

Elizabeth Smith
Department Secretary



Ricky Quattlebaum
Director

**Department of Inspector General
Office of Internal Audit**

May 16, 2022

Senator Blake Johnson, Chair
Representative Ron McNair, Chair
Highway Commission Review and Advisory Subcommittee
of the Arkansas Legislative Council
One Capitol Mall, Fifth Floor
Little Rock, AR 72201

RE: Legislative Mandate for an Annual Project Review and Efficiency Study of the Arkansas Department of Transportation (ARDOT)

Dear Senator Johnson and Representative McNair:

Pursuant to Act 298 of 2019, Guidehouse, LLP, was hired to conduct a study of “the processes and functioning of the Arkansas Department of Transportation, including without limitation the department’s processes, procedures, procurement procedures, projects, expenditures, and appeals processes.” June 17, 2020, Guidehouse, LLP, presented a *Recommendations Report* to the Highway Commission Review and Advisory Subcommittee (HCRAS) of the Arkansas Legislative Council (ALC). On November 20, 2020, the final report of the ARDOT study was adopted by the ALC. The report included thirteen recommendations to be implemented. ARDOT submitted revised rules at the HCRAS meeting on April 21, 2022; these rules are a list of action items ARDOT intends to implement to satisfy the thirteen recommendations. ARDOT is required to report regarding the status of implementing the recommendations to the HCRAS monthly.

In addition, Act 298 of 2019 requires an annual review and efficiency study of ARDOT to be conducted by the Arkansas Department of Inspector General, Office of Internal Audit (OIA), with the results of the study due to ALC no later than October 1 of each year beginning in 2023. This letter will set forth the work plan for the performance of the annual review and efficiency study, which will also be referred to as the “engagement”.

OIA is required to adhere to the International Professional Practices Framework of the Institute of Internal Auditors, which includes the International Standards for the Professional Practice of Internal Auditing (IIA Standards). ACA §25-43-1004 (h)(2) IIA Standards define internal auditing as an “independent, objective assurance and consulting activity designed to add value and

improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes" (IIA, 2016, p. 23). Therefore, in compliance with Act 298 of 2019 and IIA standards, to conduct an annual review and efficiency study, the work will include components of both assurance services and consulting services. IIA Standards allow for both types of services to be performed by internal auditors. The following discussion includes relative language quoted from the IIA Standards along with how the work performed will be accomplished for this engagement.

Assurance Services

Assurance services are defined as "an objective examination of evidence for the purpose of providing an independent assessment on governance, risk management, and control processes for the organization. Examples may include financial, performance, compliance, system security, and due diligence engagements" (IIA, 2016, p. 21). "Assurance services involve the internal auditor's objective assessment of evidence to provide opinions or conclusions regarding an entity, operation, function, process, system, or other subject matters. The nature and scope of an assurance engagement are determined by the internal auditor" (IIA, 2016, p. 2).

The assurance services component of this engagement will be the independent assessment of the status of ARDOT's implementation of the Guidehouse, LLP recommendations. Specific work may include, but is not limited to, interviews with ARDOT personnel, review of information developed and produced by ARDOT related to the recommendations, and consideration of the results to determine if the recommendations have been implemented appropriately. Audit procedures will vary depending upon the nature of the management action items being assessed and level of assurance deemed necessary for the engagement.

The annual report will include, but is not limited to:

- A summary description of actual work performed by OIA staff,
- An opinion related to the adequacy of ARDOT's implementation of each recommendation, and
- Comments necessary to highlight any concerns or challenges which are material to the engagement.

Consulting Services

Consulting services are defined as "advisory and related client service activities, the nature and scope of which are agreed with the client, are intended to add value and improve an organization's governance, risk management, and control processes without the internal auditor assuming management responsibility. Examples include counsel, advice, facilitation, and training" (IIA, 2016, p. 22). "Consulting services are advisory in nature and are generally performed at the specific request of an engagement client. The

nature and scope of the consulting engagement are subject to agreement with the engagement client” (IIA, 2016, p. 2).

The consulting component of this engagement will be the review of ARDOT’s internal control design using the most recently submitted version of ARDOT’s control self-assessment (CSA). ARDOT has participated in the past with state agencies to complete a formal CSA; thus, participation is not new to the agency. The systematic process OIA will use allows for an in-depth study of operations related to the agency achieving current objectives; generally, it is not used to bring about recommendations which would create new objectives for the agency to attain.

CSA is an exercise conducted by agency management that utilizes feedback from employees to identify and assess risks which may hinder the agency from achieving its objectives. This practice also includes management’s evaluation of the current control activities in place to prevent, detect, and mitigate the impact of the identified risks. Based on this evaluation, management may determine it is necessary to implement changes or corrective action plans.

ARDOT’s management is responsible for the internal control design of the agency. CSA is a tool which management can use to assess the current internal control design and identify weaknesses which need to be addressed. Management must decide, using a cost/benefit analysis, how to make changes to processes, procedures, or policies to give reasonable assurance the agency will meet its objectives. OIA will assist in facilitating the CSA process by working with all levels of management (lower, middle, and upper) to determine if all objectives and major risks are identified and control activities documented are those being performed. OIA will assist in evaluating the design of control activities to ensure controls are designed to mitigate the associated risks and may present recommendations to ARDOT management in instances where control activities should be strengthened.

The concepts, definitions, and principles for internal control used will be in line with the *COSO Internal Control Integrated Framework*. The goal of OIA performing these consultation services will be to promote strengthening the internal control design of ARDOT. To accomplish this goal, OIA will identify the areas of ARDOT with the highest risk based upon the rating of established factors (such as turnover rate, the amount of funds flowing through an area, and previous audits conducted, etc.) and prioritize work beginning with the areas rated with the highest risk ranking. It is anticipated that each area of ARDOT will be reviewed at least once within a five-year period due to the size of ARDOT’s operations. OIA will keep a list of recommendations and management’s progress and resolutions. Follow up on issues which ARDOT cannot immediately address will be completed in the next year.

The annual report will include, but is not limited to:

- A summary description of actual work performed by OIA staff,

- The number of risks reviewed, the number of recommendations made by OIA, and the number of internal control changes made by management in each area reviewed as a result of the work completed. Specific details can be made available upon request,
- A narrative related to areas of concern, if any exist, and
- Comments necessary to highlight any concerns or challenges which are material to the engagement.

Consideration of Other Audit Functions

We believe the work described for this engagement will not be a duplication of effort of other audit functions, including but not limited to ARDOT's Internal Audit Section, Arkansas Legislative Audit, the Federal Highway Administration, the Federal Transit Administration, or others. OIA will consider the work completed for these audits to not overburden ARDOT in the specific audited areas.

Independence

Internal auditors are independent when they can carry out their work freely and objectively. Independence permits internal auditors to render the impartial and unbiased judgments essential to the proper conduct of work performed. The OIA is organizationally independent of ARDOT. OIA personnel are independent of ARDOT management because OIA is organizationally structured as an office within the Arkansas Department of the Inspector General.

We appreciate the opportunity to perform the work, and believe this letter accurately summarizes the significant terms of our engagement. If the desired purpose differs from the one described above, or if due to the passage of time or changing conditions of the engagement environment, different or additional work is determined to be required, we will gladly revisit modification of the plan set forth in this letter.

Sincerely,



ELIZABETH THOMAS SMITH
CABINET SECRETARY
Department of the Inspector General

Reference: *The Institute of Internal Auditors IIA Standards (2016, October; effective 2017, January).*
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<https://www.theiia.org/globalassets/documents/standards/standards-2017/ippf-standards-2017-english.pdf>