



New York State Office of the State Comptroller
Thomas P. DiNapoli

Division of State Government Accountability

Quality of Internal Control Certification

Department of Economic Development



Report 2012-S-48

December 2012

Executive Summary

Purpose

To determine whether the Department of Economic Development (DED) submitted timely a quality Internal Control Certification to the Division of Budget (DOB) by April 30, 2012.

Background

In 1987, the Legislature passed the New York State Governmental Accountability, Audit and Internal Control Act (Act) requiring State agencies and public authorities to each institute a comprehensive system of internal controls over their operations. DOB requires the head of each covered State agency and public authority to certify compliance with the Internal Control Act by April 30 of each year by submitting a certification and internal control summary detailing the internal control activities undertaken during the previous year. On April 24, 2012, DED submitted its annual Internal Control Certification and reported full compliance with all provisions of the Act.

Key Findings

- DED's Internal Control Certification was submitted timely. However, we identified several areas where the quality of the certification could be improved.
- In three instances, DED's certification did not provide the required level of detail to explain the actual steps taken to implement certain provisions, including describing its internal control testing and monitoring processes and the results of its reviews of high risk activities.
- Although DED certified full compliance with all provisions of the Act, its internal audit function has not had an external quality control assessment completed as required by professional auditing standards.

Key Recommendations

- Provide appropriately detailed responses to questions as requested in the annual Internal Control Certification.
- Ensure that the internal audit function undergoes periodic external quality control assessments as required by professional audit standards.

Other Related Audits/Reports of Interest

[Office for the Prevention of Domestic Violence: Quality of Internal Control Certification \(2012-S-41\)](#)

[Office of the Medicaid Inspector General: Quality of Internal Control Certification \(2012-S-46\)](#)

[Department of State: Quality of Internal Control Certification \(2012-S-50\)](#)

**State of New York
Office of the State Comptroller**

Division of State Government Accountability

December 6, 2012

Mr. Kenneth Adams
President and CEO of Empire State Development and
Commissioner of the Department of Economic Development
633 Third Avenue
New York, NY 10017

Dear Mr. Adams,

The Office of the State Comptroller is committed to helping State agencies, public authorities and local government agencies manage government resources efficiently and effectively and, by so doing, providing accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of State agencies, public authorities and local government agencies, as well as their compliance with relevant statutes and their observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations. Audits can also identify strategies for reducing costs and strengthening controls that are intended to safeguard assets.

Following is a report of our audit entitled *Quality of Internal Control Certification*. This audit was performed according to the State Comptroller's authority under Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law.

This audit's results and recommendations are resources for you to use in effectively managing your operations and in meeting the expectations of taxpayers. If you have any questions about this report, please feel free to contact us.

Respectfully submitted,

*Office of the State Comptroller
Division of State Government Accountability*

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This report is also available on our website at: www.osc.state.ny.us

Background

Internal Controls in New York State

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.

In 1987, the Legislature passed the New York State Governmental Accountability, Audit and Internal Control Act (Act) requiring each State agency to institute a comprehensive system of internal controls over its operations. The Division of the Budget's (DOB's) Budget Policy and Reporting Manual Bulletin B-350 requires the head of each covered agency to certify compliance with the Act by April 30 of each year by submitting a Certification and Internal Control Summary describing the internal control activities undertaken during the previous year.

The current requirements in BPRM B-350 have been updated with a list of agencies required to establish and maintain an internal audit function and also require agencies to 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."* The recommendations were developed to provide agencies with an improved level of assurance that an appropriate set of controls are in place and functioning properly. Recommendations directed toward agencies relate to internal control coordination, implementation, education and training, as well as to internal audit organization, staffing, processes, and continuing education.

As the State's chief fiscal officer, the Comptroller has several responsibilities under the Act, including issuing standards for internal control, providing technical assistance to agencies and conducting audits of internal controls. All of these efforts are directed toward helping public sector managers safeguard public assets and promote accountability in government. Past audits have examined a range of topics from specific control systems at individual agencies to broader statewide issues like the operation of internal audit units. This audit is one of a series that focuses specifically on the Internal Control Certification process and whether State agencies have:

- submitted their certifications on time,
- properly answered all the questions with the appropriate level of detail, and
- maintained documentation that supports the answers given.

Answers to these questions provide insight into the adequacy of not only the agencies' internal

control systems, but also their control environment and commitment to make timely, informative and reliable information available for accountability purposes.

Department of Economic Development

The Department of Economic Development (DED) works in conjunction with the Empire State Development Corporation (ESDC) to administer State economic development programs. DED is headed by a Commissioner, who also serves as the President and CEO of ESDC. DED's mission is to promote a vigorous and growing economy, encourage the creation of new job and economic opportunities, increase revenues to the State and its municipalities, and achieve stable and diversified local economies.

DED's Internal Control Officer (ICO), who also serves as Assistant Counsel, requires each division head to complete an internal control survey identifying statutory and other functions. For each function, division heads are required to identify key risks and corresponding controls and then determine and classify the risk level as either high, medium or low. The ICO reviews and critiques all submitted internal control surveys and submits a list of high risk activities to executive management.

There are six sections of the Internal Control Certification where agencies are asked to determine whether they comply fully, partially or do not comply with the provisions of the Act. On April 24, 2012, DED submitted its annual certification and reported full compliance with all provisions of the Act.

Audit Findings and Recommendations

DED's Internal Control Certification was submitted timely (April 24, 2012) and generally exhibited the necessary quality. However, in three cases we found sufficient detail was not provided when answering the questions. We also noted an issue related to DED's internal audit function which could impact its reported level of compliance.

Agency Certification

While DED responded to all the questions in the Internal Control Certification, for three questions the agency did not provide sufficient detail. These include:

- Not describing its process for testing internal controls;
- Not describing its process for monitoring corrective actions; and
- Not describing the results of its reviews of high risk functions.

Supporting Documentation

In each area, DED officials provided us with sufficient, appropriate documentation supporting the statements made in its Internal Control Certification.

Other Issues Potentially Impacting Compliance

As part of our examination, we also noted the following issue that calls into question the degree of DED's compliance with specific provisions of the Act. Generally accepted professional auditing standards require an internal audit unit to undergo an external quality control assessment at least once every five years. Although DED reported that its internal audit unit had not undergone the required assessment, it still certified the internal audit function as fully compliant with the Act.

Recommendations

1. Provide appropriately detailed responses to questions as requested in the annual Internal Control Certification.
2. Ensure that the internal audit function undergoes periodic external quality control assessments as required by professional audit standards.

Audit Scope and Methodology

We audited the quality and timeliness of DED's 2011-2012 Internal Control Certification to determine whether it was filed in accordance with DOB requirements. To accomplish our objective, we reviewed the Internal Control Certification and all documentation of internal controls that DED used to support it. In addition, we interviewed the DED's Internal Control Officer to learn more about the internal control system. Our audit addressed the quality of the Internal Control Certification, but did not assess, nor was it intended to assess, the quality of DED's internal control system. Our audit scope included the period April 1, 2011 through August 31, 2012.

We conducted our performance audit in accordance with 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 objective.

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 to certain boards, commissions and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these functions do not affect our ability to conduct independent audits of program performance.

Authority

This audit was performed according to the State Comptroller's authority under Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law.

Reporting Requirements

A draft copy of this report was provided to DED officials for their review and comments. Officials agreed with our recommendations, provided details of their internal risk assessment and indicated they plan to have a quality assurance review completed for their internal audit unit within the next year. A complete copy of their response is included at the end of this report.

Within 90 days after final release of this report, as required by Section 170 of the Executive Law, the Commissioner of the Department of Economic Development 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 why.

Contributors to This Report

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Vision

A team of accountability experts respected for providing information that decision makers value.

Mission

To improve government operations by conducting independent audits, reviews and evaluations of New York State and New York City taxpayer financed programs.

Agency Comments

 Empire State Development

NYS DEPARTMENT OF ECONOMIC DEVELOPMENT

November 19, 2012

Mr. John Buyce
New York State
Office of State Comptroller
Division of State Government Accountability
110 State Street
Albany, NY 12236

Dear Mr. Buyce:

The New York State Department of Economic Development (“DED”) is in receipt of the Office of State Comptroller’s (“OSC”) Quality of Internal Control Certification audit report of October 2012, which details OSC’s findings with respect to its audit of DED’s internal control certification.

DED appreciates the need for a strong process regarding assessment and review of agency internal controls, since strong internal controls are a vital component of ensuring that DED uses its resources effectively to achieve its core economic development mission of providing the best possible services to the businesses, individuals and organizations DED serves while working within the current budget environment.

Response to Findings

A. DED maintains a robust process for testing internal controls, monitoring corrective actions and reviewing high risk functions.

DED feels it is important to emphasize that it conducts a robust process for testing internal controls, monitoring corrective actions and reviewing identified high risk functions. Specifically, internal control testing and monitoring is currently conducted by the Internal Audit Unit of the New York State Urban Development Corporation, doing business as Empire State Development (“ESD”), our sister agency. ESD’s Internal Audit Unit personnel assumed this responsibility in 2011, prior to which the functions of internal audit and internal control testing were inactive as a result of the prior DED internal auditor’s retirement. ESD tests DED internal controls during various audits of its programs.

To be able to address the audit and internal control review and testing needs of both ESD and DED without expending additional funds on these functions, ESD’s audit director and its two CPA audit staff members have taken the approach of developing a three-year DED audit cycle (starting in 2011) in which all higher risk functions for DED are to be audited.

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During these audits, the internal controls of a particular DED program/function are tested. Audit reports are issued as a result of those audits, and the scope and objectives of each audit is described in the corresponding report, which is supported by audit work papers. Areas noted in the DED audits as requiring corrective action are monitored and followed up on at appropriate times by the Internal Audit Unit in conjunction with DED's Internal Control Officer ("ICO").

Since mid-2011, several audits of high risk areas in DED have been (or are in the process of being) completed, each of which has included internal control testing. Since mid-2011, the Internal Audit Unit completed audits of DED's: large film tax credit program; Excelsior, Empire Zone and CAPCO programs; and minority- and woman-owned business enterprise ("MWBE") certification processes. The Internal Audit Unit is currently completing an audit of DED Finance functions, with a focus on procurement, contract administration, and disbursements. In addition, in 2010, at management's request, an audit of DED grant programs had been conducted.

With respect to reviewing high risk functions, it is important to note that DED's ICO reviews and critiques all risk/control submissions and submits a list of high risk activities to executive management to ensure they are aware of the activities in a timely manner. In addition, over the last two years, DED's ICO identified certain management information systems ("MIS") support functions and certain MWBE issues as high risk activities, based on responses to our internal control questions. Regarding the former, the ICO contacted MIS staff and discussed the lack of resources to implement a Disaster Recovery/Business Continuity Plan. To address the issue, the ICO determined a web resource was not necessary because DED is restructuring its information technology services in such a way that a Disaster Recovery/Business Continuity Plan web service will be covered by a new "cluster" state entity and would therefore be redundant and inefficient if implemented by DED at that time.

Further, the ICO identified additional personnel resources needed to perform certain MWBE functions in the regional offices as well as the need to upgrade the software system that assists the MWBE Division's processing of certification applications. The ICO addressed both issues by checking with DED's head of regional offices to ensure that additional staff were hired to address the MWBE functions that were needed. In addition, the ICO worked with the MWBE Division and the prototype of a new MWBE software application was successfully unveiled at the recent New York State MWBE Forum.

B. Although DED has not had an external quality control assessment performed recently, ESD's Audit Director maintains strict oversight over the quality of DED's internal control program.

As noted in the internal control submission, DED recognizes that it has not yet performed an external quality control assessment of its internal control practices. In that regard, the certification noted that ESD's Audit Director had assumed responsibility for the audit function of DED in 2011, without an increase above current ESD audit staffing levels of three which, prior to 2011, had been dedicated to ESD internal audit efforts.

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Importantly, the certification noted DED's intent to have a quality assessment review ("QAR") performed, but stated that focusing on rollout and implementation of DED's audit plan (a large effort for that staff of three to take on) was deemed to take precedence over expending the time that the three-person Internal Audit Unit would have had to dedicate to performing an audit self assessment and then obtaining a QAR. Given that completing the DED audit cycle was anticipated to occur by the end of 2012-13, the Internal Audit Unit planned to have a QAR done in 2013-14 or 2014-15. In light of this OSC audit report draft, the Internal Audit Unit will attempt to accelerate this, and has reached out to NYSICA members in Albany who might be able to arrange the performance and conduct of a QAR for DED and ESD, with a rough initial target date for commencement of a QAR review by the end of this fiscal year. DED will be dependent on the availability of such outside resources when determining when a QAR can be undertaken.

Conclusion

DED appreciates the OSC feedback in its audit report draft. DED looks forward to the opportunity to increase the specificity of its responses on its 2012-2013 internal control certification as well as looking to accelerate the conduct of an external quality control assessment of the ESD/DED audit function.

Respectfully,



Maria Cassidy
Acting General Counsel