## 2017-001 The Department of Ecology did not have adequate internal controls over fee collections for the vehicle emission testing program

### *Background*

The Clean Car Law (RCW 70.120A.010) requires vehicles across the state to be certified to California emission standards. New vehicles that do not meet these standards cannot be registered, licensed, rented or sold for use in Washington. For model year vehicles 1991 through 2008, an emission test is required every two years if the owner of the vehicle resides in the following counties: Clark, Spokane, Pierce, Snohomish and King, which are considered "emission-contributing areas." The law exempts vehicles over 25 years old from these emission standards.

The Department of Ecology (Department) administers a Department of Enterprise Services (DES) contract with a vendor to conduct emission tests in emission-contributing areas. When a vehicle passes an emission test, the vendor communicates the results to the Department of Licensing, enabling the vehicle's owner to renew license tabs.

The vendor must collect a fee for each emission test. Three dollars of each fee collected, net of certain expenses, is remitted to the State General Fund. The Department separately receives an appropriation from the legislature to cover program administration. The Department also receives invoices with supporting documentation from the vendor each week describing the number of emissions tests, adjustments and deductions. According to the contract, the vendor may deduct expenses such as service maintenance and wireless communication charges. The State General Fund received nearly $2.4 million in vehicle emission test fees in fiscal year 2017.

In our fiscal year 2015 accountability audit, we reported that the Department did not adequately monitor the contract to ensure the vendor accurately collected and remitted fees. The Department said it did not implement its corrective action until the end of fiscal year 2017; therefore, we chose to examine the Department's activities from June through December 2017

## *Description of Condition*

The Department did not adequately monitor its contract to ensure the vendor accurately collected and remitted fees.

The Department received invoices with supporting documentation from the vendor detailing the number of emission tests, adjustments and deductions. We found the Department verified that the amount of fee revenue deposited in the state's accounting system matched the amount shown on the invoices; however, it did not reconcile the supporting documentation to the invoice to ensure the fee revenue was accurate.

We also found the Department did not adequately review deductions the vendor made to ensure they were allowable and supported.

## *Cause of Condition*

The Department did not implement procedures to effectively monitor the vendor's fiscal activities and ensure all deductions and adjustments were allowable. The Department also was not familiar with the terms and conditions of the contract with the vendor.

## *Effect of Condition*

By not adequately monitoring the vendor's activities, the Department cannot ensure it collects all the revenue from the vendor that is owed to the state.

We examined all deductions the vendor made between June 18 and December 23, 2017 and found $1,376 in deductions were made for customer wait times that were not allowed by the contract.

## *Recommendation*

We recommend the Department:

- Improve its process for reviewing vendor invoices by reconciling supporting documentation to invoices to ensure all fee revenue has been collected
- Ensure staff responsible for performing the review understand the contract's terms and conditions
- Recover improper deductions made by the vendor

## *Department's Response*

*Ecology will include in reconciliation process, verifying supporting documentation to the invoice and ensuring the monthly vendor (Applus) report is for the same timeframe as the weekly invoices.*

*We will also work with DES and the vendor, Applus, to exclude non-legitimate waiting times from the revenue reported to Ecology. We will also work with the vendor and DES to decide if any exclusions were not appropriate per the contract.*

## *Auditor's Remarks*

We appreciate the Department's commitment to monitor and improve its internal control processes for the Vehicle Emission program.

## *Applicable Laws and Regulations*

The Revised Code of Washington 46.16A.060 states:

> Registration – Emission control inspections required – Exemptions – Educational information – Rules.
>
> (1) The department, county auditor or other agent, or subagent appointed by the director may not issue or renew a motor vehicle registration or change the registered owner of a registered vehicle for any motor vehicle required to be inspected under chapter 70.120 RCW, unless the application for issuance or renewal is: (a) Accompanied by a valid certificate of compliance or a valid certificate of acceptance issued as required under chapter 70.120 RCW; or (b) exempt, as described in subsection (2) of this section. The certificates must have a date of validation that is within twelve months of the assigned registration renewal date. Certificates for fleet or owner tested diesel vehicles may have a date of validation that is within twelve months of the assigned registration renewal date.
>
> (2) The following motor vehicles are exempt from emission test requirements:
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> > (a) Motor vehicles that are less than five years old or more than twenty-five years old;
> >
> > (b) Motor vehicles that are a 2009 model year or newer;
> >
> > (c) Motor vehicles powered exclusively by electricity, propane, compressed natural gas, liquefied natural gas, or liquid petroleum gas;

(d) Motorcycles as defined in RCW 46.04.330 and motor-driven cycles as defined in RCW 46.04.332;

(e) Farm vehicles as defined in RCW 46.04.181;

(f) Street rod vehicles as defined in RCW 46.04.572 and custom vehicles as defined in RCW 46.04.161;

(g) Used vehicles that are offered for sale by a motor vehicle dealer licensed under chapter 46.70 RCW;

(h) Classes of motor vehicles exempted by the director of the department of ecology;

(i) Hybrid motor vehicles that obtain a rating by the environmental protection agency of at least fifty miles per gallon of gas during city driving. For purposes of this section, a hybrid motor vehicle is one that uses propulsion units powered by both electricity and gas; and

(j) Collectible vehicles as defined in RCW 46.04.123.

(3) The department of ecology must provide information to motor vehicle owners:

(a) Regarding the boundaries of emission contributing areas and restrictions established under this section that apply to vehicles registered in such areas; and

(b) On the relationship between motor vehicles and air pollution and steps motor vehicle owners should take to reduce motor vehicle related air pollution.

The Revised Code of Washington 70.120A.010 states:

Department of ecology to adopt rules to implement California motor vehicle emission standards – Limitations – Advisory group – Exemptions.

(1) Pursuant to the federal clean air act, the legislature adopts the California motor vehicle emission standards in Title 13 of the California Code of Regulations, effective January 1, 2005, except as provided in this chapter. The department of ecology shall adopt rules to implement the emission standards of the state of California for passenger cars, light duty trucks, and medium duty passenger vehicles, and shall amend the rules from time to time, to maintain consistency with the California motor vehicle emission standards and 42 U.S.C. Sec. 7507 (section 177 of the federal clean air act). Notwithstanding other provisions of this chapter, the department of ecology shall not adopt the zero emission vehicle program

regulations contained in Title 13 section 1962 of the California Code of Regulations effective January 1, 2005. During rule development, the department of ecology shall convene an advisory group composed of industry and consumer group representatives. Any proposed rules or changes to rules shall be subject to review and comment by the advisory group, prior to rule adoption. The order of adoption for the rules required in this section shall include the signature of the governor. The rules shall be effective only for those model years for which the state of Oregon has adopted the California motor vehicle emission standards. This section does not limit the department of ecology's authority to regulate motor vehicle emissions for any other class of vehicle.

(2) Motor vehicles with a model year equal to or later than the first model year for which new vehicles sold to Washington state residents are required to comply with California motor vehicle emission standards are exempt from emission inspections under chapter 70.120 RCW.

(3) The provisions of this chapter do not apply with respect to the use by a resident of this state of a motor vehicle acquired and used while the resident is a member of the armed services and is stationed outside this state pursuant to military orders.

The Revised Code of Washington 43.88.160 states, in part:

Fiscal management—Powers and duties of officers and agencies.

This section sets forth the major fiscal duties and responsibilities of officers and agencies of the executive branch. The regulations issued by the governor pursuant to this chapter shall provide for a comprehensive, orderly basis for fiscal management and control, including efficient accounting and reporting therefor, for the executive branch of the state government and may include, in addition, such requirements as will generally promote more efficient public management in the state . . .

(4)(a) Develop and maintain a system of internal controls and internal audits comprising methods and procedures to be adopted by each agency that will safeguard its assets, check the accuracy and reliability of its accounting data, promote operational efficiency, and encourage adherence to prescribed managerial policies for accounting and financial controls. The system developed by the director shall include criteria for determining the scope and comprehensiveness of internal controls required by classes of agencies, depending on the level of resources at risk.

The Office of Financial Management's State Administrative and Accounting Manual (SAAM) states in part:

20.15.10 Internal control definition

Internal control is a process, effected by those charged with governance, management, and other employees, designed to provide reasonable assurance regarding the achievement of the entity's objectives relating to operations, reporting, and compliance. For purposes of Chapter 20, the state's internal control objectives are defined as the need for each agency to:

- Safeguard its assets.
- Check the accuracy and reliability of its accounting data.
- Promote operational efficiency.
- Encourage adherence to policies for accounting and financial controls.

The definition of internal control emphasizes that internal control is:

- Geared to the achievement of objectives in one or more separate but overlapping categories – operations, reporting, and compliance.
- A process consisting of ongoing tasks and activities – a means to an end, not an end in itself.
- Effected by people – not merely about policy and procedure manuals, systems, and forms, but about people and the actions they take at every level of an organization to effect internal control.
- Able to provide reasonable assurance – but not absolute assurance, to an entity's management.
- Adaptable to the entity structure or size – flexible in application for the entire entity or for a subset of an entity.

This definition of internal control is intentionally broad. It incorporates concepts that are fundamental to how entities design, implement, and operate a system of internal control and assess its effectiveness.

20.15.20 Roles and Responsibilities:

Agency management is responsible for the agency's operations, compliance and financial reporting objectives. Therefore, the adequacy of internal control to provide reasonable assurance of achieving these objectives is also the responsibility of management. That said, every state employee has a role in effecting internal control. Roles vary in responsibility and level of involvement, as discussed below.

Given agency structure and size, individuals may assume multiple roles. However, care should be taken to address the increased risk that may result from the concentration of responsibilities.

20.15.20.a

Those charged with governance are responsible for overseeing the strategic direction of the agency and obligations related to the agency's accountability. This includes overseeing the design, implementation, and operation of an effective internal control system. For most agencies, those charged with governance include the agency head and members of agency senior management. For agencies with a governing board, the board may appoint individuals to fulfill this function.

20.15.20.b

The agency head is ultimately responsible for identifying risks and establishing, maintaining, and monitoring the agency's system of internal control. If the agency head delegates this responsibility, the designated person should have sufficient authority to carry out these responsibilities. The agency head together with those charged with governance and agency management set the tone at the top that affects the control environment in particular and all other components of internal control. The agency head signs the annual Financial Disclosure Certification and, if applicable, the Federal Assistance Certification.

20.15.20.c

The internal control officer (ICO) is responsible for coordinating the agency-wide effort of evaluating internal control using the guidance in this chapter. The ICO coordinates the agency's required risk assessment and internal control monitoring activities and annually provides written assurance to the agency head as required in Subsection 20.15.30. While each agency is required to have an ICO, the ICO may perform these duties on a full-time basis or on a part-time basis as long as other duties performed are not incompatible with the ICO duties.

20.15.20.d

Agency management at all levels is responsible for internal control under their span of control. Management is responsible to communicate to agency employees their explicit or implicit control activity duties. In addition, agency management should provide channels outside normal reporting lines so agency employees can report noncompliance, problems in operations, and illegal acts.

Management is also responsible to convey the importance of internal control to all employees both by what they say and what they do. If management is willing to override controls, then the message that internal control is not important will be conveyed to employees.

20.24.10 Control activities overview:

Control activities are policies, procedures, techniques, and mechanisms that help ensure that risks to the achievement of an agency's objectives are mitigated. Control activities are performed at all levels of the agency, at various stages within business processes, and over the technology environment. They may be preventive or detective in nature. Preventive controls are designed to deter the occurrence of an undesirable event by implementing procedures to avoid them. Detective controls are designed to identify undesirable events that do occur and alert management about what has happened.

When designing and implementing control activities, management should consider cost versus benefit and the likelihood and impact of the associated risk. Building control activities into business processes and systems as they are being designed is generally more cost-effective than adding them later.

20.28.10 Monitoring overview:

Monitoring is the process of evaluating the quality of internal control performance over time and promptly addressing internal control deficiencies. Monitoring can take the form of ongoing evaluations, which are built into business processes at different levels of the agency, or separate evaluations, which are conducted periodically and vary in scope and frequency, depending on assessment of risks, effectiveness of ongoing evaluations, and other management considerations.

Monitoring of the internal control system is essential in helping internal control remain aligned with changing objectives, environment, laws, resources, and risks.

20.28.30 Monitoring versus control activities:

It can be difficult to distinguish between a review that is a control activity and one that is a monitoring activity. Some judgment is involved but determining the intent of the activity can help. An activity designed to detect and correct errors is likely a control activity, while an activity designed to ask why there were errors in the first place and assign responsibility for fixing the process to prevent future errors is likely a monitoring activity. In other words, a control activity responds to a specific risk, while a monitoring activity assesses whether controls within each of the five components of internal control are operating as intended.