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COMPTROLLER**



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**OFFICE OF THE
NEW YORK STATE COMPTROLLER**

**DIVISION OF STATE
GOVERNMENT ACCOUNTABILITY**

**DEPARTMENT OF
TRANSPORTATION**

**QUALITY OF INTERNAL
CONTROL
CERTIFICATIONS**

Report 2008-S-116

AUDIT OBJECTIVE

Our objective was to determine whether the Department of Transportation (DOT) submitted a quality internal control certification to the Division of Budget on April 30, 2008.

AUDIT RESULTS - SUMMARY

The Division of Budget (DOB) requires agencies to certify compliance with the State's Internal Control Act annually by submitting an internal control certification, which includes both an internal control summary report as well as a signed certification to attest that they met required internal control provisions.

DOT certified as required in 2007-08 by submitting both documents. However, we determined DOT did not submit a quality internal control certification to DOB by April 30, 2008. DOT's certification addressed all the requirements of Budget Policy and Reporting Manual Item B-350 including detailed responses to questions in the internal control summary. However, although DOT outlined a risk assessment process in their internal control certification, the documentation provided did not support that the 24 risk factors identified by DOT were assessed by each of its divisions. Also, DOT officials could not provide adequate documentation of their monitoring of corrective action plans.

In addition, we determined DOT officials have improperly placed the internal audit function and the internal control function, in the same Division reporting to the Director of the Audit and Civil Rights Division. Since the internal audit function is responsible for evaluating the effectiveness of an entities system of internal control, it is imperative the

individual be independent of the activities they audit.

Our audit report contains two recommendations to improve the quality of DOT's internal control certification. In addition, the report contains one recommendation to help DOT assure they are maintaining independence in their Internal Control Officer and Internal Audit responsibilities. DOT officials disagree with our report and recommendations. However, they state that they recognize the significance of the issues considered in the audit and work continuously to improve their internal control program and risk management activities.

This report, dated January 16, 2009, is available on our website at: <http://www.osc.state.ny.us>.

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BACKGROUND

Internal controls are the integration of the activities, plans, attitudes, policies, and efforts of the people of an organization working together to provide reasonable assurance that the organization will achieve its objectives and mission. While the overall purpose of internal control is to help an organization achieve its mission, internal control also helps an organization to promote orderly, economical, efficient and effective operations, and produce quality products and services consistent with the organization's mission; safeguard resources against loss due to waste, abuse, mismanagement, errors and fraud; promote adherence to laws, regulations, contracts and management directives; develop and maintain reliable financial and

management data, and accurately present that data in timely reports.

The Division of Budget's Budget Policy and Reporting Manual Bulletins B-350 and B-1177 require the head of each covered State agency and public authority to certify compliance with the State's Internal Control Act by April 30 of each year by submitting a Certification and Internal Control Summary of the internal control activities undertaken during the previous year. The current requirements in the BPRM B-350 internal control certification has been updated with a list of agencies required to establish and maintain an internal audit function and also requires agencies identify specific actions taken to implement each of the recommendations in the Internal Control Task Force report "*The New York State Internal Control Act Implementation Guide: Strengthening Compliance with the Act and Standards.*" These recommendations include specific guidance for agencies, the Internal Control Task Force, NYS Division of Budget and the NYS Comptroller's Office. The recommendations were developed to provide agencies with an improved level of assurance that an appropriate set of controls are in place within the agency and are functioning properly. Recommendations directed toward agencies relate to internal control coordination, implementation, education and training as well as internal audit organization, staffing, processes, and continuing education.

In 1967, New York State Department of Transportation (DOT) was formed to deal with the State's complex transportation system. The New York State transportation network includes: a State and local highway system that encompasses more than 113,000 highway miles and more than 16,000 bridges, an extensive 4,600-mile rail network, 513 public and private aviation facilities, and 12 major public and private ports with a budget

of over \$7 billion in appropriations for 2008-09.

DOT's mission is to ensure customers - those who live, work and travel in New York State - have a safe, efficient, balanced and environmentally sound transportation system.

The Director of the Audit and Civil Rights Division is also the Internal Control Officer. The Enterprise Risk Management Bureau and the Internal Audit Bureau report to the Director of the Audit and Civil Rights Division/Internal Control Officer. The Enterprise Risk Management Bureau is responsible for the agency risk assessment program and the Internal Audit Bureau is responsible for the internal audit program.

AUDIT FINDINGS AND RECOMMENDATIONS

Quality of Internal Control Assessment

On June 16, 2008, we asked DOT officials to provide all documentation to support statements made in their 2007-08 Internal Control Certification and internal control summary report which were submitted to the Division of Budget on April 30, 2008. DOT officials did not provide all documentation as requested at that time because the documents did not exist. Instead, agency officials waited until the closing conference and after receiving our preliminary audit findings in August to provide some documents. When we reviewed these documents, we found, and DOT officials later confirmed, that many of the documents provided were created by DOT officials after our audit began and were not developed during the certification period of April 1, 2007 through April 30, 2008.

The Division of Budget (DOB) requires agencies to certify compliance with the State's Internal Control Act annually by

submitting an internal control certification, which includes both an internal control summary report as well as a signed certification to attest that they met required internal control provisions.

In order to determine if DOT submitted a quality certification, we reviewed the certification to see if they followed the certification instructions outlined in the Budget Policy and Reporting Manual Item B-350, and followed the internal control requirements outlined in the NYS Internal Control Act Implementation Guide and the Internal Control Task Force Recommendations in the Standards for Internal Control in New York State Government which are the basis for the certification. In addition, we determined a quality certification should show evidence an agency responded to all the questions, provided explanation and detail when required, and answered the questions accurately. We also reviewed supporting documentation of the certification provided by the Commissioner to determine if the information reported was accurate.

The Commissioner certified as required in 2007-08 by submitting both documents. However, we determined she did not submit a quality internal control certification to DOB by April 30, 2008. DOT's certification addressed all the requirements of Budget Policy and Reporting Manual Item B-350 including responses to questions in the internal control summary. However, although DOT outlined a risk assessment process in their internal control certification, the documentation provided did not support that all 24 risk factors identified by DOT were used by each of its eight divisions. Also, DOT officials could not provide adequate documentation of their monitoring of corrective action plans.

The internal control summary report asks each agency to describe the review process used during 2007-08 to assure that internal controls were evaluated regularly. DOT officials responded that the Audit and Civil Rights Division conducts meetings with DOT's top management to facilitate the identification and discussion of risks, the adequacy of existing internal controls, and potential actions to manage risks or alter controls. A standard risk assessment tool which includes 24 risk factors is used to conduct these interviews which DOT calls a Strategic Risk Assessment (SRA). In addition, DOT officials told us these meetings and resulting SRAs are used to establish DOT's top ten high risk activities which are listed in the certification.

We asked DOT officials for documentation to support this risk assessment process and were provided with all eight SRAs from the eight division managers. We were also provided with a sample of SRAs completed by lower level staff in these eight divisions. Our review found that none of the SRAs reviewed had all 24 risk factors completed. Moreover, DOT officials confirmed that if we took all the SRAs completed for each of the eight divisions, we would not find one division that had documented a discussion and determination on all 24 risk factors. When we asked why risk factors would be left blank, we were told that the SRAs only document discussion on those of the 24 factors that are considered high risk for that division. DOT officials explained that risk factors may be left blank because the risk factor was discussed at the interview and it was decided that the risk factor did not pertain to that division. It would also be left blank if it was determined the risk was medium or low for that factor. However, when risk factors are left blank the Commissioner has no assurance the risk factor was properly considered during the risk assessment process. To ensure a

quality risk assessment, DOT officials should be thoroughly documenting their risk assessments showing conclusions for all 24 risk factors. We recommend that DOT officials consistently explain in the SRAs, their conclusion (not applicable and why; low, medium or high risk and why; no risk and why) on each of the 24 risk factors for each division.

The internal control summary report also asks each agency to describe the monitoring system installed to verify that corrective actions are in fact taken. DOT stated that, "An access database of identified risks is maintained. Follow-ups on identified risks are conducted as part of each annual risk assessment. Additionally, for all identified significant risks the Internal Control Officer will monitor the implementation of corrective action plans on a semi-annual basis."

Initially when we asked DOT officials to provide us with documentation to support these statements, the Director of the Enterprise Risk Management Bureau stated the access database was no longer used. When we inquired about the database again, another DOT officials stated the database was not populated with the most recently identified risks from the current certification period and is only used for historical information. Furthermore, we were told that the database only contained information on risk and did not contain comprehensive information on corrective action plans. Since the access database was not populated for the certification period and it does not include comprehensive corrective action plan information, we question why it is listed in the certification as a means for them to monitor that corrective actions have been taken. DOT officials told us that they do plan to purchase an electronic system which they will use to assist them in monitoring their corrective action plans in the future.

The New York State Internal Control Act Implementation Guide: Strengthening Compliance with the Act and Standards, states that the Internal Control Officer or other internal control staff should work with managers and monitor the implementation status of the Corrective Action Plans. The fact that DOT officials state in the internal control summary report that the Internal Control Officer **will** monitor corrective action plans for all identified significant risks on a semi-annual basis does not respond to what the Internal Control Officer or her staff **did** to monitor corrective action plans during the 2007-08 certification period.

DOT officials did provide us with a Power Point presentation that was put together for the Commissioner just prior to submission of the 2007-08 certification to DOB. This presentation outlined the risks and corrective action plans by the divisions. This shows that there is some follow-up on identified risks just prior to the certification being due. However, it does not show how corrective actions are monitored throughout the year to ensure timely implementation.

Corrective action plans are a critical part of agencies internal control program because they are used to identify internal control weaknesses. DOT should follow through on plans to purchase an electronic system to track actions taken to implement corrective action plans and develop a process that incorporates regular monitoring (not just twice a year) to ensure that divisions implement corrective actions in a timely manner.

Recommendations

1. DOT officials should consistently document in the SRAs their conclusion (not applicable and why; low, medium or high risk and why; no risk and why) on

each of the 24 risk factors for each division.

2. Follow through on plans to purchase an electronic system to track actions taken to implement Corrective Action Plans and develop a process that incorporates regular monitoring to ensure that divisions implement corrective actions in a timely manner.

Independence

Agency heads are required to appoint an Internal Control Officer who assists the agency head and other management by evaluating and improving the effectiveness of the internal control system. The Internal Control Officer is responsible for implementing and reviewing the organization's internal control efforts. In addition, according to the State Comptroller's *Standards for Internal Control in New York State Government*, the Internal Control Officer is responsible for assisting in establishing specific procedures and requirements. However, the effectiveness of these procedures and requirements must be audited by someone who was not involved in the process of putting them in place. The Internal Auditor is responsible for evaluating the effectiveness of the system of internal control and must be independent of the activities that are audited. For this reason, the Internal Auditor should not perform the role of Internal Control Officer.

Compliance with B-350 Internal Control Officer independence is an issue. B-350 states, "...The Internal Auditor function should be independent of the Internal Control Officer, but should work closely with the Internal Control Officer. Limitations should be established on internal control activities where those duties overlap. Agencies should identify impairments to the independence of

the Director of Internal Audit that may be created where the Director of Internal Audit is performing the Internal Control Officer function. Furthermore, Internal Audit units should not assume operating responsibilities, perform management functions, make management decisions, or assume other monitoring roles (e.g., Information Security Officer)."

However, DOT's Director of the Audit and Civil Rights Division is also the Internal Control Officer. As Director of the Audit and Civil Rights Division, responsibilities include the oversight of the Internal Audit Bureau and the Enterprise Risk Management Bureau. The Internal Audit Bureau handles the internal audit function and the Enterprise Risk Management is responsible for implementation of the DOT internal control program. In order to effectively maintain independence, the Internal Control Officer and Internal Audit function should be separated and the Internal Audit function should report directly to the Commissioner.

Recommendation

3. Separate the Internal Audit function and the Internal Control Officer function and have the Internal Audit function report directly to the Commissioner.

AUDIT SCOPE AND METHODOLOGY

We audited the quality of DOT's 2007-08 B-350 Internal Control Certification. To do our audit we interviewed agency officials to learn about their control activities and reviewed all documentation of internal controls provided by DOT to support their certification.

We did our performance audit according to generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain

sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members - some of whom have minority voting rights - to certain boards, commissions, and public authorities. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, they do not affect our ability to conduct independent audits of program performance.

AUTHORITY

We did this audit according to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law.

REPORTING REQUIREMENTS

Draft copies of this report were provided to DOT officials for their review and comment. Their comments were considered in preparing this report and are included as Appendix A. DOT officials disagree with our report and recommendations. However, they state that they recognize the significance of the issues considered in the audit and work continuously to improve their internal control program and risk management activities.

Within 90 days of the final release of this report, as required by Section 170 of the Executive Law, the Commissioner of the Department of Transportation shall report to the Governor, the State Comptroller, and the leaders of the Legislature and fiscal committees, advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons therefor.

CONTRIBUTORS TO THE REPORT

Major contributors to this report include David R. Hancox, Walter Irving, Melissa Little, Thalia Melendez, Sally Perry and Constance Walker.

APPENDIX A - AUDITEE RESPONSE



STATE OF NEW YORK
DEPARTMENT OF TRANSPORTATION
ALBANY, NY 12232
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Office of the State Comptroller

DEC 26 2008

Lynn Canton
Deputy Comptroller

ASTRID C. GLYNN
COMMISSIONER

December 22, 2008

DAVID A. PATERSON
GOVERNOR

Ms. Lynn Canton
Deputy Comptroller
Office of the State Comptroller
Division of State Government Accountability
110 State Street, 11th floor
Albany, NY 12236

Dear Ms. Canton:

Thank you for the opportunity to review your draft audit report, Quality of Internal Control Certifications, 2008-S-116.

As you know, the Department of Transportation (Department) attempted throughout the reporting process to clarify facts and resolve misunderstandings contained in the draft report. Since substantive concerns remain, the Department disagrees with the report and its recommendations.

Regardless of this disagreement with the report, the Department recognizes the significance of the issues considered in the audit and is continuously working on improving its internal control program and risk management activities throughout the Department. The independence of the internal audit function has been preserved by keeping it separate organizationally from the internal control function, and I remain confident that the Department will continue to have an effective system of internal controls.

Finally, I would like to acknowledge and express appreciation for the courtesies you extended in connection with this audit.

Sincerely,

Stanley Gee
Executive Deputy Commissioner

cc: Thomas Lukacs, Division of the Budget

*
Comment
1

*
Comment
2

* See State Comptroller's Comments, page 9

APPENDIX B - STATE COMPTROLLER'S COMMENTS

1. We did not misrepresent the facts nor did we misunderstand anything Department officials provided or told us. We used the same criteria and methodology on this and nine other audits of State entities, including six agencies that we determined submitted a quality internal control certification. We collected sufficient evidence to support our audit findings, conclusions and recommendations. We asked officials to provide us with all the documentation they had to support what they wrote in their internal control certification including both the internal control summary report and the signed certification attesting that they met required internal control provisions. In addition, we interviewed DOT staff to determine if what was written in the certification was, in fact, practiced. Unfortunately, DOT officials were not able to provide us with adequate documentation to support their internal control certification. In addition, DOT staff confirmed during interviews that what was written in the internal control certification was not what was always done.
2. Unfortunately, Mr. Gee is not correct in this position. There is an inherent conflict of interest with the Director of the Audit and Civil Rights Division being able to effectively maintain independence because her responsibilities include being the Internal Control officer as well as oversight of both the Internal Audit Bureau and the Enterprise Risk Management Bureau. Division of the Budget guideline B-350 states that the internal audit function should be independent of the Internal Control Officer. It also states that the Director of Internal Audit should report functionally to the agency head or audit committee. Many organizations in the private and public sector have faced scandals that were not uncovered by internal auditors because of this lack of independence. The international organization representing internal auditors, the Institute of Internal Auditors, has recognized this issue in its professional guidance indicating internal auditors are not to accept responsibility for non-audit functions. If they do, they are not functioning as internal auditors.