAIL SERVICE CENTER, RALEIGH, N.C. 27699-1501

LYNDO TIPPETT
SECRETARY

September 5, 2007

Mr. Leslie W. Merritt, Jr., CPA, CFP
State Auditor
2 South Salisbury Street
20601 Mail Service Center
Raleigh, North Carolina 27699-0601

Dear Auditor Merritt:

This is in response to the allegation through the *State Auditor's Hotline* concerning use of rental equipment by a contractor for North Carolina Department of Transportation (NCDOT) road maintenance projects in Vance and Warren Counties.

Members of your staff met with representatives of the Department and also provided us a confidential draft of the finding and recommendations dated August 17, 2007. The two areas of concern are payment for equipment not in operation and an overpayment due to a time discrepancy. I have reviewed the recommendations below, and offer my response:

Recommendations:

The Department's management should ensure contractors are paid only for the time fully operated rental equipment is in actual productive operation. To the extent practical, the Department should pursue recovery of the \$25,295 paid to the contractor in violation of NCDOT policy, as well as the \$2,000 overcharge from December 2003. Management should also provide periodic training to all maintenance staff to ensure compliance with NCDOT policies and procedures.

Response:

I am in agreement with the recommendation that NCDOT management should ensure contractors are paid only for the time Fully Operated Rental Equipment (FORE) is in actual productive operation. I am also in agreement that management should also provide periodic training to all maintenance staff to ensure compliance with NCDOT policies and procedures.

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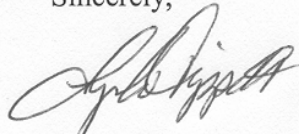
Upon discovery of the improper interpretation of the Department's FORE policies and subsequent payments, changes were made in Vance and Warren Counties to correct this practice. The contractor was counseled with regards to inclusion of all costs for support equipment into allowable hourly rate quotes for active machinery. Time supervisors were also reminded of acceptable time entry and deduction factors for this process.

Upon initial notice from members of your office regarding this audit, discussions began at the Operations Staff Meeting among all 14 Division Engineers regarding the FORE policies. A summary of these discussions was immediately provided to all division staffs through regular staff meetings in April and May of 2007. A multifaceted workgroup has been assembled to complete a thorough review of the policy, supporting documentation and internal audit processes. This effort is currently underway and department-wide training will immediately follow.

I have forwarded details of these findings to the Attorney General's Office to determine the extent to which recovery of the overpayments may be pursued with the subject contractor.

Thank you for the opportunity to respond to the recommendations in the August 17, 2007, letter. I appreciate the work of the Office of the State Auditor to help the Department improve its policies and procedures, as well as increase savings.

Sincerely,



Lyndo Tippet

LT/jbd

cc: Dan DeVane, Chief Deputy Secretary
Bill Rosser, PE, State Highway Administrator
Steve Varnedoe, PE, Chief Engineer - Operations
Jon Nance, PE, Director of Field Operations
Lacy Love, PE, Director of Asset Management
Wally Bowman, PE, Division Engineer
Steve Winstead, PE, District Engineer
Mark Foster, CFO
Beth McKay, Special Deputy Attorney General