

STATE OF NORTH CAROLINA
Office of the State Auditor



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March 1, 2021

The Honorable Senator Phil Berger, Co-Chair, Joint Legislative Commission on Governmental Operations
The Honorable Representative, Tim Moore, Co-Chair, Joint Legislative Commission on Governmental Operations
The Honorable Representative Frank Iler, Co-Chair, Joint Legislative Transportation Oversight Committee
The Honorable Representative John A. Torbett, Co-Chair, Joint Legislative Transportation Oversight Committee

Ladies and Gentlemen:

This letter presents the results of our review of the North Carolina Department of Transportation, Office of Inspector General (DOT OIG) internal audit titled "Audit of Highway Planning and Construction, Highway Division Contract Pre-Award Process."

On December 14, 2020, DOT OIG presented its report to the Joint Legislative Program Evaluation Oversight Committee (PED).

At that time, the State Auditor noted several discrepancies with the report including a conclusion that did not match the data reported, a sampling methodology that did not align with management's control process, and missing data on the total number of contracts and contract values.

The State Auditor was asked to comment on the report, but lacked sufficient time to research the discrepancies because of the late timing at which the Office of the State Auditor (OSA) received the report. The State Auditor told the Committee that her office would review the DOT OIG audit and then report back on its findings.

Our findings are presented in this letter. OSA reviewed the DOT OIG audit report and workpapers to determine if the audit was conducted in accordance with the Government Auditing Standards issued by the Comptroller General United States. As a basis for evaluating compliance with the audit standards, auditors used the performance audit review guide issued by the National Association of State Auditors, Comptrollers, and Treasurers.

OSA has discussed these findings with DOT OIG.

The results of the requested review is being presented to the Co-Chairs of the Joint Legislative Commission of Governmental Operations as well as the Co-Chairs and members of the Joint Legislative Transportation Oversight Committee since the PED has been dissolved.

If you have any questions, please do not hesitate to contact my office.

Sincerely,

Beth A. Wood

BETH A. WOOD, CPA
STATE AUDITOR

cc: The Honorable Senator Tom McInnis, Vice-Chair, Joint Legislative Transportation Oversight Committee
Members of the Joint Legislative Transportation Oversight Committee
J. Eric Boyette, Secretary, Department of Transportation

Review of Department of Transportation (DOT) Internal Audit Titled “Audit of Highway Planning and Construction, Highway Division Contract Pre-Award Process.”

Review of Internal Audit Report and Workpapers

The NC Department of Transportation OIG internal audit titled “Audit of Highway Planning and Construction, Highway Division Contract Pre-Award Process” did not comply with the Government Auditing Standards issued by the Comptroller General of the United States.

Specifically, the:

1. Audit conclusion was not supported by the findings
2. Auditors did not relate the findings to the population¹ and quantify dollar values
3. Auditors did not use their risk assessment to establish the sampling methodology
4. Sampling methodology was not designed to obtain sufficient evidence
5. Auditors did not document their consideration of information system controls
6. Auditors did not document an overall assessment of the audit evidence
7. Auditors did not extend audit procedures to determine if fraud occurred

Details are discussed below.

1. Audit Conclusion Was Not Supported by Findings

The overall audit conclusion was not supported by the findings. “Key Findings” on page 2 of the audit report state:

Highway Divisions are generally effective in managing processes related to advertising, bidding and contractor selection for Division Let, On-Call Purchase Order, and Limited Services Contracts.

However, the lack of controls reported in the findings do not support the overall conclusion that Division processes were effectively **managed**.

For example, auditors reported that:

- 11 of 14 (79%) Divisions did not have controls to verify that project funding was authorized and released before advertising for bids. (Finding 1)
- 11 of 14 (79%) Divisions did not have controls to ensure that project estimates were reviewed for accuracy and completeness. (Finding 3)
- 10 of 14 (71%) Divisions did not have controls to ensure that projects with estimated costs exceeding \$5 million were not advertised at the Division level. (Finding 3)
- 10 of 14 (71%) Divisions did not have controls to ensure that results of the bidding process were published within three business days. (Finding 9)
- 9 of 14 (64%) Divisions did not have controls to ensure that projects were advertised for the required amount of time. (Finding 4)
- 8 of 14 (57%) Divisions did not have controls to ensure all bidders were pre-qualified. (Finding 5)
- 8 of 14 (57%) Divisions did not have controls to ensure compliance with bid opening procedures. (Finding 6)

¹Population - all contracts at the 14 DOT Regional Offices. Includes Division Let, On-Call Purchase Order, and Limited Services contracts.

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GAO Audit Standards require that:

9.19 Auditors should report conclusions based on the audit objectives and the audit findings.

2. Did Not Relate Findings to the Population and Quantify Dollar Values

The audit report did not relate the instances identified to the population and quantify the results in terms of dollar value or other measures.

For example, the report did not provide the total:

- Dollar value for the population and samples of Division Let, On-Call Purchase Order, and Limited Services contracts
- Number of contracts in the population of Division Let, On-Call Purchase Order, and Limited Services contracts
- Dollar value for the contracts associated with the errors described in the findings

GAO Audit Standards require that:

9.21 Auditors should place their findings in perspective by describing the nature and extent of the issues being reported and the extent of the work performed that resulted in the findings. To give the reader a basis for judging the prevalence and consequences of these findings, auditors should, as appropriate, relate the instances identified to the population or the number of cases examined and quantify the results in terms of dollar value or other measures. If the results cannot be projected, auditors should limit their conclusions appropriately.

3. Risk Assessment Not Used to Establish Sampling Methodology

In planning the audit, the auditors performed inherent and control risk assessments. However, auditors did not apply those assessments in defining the sampling methodology to address the audit objectives.

For example:

- Auditors did not document consideration of their inherent and control risk assessments or other factors such as confidence levels, expected deviations, and tolerable error rates in determining sample sizes. Without documenting why, auditors selected samples totaling 20% of Division Let Contract values and 10% of On-Call Purchase Order Contract values. Additionally, auditors selected and revised sample sizes for Limited Services Purchase Order Contracts from 20% to 15% of total contract value without documenting a basis for either decision. (WP200, 200.1, 200.2h)
- Even though inherent and control risk assessments documented that controls and control risk varied significantly among the 14 Divisions, auditors tested compliance and controls with samples that treated the Divisions as one population. In other words, auditors used each of the three samples (one each for Division Let, On-Call Purchase Order, and Limited Services Purchase Order contracts) to evaluate 14 **different** control environments and therefore 14 **separate** populations. (WP 8.0-8.3a, 100.1, 200, 200.1, 200.2)

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GAO Audit Standards require that:

8.05 In planning the audit, auditors should assess significance and audit risk. Auditors should apply these assessments to establish the scope and methodology for addressing the audit objectives. Planning is a continuous process throughout the audit.

4. Sampling Methodology Not Designed to Obtain Sufficient Evidence

Auditors did not design the sampling methodology to obtain **sufficient**, appropriate evidence that **provided a reasonable basis** for findings and conclusions. Even though auditors determined that controls varied significantly among the 14 Divisions, auditors treated the Divisions as a single population instead of 14 separate populations.

As a result, the number of transactions sampled per Division for each transaction type (Division Let, On-Call Purchase Order, Limited Services Purchase Order contracts) was too small to provide a reasonable basis for a conclusion on compliance and controls. (WP 8.0-8.3a, 100.1, 200, 200.1, 200.2, 200.2.1)

For example:

- Only 3 - 12 sample items were selected from each Division for Division Let Contracts (WP 200.0)
- Only 1 - 6 sample items were selected from each Division for On-Call Purchase Order Contracts (WP 200.1a)
- Only 1 - 7 sample items were selected from each Division for Limited Services Purchase Order Contracts (WP 200.2, 200.2.1)

GAO Audit Standards require that:

8.06 Auditors should design the methodology to obtain sufficient, appropriate evidence that provides a reasonable basis for findings and conclusions based on the audit objectives and to reduce audit risk to an acceptably low level.

5. Consideration of Information System Controls Not Documented

Auditors did not document whether they determined if it was necessary to evaluate information systems controls when obtaining an understanding of internal control significant to the audit objectives.

While it's possible for auditors to find that information system controls are not significant to the audit objectives, it should be noted that the auditors used information systems to:

- Identify contract populations
- Extract sample items
- Obtain and review documents for compliance and control tests

GAO Audit Standards require that:

8.59 The effectiveness of significant internal controls frequently depends on the effectiveness of information systems controls. Thus, when obtaining an understanding of internal control significant to the audit objectives, auditors should also determine whether it is necessary to evaluate information systems controls.

8.60 When information systems controls are determined to be significant to the audit objectives or when the effectiveness of significant controls depends on the effectiveness of information systems controls, auditors should then evaluate the design,

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implementation, and/or operating effectiveness of such controls. This evaluation includes other information systems controls that affect the effectiveness of the significant controls or the reliability of information used in performing the significant controls. Auditors should obtain a sufficient understanding of information systems controls necessary to assess audit risk and plan the audit within the context of the audit objectives.

6. Did Not Document an Overall Assessment of Evidence

Auditors did not document an overall assessment of the collective evidence used to support the findings and conclusions.

Specifically, the auditors did not document an evaluation of their sampling methodology, sampling results, and other audit procedures to determine if the **evidence** they gathered was **sufficient** and **appropriate** to provide a reasonable basis for their findings and conclusions.

GAO Audit Standards require that:

8.108 Auditors should perform and document an overall assessment of the collective evidence used to support findings and conclusions, including the results of any specific assessments performed to conclude on the validity and reliability of specific evidence.

8.109 When assessing the overall sufficiency and appropriateness of evidence, auditors should evaluate the expected significance of evidence to the audit objectives, findings, and conclusions; available corroborating evidence; and the level of audit risk. If auditors conclude that evidence is not sufficient or appropriate, they should not use such evidence as support for findings and conclusions.

7. Didn't Extend Audit Procedures to Determine If Fraud Occurred

Auditors did not extend audit procedures to determine whether fraud had likely occurred when they identified instances that indicated a potential for collusion or fraud.

Department policy requires Divisions and contractors to prepare separate estimates of project costs. Then the Division compares its estimate to the contractor's proposal to evaluate the reasonableness of the proposed costs. Logically, there should be no instances where a Division employee prepared a contractor's estimate or vice versa.

However, in the work papers (WP 200.2) and on pages 15 and 16 of the report, auditors noted:

- 3 instances (8%) in one Division in which the preparer listed on the DOT estimate was the **same preparer** listed on the selected firm's estimate
- 1 instance (3%) in one Division in which the preparer listed on the firm estimate **was a Division employee**

Despite the questions that these instances raise, no additional work was documented for this issue.

GAO Audit Standards require that:

8.72 Assessing the risk of fraud is an ongoing process throughout the audit. When information comes to the auditors' attention indicating that fraud, significant within the context of the audit objectives, may have occurred, auditors should extend the audit steps and procedures, as necessary, to (1) determine whether fraud has likely occurred and (2) if so, determine its effect on the audit findings.