

NEW YORK STATE
ENERGY RESEARCH AND DEVELOPMENT AUTHORITY

INTERNAL CONTROL MANUAL:
Ensuring Efficiency, Accountability, and Transparency

Revised June 2014

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SECTION 1: PURPOSE; BOARD MEMBER RESPONSIBILITIES

The purpose of this manual is to set forth NYSERDA's policies and procedures for ensuring an effective system of internal controls that also promotes accountability and transparency.

Public Authorities Law, Article 9, Title 8, §2931, known as the New York State Governmental Accountability Audit and Internal Control Act ("Internal Control Act") requires NYSERDA to establish and maintain a system of internal controls. The Internal Control Act defines internal controls as a "process that integrates the activities, plans, attitudes, policies, systems, resources and efforts of the people of an organization working together, and that is designed to provide reasonable assurance that the organization will achieve its objectives and mission" (Article 9, §2930).

The Internal Control Act lists specific objectives of an internal control system including, but not limited to:

- the safeguarding of assets;
- checking the accuracy and reliability of accounting data and financial reporting;
- promoting the effectiveness and efficiency of operations;
- ensuring compliance with applicable laws and regulations; and
- encouraging adherence to prescribed managerial policies.

The Public Authorities Accountability Act of 2005, which amends various sections of the Public Authorities Law, seeks to ensure greater efficiency, openness and accountability for the State's public authorities by codifying model governance principles, removing legal impediments that prevent full implementation of model governance principles, establish a new public authorities office within the Executive Department to provide additional oversight and ensure full compliance with the principles, and allow for the creation of an independent inspector general to ensure greater accountability for public authority activities and operations.

As explained below and through their review and approval of various guidelines, reports, planning documents, and other activities of NYSERDA staff, NYSERDA's Board Members are actively engaged in overseeing NYSERDA use of processes, policies, and procedures that accomplish NYSERDA's mission through an effective system of internal controls that incorporates accountability and transparency.

Board Member Internal Control Responsibilities. The Internal Control Act requires that the governing board of NYSERDA:

- establish and maintain for NYSERDA guidelines for a system of internal control that are in accordance with this article and internal control standards;
- establish and maintain for NYSERDA a system of internal control and a program of internal control review. The program of internal control review shall be designed to identify internal control weaknesses, identify actions that are needed to correct actions and periodically assess the adequacy of NYSERDA's ongoing internal controls;
- make available to each Board Member, officer and employee a clear and concise statement of the generally applicable managerial policies and standards with which he or she is expected to comply. Such statement shall emphasize the importance of effective internal control to NYSERDA and the responsibility of each Board Members, officer and employee for effective internal control;

- designate an internal control officer, who shall report to the head of NYSERDA, to implement and review the internal control responsibilities established pursuant to this section;
- implement education and training efforts to ensure that Board Members, officers and employees have achieved adequate awareness and understanding of internal control standards and, as appropriate, evaluation techniques; and
- periodically evaluate the need for an internal audit function.

Board Member Accountability Responsibilities, The Public Authority Accountability Act of 2005 requires the Board Members to:

- execute direct oversight of NYSERDA's President and CEO and other senior management in the effective and ethical management of NYSERDA;
- understand, review and monitor the implementation of fundamental financial and management controls and operational decisions of NYSERDA;
- establish policies regarding the payment of salary, compensation and reimbursements to, and establish rules for the time and attendance of the President and CEO and senior management;
- adopt a code of ethics applicable to each officer, director and employee that, at a minimum, includes the standards established in section seventy-four of the public officers law;
- establish written policies and procedures on personnel including acts of wrongdoing, misconduct, malfeasance, or other inappropriate behavior by an employee or Board Member of NYSERDA, investments, travel, the acquisition of real property and the disposition of real and personal property and the procurement of goods and services;
- adopt a defense and indemnification policy and disclose such plan to any and all prospective Board Members; and
- attend State approved training, including such continuing training as may be required to remain informed of best practices, regulatory and statutory changes relating to the effective oversight of the management and financial activities of public authorities and to adhere to the highest standards of responsible government.

Through all of the processes, policies, and procedures set forth in this manual, the three underlying manuals (the Personnel Handbook, Information Security Policies Manual, Accounting Policies and Procedures Manual, and Operations and Procedures Manual), and through its review and approval of a diverse set of guidelines, reports, planning documents and more detailed Committee review of staff activities, NYSERDA's Board Members comply with these statutory requirements.

NYSERDA's Board has established the following standing committees:

Audit and Finance Committee. The Audit and Finance Committee is a standing advisory committee of the Authority. The Committee has not fewer than three or more than six Board Members. The Committee shall consist of not less than three independent Board Members who shall constitute a majority on the Committee and who shall possess the necessary skills to understand the duties and function of the Committee, provided, however, that in the event that there are less than three independent Members, the Members may appoint non-independent Members, provided that the independent Members constitute a majority of the Members of the Committee. In addition, the membership of the Committee includes the Chair of the Authority who serves ex-officio and who enjoys all the rights and privileges of membership, including the right to vote. A majority of the members of the Committee then in office, not including the Chair of the Authority, gathered together in the presence of each other or through the use of

videoconferencing, constitutes a quorum, and the Chair of the Authority if present counts toward a quorum. Members of the Committee shall be familiar with corporate financial and accounting practices.

The Audit and Finance Committee recommends the hiring of a certified independent accounting firm, establishes the compensation to be paid, and provides direct oversight of the performance of the independent audit performed, reviews the annual financial statements of the Authority prior to submission for approval to the Board Members of the Authority, reviews proposals for the issuance of debt by the Authority and makes recommendations, and may examine and consider such other matters in relation to the internal and external audit of the Authority's accounts, the Authority's financings, and in relation to the financial affairs of the Authority and its accounts as the Audit and Finance Committee may determine to be desirable.

Program Planning Committee. The Program Planning Committee is a standing advisory committee of the Authority. The Committee has not fewer than three or more than six Board Members, who are elected from among the Board Members of the Authority other than the Chair. A majority of these committee members are other than Board Members of the Authority who serve ex-officio. In addition, the membership of the Committee includes the Chair of the Authority, who serves ex-officio and who enjoys all the rights and privileges of membership, including the right to vote. A majority of the members of the Committee then in office, not including the Chair, gathered together in the presence of each other or through the use of videoconferencing, constitutes a quorum, and the Chair of the Authority if present counts toward a quorum.

The Program Planning Committee reviews the annual updating of the Authority's Multi-Year Strategic Program Plan; and preparation of the portions of the Authority's annual budget related to the energy research and development programs, the energy services programs, the energy analysis program, and the economic development program; and provides guidance to the Authority's officers and employees in the preparation of those plans and those portions of the budget; and considers such other matters related to the Authority's energy research and development programs, energy services programs, energy analysis program, and economic development program as the officers of the Authority may refer to the Committee.

Waste and Facilities Management Committee. The Waste and Facilities Management Committee is a standing advisory committee of the Authority. The Committee has not fewer than three or more than six members, who are elected from among the Board Members of the Authority other than the Chair. A majority of these committee members are other than Board Members of the Authority who serve ex-officio. In addition, the membership of the Committee includes the Chair of the Authority, who serves ex-officio and who enjoys all the rights and privileges of membership, including the right to vote. A majority of the members of the Committee then in office, not including the Chair of the Authority, gathered together in the presence of each other or through the use of videoconferencing, constitutes a quorum, and the Chair of the Authority if present counts toward a quorum.

The Waste and Facilities Management Committee reviews the Authority's program and plans for management of the Western New York Nuclear Service Center, including the West Valley Demonstration Project, and for radioactive waste policy and nuclear coordination; reviews the preparation of the Authority's annual West Valley site management program and radioactive waste policy and nuclear coordination budgets; provides guidance to the Authority's officers and

employees in the preparation of the plans and in preparation of such annual program budgets; and considers such other matters related to West Valley site management and radioactive waste policy and nuclear coordination programs as the Officers of the Authority may refer to such Committee.

Governance Committee. The Governance Committee is a standing advisory committee of the Authority. The Committee shall consist of not less than three independent Members who shall constitute a majority on the Committee and who shall possess the necessary skills to understand the duties and function of the Committee, provided, however, that in the event that there are less than three independent Members, the Members may appoint non-independent Members, provided that the independent Members constitute a majority of the Members of the Committee. The Committee has not fewer than three or more than six members. In addition, the membership of the Committee includes the Chair of the Authority who shall serve ex-officio and who enjoys all the rights and privileges of membership, including the right to vote. A majority of the members of the Committee then in office, not including the Chair of the Authority, gathered together in the presence of each other or through the use of videoconferencing, constitutes a quorum, and the Chair of the Authority if present counts toward a quorum.

The Governance Committee keeps the Board Members informed of current best practices, reviews corporate governance trends, updates the Authority's corporate governance principles, as necessary, recommend updates to the corporate governance principles, advises appointing authorities on the skills and experience required of Board Members, examine ethical and conflict of interest issues, perform Board self-evaluation, and recommend By-laws which include rules and procedures for conduct of Board business.

All meetings of the Authority subject to the Open Meetings Law will be broadcast on the Internet.

Board Member Compliance with Lobbying Laws

Procurement Lobbying: State Finance Law Sections 139-j and 139-k applies to all solicitations issued and procurements under active consideration that may result in a procurement contract in an amount in excess of \$15,000. Such solicitations and procurements under consideration must: (1) designate individuals at NYSERDA who may be contacted about the procurement by persons attempting to influence the procurement process (*i.e.*, offerers and persons hired by the offerer who attempt to influence the procurement), and (2) outline NYSERDA's procedures relating to contacts that are not permitted under the State Finance Law. All solicitations and procurements will identify NYSERDA employees, and not Board Members, as the individuals that may be contacted under such circumstances.

The responsibility to record information about contacts that reasonably appear to be attempts to influence the procurement process applies during the "restricted period." The restricted period begins once NYSERDA has made a decision to initiate procurement and extends until execution of the contract. It begins again at any time a modification to the contract is proposed and extends until the modification is executed.

The decision to initiate procurement occurs at the earliest of: (1) the Project Development Management Committee's or Management Review Committee's approval of the proposed issuance of a solicitation, (2) an employee's receipt of a proposal for a program project that does not meet the definition of Competitive Procurement Method under the Procurement Contract Guidelines, or (3) at such other time when a determination is made to proceed with an

administrative procurement. At this time and until the time a contract is executed, Board Members must: (1) record information regarding contacts that reasonably appear to be attempts to influence the procurement process within the restricted period, and (2) submit the record to NYSERDA's Director of Contract Management who will maintain such records in the appropriate file. The record is to include the contact including the name, the organization, the address, the telephone number, the place of principal employment, and the occupation of the contact and whether the person or organization making the contact is a "potential contractor" or is retained, employed, or designated by the potential contractor to appear before or to contact the agency regarding the procurement.

Failure to comply with the requirements may result in a contractor being barred from governmental procurements. Board Members should contact the General Counsel if they have any questions concerning these requirements.

Project Sunlight: Project Sunlight, a component of the Public Integrity Reform Act of 2011, is intended to provide the public with an opportunity to see when outside individuals and entities are interacting with—and attempting to influence—state government decision-makers in particular ways. Project Sunlight requires the reporting in an online database of all interactions that constitute "appearances" between "covered individuals" inside NYSERDA and "covered individuals" outside NYSERDA concerning one of five designated Project Sunlight subject areas.

An "appearance" is an in-person meeting, telephonic conversation, or video conference that is a substantive interaction meant to influence state government decision-making. The location, formality, and initiator of the interaction are irrelevant. Excluded from "appearance" are all written communications; administrative or ministerial interactions; purely informational exchanges; interactions regarding legislation or the budget; and meetings that are open to the public. NYSERDA "covered individuals" are those individuals designated as "policy-makers," which includes Board Members. "Covered individuals" outside NYSERDA include internal and external representatives of outside entities, individuals representing themselves, and representatives of advocacy groups. Not included are employees of other state agencies and of other governments; state elected officials, executive and legislative employees, judges, and employees of the judiciary; representatives of the media; and persons under the age of 18. An "appearance" between "covered individuals" must be reported if it concerns one of five designated subject areas: procurement (outside of the restricted period defined by the Procurement Lobbying Law), regulatory matters, rule making, judicial or quasi-judicial proceedings, and rate making.

Reportable appearances must be timely recorded in the database, within five business days after they occur. NYSERDA covered individuals complete the Project Sunlight reporting form available on NYSERDA's intranet and emails it to the dedicated email inbox: projectsunlight@nyserda.ny.gov. NYSERDA's Project Sunlight Liaison, designated by the General Counsel, coordinates and oversees NYSERDA's reporting efforts. Board Members should contact the Project Sunlight Liaison or General Counsel if they have any questions concerning these requirements.

Regulatory Lobbying: Public Authorities Law §2987 requires every Member, Officer, or employee to record all contacts, whether oral or written, that are an attempt to influence the adoption or rejection of any rule or regulation having the force and effect of law that is issued by NYSERDA. The record must include the day and time of the contact, the identity of the lobbyist,

and a general summary of the substance of the contact. NYSERDA shall maintain these records for not less than seven years.

INTERNAL CONTROL POLICY

It is the responsibility of every employee to abide by the requirements of the internal controls system. All employees are expected to be aware of NYSERDA's internal controls system and regularly consider the system in performing their tasks. NYSERDA has prepared a Code of Conduct, attached hereto as Appendix B, summarizing a number of basic standards and State and Federal laws which NYSERDA employees are required to follow. The Code of Conduct sets forth NYSERDA's expectations that its employees conduct themselves in an honest and ethical manner and is provided to all employees.

If an employee identifies a potential weakness in, or deviation from, NYSERDA's internal control systems or generally accepted systems of internal controls, he or she shall report such potential weakness or deviation immediately in accordance with NYSERDA's Whistleblower Policy, attached hereto as Appendix C.

INTERNAL CONTROL SYSTEM

The procedures herein establish checks and balances over NYSERDA's administration and operations practices, financial and accounting practices and personnel practices, regularly reviewing the adequacy of the controls, especially in areas of highest vulnerability, revising those controls as necessary to reflect organizational changes, new program mandates or staffing adjustments, and taking corrective action when internal control weaknesses are identified. NYSERDA stresses to its Directors and they to their staffs the importance of communicating and adhering to the policies and procedures in the Internal Control System.

The Internal Control Officer is responsible for assisting with the implementation and review of the internal control system and for implementing education and training of staff.

All employees and officers have access to all the manuals that comprise the internal control system which are:

- Internal Control Manual – the compilation of the accounting, operating and administrative controls of NYSERDA as described more fully in the following manuals:
- Operations and Procedures Manual – details the policies and procedures followed in planning and implementing NYSERDA's programs and administration, including its contracting process to ensure compliance with State statutes, regulatory requirements and Executive Orders;
- Accounting Policies and Procedures Manual – details the financing and accounting practices; and
- Personnel Handbook – details NYSERDA's personnel practices and policies which apply to all employees.
- Information Security Policies Manual – details policies regarding computer information system policies and procedures.

This manual also summarizes the primary functions and control objectives of each of NYSERDA's assessable units. Assessable units are defined in the Comptroller's Internal Control Standards, as units

which perform a distinct function or service and/or that fulfill a law, regulation or mandate. NYSERDA's assessable units include:

- Energy Research and Development, Energy Services
- Energy Analysis
- Radioactive Waste Management
- Bond Financing
- Contracts Management
- Accounting
- Human Resources
- Computer Systems
- Counsel's Office
- Governmental Affairs
- Communications
- Marketing and Economic Development
- Consumer Services and Events Management
- Internal Audit

All staff shall maintain NYSERDA records in accordance with the General Retention and Disposition Schedule for New York State Government Records.

INTERNAL CONTROL TRAINING AND AWARENESS

The Internal Control Officer shall coordinate training and awareness activities to ensure that all NYSERDA employees have an understanding of internal control principles and how they relate to the performance of their work assignments.

In addition, the Internal Control Officer and executive management shall periodically communicate to NYSERDA staff regarding internal control principles and responsibilities, not less frequently than once each year.

INTERNAL CONTROL REVIEW PROCESS

The Internal Control Officer shall coordinate a process of organization-wide risk assessment not less frequently than once every three years. The risk assessment shall identify significant risks which threaten the achievement of unit/organizational objectives, the controls in place to eliminate or mitigate these risks, and an assessment of the relative likelihood of occurrence and the impact of such risks (using a rating system to be established by executive management). Each risk assessment shall be reviewed and approved by the manager's supervisory personnel through executive management, and shall also be provided to the Director of Internal Audit for review and comment. The results of the organization wide risk assessment shall be communicated to the Audit and Finance Committee for review and comment.

In addition, the Internal Control Officer shall convene a multi-disciplinary internal control working group not less frequently than once a year to review NYSERDA's internal control policies and procedures, organizational structure and inventory of functions, and to consider and recommend changes to improve internal controls.

The Internal Control Officer shall be responsible for monitoring the implementation of corrective actions which result from internal control reviews, internal control testing, internal audit reports, or reports issued

by external auditors related to internal control matters. The Internal Control Officer shall provide a report to the President and CEO not less frequently than annually summarizing the status of all such corrective actions.

INTERNAL CONTROL TESTING

To supplement the ongoing evaluation of the adequacy of NYSERDA's internal controls, NYSERDA shall conduct periodic compliance testing, at least annually, to determine the extent to which staff follow prescribed policies and procedures.

ANNUAL REPORTING

NYSERDA prepares the annual report required by Section 2800 of the Public Authorities Law and submits it to the Board Members for review and approval. The report is certified in writing by the President and CEO and the Treasurer that based on his or her knowledge the information provided therein is accurate, correct and does not contain any untrue statement of material fact, does not omit any material fact which, if omitted, would cause the financial statements to be misleading in light of the circumstances under which such statement are made and fairly presents in all material respects the financial condition and results of operations of NYSERDA as of and for the periods presented in the report.

Attached as part of the annual report is a copy of the annual independent audit report, performed by a certified public accounting firm in accordance with generally accepted government auditing standards, and management letter with any other external examination of the books and accounts (other than reports of any examinations made by the State Comptroller).

This annual report is submitted to the persons designated by Sections 2800 and 2802 of the Public Authorities Law.

NYSERDA also submits the annual internal control certification and report in accordance with requirements established by the Division of the Budget.

SECTION 2: ENERGY PROGRAMS

(ENERGY EFFICIENCY SERVICES, RESIDENTIAL EFFICIENCY SERVICES, NEW YORK CITY REGIONAL OFFICE, CLEAN ENERGY RESEARCH AND MARKET DEVELOPMENT, AND ENERGY EFFICIENCY RESEARCH)

Primary Functions

Program Planning
Program Development
Project Development
Project Management
Metrics Reporting

Controls

Program Planning

NYSERDA's Multi-Year Strategic Program Plan (Plan) includes goals, objectives, and funding for each program. Staff presents the Plan to NYSERDA's Program Planning Committee annually for review and approval. The Program Planning Committee is composed of NYSERDA Board members and is charged with reviewing, amending, and recommending approval of the Plan to the members of the Board. NYSERDA's Board must approve the Plan before it can be implemented by NYSERDA.

Program Development

Programs must operate in manner that is consistent with the Plan as approved by NYSERDA's Board. Programs must operate in a manner that is also consistent with any approved operating plan, funding agreement, Public Service Commission Order, law or regulation related to the program funding source. The Vice President for Operations and Energy Services shall be responsible for the Authority's operations and the discharge of the Authority's energy services programs. The Vice President for Technology and Strategic Planning shall be responsible for the energy research, planning, and analysis functions of the Authority. The Directors of the energy services programs report to the Vice President for Operations and Energy Services. The Directors of the research and development programs report to the Vice President for Technology and Strategic Planning. The Director of each program is primarily responsible for development and implementation of their program, for consistency with the Board-approved Plan, and for ensuring the collection and tracking of all required information and metrics needed for compliance filings according to the Public Authorities Law and other statutory and administrative requirements.

Project Development

Projects selected for funding must be consistent with the goals and objectives of the Plan. Pursuant to NYSERDA's Procurement Contracts Guidelines, as adopted by the Board, NYSERDA competitively procures goods and personal services contracts in all program areas. The only exceptions to this policy approved by the Board are: (1) goods or services valued at \$50,000.00 or less; (2) the goods, personal services, Authority program work, or other administrative services involved are expected to cost \$200,000 or less and are procured from a Minority Business Enterprise or Women-Owned Business Enterprise; (3)

unsolicited proposals submitted at the sole initiative of the proposer, not duplicating work being performed, not in the project planning request stage, and involving unique, innovative, and unusually meritorious methods or ideas; and (4) the Chair or President and CEO determines and certifies that a sole source contract is justified.

Before solicitations are issued to the public, a Project Planning Request (PPR) form describing the proposed solicitation must be approved by a multi-disciplinary team (Team) comprised of: the Program Manager, the Program Director, an assigned attorney from Counsel's Office, and an assigned contract administrator from the Contracts Management department. Once approved by the Team, the request is presented for approval to the Program Development and Management Committee (PDMC). The PDMC is a panel chaired by the President and CEO, or designee, and internal experts from NYSERDA who conduct a peer review of the PPR. The Director of Contract Management prepares written minutes from the PDMC meeting to document any recommendations and the PDMC's approval or denial of the request. Once the PPR is approved by the PDMC, the solicitation is prepared and reviewed and approved by the Team. The Project Manager completes the necessary authorization forms. The PDMC or Vice President for Operations and Energy Services determines whether the solicitation should be reviewed by a Technical Evaluation Panel (TEP) before it is issued.

Responses to competitive solicitations are reviewed by a TEP composed of participants recommended by the Project Manager and approved by the Director of the involved program. Each TEP must include at least three outside experts. If more than one program area funds a solicitation, Directors of all participating program areas must approve the participants in the TEP. TEPs shall include a number of outside reviewers at least equal to the number of NYSERDA staff reviewers, except that in the case of TEPs for system benefits charge (SBC) funded and Energy Efficiency Portfolio Standard (EEPS) funded projects, TEPs shall have more outside reviewers than NYSERDA staff, and shall include representation from the NYS Department of Public Service.

The TEP shall rank responses to solicitations based upon criteria presented in the solicitation. This may include a mix of technical merit, business experience, cost, and impacts to New York State. The Project Manager summarizes in writing the recommendations of the TEP. The Project Manager then convenes a meeting of the Team to review the recommendations of the TEP and make final recommendations to a Management Review Committee (comprised of the Vice President for Operations and Energy Services, the Vice President for Technology and Strategic Planning, the Director of Contract Management, and the General Counsel) for approval of the contract(s) to be awarded. At the discretion of either Vice President, the results may be presented to the PDMC.

If substantial programmatic reasons exist, changes can be made to the rank order recommended by the TEP. Acceptable substantial programmatic reasons include: projects do not have sufficient New York State presence; projects are not consistent with the Plan approved by the Board; and projects are duplicative of work already being done by NYSERDA. Changes to the rank order based upon substantial programmatic reasons must be approved by the President and CEO or designee.

In the case of non-competitive proposals, proposals are reviewed by a Technical Review Committee (TRC) prior to proceeding to contract, unless such review is waived by the PDMC. TRCs have participation requirements similar to those described above for TEPs and are composed of NYSERDA staff and outside reviewers. TRCs shall provide a recommendation for funding non-competitive projects, and the approval of each project shall be reviewed and approved by Management Review Committee or, at the request of either Vice President, by the PDMC.

Project Management

The Project Manager is responsible for developing, in conjunction with the contractor, a clear and defined project statement of work (SOW), budget, and implementation schedule. The Project Manager is responsible for monitoring and oversight of the contractor's performance to ensure that it adheres to the work required under the contract while anticipating and resolving technical and administrative problems arising during the project. Project Managers communicate with contractors, review progress reports, conduct site visits, review and approve contractor invoices, review and approve technical reports, and approve final project reports.

Metrics reporting

Programs shall be responsible for collecting all relevant data to measure program progress according to predetermined metrics, such as data that can be used to address the anticipated energy, environmental and economic benefits that are realized by projects, and as required by each operating plan or reporting requirement. All estimates shall reference credible sources and estimating procedures, and all assumptions shall be documented. This data will also be used to evaluate program impacts and progress towards goals.

SECTION 3: NY GREEN BANK

Primary Functions

Business Planning
Business Operation
Procurement Activities
Financial Investments
Portfolio Management
Metrics Reporting

Controls

Business Planning

In addition to participating in NYSERDA's Multi-Year Strategic Program Plan, as described in Section 2, Program Planning, above, the NY Green Bank develops an annual Strategic and Business Plan (Business Plan). NY Green Bank staff presents the Business Plan to the NY Green Bank's Investment and Risk Committee (IRC) annually for review and approval. The IRC is composed of the Chair of NYSERDA, President and Chief Executive Officer of NYSERDA, Treasurer of NYSERDA, President of NY Green Bank, and one or more NY Green Bank Managing Directors. The IRC is charged with reviewing and approving the Business Plan. The IRC must approve the Business Plan before it can be implemented by the NY Green Bank.

Business Operation

The NY Green Bank must operate in a manner that is consistent with the Business Plan, as approved by the IRC. In addition, the NY Green Bank must operate in a manner that is consistent with any approved operating plan, funding agreement, Public Service Commission Order, law or regulation related to its funding source(s).

The NY Green Bank's President reports to the President of NYSERDA, and Managing Directors report to the President of the NY Green Bank. In its operations, the NY Green Bank follows the NY Green Bank Operations and Procedures Manual, which is incorporated by reference into NYSERDA's Operations and Procedures Manual, forms part of NYSERDA's system of internal controls, and is designed to supplement existing NYSERDA controls.

The President of the NY Green Bank is primarily responsible for oversight of the operations of the NY Green Bank in a manner that is consistent with the Business Plan and the NY Green Bank Operations and Procedures Manual, and for ensuring the collection and tracking of all required information and metrics needed for compliance filings according to the Public Authorities Law and other statutory and administrative requirements.

Procurement Activities

When the NY Green Bank procures goods and services, it does so subject to NYSERDA's Procurement Guidelines, as adopted by the Board, and the procedures summarized in Section 2, Project Management, above.

Financial Investments

Financial transactions selected for funding must be consistent with the goals and objectives of the Business Plan. NY Green Bank's origination of clients, partners and potential transactions results from interactions with market participants who submit proposals that either: (i) respond to a NY Green Bank-specific solicitation and/or other publication of NY Green Bank's investment criteria (a Competitive Opportunity) or (ii) identify a NY Green Bank role consistent with its mandate, but which does not strictly fall within the definition of "Competitive Opportunity" (Strategic Opportunity).

While open and public competitive processes are favored in the origination of NY Green Bank partners, clients and transactions, it is nevertheless recognized that there may be circumstances in which the strategic mission of NY Green Bank is best served by undertaking one or more Strategic Opportunities. Strategic selection methods may be utilized if it is determined by NY Green Bank management, with approval from the IRC, that the opportunity: (i) is presented by a private sector party with exceptional, relevant experience and expertise; (ii) is one-of-a-kind by virtue of location, high visibility, probability of a successful closing or leverage with other already committed private or public funding or possesses other unique attributes; (iii) has exceptionally strong compatibility with the strategic objectives and mandate of NY Green Bank; (iv) represents an urgent need as a result of public exigency or emergency, or would become unavailable as a result of delay, or would take an unacceptable length of time for a similar opportunity to reach the same level of readiness; and/or (v) relates to the next phase of a multiphase proposal or the expenditure is necessary to support or protect an existing NY Green Bank investment or initiative.

Competitive Opportunities are designed to comply with the definition of a "competitive procurement" set forth in the Office of the State Comptroller Rules, Part 206 to NYCRR Title 2 (Comptroller's Regulations). For any proposed Strategic Opportunity involving NY Green Bank funding that will exceed \$1 million, NY Green Bank staff consults with NYSERDA's Counsel's Office regarding the application of the Comptroller's Regulations.

Prior to issuing a solicitation for a Competitive Opportunity, or to undertake a Strategic Opportunity, NY Green Bank staff develops a summary thereof (Opportunity Summary) for review and approval by the IRC. Once an Opportunity Summary for a Competitive Opportunity is approved by the IRC, NY Green Bank personnel prepares that solicitation in collaboration with NYSERDA's Contract Administrator and Counsel's Office. The solicitation takes into account any comments or qualifications made by the IRC in conjunction with its approval. In the case of an Opportunity Summary for a Strategic Opportunity, once approved by the IRC, NY Green Bank initiates due diligence.

For Competitive Opportunities, a proposal evaluation and scoring committee, consisting of at least three (3) internal members who are designated by the President of NY Green Bank, evaluates proposals for transactions arising from NY Green Bank solicitations and recommends those opportunities that best meet NY Green Bank's published investment criteria. Opportunities recommended by the committee will be subject to more detailed exploration and analysis.

For proposals selected for further exploration, whether as the result of a Competitive or Strategic Opportunity, NY Green Bank staff further evaluates and negotiates the proposed transaction and will

prepare a Greenlight Memorandum (except in extraordinary circumstances that may permit a proposal to be immediately submitted to the IRC), which provides an analysis of the transaction. A Greenlight Committee, composed of a majority of the IRC, reviews those transactions selected by staff for advancement, and may reject, approve, make recommendations, or require contingencies in regards to a proposed transaction. When transactions are being considered, members of the Greenlight Committee and IRC will recuse themselves where there are any conflicts of interest. For transactions approved by the Greenlight Committee, NY Green Bank staff continues to evaluate and negotiate the proposed transaction. A Transaction Approval Memorandum, which provides a comprehensive analysis of a transaction, is then presented to the IRC for review and approval. The IRC may reject, approve, make recommendations, or require contingencies to any proposed transaction.

Following transaction approval by the IRC, assigned staff, along with any retained consultants, will then proceed to finalize any remaining diligence and all transaction documentation, taking into account any recommendations and contingencies expressed by the IRC. Only after transaction approval and only if the agreements are according to all material aspects of the transaction approval may a binding commitment or documentation be executed.

Portfolio Management

NY Green Bank monitors its funded and unfunded commitments on a quarterly basis, providing a detailed review of each transaction for internal review as well as information on metrics (both internal and those for disclosure through required periodic public reporting). The IRC reviews portfolio reports, and will make portfolio-related recommendations, as well as recommendations on the disposition of transaction waivers, amendments, and restructurings as may be required or presented for approval.

Metrics Reporting

The NY Green Bank shall be responsible for collecting certain data to support the calculation and reporting of agreed operational, risk management and financial metrics. In addition, the NY Green Bank, in collaboration with other Authority staff, shall collect and process certain data required to assess the anticipated energy, environmental and economic benefits, as well as financial market impacts, that are realized by projects, and as required by any applicable Public Service Commission Order or reporting requirement. All estimates shall reference credible sources and estimating procedures, and all key assumptions shall be documented. This data will be used to evaluate impacts and progress towards goals.

SECTION 4: ENERGY ANALYSIS

Primary Functions

- Energy Planning, Modeling and Forecasting
 - State Energy Planning
 - Federal Energy Policy and Planning
 - Modeling and Forecasting
- Energy Assurance and Contingency Planning
 - Energy Data Clearinghouse
 - Energy Markets Monitoring and Intelligence
 - State Energy Emergency Planning and Response
 - Radioactive Waste Policy and Nuclear Coordination
- Energy Policy and Program Development
 - State Energy Policy Development
 - NYSERDA Program Development
 - NYSERDA Strategic Planning
 - Regulatory Affairs and Administrative Proceedings
- Program Evaluation

Control Objectives

Energy Planning, Modeling and Forecasting

Statewide Energy Planning

Energy Analysis provides a coordinating and leadership role on behalf of NYSERDA in the development and preparation of the statutorily-mandated State Energy Plan. Energy Analysis oversees the overall State Energy Plan process, including scope development, coordination of participating agencies and authorities, stakeholder outreach, scheduling, deliverables from other agencies, writing, editing, and document and website management.

The President and CEO of NYSERDA serves as the Chair of the Energy Planning Board, which consists of the chief executives from the 15 designated agencies and authorities who have responsibilities that affect or are affected by energy policy. The Director of Energy Analysis serves as the Director of the Energy Coordinating Working Group, which functions as the staff arm of the Energy Planning Board. Analyses, documents and all costs associated with the coordination, development and production by Energy Analysis staff to support the State Energy Plan process are reviewed by the Energy Analysis Director and ultimately by the Chair of the Energy Planning Board.

Modeling and Forecasting

Energy Analysis performs quantitative analyses using a wide range of analytical tools to provide the underpinnings for State policy and program development, regulatory initiatives, and energy decision-making. Responsibility for review, accuracy, and relevance of the various analyses and discussion papers developed is generally held by either the Program Manager or Program Director depending on the nature and sensitivity of the assignment.

Energy Assurance and Contingency Planning

Energy Data Clearinghouse

Energy Analysis serves as a source for NY State energy-related data and information. This program collects, compiles, maintains, and publishes a wide range of energy data, making extensive use of NYSERDA's web site to reach stakeholders. Information is reviewed by the responsible Program Manager and Program Director prior to release.

Energy Markets Monitoring & Intelligence

Energy Analysis monitors New York's major energy supply industries, including petroleum (liquid fuels), natural gas, coal, and electricity. Responsibility for review, accuracy, and relevance of the various analyses and discussion papers developed is generally held by either the Program Manager or Program Director depending on the nature and sensitivity of the assignment.

State Energy Emergency Planning and Response

Under Section 5-117 of the Energy Law, NYSERDA is responsible for developing and maintaining the New York State Energy Emergency Plan. Energy Analysis works with numerous State agencies including the Department of Public Service, Emergency Management Office, and Office of Homeland Security. Energy Analysis maintains a process for annual review and update of the Energy Emergency Plan to assure the Plan is accurate, timely, and can be readily implemented as needed.

Radioactive Waste Policy and Nuclear Coordination.

As required by Section 1854-d(1) of Public Authorities Law and Part 502 of Chapter XI of Title 21 NYCRR, Energy Analysis collects and maintains data on the generation of low-level radioactive waste by facilities in the State and the subsequent storage, treatment, and disposal of that waste. It reports this information annually to the Governor and Legislature, which is reviewed by NYSERDA executive management prior to completion. NYSERDA is the State's lead agency for addressing radioactive waste policy issues. Pursuant to NYSERDA's mandate under Section 7-101 of the Energy Law, Energy Analysis coordinates the State's radioactive materials regulatory programs, and the State's oversight of nuclear power plant activities. Staff also provides technical nuclear engineering support to the New York State Department of Health as part of the State's nuclear power plant emergency preparedness and response program. Significant issues, communications and reports are reviewed and approved by senior management as appropriate.

Energy Policy and Program Development

State Energy Policy Development

Energy Analysis supports, coordinates or leads in the development of specific energy policies, and provides both quantitative and qualitative analysis of policy development and program implementation support. Areas of policy development support work include environmental, fuel and electricity financial and trading markets. Energy Analysis provides draft policy initiative documents to Senior Management for approval prior to being distributed outside of NYSERDA.

NYSERDA Program Development

Program offerings within NYSERDA are planned and designed in a cooperative manner. Energy Analysis participates in this process to help insure that the programs as designed and delivered are likely to achieve or exceed their stated goals and can be properly evaluated. In addition, as evaluation findings and conclusions are completed on specific programs, Energy Analysis provides a formal feedback loop to the program implementation teams for improved program design and delivery, as warranted.

NYSERDA Strategic Planning

Annually, Energy Analysis manages development of NYSERDA's Strategic Plan, which describes how the Authority will pursue its mission, goals, and objectives over the ensuing three years. Energy Analysis meets with senior management and program staff to discuss and evaluate goals and strategy options, and reviews and researches program planning documents. Energy Analysis prepares a draft and a final version of the Plan, which is reviewed by senior management before sending to the Program Planning Committee and the Board for approval.

Regulatory Affairs and Administrative Proceedings

Energy Analysis actively monitors NYSERDA's interests in regulatory and administrative proceedings related to the State's energy and environmental policy goals, including those of the New York State Public Service Commission and Department of Environmental Conservation rulemakings. Energy Analysis staff participates on internal teams with Counsel and other program staff to address particular issues or proceedings, helping to compile and analyze data, and prepare formal submissions, which are approved by senior management prior to submission.

Program Evaluation

Energy Analysis is responsible for evaluating NYSERDA's energy efficiency and renewable energy deployment, market transformation, and R&D programs. Program Evaluation is structured to assess the effectiveness of programs toward achieving the State's public policy goals. Energy Analysis conducts evaluation using competitively selected, expert evaluation contractors who measure and verify impacts attributable to NYSERDA's program activities and examine program efficiency and effectiveness.

NYSERDA reports monthly, quarterly, and annually on the performance of various programs to the Governor, the New York State Legislature, the Public Service Commission, other program sponsors, advisory groups and stakeholders based upon reporting requirements established by the program sponsor. NYSERDA program staff and management are integral to the evaluation process, providing both data inputs and acting on recommendations. Evaluation and status reports are reviewed by NYSERDA's Senior Management prior to being finalized.

Federal Energy Policy and Planning

Energy Analysis maintains relationships with national organizations and stakeholders in the energy arena in order to influence policy and program agendas, to track emerging policy trends and to coordinate NYSERDA responses based on the possible impact on existing or future programs, with senior management approval. In addition, Energy Analysis identifies and works with other staff to pursue high value opportunities for collaboration with other state agencies, regional organizations, and neighboring states, with the goal of leveraging our resources and creating a larger impact. Energy Analysis in

cooperation with other staff also tracks federal solicitations to develop partnerships and high quality responses in areas consistent with NYSERDA's program and policy objectives.

SECTION 5: RADIOACTIVE WASTE MANAGEMENT

Primary Functions

- Management of NYSERDA's activities in the West Valley Demonstration Project (WVDP)
- Management of the State Licensed Disposal Area and Retained Premises of the Western New York Nuclear Service Center (WNYNSC)

Controls

The West Valley Demonstration Project Act - The WVDP Act directs the U.S. Department of Energy (DOE) to carry out a demonstration project on high-level radioactive waste solidification and decommissioning at the WNYNSC. The WVDP Act directs DOE and NYSERDA to enter into a Cooperative Agreement to carry out the WVDP. The WVDP Act also stipulates that the federal government will pay 90 percent of the WVDP costs and New York State will pay 10 percent.

Cooperative Agreement Between United States Department of Energy and New York State Energy Research and Development Authority on the Western New York Nuclear Service Center at West Valley, New York - The Cooperative Agreement lays out a framework between DOE and NYSERDA on the implementation of the WVDP. The Agreement stipulates that DOE has the sole responsibility for carrying out the Project, but also provides for continued consultation and coordination between DOE and NYSERDA during the conduct of the WVDP. The Cooperative Agreement also provides for NYSERDA's participation in DOE's procurement process for selecting the management and operations contractor for the WVDP. NYSERDA provides DOE with input on WVDP activities, progress, plans, funding, issues and concerns, and participates in WVDP meetings with the public, regulators, technical consultants and experts and other stakeholders.

Consent Decree - The Consent Decree, filed with and approved by the U.S. District Court, resolves the majority of claims brought in a lawsuit filed by NYSERDA and New York State against DOE and the federal government regarding cost allocation for cleanup at the WNYNSC. In addition to the 90/10 cost split identified in the WVDP Act and the Cooperative Agreement for WVDP facilities, the Consent Decree identifies a specific cost split between NYSERDA and DOE for all remaining facilities and contamination at the WNYNSC. The Consent Decree is implemented in accordance with a Consultation Agreement prepared by DOE and NYSERDA.

Waste and Facilities Management Committee - The West Valley Site Management Program reports to NYSERDA's Board through its Waste and Facilities Management Committee. The Waste and Facilities Management Committee is provided with routine updates on WVSMP activities, accomplishments, issues, and other noteworthy items. The Committee provides guidance to the West Valley Site Management Program Director in regard to West Valley activities for the WVDP and the State License Disposal Area (SDA). The Chair of the Committee reports on the West Valley program to the full Board.

Regulatory Requirements – Work performed at the SDA is subject to numerous regulatory requirements and mechanisms, including a Radioactive Materials License issued by the NYS Department of Health, a Radiation Control Permit and a State Pollutant Discharge Elimination System permit issued by the New York State Department of Environmental Conservation, and a Consent Order issued by the NYS Department of Environmental Conservation and the U.S. Environmental Protection Agency. NYSERDA

must also comply with all other applicable State and federal regulations, including regulations for hazardous waste generation, management, and disposal; worker industrial safety; wetland protection; and environmental review.

Written Plans and Procedures – Written plans and procedures provide the mechanism for implementing the regulatory requirements identified above and for implementing additional best management practices. Plans and procedures are prepared by technical staff or contractors, and are reviewed and approved by the SDA Program Manager before they are incorporated into the program for implementation. Radiation Safety and Health and Safety plans and procedures are also reviewed and approved by the Program Director and Radiation Safety Committee or Safety Committee before they are incorporated into the program for implementation.

Radiation Safety Committee – The WVSMP Radiation Safety Committee oversees the WVSMP's Radiation Protection Program, ensuring that all individuals who work with, or in the vicinity of radioactive materials at the SDA have sufficient training and experience to perform their duties safely and in accordance with applicable NYS Department of Health regulations and the Radioactive Materials License. The Radiation Safety Committee also ensures that all uses of radioactive materials at the SDA is conducted in a safe manner and in accordance with applicable regulations.

Safety Committee – The West Valley Site Management Program Safety Committee oversees the WVSMP Health and Safety Program to establish policies, administrative controls and procedures to protect workers at the SDA and other NYSEERDA-controlled areas of the WNYNSC in accordance with applicable Occupational Safety and Health Administration and NYS Department of Labor regulations. The Safety Committee also provides guidance to the Safety and Health Supervisor on the implementation of the Safety and Health Program.

Project Initiation Request Committee – The Project Initiation Request Committee reviews all potential contract actions at an early stage to provide initial WVSMP management review and input on all activities requiring NYSEERDA contract actions, in accordance with NYSEERDA procurement requirements. The Committee evaluates and provides input on the purpose and need for the activity, the contracting approach, funding considerations, resource needs and availability, and staff involvement.

SECTION 6: BOND FINANCING

Primary Functions

- Issue tax-exempt bonds for utilities and other qualifying entities to finance eligible facilities
- Administer utility bonds previously issued

Controls

Issue tax-exempt bonds for qualified entities to finance eligible facilities

Proposed financings are reviewed for eligibility by both NYSERDA staff and independent bond counsel.

An intent to issue new tax-exempt bonds may initially be evidenced by the approval of an inducement resolution or declaration of intent by the Audit and Finance Committee of NYSERDA's Board. The purpose of the inducement resolution or declaration of intent is to preserve, under the Federal Internal Revenue Code, the eligibility of the costs incurred from the date the action is taken to the date of the future financing for tax-exempt status.

New financings and refundings also require the approval of an implementing resolution adopted by NYSERDA's Board.

In addition to NYSERDA approval:

- The State Comptroller must approve bonds issued through a private negotiation sale, instead of public bid. As Chair of the State Securities Coordinating Committee, the Comptroller also oversees scheduling of major State and public authority financings.
- The Commissioner of the Department of Taxation and Finance approves certain arrangements of a bond sale, such as procedures for the security, collection, and investment of bond proceeds.
- The Public Authorities Control Board (PACB) reviews and approves the adequacy of the financial security of the bond issue.
- The Governor approves the minutes of NYSERDA's Board meetings. The Internal Revenue Code, also requires the Governor's approval for new bond financings that qualify as private activity bonds.

Administer bonds previously issued

The Finance Department prepares billings for annual administrative fees as summarized in the bond documents.

SECTION 7: CONTRACTS MANAGEMENT

Primary Functions

- Manage procurement and contracting process
- Contract management and administration

Controls

Manage procurement and contracting process

The Director of Contract Management approves all procurements and contracts and ensures that they are consistent with NYSERDA's Procurement Guidelines and applicable Executive Orders and other requirements.

The Director of Contract Management reports quarterly to the Board on NYSERDA's compliance with the Procurement Guidelines.

Duties are segregated between procurement, contract negotiation, and contract execution.

NYSERDA maintains standard contract terms and conditions. Significant exceptions to terms and conditions are identified for contract execution.

Contract Management staff provide training to staff on procurement and contracting policies and procedures to ensure compliance.

Each solicitation issued by the Authority shall designate the person(s) who may be contacted by offerers related to procurement pursuant to Section 139-j of the State Finance Law. Generally, any communication from an outside party which could reasonably be considered an attempt to influence the procurement may only be made to the designated person(s) in the solicitation..

Contract management and administration

The Contracts Management unit maintains electronic and paper central files including solicitations and contractual agreements.

The Contract Management unit is responsible for verifying compliance with contractual obligations, particularly provision for insurance and recoupment.

SECTION 8: ACCOUNTING

Primary Functions

- Preparation and approval of annual Budget and Financial Plan
- Maintenance of accounting records and systems and preparation of financial statements
- Cash and investments management
- Revenue processing
- Payment processing
- Payroll Processing
- Fixed assets

Controls

Preparation and approval of annual Budget and Financial Plan

A proposed Budget and Financial Plan are initially prepared by Authority staff in accordance with generally accepted accounting principles on a modified accrual basis. Included are a corresponding proposed Budget and Financial Plan prepared on a cash basis, based on reasonable assumptions and methods of estimation. They are presented in a manner consistent with the Authority's programs and functions and include detailed estimates of revenues and expenditures for each program or function.

The proposed Budget and proposed Financial Plan are made available for public inspection, through posting on NYSERDA's website, no less than 60 days before the start of the fiscal year and at least 30 days before approval by the Board Members.

NYSERDA's proposed Budget and proposed Financial Plan are accompanied by:

- a description of the budget process, including the dates of key Budget decisions;
- a description of the principal Budget assumptions, including sources of revenues, staffing and future collective bargaining costs, and programmatic goals;
- a self-assessment of budgetary risks;
- a revised forecast of the current year's budget;
- a reconciliation that identifies changes in estimates from the projections in the previously approved budget and financial plan;
- a projection of the number of employees, including sources of funding, the numbers of full-time and full-time equivalents, and functional classifications;
- a statement of each revenue-enhancement and cost-reduction initiative that represents a component of any gap-closing program and the annual impact on revenues, expenses and staffing;
- a statement of the source and amount of any material non-recurring resource that is planned for use in any given fiscal year;
- a statement of any transactions that shift material resources from one year to another and the amount of any reserves;
- a statement of borrowed debt projected to be outstanding at the end of the fiscal year covered by the proposed Budget or proposed Financial Plan, the planned use or purpose of debt issuances, scheduled debt service payments for both issued and proposed debt, the principal amount of proposed debt and assumed interest rate(s), debt service for each issuance as a percentage of total

pledged revenues listed by type or category of pledge revenues, cumulative debt service as a percentage of available revenues, and the amount of debt that can be issued until legal limits are met;

- a statement of the annual projected capital cost broken down by category and sources of funding, and for each capital project, estimates of the annual commitment, total project cost, expected date of completion and the annual cost for operating and maintaining those capital projects or capital categories that, when placed into service, are expected to have a material impact on the operating budget; and
- a certification by the President and CEO that, to the best of his or her knowledge and belief after reasonable inquiry, the proposed Budget and proposed Financial Plan are based on reasonable assumptions and methods of estimation.

As part of the annual budget process, NYSERDA staff prepare working papers that detail the assumptions and methods of estimation used in preparing the proposed Budget and proposed Financial Plan.

The proposed Budget and Financial Plan are then submitted to NYSERDA's Board Members for approval in accordance with Section 2801 of the Public Authorities Law. After approval, the approved Budget and Financial Plan are submitted to the persons designated in such Section 2801 to receive such Budget and Financial Plan. This includes submitting copies of the approved Budget and Financial Plan to the State Comptroller within 7 days of approval by the Board Members, subject to approval by the Governor pursuant to Section 1854 of the Public Authorities Law. The approved Budget and Financial Plan are also made available for public inspection, through posting on NYSERDA's website, not less than 7 days before the start of the fiscal year.

Thereafter, the Treasurer provides quarterly updates to the Board Members on the status of actual revenues and expenses compared to the Budget targets. The Treasurer also provides the Board Members with a written mid-year report to explain and quantify material variances that are due to timing or have a budgetary impact, and provide an assessment of the impact. The report includes the status of capital projects, including but not limited to commitments, expenditures and completions, and an explanation of material cost overruns and delays. Subsequent changes to the Budget and the Financial Plan are made, as required, subject to approval by the Board Members.

Through posting on NYSERDA's website, not less than 90 days after the close of each fiscal year, the Treasurer publically posts actual versus estimated Budget results. The Treasurer also notifies the Board Members and the State Comptroller, in writing, at any point during the fiscal year when he or she learns of any adverse development that would materially affect the Budget or Financial Plan.

Maintenance of accounting records and systems and preparation of financial statements

As required by statute, NYSERDA's annual financial statements, which are prepared in accordance with generally accepted accounting principles and accounting standards promulgated by the Governmental Accounting Standards Board, are audited by independent auditors selected by the Audit and Finance Committee and the Board. In addition, the Treasurer provides quarterly financial statements to the Board, including a comparison of actual results against budgeted amounts. Expenditure statements are also provided quarterly to Program Directors, Program Managers and department heads.

Accounting prepares, reviews and/or signs tax reporting forms (eg., payroll/employment taxes, informational reporting of exemptions, taxable fringe benefits and other payments) required by Federal, State and local regulations.

NYSERDA ensures compliance with Federal, State, and Local tax reporting obligations of NYSERDA. In addition, NYSERDA solicits a tax compliance review from an independent accounting firm as deemed necessary, but not less than once every three years, to review NYSERDA's compliance with applicable tax regulations.

Cash and investments management

The Commissioner of Taxation and Finance serves as fiscal agent to NYSERDA pursuant to statute. There are no funds under NYSERDA's direct control. The fiscal agent, at the direction of NYSERDA, actually purchases, sells, and retains custody, where appropriate, of NYSERDA investments.

NYSERDA is subject to the provisions of Public Authorities Law Section 2925, the Office of the State Comptroller's "Investment Guidelines for Public Authorities," the provisions of NYSERDA's enabling legislation concerning NYSERDA investments, and NYSERDA's own "Investment Guidelines, Operative Policy and Instructions." At least annually, the Audit and Finance Committee of NYSERDA's Board reviews and evaluates NYSERDA's investment program results and approves any revisions to the Guidelines.

Duties are segregated between receipt and custody, depositing, recording, and reconciling cash and checks received.

The purchase and sale of investments is authorized by the Treasurer (or in his/her absence, the Controller and Assistant Treasurer, or any NYSERDA Officer), according to policy guidelines. Duties are segregated between authorization and recording of investments.

Receipts are deposited promptly, generally weekly.

The fiscal agent reconciles cash and investment accounts monthly. NYSERDA staff independently reconcile this data with the accounting records.

Revenue processing

Proper segregation of duties exists in the initiation, recording, and reconciliation of revenues. Only Accounting staff not responsible for cash reconciliations or deposits are authorized to prepare invoices.

A list of outstanding invoices is produced monthly and reconciled with the general ledger. Notices are sent for any outstanding invoices more than 30 days past due. The Controller and Assistant Treasurer, with the assistance of the Senior Energy Accountant, is responsible for following up on delinquent accounts.

An account receivable may only be written-off after all reasonable collection efforts have been exhausted and requires the approval of the Treasurer. The Treasurer must also approve any deferred payment arrangements.

Accounts receivable more than 120 days past-due may be submitted to a private collection agency or the Attorney General's Office for collection.

As an alternative to receiving payments from RD&D program contractors through recoupment, and in an effort to assist in growing small businesses, NYSERDA may instead elect to take an equity position in an

RD&D contractor. When deemed appropriate, an equity investment is consummated through a negotiated Stock Purchase Agreement, which outlines the terms and conditions of NYSERDA's investment.

Payment processing

Section 2880 of the Public Authorities Law requires that payment be made to vendors within 30 days on all valid invoices. Failure to do so will result in the payment of interest.

Accounting staff prepares a weekly report of outstanding vouchers and their due dates which is reviewed by the Controller or Treasurer. NYSERDA reports annually to the Board at the June meeting on its compliance with the prompt payment policy.

Prior to payment, proper authorization must exist for payments to contractors.

All contracts or purchase orders must be signed by an Officer. Contracts or agreements in excess of \$1,000,000 must be signed by the President and CEO. Generally, goods and services in excess of \$5,000 require a written contract or purchase order.

Accounting staff monitor all payments, assuring that all invoices are mathematically correct, contain proper documentation, are within authorized funding limits, and are in accordance with the terms and conditions of the contract or purchase order.

Additional approval for payment is required from the Project Manager for payments under program contractual agreements, or from the Program Manager or department head, for administrative costs.

NYSERDA checks require the signature of the Commissioner of Taxation and Finance, NYSERDA's fiscal agent. Payees electing to receive payment from NYSERDA by electronic transfer provide the necessary information and authorization in writing. Approval for disbursements is noted on a warrant request, which must be signed by an authorized signatory: the Controller and Assistant Treasurer or any NYSERDA Officer. For payees receiving payment by electronic transfer, the automated accounting system produces an electronic file containing necessary banking information for payees, which is transmitted to the Dept. of Taxation and Finance for comparison against the warrant authorization and transmission to the bank for processing the electronic transfers.

NYSERDA's integrated financial management system provides for automated, role-based security that properly segregates user access to functions for vendor accounting information addition and maintenance, invoice entry, invoice approval, and payment preparation. In addition, the system's budgetary management system prevents expenditure or encumbrance of funds in excess of authorized program funding.

Payroll Processing

NYSERDA's President and CEO, or designee authorizes in writing payroll additions or salary changes. The Director of Human Resources provides notice, in writing, of any salary deletions. Human Resources staff initiates all ministerial changes such as benefit changes in accordance with requests submitted by employees.

All employees are required to maintain daily time records on a bi-weekly basis, using the automated time and attendance system. Employee timesheets require approval by the individual's supervisor.

NYSERDA uses a computerized payroll system to calculate and process payroll and checks. Access to the system is password restricted to only those individuals in the Accounting unit with responsibility for processing payroll.

Fixed assets

Accounting staff maintain a computerized fixed asset system, ensuring that all items of equipment are identified by location, and that the fixed asset ledger is reconciled to the general ledger. Only assets with a dollar value in excess of \$500 are recorded.

The disposition of real property and personal property shall be in accordance with the Guidelines, Operative Policy, and Instructions for the Disposal of Real and Personal Property. The Treasurer is responsible for ensuring compliance with these guidelines, including the preparation of an annual report listing all real property of the Authority and a description of all real and personal property disposed of during such period.

Financial Statements

NYSERDA prepares annual financial statements in accordance with generally accepted accounting principles (GAAP) applicable to state and local government entities, which are approved by the Board at the June meeting. The annual financial statements include a comparison of actual results versus financial projections and a certification by the Officers and the Director of Internal Audit that the financial statements and disclosures fairly present, in all material respects, the operations and financial condition of NYSERDA. NYSERDA's most recent annual financial statements are made available on the NYSERDA web site. Interim quarterly financial statements are also provided to the Board.

Financial statements are audited by an outside independent accounting firm selected by the Audit and Finance Committee and Board. The independent auditors are selected in accordance with the requirements of Section 2802 of the Public Authorities Law and are prohibited from providing non-audit services to NYSERDA contemporaneously with the audit, except as provided in Section 2802 of the Public Authorities Law. Non-audit services include bookkeeping or other services related to the accounting records or financial statements of NYSERDA; financial information systems design and implementation; appraisal or valuation services, fairness opinions or contribution-in-kind reports; actuarial services; internal audit outsourcing services; management functions or human services; broker or dealer, investment advisor, or investment banking services; and legal services and expert services unrelated to the audit.

The independent auditors must timely report to the Audit and Finance Committee all critical accounting policies and practices to be used, all alternative treatments of financial information within generally accepted accounting principles that have been discussed with Authority management officials, ramifications of the use of such alternative disclosures and treatments, and the treatment preferred by the certified independent public accounting firm; and other material written communications between the independent auditors and NYSERDA management, such as the management letter along with management's response or plan of corrective action, material corrections identified or schedule of unadjusted differences, where applicable.

The audit partner or lead audit partner responsible for reviewing the audit must not have performed audit services for the Authority in each of the five previous fiscal years.

SECTION 9: HUMAN RESOURCES

Primary Functions

- Recruit employees
- Manage compensation functions to appropriately reward employees
- Manage performance programs to reinforce and correct behaviors
- Manage employee benefits programs
- Conduct employee training

Controls

Recruit employees: Prohibited Actions

All NYSERDA positions are filled based on merit. A position posting containing minimum education and skill levels are established for every position. Reference, employment, and education information is verified for all prospective employees. The President and CEO, Treasurer, or Director of Internal Audit cannot have been employed by the Authority's independent auditors during the two-year period preceding an audit.

NYSERDA prohibits the hiring of relatives or domestic partners of Members of the Board or NYSERDA employees.

No employee involved in recruiting, interviewing, or hiring applicants for employment or making promotional, disciplinary, or other employment decisions may ask any such applicant or employee to reveal their party affiliation, whether he or she has made campaign contributions, or whether the candidate voted for any elected official or candidate for elective office.

Manage compensation functions to appropriately reward employees

Merit payment recommendations are reviewed and approved by the Director of Human Resources and the Officers for conformance with NYSERDA's policies.

Manage performance programs to reinforce and correct behaviors

An Individual Performance Agreement (IPA) is drawn up between each employee and employee's supervisor which summarizes the employee's job responsibilities and specific performance objectives which are used for the performance evaluation each six months (oral in April and written in October). The IPA also summarizes planned training and development activities.

Performance Improvement Plans are completed by supervisors and approved by Human Resources for employees whose performance warrants significant improvement.

Manage employee benefits programs

Human Resource staff provides assistance to employees with enrollment, changes, or answering questions for various NYSERDA-sponsored employee benefit programs.

Special benefits, such as flexible work hours or part-time work are evaluated on a case-by-case basis with approval from the employee's supervisor and the Director of Human Resources to ensure consistent and equitable application.

Conduct employee training

Human Resources sponsors various Authority-wide employee training programs using internal and external trainers. Individual employee training and professional development needs are generally identified as part of the evaluation process. Requests are approved by the direct supervisor, Program Director, and Director of Human Resources.

SECTION 10: COMPUTER SYSTEMS

Primary Functions

- Procure, operate and maintain computer hardware and software
- Maintain security of computer hardware and software
- Provide training to staff on computer hardware and software usage
- Maintain Authority Web Site

Controls

Procure, operate and maintain computer hardware and software

The Director of Information Technology and Treasurer must approve the purchase of computer hardware or software.

The IT unit maintains a help desk during normal business hours to respond to staff questions and problems with NYSERDA hardware or software.

An Information Technology Governance Committee, comprised of all Program Directors and administrative department heads, serves in an advisory capacity to an Information Technology Governance Board. The Information Technology Governance Board is comprised of most of the Officers, and is tasked with the review, approval, prioritization and mentoring of information technology projects which require more than 40 hours of NYSERDA staff effort, have a project duration anticipated to be 3 months or more, or require an expenditure of more than \$25,000 of consultant resources to deploy.

All information technology development projects shall conform with system development life cycle standards including user requests, approval, documentation of technical and functional requirements, testing and implementation, with controlled access and migration of changes between development and operating environments.

Maintain security of computer hardware and software

The Information Security Officer is the central point of contact for all information security matters. He or she reports independently to the Treasurer. The duties of the Information Security Officer are segregated from the operation of the information technology systems.

All electronic data stored on the network file server is automatically backed up to magnetic tape on a nightly basis. While on-site, the tapes are stored in a fire proof safe. Once daily a tape is generated and couriered off-site for storage. After 7 days, a tape is reused. The last tape of the month is not reused and remains in a fire-proof safe. This results in a 7-day rolling backup with 12 monthly backup tapes generated per year.

Staff are encouraged to store any data considered critical to the operation of NYSERDA on the network server, rather than on staff personal computers. This allows the data to become part of the automatic backup and disaster recovery procedures.

Electronic data stored on personal computers is backed up by the staff member to whom the computer is assigned. As an additional level of protection, non-sensitive personal computer backup media can be stored off-site, either at the staff member's home or at NYSERDA's off-site storage locations.

Every reasonable effort is taken to ensure access to the network is restricted to valid users, and each user is given a password. The password can be changed by the user at any time or by the system administrator. System integrity is maintained by restricting network user privileges and by centralizing management duties to a password protected system administrator. Only the system administrator can alter network programs, security or operations. Physical access to the network computer systems equipment is limited to authorized staff.

All data stored on the network or personal computers is considered NYSERDA work product. Personal or private use of NYSERDA computers or systems is discouraged. However, computers may be used for incidental and necessary personal purposes, provided that such use is in a limited amount and duration and does not conflict with the proper exercise of the employee's duties.

Recovery from the physical destruction of the network computer system is accomplished by using the most recent backup tapes available and restoring data to another computer network system. At that time, single users can access critical computer-based information until NYSERDA operations can be reestablished at another location. Recovery from personal or network computer failure is accomplished by using spare computers or parts and restoring lost data from backup media. In some situations, accidentally deleted data can be recovered with the use of software utilities available to the system administrator.

To protect NYSERDA's computer systems against the introduction or spread of a computer virus, the network server and staff personal computers have been equipped with virus protection software. The virus protection software is configured for automatic checking and system shielding to detect and contain viruses as soon as possible. Network server files are scanned for viruses each time they are used while personal computer files are scanned once per day when the user first logs onto the LAN. The virus protection software also enables staff to manually scan hard drives and diskettes as needed. In addition, portable computers that are signed out are scanned upon being returned.

Employees may borrow certain equipment for use outside NYSERDA for a finite length of time. The employee must sign the hardware out from the Operations Support Manager or his/her designee.

Electronic mail (E-mail) services are provided to NYSERDA staff via the computer network and Internet. Personal or private use of the E-mail system is discouraged. However, the E-mail system may be used for incidental and necessary personal purposes, provided that such use is in a limited amount and duration and does not conflict with the proper exercise of the employee's duties.

It is NYSERDA's policy to adhere to the stipulations of the license agreement and the copy protection laws which apply to a software package. Illegal copying of NYSERDA software, or use of illegal copies of software packages on any of NYSERDA's computers, is not permitted. In the event that an illegal copy of software is found on the premises, it will be destroyed immediately.

Non-NYSERDA software may not be copied or installed on NYSERDA computers without written authorization from the Operations Support Manager.

Every staff member of NYSERDA is assigned a computer and is given access to the network. It is the responsibility of each staff member to protect NYSERDA's investment in computer technology. The computers and software provided by NYSERDA for staff use are to be used for NYSERDA business purposes only. While employed by NYSERDA, each staff member shall be responsible for all assigned computer items. Staff members shall report immediately any lost, damaged or missing items.

The Information Technology unit records the serial number of each piece of equipment provided to each staff member; maintains a record of manuals and software programs provided to staff members; and updates these records as equipment, manuals and software are added or removed.

As part of the employee exit interview process, the Operations Support Manager, or the Office Administrator at West Valley, signs the Exit Clearance Form, described in NYSERDA's Personnel Handbook, indicating that all assigned computer equipment, manuals and disks have been returned. All discrepancies must be cleared before the final paycheck can be released.

Provide training to staff on computer hardware and software usage

Information Technology unit staff conduct one-on-one or group training on various software applications and computer technology or can research and recommend outside training when requested.

Maintain Authority Web Site

The Information Technology unit is responsible for maintaining the Authority's web site(s) based on requests approved by the Marketing and Economic Development department. At a minimum, the web site shall include a description of NYSERDA's mission, current activities, most recent financial reports, current year budget, its most recent independent audit report, and Guidelines, Operative Policy and Instructions for the Disposal of Real and Personal Property.

SECTION 11: COUNSEL'S OFFICE

Primary Functions

- Provides legal advice and drafts legal opinions and documents for NYSERDA.
- Provides legal advice and oversight of the contracting process
- The Office of the General Counsel provides guidance to the Communications department in responding to Freedom of Information Law (FOIL) requests.
- Renders advice concerning all NYSERDA programs and policies by participating in Teams and PDMC.
- As designated by the President and CEO, a Counsel's Office attorney serves as NYSERDA's ethics officer.
- Reviews NYSERDA related proposed legislation and regulations by providing assistance to the Governmental Affairs Director.
- Assists in the drafting of NYSERDA's rules and regulations and reviews NYSERDA's applications for permits and environmental assessments.
- Performs the secretarial function for the standing committees of the Board.
- Coordinates NYSERDA records management systems

Controls

Provides legal advice for all NYSERDA matters.

General Counsel represents NYSERDA's interests in legal actions or proceedings and consults with executive management as deemed necessary.

Upon receipt of notice that an offerer has made contact with someone other than the Designated contact with respect to a procurement for a reason inconsistent with subsection 3 of Section 139-j of the State Finance Law, the ethics officer will immediately investigate the allegation, in accordance with the procedures set forth in, and make a determination as required by, such Section 139-j. A finding that an offerer has knowingly and willfully violated subsection 3 of Section 139-j of the State Finance Law will result in a finding of non-responsibility for such offerer as required by such section.

NYSERDA's President and CEO designates a Records Management Officer and has currently designated a member of Counsel's Office to act in that capacity. In consultation with the New York State Archives, the Records Management Officer is tasked with implementing the records management system, and providing staff with guidelines for maintaining records.

As part of the records management system, NYSERDA has adopted the General Retention and Disposition Schedule for New York State Government Records as issued by the New York State Archives Government Records Services. No record may be destroyed without the express consent of the Records Management Officer in accordance with the General Retention and Disposition Schedule for New York State Government Records, which is located on NYSERDA's intranet.

SECTION 12: GOVERNMENTAL AFFAIRS

Primary Functions

- To serve as a liaison between NYSERDA and all elected officials
- To address inquiries from the Governor's office, members of the federal and State legislature, as well as local government officials

Controls

Records

The Office of Governmental Affairs tracks federal and State legislation that directly impacts energy-efficiency and environmental conservation policies, as well as legislation that may have other potential implications for NYSERDA and its stakeholders. Additionally, staff monitors legislative hearings, assists with the preparation of testimony for hearings, and coordinates the management of NYSERDA's legislative agenda.

The Director of External Affairs will maintain all records of contacts, whether oral or written, that are an attempt to influence the adoption or rejection of any rule or regulations having the force and effect of law that is issued by NYSERDA.

SECTION 13: COMMUNICATIONS

Primary Functions

- Responds to media and public inquiries on programs and acts as a liaison to the Governor's Press and Scheduling Offices
- Issues news releases and arranges media events
- Responsible for responding to Freedom of Information Law (FOIL) requests with guidance from Counsel's Office

Controls

Responds to media and public inquiries on programs

Staff receiving phone calls, messages or other inquiries from the print or electronic media (including freelance journalists or reporters) are required to immediately forward such inquiries to Communications staff for response. As appropriate, Communication staff discusses responses with technical, legal, contracts, or administrative staff.

Issues news releases and arranges media events

Communications staff are responsible for news releases regarding NYSERDA news, events, and programs. Communications works with the staff responsible for programs or events to draft a Press Release. Press releases are reviewed and approved by the Director of Communications (or designee), the President and CEO, and other parties involved.

Communication staff review NYSERDA-funded projects with special attention to the technology transfer components. Communication staff works with staff from other departments on technology transfer efforts that require communications expertise.

Communication staff are also responsible for targeting information to appropriate audiences to maximize the effectiveness of NYSERDA's outreach efforts.

Responding to Freedom of Information Requests

The Director of Communications assigns and oversees a records access officer to respond to Freedom of Information Law (FOIL) requests with guidance from the Office of the General Counsel.

SECTION 14: MARKETING AND ECONOMIC DEVELOPMENT

Primary Functions

- Produce marketing materials and publications
- Provide financial and technical assistance to improve the State's business climate through strategic partnerships and promoting various NYSERDA programs
- Produces and distributes general and technical reports about NYSERDA and its programs

Controls

Marketing materials and publications

Department staff work with program staff to produce effective marketing materials (reports, brochures, case studies and fact sheets, paid advertising, displays, direct mail, exhibits, videos, presentations, conference materials, website content, and marketing collateral). Materials are reviewed and approved by department personnel and program staff. Staff coordinate and monitor external mailings, monitor for report archives and accessibility of reports and website materials, and obtain approvals for use of non-NYSERDA photography and content. Staff procure marketing/graphics-related services and materials and monitor contracted activities to ensure appropriate quality control, as well as coordinating materials produced using internal staff resources.

Economic Development

Staff maintain close working relationships with local, regional, and State economic development organizations, and provide information on NYSERDA program offerings.

Staff also manage the Energy Smart Communities Coordinators throughout the State to ensure accurate and timely representation of NYSERDA programs.

SECTION 15: CONSUMER SERVICES AND EVENTS MANAGEMENT

Primary Functions

- Provide consumer information
- Manage and coordinate NYSERDA marketing events

Controls

Consumer Services

The department maintains a toll-free telephone inquiry line for consumer information and manages similar services performed by an outside fulfillment contractor. Staff maintains up-to-date knowledge of NYSERDA programs and eligibility criteria to respond properly to questions.

Events Management

Staff identify appropriate events, conferences, and exhibit opportunities for NYSERDA program marketing, and provide conference and meeting support including venue selection and contracting, equipment and facility logistics, and developing marketing materials. The department maintains a NYSERDA-wide events calendar to provide for coordination of activities.

SECTION 16: INTERNAL AUDIT

The Authority shall maintain an internal audit function, consistent with Public Authorities Law Section 2932. The internal audit activity will be governed by adherence to mandatory guidance established by The Institute of Internal Auditors, including, the *International Standards for the Professional Practice of Internal Auditing*, the *Code of Ethics*, and the *Definition of Internal Auditing*.

The purpose of the Authority's internal audit function is to provide an independent and objective assessment of, and to make recommendations for improving, Authority's operations and its system of internal control. This is to be accomplished through a systematic, disciplined approach of evaluating the effectiveness of, and when appropriate recommending improvements to, risk management, control, and governance processes.

Under the internal audit function, the Authority shall both examine and evaluate the adequacy and effectiveness of the Authority's system of internal controls and monitor adherence to such system in carrying out its operations. The scope of internal audits may include, but are not limited to, evaluating whether the following objectives have been achieved: risks are appropriately identified and managed; significant financial, managerial, and operating information is accurate, reliable, and timely; activities are in compliance with policies, standards, procedures referenced in the Authority's Internal Control Manual, Personnel Manual, Operations and Procedures Manual, and Accounting Policies and Procedures Manual, and applicable laws and regulations; resources are acquired and used efficiently and economically and adequately protected; and stated programs, plans, or objectives are achieved.

The internal audit function shall be directed by a Director of Internal Audit, who shall be appointed by the Board Members, as determined by the Audit and Finance Committee. Selection of the Director of Internal Audit shall be based upon his or her internal auditing credentials, including knowledge, skills, experience, and professional certifications necessary to perform the responsibilities described in this section. The Director of Internal Audit shall report functionally to the Authority's Audit and Finance Committee.

The Director of Internal Audit shall, consistent with the goals of the internal audit function, develop an annual audit plan using a risk-based methodology for review and approval by the Audit and Finance Committee, and update it periodically, including revising it to include special tasks or projects requested by the Audit and Finance Committee or the President and CEO; implement the approved audit plan; provide to the Audit and Finance Committee an annual assessment on the adequacy and effectiveness of the Authority's process for controlling its activities, including potential improvements to those processes; periodically prepare information on the status and results of the annual audit plan and any updates to the plan for submission to the Audit and Finance Committee; coordinate and consult with Authority staff on, and evaluate and assess, significant new or changes to programs, operations, and control processes and their implementation; report material and significant issues related to the processes for controlling the Authority's activities to the Audit and Finance Committee, including, but not limited to, any identified fraudulent activities; advise the Audit and Finance Committee of emerging trends and practices in internal auditing; and coordinate the internal audit function with those of the Authority's independent external auditors to provide optimal audit coverage to the Authority at a reasonable overall cost and the Authority's Internal Control Officer to ensure efficient and effective use of resources.

The Director of Internal Audit shall have unrestricted access to all functions, records, property and personnel necessary to perform audits; have full and free access to the Audit and Finance Committee;

develop scopes of work and apply the techniques required to accomplish the audit objectives contained in the annual audit plan; and have such assistance of Authority personnel as is necessary to perform audits.

The Director of Internal Audit shall not be responsible for any duties which would impair his/her independence, such as: performing any operational duties for the Authority; initiating or approving accounting transactions external to the internal audit function, or directing the activities of any Authority employee not employed in the internal audit department, except to the extent such employees have been appropriately assigned to auditing teams or to otherwise assist the internal audit function.

SECTION 17: DISCRETIONARY FUNDS

The expenditure of the Authority's discretionary funds must relate directly to an enumerated power, duty, or purpose of the Authority. Public funds may not be used to purchase items that are considered personal expenses or that are intended to personally benefit a Member, Officer, or employee. The Authority may not use discretionary funds for purchases that are not necessary to advance the mission of the Authority, including supporting the private or personal interests of the Members, Officers, or employees of the Authority.

Examples of inappropriate use of discretionary funds may include, but are not limited to, the purchase of flowers and gifts for Members, Officers, employees, or family members; celebrations for special occasions; charitable contributions or sponsorships; renewal of professional licenses; personal use of Authority vehicles; and costs to purchase or mail holiday cards or expressions of sympathy.

The Authority's handbooks and manuals provide further guidance regarding appropriate uses of the Authority's discretionary funds for expenses directly related to an enumerated power, duty, or purpose of the Authority. The additional guidance sets forth a process for approving discretionary expenditures and indicates the individual authorized to approval such expenditures. The Personnel Handbook contains specific policies regarding reimbursement for food while traveling, professional memberships, use of Authority equipment and vehicles, and tuition reimbursement. The Operations and Procedures Manual details the Authority's policies regarding sponsorships and the purchase of food for meetings and conferences. The Code of Conduct details additional policies regarding use of Authority equipment and vehicles.

APPENDIX A

New York State Comptroller Standards for Internal Control in New York State Government (Revised October 2007)

INTRODUCTION

The New York State Governmental Accountability, Audit and Internal Control Act of 1987 (Internal Control Act) required State agencies and other organizations to promote and practice good internal control and to provide accountability for their activities. In 1999, this legislation was made permanent and the State Finance Law was amended to require the State Comptroller to issue internal control standards for State agencies and other organizations.

To fulfill this requirement, the State Comptroller developed the internal control standards contained in the publication: "*Standards for Internal Control in New York State Government.*" These standards have been compiled from those advocated by leading authorities in the field of internal control. All organizations subject to audit by the Office of the State Comptroller are expected to adhere to these standards, and will be evaluated accordingly in any audits that are performed by that Office.

Internal control is defined as the integration of the activities, plans, attitudes, policies, systems, resources and efforts of the people of an organization working together to provide reasonable assurance that the organization will achieve its objectives and mission. Thus, internal control is focused on the mission of the organization, and this mission must be kept in mind when evaluating the appropriateness of specific internal control practices.

The fundamental principles of internal control are rooted in well established organizational techniques and practices. These techniques and practices can best be understood as internal control if they are placed in the following conceptual framework: the five basic components of internal control (control environment, communication, assessing and managing risk, control activities, and monitoring) and the two supporting activities (evaluation and strategic planning). Accordingly, this publication is organized on the basis of this conceptual framework.

The application of internal control is dynamic, and practices that fit past circumstances may need to be adjusted as those circumstances change. To keep your self informed about developments in the field of internal control and learn what other organizations are doing to meet their internal control needs, you can consult the professional literature, visit relevant web sites, join professional accountability organizations, and attend training programs on the subject of internal control. Some of these potential sources of information are listed in the appendix to the publication.

PART I NEW YORK STATE'S INTERNAL CONTROL FRAMEWORK

The State of New York is a very large enterprise with an economy approximately the size of Canada. It is larger than most of the Fortune 500 companies. The similarities between New York State government and big business do not end with economic comparisons. Government and many private sector companies are

large organizations with many people, multiple processes, diverse products and services and numerous customers. In order to succeed, both government and business should manage their operations effectively. While there are many different styles of effective management, there is one common feature among them -attention to internal control and risk management.

Everyone experiences internal control in their daily business activities as well as in their personal lives. Yet it is a subject that is very often misunderstood, ignored or undervalued. Internal control helps bring order, direction and consistency to our lives and our organizations. So, how can a subject of such importance be so unappreciated? The answer may lie in the need to better define internal control and what it does. This publication is intended to explain to New York State government employees how internal control plays an important part in their daily work activities.

Government managers should be able not only to account for funds spent on a program, but also to demonstrate the value of the program and its accomplishments. An effective system of internal control can give managers the means to provide accountability for their programs, as well as the means to obtain reasonable assurance that the programs they direct meet established goals and objectives. While managers have a significant impact on an organization's system of internal control, every employee of the organization has a responsibility and a role in ensuring that the system is effective in achieving the organization's mission.

Although an internal control system can vary widely among organizations, the standards for a good system are generally the same. The standards presented in this publication are applicable to all State government organizations. You should view them as the minimally acceptable standards for New York State government organizations.

These standards are not new ideas; many of the concepts are currently part of your existing operations. You should view this information as a guide for evaluating your organization's system of internal control. More information about internal control is available in libraries, from professional organizations or from experts on the subject, including the Office of the State Comptroller.

DEFINITION OF INTERNAL CONTROL

Many groups and organizations have published standards and guidelines on internal control and defined it in various ways. Each of those definitions has captured the basic concept of internal control using different words. The definitions are similar in recognizing internal control's extensive scope, its relationship to an organization's mission, and its dependence on people in the organization.

Internal control is focused on the achievement of the organization's mission. Therefore, it is essential that an organization have a clearly stated mission that is known and understood by everyone in the organization. It is also important to understand that, while good internal control will provide "reasonable assurance" goals and objectives are met, good internal control cannot guarantee organizational success. However, goals and objectives are much less likely to be met if internal control is poor.

Internal control is defined as follows:

Internal control is 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.

This definition establishes that internal control:

- affects every aspect of an organization: all of its people, processes and infrastructure;
- is a basic element that permeates an organization, not a feature that is added on;
- incorporates the qualities of good management;
- is dependent upon people and will succeed or fail depending on the attention people give to it;
- is effective when all of the people and the surrounding environment work together;
- provides a level of comfort regarding the likelihood of achieving organizational objectives; and
- helps an organization achieve its mission.

FOUR PURPOSES OF INTERNAL CONTROL

While the overall purpose of internal control is to help an organization achieve its mission internal control also helps an organization to:

1. Promote orderly, economical, efficient and effective operations, and produce quality products and services consistent with the organization's mission.
2. Safeguard resources against loss due to waste, abuse, mismanagement, errors and fraud.
3. Promote adherence to laws, regulations, contracts and management directives.
4. Develop and maintain reliable financial and management data, and accurately present that data in timely reports.

ORGANIZATIONAL ROLES

Every member of an organization has a role in the system of internal control. Internal control is people-dependent. It is developed by people; it guides people; it provides people with a means of accountability; and people carry it out. Individual roles in the system of internal control vary greatly throughout an organization. Very often, an individual's position in the organization determines the extent of that person's involvement in internal control.

The strength of the system of internal control is dependent on people's attitude toward internal control and their attention to it. Executive management needs to set the organization's "tone" regarding internal control. If executive management does not establish strong, clearly stated support for internal control, the organization as a whole will most likely not practice good internal control. Similarly, if individuals responsible for control activities are not attentive to their duties, the system of internal control will not be effective. People can also deliberately defeat the system of internal control. For example, a manager can override a control activity because of time constraints, or two or more employees can act together in collusion to circumvent control and "beat the system." To avoid these kinds of situations, the organization should continually monitor employee activity and emphasize the value of internal control.

While everyone in an organization has responsibility for ensuring the system of internal control is effective, the greatest amount of responsibility rests with the managers of the organization. Management has a role in making sure that the individuals performing the work have the skills and capacity to do so, and, to provide employees with appropriate supervision, monitoring, and training to reasonably assure that the organization has the capability to carry out its work. The organization's top executive, as the lead manager, has the ultimate responsibility. The Internal Control Act provides that, the top executive is responsible for establishing the organization's system of internal control, and is also responsible for (1)

establishing a system of internal control review, (2) making management policies and guidelines available to all employees, and (3) implementing education and training about internal control and internal control evaluations. To the extent that the top executive authorizes other managers to perform certain activities, those managers become responsible for those portions of the organization's system of internal control. The law further requires the head of the organization to designate an internal control officer who reports to him or her. Drawing on knowledge and experience with internal control matters, the internal control officer is a critical member of the management team who assists the agency head and other management officials by evaluating and improving the effectiveness of the internal control system. While the internal control officer has responsibility for both implementing and reviewing the organization's internal control efforts, the organization's managers are still responsible for the appropriateness of the internal control system in their areas of operation. The internal control officer helps establish specific procedures and requirements; the effectiveness of these procedures and requirements must be audited by someone who was not involved in the process of putting them into place. In contrast, the organization's internal auditor is responsible for evaluating the effectiveness of the system of internal control. This individual must be independent of the activities that are audited. For this reason, in most instances, the internal auditor cannot properly perform the role of internal control officer.

PART II FIVE COMPONENTS OF INTERNAL CONTROL CONTROL ENVIRONMENT

Control environment is the attitude toward internal control and control consciousness established and maintained by the management and employees of an organization. It is a product of management's governance, that is, its philosophy, style and supportive attitude, as well as the competence, ethical values, integrity and morale of the people of the organization. The control environment is further affected by the organization's structure and accountability relationships. The control environment has a pervasive influence on the decisions and activities of an organization, and provides the foundation for the overall system of internal control. If this foundation is not strong, if the control environment is not positive, the overall system of internal control will not be as effective as it should be.

The following describes how management is responsible for creating a positive control environment, and how employees are responsible for helping to maintain this environment.

Governance is the influence on an organization exercised by the executive body or the chief executive which/who governs it. The executive body may be a board of directors, board of trustees, council, legislature or similar entity. The chief executive may be the president, chancellor, commissioner, chief judge or an individual elected or appointed as the highest ranking person in the organization.

Their governance responsibilities are usually founded in a constitution, charter, laws, by-laws, regulations and other similar documents. The leadership, actions and tone established and practiced by the governing body/executive can have a profound impact on how the employees of the organization perform their responsibilities, which in turn affects the achievement of the organization's mission.

Among the critical areas influenced by the governing body/executive are:

- approving and monitoring the organization's mission and strategic plan;
- establishing, practicing, and monitoring the organization's values and ethical code;
- overseeing the decisions and actions of senior managers;
- establishing high-level policy and organization structure;

- ensuring and providing accountability to stakeholders;
- establishing the overall management style, philosophy and “tone”; and
- directing management oversight of key business processes.

Ethical Values and Integrity are key elements contributing to a good control environment. Ethical values are the standards of behavior that form the framework for employee conduct. Ethical values guide employees when they make decisions. Management addresses the issue of ethical values when it encourages:

- commitment to honesty and fairness;
- recognition of and adherence to laws and policies;
- respect for the organization;
- leadership by example;
- commitment to excellence;
- respect for authority;
- respect for employees' rights; and
- conformance with professional standards.

People in an organization have personal and professional integrity when they adhere to ethical values. While it is management's responsibility to establish and communicate the ethical values of the organization, it is everyone's responsibility to demonstrate integrity. Management encourages integrity by:

- establishing and publishing a code of conduct;
- complying with the organization's ethical values and code of conduct;
- rewarding employee commitment to the organization's ethical values;
- establishing methods for reporting ethical violations; and
- consistently enforcing disciplinary practices for all ethical violations.

Management Operating Style and Philosophy reflects management's basic beliefs regarding how the people and activities of an organization should be managed. There are many styles and philosophies. Although none are inherently right or wrong, some may be more effective than others in helping a particular organization accomplish its mission. Management should practice the most effective style and philosophy for the organization, making sure that they reflect the ethical values of the organization, and positively affect staff morale. Management should practice and clearly communicate and demonstrate these beliefs to staff and periodically evaluate whether the style and philosophy are effective and are practiced consistently.

Management's philosophy and style can be demonstrated in such areas as: management's approach to recognizing and responding to risks (both internal and external); acceptance of regulatory control imposed by others; management's attitude toward internal and external reporting; the use of aggressive or conservative accounting principles; the attitude of management toward information technology and accounting functions; and management's support for and responsiveness to internal and external audits and evaluations.

Competence is a characteristic of people who have the skill, knowledge and ability to perform tasks. Management's responsibility for ensuring the competency of its employees should begin with establishing appropriate human resource policies and practices that reflect a commitment to:

- establishing levels of knowledge and skill required for every position;
- verifying the qualifications of job candidates;
- hiring and promoting only those with the required knowledge and skills; and
- establishing training programs that help employees increase their knowledge and skills.

Management should also ensure that employees have what they need to perform their jobs, such as equipment, software and policy and procedure manuals as well as the tools and support they need to perform their tasks.

Morale is the attitude people have about their work, as exhibited by their confidence, discipline and willingness to perform tasks. Management should recognize the importance of good morale in an effective control environment. People's attitude about their jobs, work environment and organization affects how well they do their jobs. Management should monitor the level of staff morale to ensure employees are committed to helping the organization accomplish its mission. Management should also take actions to maintain high morale. Such actions should provide staff with a sense that:

- their opinions and contributions are welcomed, valued and recognized;
- the organization is willing to help improve their level of competency;
- there is opportunity for continuous improvement;
- they have a stake in the mission, goals and objectives of the organization;
- the organization's appraisal and reward systems are fair and consistent; and
- the lines of communication are open.

Supportive Attitude is a disposition that encourages desired outcomes. Since internal control provides management with reasonable assurance that the organization's mission is being accomplished, management should have a supportive attitude toward internal control that permeates the organization. Executive management should set a tone that emphasizes the importance of internal control. Such a tone is characterized by:

- minimal and guarded use of control overrides;
- support for conducting control self-assessments and internal and external audits;
- responsiveness to issues raised as the result of the evaluations and audits; and
- ongoing education to ensure everyone understands the system of internal control and their role in it.

Mission is the organization's reason for existing. It provides a sense of direction and purpose to all members of the organization, regardless of their position, and provides a guide when making critical decisions. During periods of change, it provides cohesion to the organization and helps keep it on its proper course. Without a clearly defined and communicated mission, an organization may drift aimlessly and accomplish little.

The mission of an organization should be a statement, approved by executive management and/or the governing board of the organization. Management should tell employees about the organization's mission and explain how their jobs contribute to accomplishing the mission. The mission statement will be most effective if all employees perceive they have a personal stake in it.

As time passes, both internal and external changes can affect the organization's mission. Therefore, management should periodically review the mission and update it, as necessary, for adequacy and relevancy.

Structure is the framework in which the organization's plans are carried out. It should define the functional sub-units of an organization and the relationships among them.

An organization chart can provide a clear picture of the authority and accountability relationships among functions. The chart should be provided to all employees to help them understand the organization as a whole, the relationships among its various components and where they fit into the organization. Management should review this chart periodically to ensure it accurately reflects the organization's structure.

Management should delegate authority and responsibility throughout the organization. Management is responsible for organizing the entity's authority and accountability relationships among various functions to provide reasonable assurance that work activities are aligned with organizational objectives. With increased delegation of authority and responsibility, there is a need to provide qualified and continuous supervision, and to monitor results. Supervision throughout the organization helps ensure that employees are aware of their duties and responsibilities, and know the extent to which they are accountable for activities.

COMMUNICATION

Communication is the exchange of useful information between and among people and organizations to support decisions and coordinate activities. Information should be communicated to management and other employees who need it in a form and within a time frame that helps them to carry out their responsibilities. Communication with customers, suppliers, regulators and other outside parties is also essential to effective internal control.

Information can be communicated verbally, in writing and electronically. While verbal communication may be sufficient for many day-to-day activities, it is best to document important information. This provides a more permanent record and enables managers and others to review the information.

Information should travel in all directions to ensure that all members of the organization are informed and that decisions and actions of different units are communicated and coordinated. A good system of communication is essential for an organization to maintain an effective system of internal control. A communication system consists of methods and records established to identify, capture and exchange useful information. Information is useful when it is timely, sufficiently detailed and appropriate to the user.

Management should establish communication channels that:

- provide timely information;
- can be tailored to individual needs;
- inform employees of their duties and responsibilities;
- enable the reporting of sensitive matters;
- enable employees to provide suggestions for improvement;
- provide the information necessary for all employees to carry out their responsibilities effectively;
- convey top management's message that internal control responsibilities are important and should be taken seriously; and
- convey and enable communication with external parties.

Communication is not an isolated internal control component. It affects every aspect of an organization's operations and helps support its system of internal control. The feedback from this communication network can help management evaluate how well the various components of the system of internal control are working.

ASSESSING AND MANAGING RISK

Risk should be assessed and managed through an organization-wide effort to identify, evaluate and monitor those events that threaten the accomplishment of the organization's mission. For each risk that is identified, management should decide whether to accept the risk, reduce the risk to an acceptable level, or avoid the risk.

PREPARING TO ASSESS RISK

Management should first ensure that it has identified all the operational and control objectives throughout the organization. Control objectives are generally derived from the four purposes of internal control (as defined in Part I) and are stated in terms that reflect the responsibilities of the organization's sub-units. For example, the following two control objectives are derived from the first two purposes of internal control:

- *Ensure all applications are processed accurately* (from the first purpose of internal control: to promote orderly, economical, efficient and effective operations, and produce quality products and services consistent with the organization's mission).
- *Ensure access to electronic files is restricted to authorized personnel* (from the second purpose of internal control: to safeguard resources against loss due to waste, abuse, mismanagement, errors and fraud).

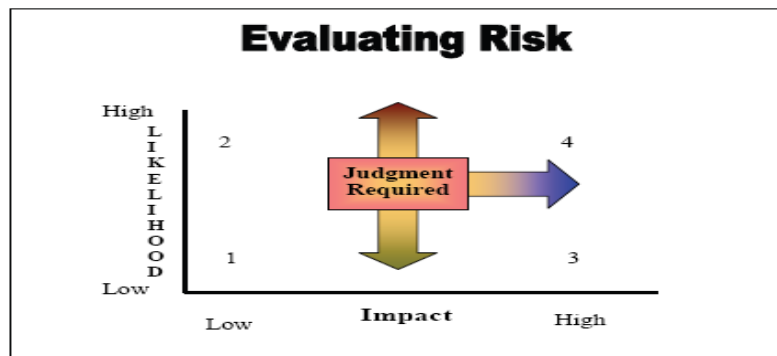
After identifying all the operational and control objectives, managers should identify all the risks associated with each objective (i.e., the events that would threaten the accomplishment of each objective). These risks can be both internal (e.g., human error, fraud, system breakdowns) and external (e.g., changes in legislation, natural disasters). It is essential that managers within the organization identify the risks associated with their respective objectives.

RISK ASSESMENT PROCESS

Management should evaluate each identified risk in terms of its impact and its likelihood of occurrence, as follows:

Impact is the effect an unfavorable event would have on the organization if the event were to occur. This effect could be some type of harm or an opportunity that would be lost. If possible, this effect should be quantified. At the very least, this effect should be described in terms that are specific enough to indicate the significance of the risk.

Likelihood of occurrence is the probability that an unfavorable event would occur if there were no control activities (as described in the following section) to prevent or reduce the risk. A likelihood of occurrence should be estimated for each identified risk



The above chart graphically depicts a reasonable approach to evaluating risks, with quadrant 1 representing the lowest priority and quadrant 4 representing the highest priority risk. Management should use judgment to establish priorities for risks based on their impact and their likelihood of occurrence. Risks should be ranked in a logical manner, from the most significant (high impact) and most likely to occur (high likelihood) - as indicated in quadrant 4 - to the least significant (low impact) and least likely to occur (low likelihood), as indicated in quadrant 1 of the graph.

For example, a program manager has two cash accounts. One is the office petty cash fund and the other is for fees and fines from a program activity. Most people would consider the petty cash to be a quadrant 1 or 2 assessment. When you discover the fees and fines, which are substantial in amount, are stored in an open location and there is a six-month backlog in processing them, this would be a quadrant 4 assessment. Your job is to drive down the level of risk from quadrant 4 to a lower level.

Management should use the information obtained from this assessment to help determine:

- how to manage risk;
- how to prevent or reduce risk; and
- how to manage risk during change.

MANAGING RISK

Executive management should provide guidance to managers throughout the organization to help them assess the level and the kinds of risk that are acceptable and not acceptable. Using this guidance and the risk assessment information, managers should determine whether to accept the risk in a given situation, prevent or reduce the risk, or avoid the risk entirely. For example, in deciding how to manage the risk that unauthorized persons could gain access to electronic files, managers should consider the following possibilities:

- *Accept the risk: Do not establish control activities* - Management can accept the risk of unauthorized access because the consequences of such access are not significant; for example, the files may contain data that is not sensitive. Management might also choose to accept the risk if the cost of the associated control activities is greater than the cost of the unfavorable event.
- *Prevent or reduce the risk: Establish control activities* - Management cannot accept the current level of risk of unauthorized access because the files contain confidential or otherwise inherently valuable data. Therefore, management establishes control activities that are intended to prevent the risk of unauthorized access, or at least reduce the risk to an acceptable level. However, the

risk is prevented or reduced only as long as the control activities function as intended.

- *Avoid the risk: Do not carry out the function* - Management determines that it cannot tolerate any risk of unauthorized access to the files or that it cannot adequately control such access. For example, a file may contain extremely sensitive data, or access controls may not be feasible. In this case, management may decide that the impact of any unauthorized access to this file would be too risky or that access is too difficult or too costly to control. Therefore, management decides not to carry out this function (i.e., decides not to maintain the data).

PREVENTING OR REDUCING RISK

When preventing risk or reducing it to an acceptable level, management should use risk assessment information to help identify the most effective and efficient control activities available for handling the risk. Specifically, management should answer the following questions:

- *What is the cause of the risk?* Management should consider the reason the risk exists to help identify all the possible control activities that could prevent or reduce the risk.
- *What is the cost of control vs. the cost of the unfavorable event?* Management should compare the cost of the risk's effect with the cost of carrying out various control activities, and select the most cost-effective choice.
- *What is the priority of this risk?* Management should use the prioritized list of risks to help decide how to allocate resources among the various control activities used to reduce the risks. The higher the priority, the greater the resources allocated to the control activities intended to reduce the risk.

Management should maintain its analysis and interpretation of the risk assessment information as part of its documentation of the rationale that supports its risk management decisions. Management should review these decisions periodically to determine whether changes in conditions warrant a different approach to managing, preventing and reducing risk.

MANAGING RISK DURING CHANGE

When change occurs in an organization (e.g., new processes, new systems, significant changes in job responsibilities, reorganizations, significant changes in personnel), it often affects the control activities that were designed to prevent or reduce risk. In order to properly manage risk, management should monitor any change to ensure that each risk continues to be managed as change occurs. Management should inform employees responsible for managing the organization's most critical risks about any proposed changes that may affect their ability to manage those risks. Managers should continually monitor the factors that can affect the risks they have already identified as well as other factors that could create new risks.

CONTROL ACTIVITIES

Control activities are tools - both manual and automated - that help identify, prevent or reduce the risks that can impede accomplishment of the organization's objectives. Management should establish control activities that are effective and efficient.

When designing and implementing control activities, management should try to get the maximum benefit at the lowest possible cost. Here are a few simple rules to follow:

- The cost of the control activity should not exceed the cost that would be incurred by the organization if the undesirable event occurred.
- Management should build control activities into business processes and systems as the processes and systems are being designed. Adding control activities after the development of a process or system is generally more costly.
- The allocation of resources among control activities should be based on the significance and likelihood of the risk they are preventing or reducing.

Many different control activities can be used to counter the risks that threaten an organization's success. Most control activities, however, can be grouped into two categories: prevention and detection control activities.

- Prevention activities are designed to deter the occurrence of an undesirable event. The development of these controls involves predicting potential problems before they occur and implementing ways to avoid them.
- Detection activities are designed to identify undesirable events that do occur, and alert management about what has happened. This enables management to take corrective action promptly.

Prevention controls tend to be more expensive than detection controls. Costs and benefits should be assessed before control activities are implemented. Management should also remember that an excessive use of prevention controls can impede productivity. No one control activity provides all of the answers to risk management problems. In some situations, a combination of control activities should be used, and in others, one control activity could substitute for another. The following are descriptions of some of the more commonly used control activities. This is by no means an exhaustive listing of the alternatives available to management.

DOCUMENTATION

Documentation involves preserving evidence to substantiate a decision, event, transaction or system. All documentation should be complete, accurate and recorded timely. Documentation should have a clear purpose and be in a usable format that will add to the efficiency and effectiveness of the organization. Examples of areas where documentation is important include critical decisions, significant events, transactions, policies, procedures and the system of internal control.

Critical decisions and significant events usually involve executive management. These decisions and events usually result in the use, commitment, exchange or transfer of resources, such as in strategic plans, budgets and executive policies. By recording the information related to such events, management creates an organizational history that can serve as justification for subsequent actions and decisions and will be of value during self-evaluations and audits.

Documentation of transactions should enable managers to trace each transaction from its inception through its completion. This means the entire life cycle of the transaction should be recorded, including: (1) its initiation and authorization; (2) its progress through all stages of processing; and (3) its final classification in summary records. For example, the documentation for the purchase of equipment would start with the authorized purchase request, and continue with the purchase order, the vendor invoice and the final payment documentation.

Documentation of policies and procedures is critical to the daily operations of an organization. These documents set forth the fundamental framework and the underlying methods and processes all employees rely on to do their jobs. They provide specific direction to and help form the basis for decisions made every day by employees. Without this framework of understanding by employees, conflict can occur, poor decisions can be made and serious harm can be done to the organization's reputation. Further, the efficiency and effectiveness of operations can be adversely affected.

The documentation of an organization's system of internal control should include the organization's structure, policies, assessable units, control objectives and control activities. The various aspects of a system of internal control can be represented in narrative form, such as in policy and procedure manuals, and/or in the form of flowcharts or matrices.

APPROVAL AND AUTHORIZATION

Approval is the confirmation or sanction of employee decisions, events or transactions based on a review. Management should determine which items require approval based on the level of risk to the organization without such approval. Management should clearly document its approval requirements and ensure that employees obtain approvals in all situations where management has decided they are necessary. For example, a manager reviews a purchase request from an employee to determine whether the item is needed. Upon determining the need for the item, the manager signs the request indicating approval of the purchase.

Authorization is the power management grants employees to carry out certain duties, based on approval received from supervisors. Authorization is a control activity designed to ensure events or transactions are initiated and executed by those designated by management. Management should ensure that the conditions and terms of authorizations are clearly documented and communicated, and that significant transactions are approved and executed only by persons acting within the scope of their authority. For example, a manager may be authorized by his/her supervisors to approve purchase requests, but only those up to a specified dollar amount.

VERIFICATION

Verification is the determination of the completeness, accuracy, authenticity and/or validity of transactions, events or information. It is a control activity that enables management to ensure activities are being done in accordance with directives. Management should determine what needs to be verified, based on the risk to the organization if there were no verification. Management should clearly communicate and document these decisions to those responsible for conducting the verifications. An example of verification is ensuring that a fair price has been obtained in a purchase and funds are available to pay for the purchase.

SUPERVISION

Supervision is the ongoing oversight, management and guidance of an activity by designated employees to help ensure the results of the activity achieve the established objectives. Those with the responsibility for supervision should:

- monitor, review and approve, as appropriate, the work of those performing the activity to ensure the work is performed correctly;
- provide the necessary guidance and training to help minimize errors and waste and to ensure that employees understand and follow management directives; and
- clearly communicate the duties and responsibilities assigned to those performing the activities.

An example of supervision is when an assigned employee (supervisor) reviews the work of another employee processing a purchase order to determine whether it is prepared accurately and completely, and has been properly authorized. The supervisor then signs the order to signify his/her review and approval. However if there are any errors, the supervisor would return the order to the employee and explain how to complete the request properly.

SEPARATION OF DUTIES

Separation of duties is the division of key tasks and responsibilities among various employees and sub-units of an organization. By separating key tasks and responsibilities - such as receiving, recording, depositing, securing and reconciling assets - management can reduce the risk of error, waste, or wrongful acts. The purchasing cycle is an area where the separation of duties can minimize the risk of inappropriate, unauthorized or fraudulent activities. Specifically, the various activities related to a purchase (initiation, authorization, approval, ordering, receipt, payment and recordkeeping) should be done by different employees or sub-units of an organization. In cases where tasks cannot be effectively separated, management can substitute increased supervision as an alternative control activity that can help prevent or reduce these risks.

SAFEGUARDING ASSETS

The safeguarding of assets involves restricting access to resources and information to help reduce the risk of unauthorized use or loss. Management should protect the organization's equipment, information, documents and other resources that could be wrongfully used, damaged or stolen. Management can protect these resources by limiting access to authorized individuals only. Access can be limited by various means such as locks, passwords, electronic firewalls and encryption. Management should decide which resources should be safeguarded and to what extent. Management should make this decision based on the vulnerability of the items being secured and the likelihood of loss.

REPORTING

Reporting is a means of conveying information. It serves as a control when it provides information on issues such as timely achievement of goals, budget status and employee concerns. Reporting also helps to promote accountability for actions and decisions. An example of a report that serves as a control activity would be one that compares purchasing activities with the approved budget, indicating and explaining significant variances between the two.

CONTROL ACTIVITIES FOR INFORMATION TECHNOLOGY

While some of the control activities relating to information technology (IT) are the responsibility of specialized IT personnel, other IT control activities are the responsibility of all employees who use computers in their work. For example, any employee may use:

- encryption tools, protocols, or similar features of software applications that protect confidential or sensitive information from unauthorized individuals;
- back-up and restore features of software applications that reduce the risk of lost data;
- virus protection software; and
- passwords that restrict user access to networks, data and applications.

IT control activities can be categorized as either general or application controls. General controls apply to all computerized information systems - mainframe, minicomputer, network and end user environments. Application controls apply to the processing of data within the application software.

General and application controls are interrelated. General controls support the functioning of application controls, and both types of controls are needed to ensure complete and accurate information processing.

GENERAL CONTROLS

General controls are concentrated on six major types of control activities: an entity-wide security management program; access controls; application software development and change; system software controls; segregation of duties; and service continuity.

An organization-wide security management program includes a comprehensive, high level assessment of risks to information systems. Organizations should have a plan that clearly describes the organization's security management program and policies and the procedures that support it, including procedures for the secure storage and disposal of sensitive information. Organizations should also establish a structure to implement and manage the security program with security responsibilities clearly defined. In addition, organizations should monitor the effectiveness of the security program and make changes as needed.

Access security controls are physical and software processes to prevent or detect unauthorized access to systems and data. These controls protect the systems from inappropriate access and unauthorized use by hackers and other trespassers or inappropriate use by agency personnel. Specific control activities may include restrictions on users allowing access only to the system functions they need to perform their assigned duties; software and hardware "firewalls" to restrict access to assets, computers, and networks by external persons; frequent changes of passwords and deactivation of former employees' passwords; frequent changes of dial-up numbers; and use of dial-back access.

Application software development and change control provides the structure for the safe development of new systems and the modification of existing systems. Control activities should include: system documentation requirements; authorizations for undertaking projects; and reviewing, testing, and approving development and modification activities before placing systems into operation.

System software control is the controlling and monitoring of access to use and changes made to system software, including: security procedures over the acquisition, implementation, and maintenance of all system software; data-based management systems; telecommunications; security software; and utility programs.

The concept of segregation of duties in a computer environment is the same as in a manual process. Key tasks and responsibilities should be divided among various employees and sub-units of the computer operations. No one individual should control all of the primary elements of a transaction, event or process. Identifying incompatible duties and implementing policies to separate those duties can be monitored through the use of access controls as well as by implementing operating procedures, supervision, and the review of employee activities.

Service continuity is concerned with maintaining or reestablishing the activities or level of service provided by an organization in the event of a disaster or other damaging occurrence. It is critical that an organization have backup and recovery procedures, and contingency and disaster plans. Data center and client-server operation controls involve steps to prevent and minimize potential damage to hardware and software and the interruption of service through the use of data and program backup procedures. Such procedures include: off-site storage of backup data; environmental controls; staff training; and hardware maintenance and management. Organizations should develop, document, and periodically test their contingency plans.

APPLICATION CONTROLS

Application controls help ensure that transactions are valid, properly authorized, and processed and reported completely and accurately. These controls also take into account the whole sequence of transaction processing from the preparation of the initial source document or online data entry, to the creation and use of the final output. As such, application controls consist of input, processing, and output controls:

- Input controls include processes for verifying data accuracy and completeness upon data-entry to a system. These controls also provide specific mechanisms for input authorization, data conversion, data editing and error handling.
- Processing controls help ensure that data remains complete and accurate during updating, and that the application programs perform as intended.
- Output controls help ensure that system-generated information is accurate, properly recorded, and received or reviewed by authorized individuals only.

As information technologies advance and internet use increases, modifications will have to be made in each organization's specific IT control activities. However, the basic requirements of control will not change. As more powerful computers place more responsibility for data processing in the hands of the end users and as internet use grows, organizations must be prepared to implement the controls necessary to maintain an effective system of internal control.

This information is not meant to be a complete explanation of all IT control activities. Additional guidance has been issued by the New York State Office of Cyber Security & Critical Infrastructure Coordination and by the New York State Office for Technology. Further guidance can also be obtained from sources such as the Information Systems Audit and Control Foundation's *Control Objectives for Information and Related Technology* and the Federal Government's National Institute for Standards and Technology's Special Publications.

MONITORING

Monitoring is the review of an organization's activities and transactions to assess the quality of performance over time and to determine whether controls are effective. Management should focus monitoring efforts on internal control and achievement of the organization's mission. For monitoring to be most effective, all employees need to understand the organization's mission, objectives, risk tolerance levels and their own responsibilities.

Everyone within an organization has some responsibility for monitoring. The position a person holds in the organization helps to determine the focus and extent of these responsibilities. Therefore, the monitoring performed by staff, supervisors, mid-level managers and executives will not have the same focus, as follows:

- **Staff** - The primary focus of staff should be on monitoring their own work to ensure it is being done properly. They should correct the errors they identify before work is referred to higher levels for review. Management should educate staff regarding control activities and encourage them to be alert to and report any irregularities. Because of their involvement with the details of the organization's daily operations, staff has the best vantage point for detecting any problems with existing control activities. Management should also remind staff to note changes in their immediate internal and external environments, to identify any risks and to report opportunities for improvement.
- **Supervisors** - Supervision is a key element of monitoring. Supervisors should monitor all activities and transactions in their unit to ensure that staff are performing their assigned responsibilities, control activities are functioning properly, the unit is accomplishing its goals, the unit's control environment is appropriate, communication is open and sufficient, and risks and opportunities are identified and properly addressed.
- **Mid-Level Managers** - Mid-level managers should assess how well controls are functioning in multiple units within an organization, and how well supervisors are monitoring their respective units. The focus of these managers should be similar to that of supervisors, but extended to cover all the units for which they are responsible.
- **Executive Management** - Executive management should focus their monitoring activities on the major divisions of the organization. Because of this broader focus, executive managers should place even more emphasis on monitoring the achievement of the organization's goals. Executive managers should also monitor for the existence of risks and opportunities in either the internal or external environment that might indicate the need for a change in the organization's plans.

Management should ensure that it takes the proper actions to address the results of monitoring. For example, management may decide to establish new goals and objectives to take advantage of newly identified opportunities, may counsel and retrain staff to correct procedural errors, or may adjust control activities to minimize a change in risk.

The monitoring performed by staff, supervisors, mid-level managers and executives should focus on the following major areas:

- **Control Activities** - Control activities are established to prevent or reduce the risk of an unfavorable event from occurring. If these activities fail, the organization becomes exposed to

risk. Control activities can fail when controls are overridden, or when there is collusion for fraudulent purposes. Therefore, management should establish procedures to monitor the functioning of control activities and the use of control overrides. Management should also be alert to signs of collusion. Effective monitoring gives management the opportunity to correct any control activity problems and to control the risk before an unfavorable event occurs.

- **Mission** - Monitoring activities should include the development and review of operational data that would allow management to determine whether the organization is achieving its mission. This can be achieved by periodic comparison of operational data to the organization's strategic plan.
- **Control Environment** - Executive management should monitor the control environment to ensure that managers at all levels are maintaining established ethical standards of behavior and that staff morale is at an appropriate level. Managers should also ensure that the staff is competent, that training is sufficient and that management styles and philosophies foster accomplishment of the organization's mission.
- **Communication** - Managers should periodically verify that the employees they are responsible for are receiving and sharing information appropriately, and that this information is timely, sufficient and appropriate for the users. Management should ensure that there are open lines of communication, which fosters reporting of both positive and negative results.
- **Risks and Opportunities** - Managers should also monitor the organization's internal and external environment to identify any changes in risks and the development of opportunities for improvement. If changes are identified, managers should take appropriate action to address these new or changed risks and opportunities. Management should recognize that delays in responding to risks could result in damage to the organization and a missed opportunity may result in a loss of new revenue or savings.

PART III SUPPORTING ACTIVITIES

Evaluation, strategic planning and internal audit are all activities that support a good system of internal control. They provide management with additional tools to help ensure that the mission of the organization will be achieved.

EVALUATION

Evaluation is the process management uses to determine whether:

- the organization will likely achieve its goals and objectives;
- the elements of the organization's system of internal control are functioning effectively; and
- risks to the organization and opportunities for improvement are being identified.

It is important to note the distinction between evaluation and monitoring. Monitoring involves performing daily or routine procedures - like supervision, transaction review and problem resolution - that help to ensure operations are in compliance with the organization's system of internal control. Evaluation, on the

other hand, involves doing periodic assessments of the organization's performance compared to established expectations or measurement standards.

Evaluation can be accomplished through self-assessment and independent review. Self-assessment should be the primary basis for evaluation. Regular self-assessment helps management detect problems early, and thus minimizes the costs of these problems. Self assessments should be scheduled regularly, and should be performed throughout the organization. The frequency of self-assessment should be based, in part, on the results of the organization's risk assessment process. Independent reviews can be performed by external auditors, consultants, and internal auditors who are independent of the operations to be reviewed. Such reviews should not be a substitute for routine self-assessments, but should serve to supplement them.

To perform an orderly, systematic evaluation of an organization's system of internal control, management should segment the organization into "assessable units." Assessable units are not usually the functional sub-units found on an organization chart (e.g., a bureau), but are segments of them. For example, a bureau may have five or more assessable units in it, each of which performs a distinct function.

An assessable unit has certain primary characteristics. It has an ongoing, identifiable purpose that results in the creation of a service or product (used either internally or externally) and/or that fulfills a law, regulation or other mandate. An assessable unit should be large enough to allow managers to evaluate a significant portion of the activity being examined, but not so large that managers cannot perform a meaningful evaluation without extensive time and effort.

Management should maintain a listing of the assessable units along with the purpose and objectives of each assessable unit, and use it when planning any review of the system of internal control.

The managers of the assessable units should have the responsibility for determining the effectiveness of the system of internal control within their respective units. Managers should ask such questions as:

- Do the unit's objectives provide it with a clear direction?
- Do people in the unit understand the objectives, and how achievement of the objectives helps to accomplish the organization's mission?
- Does the control environment help to foster achievement of the unit's objectives?
- Does the unit have a means of effectively identifying and managing risk?
- Has unit management established the controls needed to minimize risk?
- Are the controls functioning as designed?
- Are the controls both effective and efficient in accomplishing their purpose?
- Does the unit receive the timely, accurate and useful information needed to achieve its objectives?
- Are communication lines sufficient to meet the needs of senders and receivers of information?
- Is monitoring within the unit effective in ensuring that daily operations are in compliance with the system of internal control?
- Is the unit effectively monitoring the accomplishment of objectives, the control environment and the communication process?
- Does monitoring adequately identify changes in the internal or external environment?

Management should assess accomplishment of the mission at all levels of the organization on a regular basis. At production or operational levels, management should compare the actual accomplishments of

the specific sub-units with their operational plans and objectives. Management should compare the actual accomplishments of the major organizational divisions with strategic plans and organizational objectives. In addition, any new risks or opportunities that are identified in the assessment process may result in changes to the organization's objectives, or modification of its mission.

All aspects of the self-assessment process should be documented, including the evaluation methodologies, the sources and types of information used, reporting relationships, any deficiencies identified, and any corrective action recommended. The results of the assessment should be communicated throughout the organization, and management should have processes in place to ensure that appropriate and prompt actions are taken to address any deficiencies identified. Management should include a review of these corrective actions in a subsequent evaluation process to determine if they have produced the desired outcomes.

STRATEGIC PLANNING

Strategic plans are the courses of action that will enable an organization to achieve its objectives and goals. Planning should begin at the top levels of management with a strategic plan that focuses on the long-range direction of the organization. The strategic planning process should include establishing the organization's broad organizational objectives and developing the strategies that should be followed to achieve them. Based on the direction provided by the organization's strategic plan, management should develop plans for each major organizational division with a long-range focus specific to that division. The division plans guide managers in developing shorter-range operational plans for each of the major functions performed within their respective divisions.

OBJECTIVES

Objectives are the organization's desired outcomes. They are a product of the planning process and are necessary for coordinating efforts within an organization. Without clearly defined objectives, employees could be working inefficiently, ineffectively and/ or in conflicting directions.

Objectives can be organizational or operational. Management derives organizational objectives from the mission and often develops them during the strategic planning process. They are long range, broad statements, which define the desired outcomes of the organization as a whole. Good organizational objectives can serve as starting points for more specific and detailed objectives within the sub-units (i.e., divisions, departments, bureaus and assessable units) of the organization. They also serve as standards for evaluating overall organizational performance.

Management derives operational objectives from the broad organizational objectives. Operational objectives are shorter-range, more specific and define the desired outcomes of each of the organization's sub-units. They should be structured in a hierarchy so that each sub-unit's accomplishment of its operational objectives helps the next higher level achieve its operational objectives, all of which helps management meet its organizational objectives.

All objectives should be in writing. Management should provide employees with written organizational and operational objectives along with the mission statement. Management should ensure that employees understand the objectives and how their work helps to achieve them.

Finally, just as changes in the environment can affect the adequacy and relevancy of the mission statement, these same factors can also affect an organization's objectives. For an organization to function effectively and grow, it should periodically reassess its organizational and operational objectives.

GOALS

Goals are objectives translated into specific, measurable targets. They are quantifiable and provide a means for assessing the accomplishment of objectives.

Management should translate all objectives into attainable goals. Progress toward these goals can help measure accomplishment of an objective. Sometimes it is difficult to translate an objective into a quantifiable goal. In such instances, management should identify some other appropriate indirect.

OPERATIONAL PLANS

Managers at all levels should be able to use operational plans to determine the priority and timing of objectives, to resolve conflicts between objectives, to establish the organization's policies and procedures, and to help set budgets, schedules and resource assignments. Planning should be based on the most objective and accurate information available. All planning processes should identify the most efficient alternatives available for accomplishing the objectives.

The plans should be provided to and understood by everyone who must follow them. Management should also establish a process that identifies how and when plans should be changed to reflect both changing conditions and the availability of more accurate information. Plans should be flexible enough to allow for such changes.

INTERNAL AUDIT

Internal audit functions add value to an organization's internal control system by bringing a systematic, disciplined approach to the evaluation of risk and by making recommendations to increase the effectiveness of risk management efforts, improve the internal control structure and promote good corporate governance. The Legislature, in passing the Internal Control Act, recognized the internal audit function's key role in supporting the internal control system and, as such, made the Division of the Budget responsible for designating which State agencies would be required to maintain internal audit units. The Division of the Budget makes this determination based in part on the size, nature and/or complexity of agency operations. Other entities may choose to establish an internal audit function as part of their management of risks and resources. In either case, the Internal Control Act requires that these units be organized and operated in accordance with professional audit standards; in particular *The Standards for the Professional Practice of Internal Auditing* promulgated by the Institute of Internal Auditors. This section, with consideration of the recommendations promulgated in 2006 by the New York State Internal Control Task Force, further interprets those standards as they apply to New York State entities and as such, forms the minimum expectations for the organization and operation of internal audit units within New York State government. Other organizational aspects related to the formation of an internal audit unit, including minimum qualifications for internal audit directors, are addressed by the Division of the Budget in Item B-350 of its Budget Policy and Reporting Manual entitled *Government Internal Control and Internal Audit Requirements*.

Auditor Independence and Compatibility with Other Duties

A major underlying principle of professional audit standards is that the internal audit function must be organizationally independent of other business activities and free from interference in establishing the scope of its work and the communication of results. This organizational alignment promotes objectivity and allows the auditor to maintain an impartial, unbiased attitude and avoid conflicts of interest. Internal audit independence and objectivity are important to credibility and are hallmarks of executive management's commitment to promoting a strong, introspective approach to corporate governance. These values provide a basis that executive managers, audit committees and third parties can rely upon when considering the internal auditor's findings and recommendations. To ensure independence and objectivity, the internal audit function should ideally be organized under the chief executive and report directly to any audit committee, board of directors or other governing authority that may exist. As a practical matter, internal audit directors in State entities may report to the deputy head of their organizations, such as the executive deputy commissioner, provided that person does not have line management responsibilities.

Auditor independence also entails refraining from duties that are incompatible with the objective appraisal of operations. Internal auditors should therefore avoid assuming operational responsibilities or engaging in other activities that may impair their independence, including functioning as their entity's Internal Control Officer (ICO). On the most basic level, the ICO duties are defined as working with appropriate agency personnel to coordinate the internal control activities, and to ensure that the agency's internal control program meets the requirements established in agency policy. The ICO role is therefore a management function that requires decisions about the overall design and implementation of the internal control system and as such, is generally incompatible with the role of the internal auditor. Similarly, internal auditors should also avoid functioning as their entity's Information Security Officer (ISO), as this role not only requires specialized expertise, but can also require the auditor to perform management functions or make management-level decisions.

As a practical matter, smaller agencies may not have sufficient resources to fully separate their internal audit, internal control and information security functions. In these situations, the internal auditor should limit his/her role to the extent possible, being careful to avoid decision making in areas such as the specific type of controls needed or the quality of controls in place. For example, if the internal auditor undertakes any internal control responsibilities, there needs to be clear communication, as part of that process, that agency managers are responsible for maintaining an appropriate system of internal controls. Further, the agency's annual internal control certification, as well as any subsequent audits of the internal control system, should each fully disclose the internal auditor's role in the internal control process.

Separation of the internal control and internal audit functions does not preclude a strong working relationship that can create synergies between the two activities. Creating a sense of unanimity between the internal control and internal audit functions will improve the overall internal control culture of an agency. The internal control and internal audit functions reinforce one another when:

- The internal auditor uses internal control reports when planning audits;
- The auditor consistently evaluates and reports on compliance with internal control requirements in audit reports, as part of the auditor's assessment of internal controls;

- The internal control officer reviews internal audit reports on a regular basis to ensure that agency managers incorporate significant risks, findings and recommendations into the internal control system; and
- Follow-up audits address whether significant risks, findings and recommendations have been addressed and incorporated into the agency's internal control system.

Adopting these steps will provide the internal auditor and ICO with continuous feedback on the quality of the internal control system and, as a result, lower the risk that the system may be ineffective or lose its effectiveness over time.

Maintenance of auditor objectivity also requires a continuing assessment of each auditor's relationship with the operations she or he audits. Internal audit units therefore need to establish procedures to identify personal impairments to independence and should obtain information concerning potential conflicts of interest and bias from audit staff at least annually. Auditors should also immediately report any new impairment that arises to their internal audit director.

RISK-BASED AUDIT PLANNING

Internal audit units exist in major part in New York State due to the provisions of the Act, which focuses largely on control systems internal to the entity. In fact, the Act specifically requires that the internal audit function shall evaluate the agency's internal controls and operations. To fulfill this responsibility, the internal audit units must devote resources to examining their organization's internal operations and cannot simply audit outside parties that conduct business with their organizations, such as contractors, grantees or service providers. Still, the Act does not specify the minimum level of audit resources that must be devoted to internal activities, and there is no expectation that all internal audit resources be directed internally. Rather, the appropriate allocation is best determined as part of a larger analysis of risks facing the particular entity.

The Director of Internal Audit in each State agency should periodically develop a risk-based plan of audit engagements to determine the priorities for the internal audit activity. This audit plan should be primarily based on a risk assessment, which is updated at least annually. As part of this assessment, the internal audit unit should review and test documentation maintained by the agency's Internal Control Officer in support of the entity's annual certification. Depending on the results of these tests, the internal audit unit may be able to form a basis to rely on the certification or may decide to set it aside and conduct its own separate review of internal controls. When audits of internal control systems are performed, the auditor should identify the specific objectives of the examination and should consider examining each of the five elements of internal control discussed in these Standards: control environment, information and communication, assessing and managing risk, control activities and monitoring. Depending on the needs of the agency, the audit unit may need to expand the scope of their inquiry even further.

Senior management and governing board input (where applicable) should also be considered in audit planning process to ensure the plan of engagements is consistent with the organization's goals. Further, the auditor should share information and coordinate activities with other internal and external providers of relevant assurance and consulting services, both to ensure proper coverage and to minimize duplication of efforts. The Director of Internal Audit should communicate the audit plan and the associated resource requirements, including any significant interim changes, to senior management and to the board for review and approval. The Director of Internal Audit should also communicate the impact of any resource

limitations and should ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.

CONTINUING PROFESSIONAL EDUCATION

To be effective in a changing world, all audit staff need to maintain and enhance their technical competence through a program of continuing education. Professional audit standards, as well as various professional licensing programs including the Certified Internal Auditor and the Certified Public Accountant are all subject to periodic continuing education requirements. The Internal Control Task Force report provides an extensive discussion on the need for continuing education and training of the State's internal auditors. The consensus recommendation is that each auditor is required to obtain at least 80 hours of continuing professional education every two years, with not less than 20 hours obtained during any single year. This requirement is consistent with the level of training required of other professionals conducting audits of government programs. The Task Force report appendix entitled *Guidance on Continuing Education Requirements for New York State Internal Auditors* provides a more detailed discussion of these requirements, and is incorporated by reference as part of these standards.

COMMUNICATIONS

Communication is also a critical factor in ensuring that internal audit operations provide maximum value to the organization. Professional standards require periodic meetings between the internal auditor, executive management and any governing board or audit committee that may exist. These meetings are essential to ensure the independence, effectiveness and accountability of the internal audit activity and should be held at least quarterly. The timely distribution of internal audit reports is another integral way that communication supports the independence, effectiveness and credibility of the internal audit organization. Distributing the audit reports to all stakeholders, including executive management, provides reasonable assurance that the agency will take action on the findings and recommendations contained therein. The internal audit director should be responsible for the distribution of each audit report and should provide copies to the agency head, the deputy head, the internal control officer, the audit committee (if applicable) and the head of the audited operation. Any further distribution of audit reports should be made only with the knowledge and permission of executive management.

MONITORING AUDIT FINDINGS

The Internal Control Act requires internal auditors identify internal control weaknesses that have not been corrected and make recommendations to correct those weaknesses. To accomplish this, each unit needs to establish and maintain a system to monitor the disposition of audit recommendations communicated to management. The auditor should document the rationale in deciding which audit recommendations should be followed up on and when, in contrast with recommendations where no follow-up is needed. The auditor should also follow up with management to document either that audit recommendations have been effectively implemented, or that senior management has accepted the risk of not implementing the recommendations. To the extent agreed upon with management, the internal audit unit should also monitor the disposition of recommendations arising for any non-audit services.

MAINTAINING AUDIT DOCUMENTATION

Internal audit units should maintain documentation for each audit and subsequent follow-up. This documentation should contain sufficient information to enable an experienced auditor who has no previous connection with the audit to ascertain the evidence that supports the auditors' significant

judgments and conclusions. Each internal audit unit should establish a formal policy that clearly delineates who is responsible for reviewing audit documentation prepared by various staff levels and when that review should occur.

Audit documentation is the auditors' property and should be kept under their control. The auditors should know exactly where all pieces of documentation are at all times during the conduct of the audit. Approval from senior management and/or legal counsel should be obtained prior to releasing copies of audit documentation and reports to external parties. When not in use, documentation should be kept in a locked file or otherwise secured so as not to be readily available to persons who are not unauthorized to access it. This includes protecting electronic information with appropriate IT security controls. Audit documentation should be retained for a minimum of seven years after the date of the audit report. For recurring audits, the documentation supporting previous audits may be filed in a centralized record retention provided an individual is assigned to maintain a record of the location of each item sent to record storage and an appropriate destruction date is scheduled for the material.

EXTERNAL QUALITY ASSESSMENT REVIEW

Professional audit standards require each internal audit organization to periodically undergo an independent review of the quality of their audit activities. The purpose of this review is to ensure that the organization's quality control system is suitably designed and consistently complied with to the extent necessary to reasonably ensure compliance with audit standards. External assessments also promote more effective and efficient internal auditing operations by identifying better practices and making recommendations intended to improve performance. Periodic quality assessments are also an important means of reinforcing management's confidence in the work of the internal audit unit. As such, each internal audit unit in New York State government must have an appropriate external quality assessment review performed at least once during every five year period.

APPENDIX B

New York State Energy Research and Development Authority

CODE OF CONDUCT

A Guide for NYSERDA Employees

Introduction

To maintain the confidence of the public, all NYSERDA employees shall conduct business in an honest and ethical manner, reflecting such values as integrity, fairness, and trustworthiness. This Code of Conduct summarizes a number of basic standards and State and Federal laws that NYSERDA employees and Board Members of NYSERDA are required to follow while acting in that capacity on behalf of the organization.

This Code of Conduct is not intended to cover all situations and answer all questions. Additional administrative guidance and direction can be found in NYSERDA's policy and procedure manuals. Legal guidance and direction is available through NYSERDA's Ethics Officer, who is an attorney in the Counsel's Office. Questions about a specific situation should be directed to your supervisor, the Director of Internal Audit, the Manager of Human Resources, the Counsel's Office, or NYSERDA Officers. Additionally, you may contact the New York State Joint Commission on Public Ethics directly about any questions or issues.

General Conduct

You are expected to maintain the standards of conduct described in this Code of Conduct. You must:

- Conduct yourself in a manner that is consistent with NYSERDA policies and procedures and the State and Federal laws that apply to you as a NYSERDA employee.
- Conduct yourself in a manner that is consistent with the public trust and the proper performance of your duties, including refraining from engaging in outside activities that would impair your independence of judgment.
- Conduct business with NYSERDA contractors in a manner that does not give the impression that any person can improperly influence you or unduly enjoy your favor.

(See Personnel Handbook Section 2 and cited references)

Conflicts of Interest

As a public employee, you are bound by the Public Officers Law and must endeavor to pursue a course of conduct that will not raise suspicion among the public that you are likely to be engaged in acts of violation of your public trust. You must not use your official position to secure special privileges for yourself or others or engage in outside business activities that might interfere with or compromise your ability to perform your official NYSERDA duties. Actual or potential conflicts of interest with individuals or entities doing business with NYSERDA should be disclosed to supervisory personnel immediately *(See Appendix C: Whistleblower Policy)*.

You may not engage in outside activities that would conflict with scheduled work hours or that would impair your judgment or compromise or interfere with your ability to properly perform your duties. You may not use NYSERDA time, materials, equipment, or other assets in connection with outside activities. NYSERDA employees who are designated policymakers must obtain approval before engaging in any outside activity if the amount to be earned exceeds \$1,000 annually.

The New York State Joint Commission on Public Ethics publishes opinions concerning the Public Officers Law, including what constitutes a conflict of interest and can be an additional source of guidance. *(See Personnel Handbook Section 2 and the references cited in Section 2)*

Improper Gifts

No gift of **any** value may be accepted if it would constitute a substantial conflict with the proper discharge of your duties. In addition, Section 73(5) of the Public Officers Law prohibits you from directly or indirectly soliciting, accepting, or receiving any gift that has more than nominal value where the circumstances would reasonably permit the inference that the gift:

- was intended to influence you, or could reasonably be expected to influence you, in the performance of your duties; or
- was intended as a tip, reward, or sign of appreciation for your official action.

A gift may be in many forms including, but not limited to, money, property, service, loan, travel, meals, special favors, refreshments, entertainment, hospitality, promise, or discount.

The New York State Joint Commission on Public Ethics has issued regulations on gifts, and issues opinions concerning the Public Officers Law, including what constitutes acceptable and unacceptable gifts, and can be an additional source of guidance. *(See Personnel Handbook Section 2, the cited references in Section 2 and Appendix B, and the New York State Joint Commission on Public Ethics opinions and interpretations)*

Discriminatory Practices or Harassment

Discriminating against or harassing other employees or contractors on the basis of race, religion, sex, national origin, age, disability, marital status, or sexual orientation is strictly prohibited. *(See Personnel Handbook Section 11 and the references cited in Section 11)*

Confidential Information

Confidential, proprietary, and trade-secret information acquired by you in the course of your official duties may not be disclosed or used to further your or another's personal interests, including financial interests. *(See Public Officers Law section 74(3)(c), Personnel Handbook Section 2 and cited references, and Operations and Procedures Handbook Section 4.5)*

Financial Interests

You should not retain or obtain a financial interest in any person or organization that does business with NYSERDA if you are or are likely to participate or be involved in the decision-making process at NYSERDA in a matter involving that person or organization.

You should not provide inside information to any person except in carrying out NYSERDA's corporate purposes, or give advice or make recommendations or suggestions to another person on the basis of inside information. *(See Personnel Handbook Appendix B)*

Controlled Substances and Alcohol

The sale, attempt to sell, possession, or purchase of non-prescribed controlled substances while at the workplace or while performing in a work-related capacity is prohibited. Employees also are prohibited from being impaired by controlled substances or alcohol while on the job or on the work site. *(See Personnel Handbook Section 17)*

Use of NYSERDA Assets

You are expected to use all equipment, materials, and other office property in a responsible manner. Employees should not use NYSERDA time, property, equipment, or supplies for personal use or private gain. This includes, but is not limited to, NYSERDA's telephones, computer systems, personal digital assistants, stationary, supplies, copiers, postage, internal office, mail, inter-city couriers, and vehicles. Certain personal use is not prohibited when it is incidental, necessary, and limited in number and duration, such as the reasonable personal use of telephones and electronic mail, and does not conflict with the proper exercise of the employee's duties. NYSERDA's President and CEO has unrestricted use of NYSERDA fleet vehicles, as provided in and subject to the requirements of the NYS Division of Budget's Policy D-750 on State Vehicles. *(See Personnel Handbook Section 2)*

Political Activity

Employees are under no obligation to contribute to any political fund or perform any political service. Employees may not use job-related influence to force political activity on the part of others nor may others make the demand on them. You may not require employees or potential employees and contractors or potential contractors to reveal information on party affiliation or campaign contributions. Should you intend to run for political office, you should obtain your supervisor's and Counsel's Office concurrence that the public office to be sought will not interfere with your official NYSERDA duties and is allowed under State and Federal Law. Policymakers seeking public office for which more than nominal compensation will be paid must first obtain the approval of the New York State Joint Commission on Public Ethics. *(See Personnel Handbook Section 2 and State Ethics Commission regulations Section 932)*

Reporting Violations

In accordance with NYSERDA's Whistleblower Policy, you must remain alert to possible violations of law, policy, or public trust, everywhere in NYSERDA. Section 55(1) of the Executive Law requires all state officers and employees to promptly report to the State Inspector General any information concerning corruption, fraud, criminal activity, conflicts of interest, or abuse by another state officer or employee relating to his or her employment.

You must cooperate in any official investigation of a violation.

Retaliation against any employee who in good faith reports a violation of law, policy, or public trust is prohibited. *(See Whistleblower Policy and Personnel Handbook Section 11)*

Resources Available

Internal

Mark Mitchell, Director of Internal Audit

Jeff Pitkin, Internal Control Officer

Hal Brodie, General Counsel (and all other Counsel's Office staff)

External

Fraud and Abuse Hotline 1-866-219-1122

NYS Joint Commission on Public Ethics 518-408-3976

NYS Office of the Inspector General 1-800-367-4448

Authorities Budget Office 1-800-560-1770

APPENDIX C

WHISTLEBLOWER POLICY

April 2012

PURPOSE

It is the policy of NYSERDA to afford certain protections to individuals who, in good faith, report violations of NYSERDA's Code of Ethics or other instances of potential wrongdoing within NYSERDA. The Whistleblower Policy and Procedures set forth below are intended to encourage and enable employees to raise concerns in good faith within NYSERDA and without fear of retaliation or adverse employment action.

DEFINITIONS

Good Faith: Information concerning potential wrongdoing is disclosed in "good faith" when the individual making the disclosure reasonably believes such information to be true and reasonably believes that the information constitutes potential wrongdoing.

NYSERDA Employee: All NYSERDA board members, officers, and staff whether full-time, part-time, employed pursuant to contract, employees on probation, and temporary employees.

Personnel action: Any action affecting compensation, appointment, promotion, transfer, assignment, reassignment, reinstatement, or evaluation of performance.

Whistleblower: Any NYSERDA Employee who in good faith discloses information concerning wrongdoing by another NYSERDA Employee, or wrongdoing concerning the business of NYSERDA itself.

Wrongdoing: Any alleged corruption, fraud, criminal or unethical activity, misconduct, waste, conflict of interest, intentional reporting of false or misleading information, or abuse of authority engaged in by a NYSERDA Employee that relates to NYSERDA.

SECTION I: REPORTING WRONGDOING

All NYSERDA Employees who discover or have knowledge of potential Wrongdoing concerning board members, officers, or employees of NYSERDA; or a person having business dealings with NYSERDA; or concerning NYSERDA itself, shall report such activity in accordance with the following procedures:

a) All NYSERDA Employees who discover or have knowledge of Wrongdoing shall report such Wrongdoing in a prompt and timely manner.

b) The NYSERDA Employee shall disclose any information concerning Wrongdoing either orally or in a written report to his or her supervisor, or to the Director of Internal Audit, an Officer, any member of

Counsel's Office, an independent Fraud and Abuse Hotline service available to NYSERDA employees, the Ethics Officer, a representative from human resources.

c) The identity of the whistleblower and the substance of his or her allegations will be kept confidential to the maximum extent possible.

d) Upon receipt of an allegation of Wrongdoing, the individual to whom the potential Wrongdoing is reported shall notify the General Counsel, and the General Counsel shall determine who will conduct the investigation. Once the investigation is complete, the General Counsel or the individual who conducted the investigation shall provide to the President and CEO a summary report, which shall include a recommendation for resolving the matter. The Director of Internal Audit shall advise the Audit and Finance Committee at its next regularly scheduled meeting of any material or significant weaknesses or deviations identified in such report.

e) The individual to whom the potential Wrongdoing is reported may refer such information to the Authorities Budget Office or an appropriate law enforcement agency where applicable.

f) Allegations of corruption, fraud, criminal activity, conflicts of interest or abuse by a NYSERDA Employee or any persons having business dealings with NYSERDA must be reported to the State Inspector General.

g) All NYSERDA Employees shall cooperate fully with internal investigations and investigations by the State Inspector General pertaining to NYSERDA operations.

h) All reports and draft reports delivered to NYSERDA by the State Inspector General shall be reviewed by the Audit and Finance Committee, which shall serve as the point of contact on such reports.

i) Should a NYSERDA Employee believe in good faith that disclosing information within NYSERDA pursuant to Section 1(a) above would likely subject him or her to adverse personnel action or be wholly ineffective, the NYSERDA Employee may instead disclose the information to the Authorities Budget Office or an appropriate law enforcement agency, if applicable. The Authorities Budget Office's toll free number (1-800-560-1770) should be used in such circumstances.

SECTION II: NO RETALIATION OR INTERFERENCE

No NYSERDA Employee shall retaliate against any Whistleblower for the disclosure of potential Wrongdoing, whether through threat, coercion, or abuse of authority; and, no NYSERDA Employee shall interfere with the right of any other NYSERDA Employee by any improper means aimed at deterring disclosure of potential Wrongdoing. Any attempts at retaliation or interference are strictly prohibited. In addition:

a) No NYSERDA Employee who in good faith discloses potential violations of the NYSERDA Code of Conduct or other instances of potential Wrongdoing, shall suffer harassment, retaliation or adverse personnel action as a result of such disclosure.

b) All allegations of retaliation against a Whistleblower or interference with an individual seeking to disclose potential Wrongdoing shall be thoroughly investigated by NYSERDA.

c) Any NYSERDA Employee who retaliates against or attempts to interfere with any individual for disclosing or attempting to disclose potential violations of the NYSERDA Code of Conduct or other instances of potential Wrongdoing is subject to discipline, which may include termination of employment.

d) Any allegation of retaliation or interference will be taken and treated seriously and irrespective of the outcome of the initial complaint, such allegation will be treated as a separate matter.

SECTION III: OTHER LEGAL RIGHTS NOT IMPAIRED

The Whistleblower Policy and Procedures set forth herein are not intended to limit, diminish, or impair any other rights or remedies that an individual may have under the law with respect to disclosing potential Wrongdoing free from retaliation or adverse personnel action.

a) Specifically, these Whistleblower Policy and Procedures are not intended to limit any rights or remedies that an individual may have under the laws of the State of New York, including but not limited to the following provisions: Civil Service Law § 75-b, Labor Law § 740, State Finance Law § 191 (commonly known as the “False Claims Act”), and Executive Law § 55(1).

b) With respect to any rights or remedies that an individual may have pursuant to Civil Service Law § 75-b or Labor Law § 740, any NYSERDA Employee who wishes to preserve such rights shall prior to disclosing information to a government body, have made a good faith effort to provide the appointing authority or his or her designee the information to be disclosed and shall provide the appointing authority or designee a reasonable time to take appropriate action unless there is imminent and serious danger to public health or safety. (See Civil Service Law § 75-b[2][b]; Labor Law § 740[3]).