



**A SPECIAL PERFORMANCE AUDIT
OF THE
DEPARTMENT OF TRANSPORTATION'S**

SECURE INVENTORY MANAGEMENT SYSTEM

DECEMBER 2007

December 18, 2007

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania
225 Main Capitol Building
Harrisburg, PA 17120

Dear Governor Rendell:

This report contains the results of the Department of the Auditor General's special performance audit of the Department of Transportation's (PennDOT) Secure Inventory Management System (SIMS) for the period January 1, 2003 through December 31, 2005. This audit was conducted pursuant to Sections 402 and 403 of the Fiscal Code and in accordance with *Government Auditing Standards* which are applicable to performance audits and issued by the Comptroller General of the United States.

Our audit found that PennDOT's controls over the inventory to produce Pennsylvania (PA) driver licenses and identification (ID) cards were inadequate. As a result, the risk of potential fraud and abuse, including identity theft and the production of illegally produced PA driver licenses and ID cards, is high. Control weaknesses found included a lack of segregation of duties at both the warehouse and the photo license centers, inadequate training and procedures, and insufficient monitoring and oversight by PennDOT. In addition, we noted that PennDOT failed to include contractual provisions requiring an independent audit/review of PennDOT's contractors' internal control structures. As a result, PennDOT has no assurance that the contractors' controls relevant to the production of driver licenses and ID cards are suitably designed, operational, and sufficient.

We offer 11 recommendations to strengthen the controls over the high security inventory to produce PA driver licenses and ID cards, thereby reducing the risk of potential fraud and abuse.

We are pleased to report that PennDOT has taken a proactive role in strengthening certain controls we identified as weaknesses during the course of the audit. Additionally, we appreciate the cooperation exhibited by PennDOT and its willingness to implement many of our recommendations. We will follow up at the appropriate time to determine whether and to what extent all recommendations have been implemented.

Sincerely,

JACK WAGNER
Auditor General

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EXECUTIVE SUMMARY

The Pennsylvania Department of Transportation (PennDOT) is responsible for managing the Commonwealth's driver licensing program, including directing and overseeing the 97 photo license centers throughout the Commonwealth and contracting with the Pennsylvania Industries for the Blind and Handicapped (PIBH) to take photos for Pennsylvania (PA) driver licenses and Identification (ID) cards. Customers are required to go to a photo license center with proper identification and a PennDOT-issued camera card to obtain a PA drivers license and ID card.

To implement the digital imaging technology program of the PA driver license and ID card program, PennDOT contracted with a Prime Contractor to develop a Secure Inventory Management System (SIMS). The Prime Contractor was to be paid on a cost per card basis of approximately \$1.64 for an estimated 2.6 million cards per year not to exceed \$21.8 million over a 60-month period. The Prime Contractor, in turn, subcontracted for services to provide efficient management of high security card stock and laminate overlay (high security inventory) and warehouse operations, including receiving, storing and tracking the high security inventory.

Weaknesses in controls over the high security inventory at PA photo license centers and at the warehouse, and PennDOT's failure to require an independent audit/review of its contractors' control policies and procedures and operating effectiveness are discussed in the main body of this report and summarized below:

FINDINGS	SUMMARY
<i>Finding No. 1 – Control Weaknesses Found Over High Security Inventory Maintained at Photo License Centers</i>	In addition to 1,500 blank PA licenses and ID cards reported as stolen on March 1, 2005, and a roll of laminate overlay consisting of 100 holographic overlays being reported as stolen in October 2003 at the same photo license center, six other photo license centers notified PennDOT that six used rolls of laminate overlay, used to affix a reflective hologram to PA driver licenses and ID cards, could not be accounted for. Some of the control weaknesses found over high security inventory included differences between the inventory reported as used and the number of PA driver licenses and ID cards issued; voided licenses were not properly accounted for; and standardized forms to track high security inventory either not properly signed or not properly completed. PennDOT's lack of an adequate system of controls contributed to these problems.
HIGHLIGHTS OF RECOMMENDATIONS	
PennDOT should: <ul style="list-style-type: none"> • provide adequate training to ensure inventory forms are properly completed and reviewed; • ensure adequate segregation of duties over physical inventory counts; and • develop and implement standard operating procedures to ensure that sensitive documents are secured and controlled. 	

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<i>Finding No. 2 – Control Weaknesses Found at the Warehouse Storing High Security Inventory</i>	Only one warehouse employee has responsibility for receiving, shipping, tracking and destroying high security inventory as well as producing duplicate PA driver licenses and ID cards. We noted during on-site testing that a sleeve of 500 blank cards used for producing PA driver licenses and ID cards was found missing in January 2005 by the warehouse employee. In determining the timeliness of destroyed voided cards and used laminate rolls returned to the warehouse, we found that, from March 2005 through July 2005 and during October 2005, an average of 113 shipments were not removed from SIMS, indicating a large backlog of high security inventory awaiting destruction at the warehouse. We also noted that eight shipments consisting of 38 used rolls of laminate and an undetermined number of voided cards were reported as shipped from photo license centers but never reported by the warehouse as received or destroyed. PennDOT failed to ensure adequate segregation of duties at the warehouse.
HIGHLIGHTS OF RECOMMENDATIONS	
PennDOT should: <ul style="list-style-type: none"> • segregate duties at the warehouse to better control high security inventory; and • include language in contracts to ensure adequate oversight and segregation of duties. 	

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FINDINGS	SUMMARY
<p><i>Finding No. 3 – Weaknesses Noted in PennDOT’s Oversight of High Security Inventory Used to Produce PA Driver Licenses and ID Cards</i></p>	<p>We found a number of weaknesses, including individuals accessing SIMS without unique user IDs and password, reconciliations not performed between the number of driver licenses and ID cards issued per the SIMS’ data file and the number issued per the Prime Contractor’s invoices; and analytical reviews comparing the usage of blank cards to the usage of laminate overlays not performed. We found that, during a 21-month period of April 2004 through December 2005, monthly contractor invoices sent to PennDOT for the number of PA driver licenses and ID cards issued did not agree with the number in the SIMS data files. In addition, a comparison of the number of laminate overlays used to the number of blank cards used during the same 21-month period revealed a greater than a 3:1 ratio by nine photo licenses centers. Lack of adequate contract provisions and control procedures contributed to these weaknesses.</p>
HIGHLIGHTS OF RECOMMENDATIONS	
<p>PennDOT should:</p> <ul style="list-style-type: none"> • enhance SIMS to produce edit reports and allow the use of unique user IDs and passwords; • review adjusting entries to high security inventory records to ensure accuracy, accountability, and proper authorization; • review the Prime Contractor’s invoices for accuracy; and • compare laminate and card usage by photo license center to identify potential problems or irregularities. 	

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FINDINGS	SUMMARY
<i>Finding No. 4 – Weakness in PennDOT Management’s Oversight of Service Organizations Used to Manage the Operation of the Driver Licensing Program</i>	PennDOT did not contractually require the Prime Contractor and Software Developer to provide an independent audit/review of their control policies and procedures and operating effectiveness. As a result, PennDOT has limited assurance as to the effectiveness of each service organization’s ability to meet security objectives.
HIGHLIGHTS OF RECOMMENDATIONS	
PennDOT should require each service organization to obtain an independent audit/review of its control structure policy and procedures relevant to the security objectives of the driver licensing program.	

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BACKGROUND

The Pennsylvania Department of Transportation (PennDOT) is responsible for managing the Commonwealth's driver licensing program as authorized by the Vehicle Code. The Bureau of Driver Licensing, accountable to PennDOT's Deputy Secretary for Safety Administration, directs and oversees driver and photo license centers throughout the Commonwealth.

According to information from PennDOT's website, the number of licensed drivers in Pennsylvania for each of the past four years are shown in the following table:

Number of Licensed Drivers

Calendar Year	Licensed Drivers
2003	8,369,579
2004	8,430,147
2005	8,489,911
2006	8,566,282

PennDOT conducts driver examinations and processes all driver license-related applications, including requests for duplicates, identification (ID) cards, driver license renewals, replacements, and changes of address. In addition, PennDOT employees issue duplicate Pennsylvania (PA) driver license and ID cards at 52 of the driver license centers. As of October 1, 2007, PennDOT directs and oversees 97 photo license centers throughout the Commonwealth and contracts with the Pennsylvania Industries for the Blind and Handicapped (PIBH). PIBH's license technicians are responsible for taking a photo when presented with a PennDOT-issued camera card and proper identification, and then providing the PA driver's license or ID card to the customer.

In June 2000, PennDOT contracted with a Prime Contractor to implement the digital imaging technology program of the PA driver license and ID card program. Digitized driver license and ID card production electronically captures the cardholder's photo image and signature. During production, security laminate (including a unique reflective hologram) affixes to the card, enhancing security of the final product. According to the contract, the Prime Contractor was to be paid on a cost-per-card basis of approximately \$1.64 for an estimated 2.6 million cards per year, not to exceed \$21.8 million over the initial 60-month contract period.

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BACKGROUND

The prime contract included the development of the Secure Inventory Management System (SIMS), as well as provisions for supplying computer hardware (workstations, imaging technology, printers, and storage equipment), software, high security inventory, warehousing service, training, system operations, on-going support, and central production operations for non-over-the-counter duplicate PA driver licenses and ID cards.

The Prime Contractor subcontracted SIMS to a Software Developer, described as a provider of sophisticated software solutions that would enable efficient management of high security inventory. Additionally, during the contract period, the Prime Contractor subcontracted warehouse operations, central production of duplicate PA driver licenses and ID cards, and certain system maintenance operations to two different Warehouse Operators. The Warehouse Operator's responsibilities included receiving, storing, and tracking high security inventory, as well as destroying voided or used high security inventory.

Weaknesses in controls over high security inventory at photo license centers and at the warehouse, and the need for enhanced oversight of service organizations are discussed in this special performance audit of SIMS.

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AUDIT OBJECTIVES, SCOPE, AND METHODOLOGY

Objectives

The objectives of this special performance audit were to determine:

- The adequacy of controls of the inventory system, including those designed to safeguard assets from waste, misuse and theft of items (See Findings 1 through 4); and
- Whether additions, deletions and other types of changes to the inventory were timely and accurately recorded (See Findings 1 and 2).

Scope

The audit encompassed PennDOT's controls and processes for high security inventory used to produce PA driver licenses and ID cards. This included the SIMS as well as manual controls and processes. The audit covered the period January 1, 2003 through December 31, 2005 and was conducted in two phases: the initial audit period was January 1, 2003 through March 31, 2004 and the extended audit period was April 1, 2004 through December 31, 2005.

Methodology

The methodology in support of the audit objectives included:

- observing operations and interviewing personnel in charge at the warehouse and various photo license centers to test the adequacy of controls over the inventory of high security card stock and laminate overlay (high security inventory);
- reviewing PennDOT's oversight controls over photo license centers and procedures for monitoring contractors and subcontractors for compliance with contract provisions to ensure that security over high security inventory is being properly maintained;
- performing analytical review procedures to determine the reasonableness of the amount of high security inventory used;

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- obtaining a general understanding of SIMS to ensure that controls are in place over access to SIMS and that entries to SIMS are adequately tracked by individual users;
- ensuring that billings received from contractors and subcontractors are reasonable; and
- determining if PennDOT has adequate follow-up procedures in place when discrepancies/problems are noted with the physical count of high security inventory.

FINDINGS AND RECOMMENDATIONS



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FINDINGS AND RECOMMENDATIONS

Finding No. 1 - Control Weaknesses Found Over High Security Inventory Maintained at Photo License Centers

Condition: PennDOT maintains 97 photo license centers for taking photos and printing PA driver licenses and ID cards. PennDOT contracts with the PIBH to perform these services. Of the 97 photo license centers, 70 also serve as Driver License Examination (DLE) locations. Of the 70 who provide DLE services by PennDOT employees, including administering driver examinations, 52 also print duplicate PA driver licenses and ID cards for customers who have lost or had their PA driver licenses and ID cards stolen. There are also seven “specialty sites” that can issue PA driver licenses and ID cards. These include the four sites at the River Office Complex (ROC): Counter Duplicate, Messenger Duplicate, Valid-Without-Photo (VWOP) Workstation, and Test Duplicate System, as well the Legislative Duplicate, Penn Mobile Photo Workstation, and Central Duplicating.

As part of our audit of PennDOT’s high security inventory used to produce PA driver licenses and ID cards, we performed on-site visits/testwork on 15 photo license centers. During our testing, we noted that a United Parcel Service driver was robbed on March 1, 2005 of 1,500 blank PA driver licenses and ID cards while making a delivery to one of the photo license centers. Also, on October 4, 2003, at the same photo license center, PennDOT classified a roll of laminate (consisting of 100 holographic overlays which could produce as many as 100 PA driver licenses and ID cards) as having been stolen. Although these instances were immediately reported to local police, the items were never recovered. In addition, six other sites gave notice to PennDOT of six used rolls of laminate overlay (which could produce as many as 600 PA driver licenses and ID cards) that either could not be accounted for or were sent to the warehouse for destruction, but were never reported by the warehouse as being received. Therefore, we were unable to verify whether these rolls of laminate were new or used and, to date, PennDOT cannot account for them.

We also found the following weaknesses that were not detected by respective supervisors at the 15 photo license centers we visited/tested:

- At 10 photo license centers, standardized control forms used to track high security inventory showed differences between the inventory reported as being used and the number of PA driver licenses and ID cards issued.
- At 11 photo license centers, the beginning and ending physical counts of high security inventory were not performed or both counts were performed by the same person.
- At 14 photo license centers, the number of PA driver licenses and ID cards issued as reported on a standardized control form did not equal the number issued on the SIMS data files.

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FINDINGS AND RECOMMENDATIONS

Finding No. 1

- At 3 photo license centers, voided licenses were not being properly accounted for on standardized control forms.
- At 4 photo license centers, standardized control forms used to track high security inventory were either not properly signed or not properly completed.
- At 4 photo license centers, valid PA driver licenses and ID cards accidentally left behind by customers were not securely locked in a safe and, therefore, were prone to theft.

We also performed on-site visits at three of PennDOT's specialty sites located in Harrisburg: Counter Duplicate, VWOP Workstation, and Central Duplicating at the warehouse. Weaknesses noted at the warehouse are addressed in Finding No. 2. At the Counter Duplicate, operated by PennDOT employees, we found that the supervisor did not document and retain results of weekly physical counts of high security inventory which prevented the supervisor from comparing the results to SIMS records. Formal procedures were not in place to handle defaced and voided PA driver licenses and ID cards maintained in the supervisor's desk and accessible to other ROC employees. Additionally, the supervisor did not review or sign appropriate control forms to track high security inventory.

At the VWOP Workstation, operated by PIBH employees, we noted instances where morning physical inventory counts were not performed, a packing slip was not signed/initialed as being received, and the number of cards issued per a standardized control form did not equal the number of cards issued on the SIMS data files.

Criteria: A strong system of controls ensures that high security inventory is properly accounted for through the use of standardized control forms to track items to and from locations. Formal operating procedures also should be in place to properly account for PA driver licenses and ID cards and other sensitive documents, and provide for segregation of duties and day-by-day inventory counts with proper supervisory oversight.

Cause: The lack of an adequate system of controls whereby employees and supervisors follow established procedures on a consistent basis contributed to the problems in the high security inventory area. Also, due to the weaknesses noted above, it is apparent that additional training is necessary and that adequate segregation of duties must be in place and functioning.

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Finding No. 1

Effect: PennDOT's lack of adequate controls, training and instruction, formal operating procedures, and segregation of duties can lead to fraud and abuse, including identity theft, and production of illegally produced PA driver licenses and ID cards. Also, PennDOT's lack of procedures to properly handle voided licenses and other forms of identification can lead to identity theft. Robbery, theft, and unaccountable blank driver licenses and ID cards and laminate overlay could result in the production of numerous illegal PA driver licenses and ID cards.

Recommendations: We recommend that PennDOT:

- Ensure that adequate training and instruction to site supervisors and employees, as well as PIBH employees, is provided and required forms are completed and properly reviewed;
- Ensure that adequate segregation of duties over physical inventory counts exist; and
- Develop and implement standard operating procedures at all locations to ensure that sensitive documents are properly secured and controlled.

PennDOT Response:

Recommendations:

- 1. Ensure that adequate training and instruction to site supervisors and employees, as well as PIBH employees, is provided and required forms are completed and properly reviewed.**

Response: All employees had been trained prior to the audit. However, it was discovered that the procedures were not being followed universally. As a result, PennDOT's procedures were revised and reinforced with staff.

In addition, all license technicians attend an annual training seminar. Any issues identified throughout the year regarding completion of forms are immediately addressed and then reviewed with the entire staff at the annual training seminar. These training seminars ensure that all license technicians are up-to-date with the current inventory control procedures and have a clear understanding on how to complete the required forms.

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FINDINGS AND RECOMMENDATIONS

Finding No. 1

To ensure employees are completing required forms properly, PennDOT has a multi-tiered audit process in place. At locations that produce over-the-counter duplicates, it is the site supervisor's responsibility to ensure all required forms are completed accurately. Any issues identified are reviewed with the employee. In addition, the PennDOT District Managers audit each site's paperwork quarterly. A centralized database is maintained to record that the audit was completed and copies of the audit reports are sent to PennDOT's Central Office. Any issues identified are reviewed with the site supervisor and if necessary, disciplinary action is taken.

All the paperwork completed by the license technicians is audited within one month of completion. If the forms are not properly completed, the PIBH District Manager meets with the license technician to review the issues and provide additional training.

PennDOT also has a full time Field Audit Manager that audits each Photo License Center twice a year. Part of his audit includes a review of the SIMS paperwork. If any discrepancies are identified, a report is sent to the PIBH State Manager and a written response to what action was taken by PIBH is required.

2. Ensure that adequate segregation of duties over physical inventory counts exist.

Response: The following enhancements have been made to ensure segregation of duties exist:

- All inventory checks are performed by two license technicians where there are two or more license technicians working at a site. Each license technician verifies the inventory and balances it against the safe logs. Forty-six percent of the Photo Centers have two or more license technicians.
- District Managers perform a weekly or bi-weekly audit at each site to ensure the accuracy of the completed forms. The frequency is based upon the days of operation for each site. Sites operating four or more days a week are audited weekly; sites operating less than four days a week are audited every other week.
- The PennDOT Field Audit Manager performs SIMS checks to review inventory accuracy at each site twice a year. This includes the Valid Without Photo workstation (since July 2004) and the warehouse (as of January 2007).
- The Consumables Aging Report is run monthly (as of November 2004) and is reviewed by the PennDOT Field Audit Manager. This report identifies any rolls of laminate that have been at a site for 90 days or longer. A follow-up is conducted with each site identified to determine the status of the overlay.

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FINDINGS AND RECOMMENDATIONS

Finding No. 1

3. Develop and implement standard operating procedures at all times at all locations to ensure that sensitive documents are properly secured and controlled.

Response: PennDOT has procedures in place regarding the proper handling of secure documents. These procedures were updated and reinforced with staff in December 2006. A new procedure was also implemented in December 2006 to address sensitive documents left behind by customers. These documents are secured and only retained by the site for 2 days before being destroyed. District Managers will verify this when completing their "Site Review Checklist" which is done at least quarterly. In addition, PennDOT created a DL Site Supervisor Manual (statewide DL Supervisor Manual rollout was completed in May 2006) which includes daily observation that staff and site adhere to all policies and procedures. As needed, changes are made to this manual to address any issues identified through our own internal audits and reviews.

We also have a standard operational manual for the license technicians that includes procedures for securing and defacing invalid products. The manual was updated in January 2007 to include the proper handling of documents left behind by customers. A memo reviewing the change made to the operations manual was sent to each Photo License Center on January 25, 2007.

Audit Finding #1 indicates that there were six sites that could not account for rolls of laminate. PennDOT's audit procedures identified these discrepancies and each incident was fully investigated prior to this audit. All the rolls of laminate in question were used rolls. Although they were not recovered, each incident was investigated in detail, actions to prevent future occurrences were taken and when appropriate, liquidated damages were assessed.

In addition, formal inventory control procedures were implemented in January 2005 for the Riverfront Office Center (ROC) over-the-counter duplicate workstations.

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FINDINGS AND RECOMMENDATIONS

Finding No. 1

Auditors' Conclusion: We commend PennDOT for revising and implementing some policies and procedures to improve training, segregation of duties, and the security of highly sensitive inventory. We would like to point out that many of the procedures PennDOT describes in its response were already in place during the audit period. Some examples include the PIBH District Manager auditing all paperwork completed by the PIBH license technicians; the PennDOT Field Audit Manager auditing each photo license center twice a year, including reviewing inventory accuracy; and inventory checks being performed by two license technicians where there are two or more working at a site. Therefore, even with these controls, exceptions were found.

Some of the other procedures described by PennDOT were implemented during the audit period. Our initial test results and PennDOT's proactive reaction to them resulted in PennDOT enhancing certain procedures during the extension period. Some examples include PennDOT District Managers began auditing inventory paperwork of DLE locations; adding the Valid-Without-Photo Workstation to the PennDOT's Field Audit Manager's list to review inventory accuracy; and implementing formal control procedures for the ROC over-the-counter duplicate workstations.

Finally, PennDOT identifies other procedures it has implemented subsequent to the audit period. We have not reviewed or assessed these additional controls. However, we would like to stress the importance of the daily inventory paperwork, physical inventory counts, and sufficient management oversight. Because SIMS accounts for high security inventory by box of 500 cards or a roll of laminate with 100 overlays, it is not tracking each card or each overlay. As a result, the tracking of each card and overlay should be manually tracked using daily inventory paperwork due to its high security risk.

With respect to PennDOT's comments regarding six sites that could not account for rolls of laminate, we acknowledge that these discrepancies were identified by PennDOT. However, PennDOT emphasizing that these six rolls of laminate were "used rolls," implying that they are not a "high security" item, may not be accurate for two reasons: 1) Many sites record rolls of laminate as "used" in SIMS when they are initially taken out of inventory. Therefore, SIMS would consider rolls of laminate used before it is placed on a printer and a single overlay is removed and 2) Even if a roll of laminate was placed on the printer and used, due to printer errors as well as the process of taking the laminate on and off the printer, there may be overlays remaining on a roll. Consequently, that is why PennDOT tracks rolls of "used" laminate through to destruction. As a result, without recovering these rolls, PennDOT cannot be assured that these overlays were not improperly used.

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FINDINGS AND RECOMMENDATIONS

Finding No. 2 - Control Weaknesses Found at the Warehouse Storing High Security Inventory

Condition: PennDOT uses the SIMS for tracking high security inventory that consists mainly of blank cards and rolls of laminate overlay, along with other non-high security items. As part of our audit, we reviewed procedures and controls in effect at the warehouse where these inventories are maintained. The warehouse serves five main purposes: receiving and storing the high security inventory, shipping inventory to photo license centers across the state, maintaining the server that stores millions of digital photo images of PA driver licenses and ID cards, destroying voided cards and used laminate rolls returned to the warehouse, and producing and mailing duplicate PA driver licenses and ID cards requested by customers either online or over the phone. This last procedure is known as the “central duplicating” procedure.

PennDOT contracted the warehouse operations to the Prime Contractor, who in turn, subcontracted a majority of the warehouse operations to the Warehouse Operator. The Prime Contractor maintains one employee at the warehouse while the Warehouse Operator has three employees. However, only one is assigned to maintain PennDOT’s inventory.

The Warehouse Operator’s employee has sole responsibility for receiving, shipping, tracking and destroying high security inventory as mentioned above, as well as performing weekly physical inventory counts and agreeing the counts to SIMS. In addition, this employee is responsible for ensuring that the central duplicating procedures are performed on a daily basis.

However, all of the above procedures performed by the Warehouse Operator’s employee are conducted without supervisory oversight by the Prime Contractor. The fact that one employee is accountable for receiving, shipping, tracking and destroying the inventory of high security consumables as well as having access to digital photo images of PA driver licenses and ID cards and the ability to print and mail the cards without supervisory oversight creates a lack of segregation of duties and, therefore, is a significant control weakness.

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Finding No. 2

During our on-site test in August 2006 at the warehouse, we noted that a sleeve of blank cards (500 cards) used for issuing PA driver licenses and ID cards was missing. This discrepancy, although immediately reported to PennDOT by the Warehouse Operator's employee in January 2005, could not be explained and the discrepancy of 500 cards remained in SIMS until after our inquiry in August 2006.

Furthermore, we performed analytical review procedures to determine the timeliness of the destruction of voided cards and used laminate rolls returned to the warehouse. Our procedures utilized the SIMS "Create Return Shipment" report to summarize shipments of voided cards and used laminate rolls entered into SIMS by the sites making the shipments. As the inventory is destroyed, the shipments are to be removed from SIMS by the Warehouse Operator's employee. We found that, for 15 of 21 months tested, an average of 14 shipments were not removed from SIMS by the end of the month. However, for the months of March 2005 through July 2005 and the month of October 2005, this average increased to 113 shipments, indicating a large backlog of high security inventory awaited destruction. This backlog not only exemplifies the lack of segregation of duties through inadequate staffing, but also creates additional risks by providing an opportunity for pilferage and identity theft due to the large number of cards and laminate not timely destroyed. Although voided and used, this inventory may be manipulated for re-use.

Also during our review of the SIMS "Create Return Shipment" report, we noted that eight shipments consisting of 38 used rolls of laminate and an undetermined number of voided cards were reported as shipped from various photo license sites but never reported by the warehouse as received or destroyed.

Criteria: A strong system of controls should exist to assure an adequate segregation of duties and proper supervisory oversight of personnel. This is especially true in view of the high security items such as PA driver licenses and ID cards and the potential impact for identity theft and fraudulent license production.

Cause: Both the Prime Contractor and Warehouse Operator consider one employee adequate to handle the receiving, shipping and tracking responsibilities at the warehouse. As for the missing sleeve of cards, we were given an explanation that this was the result of a possible undiscovered problem in the SIMS software. However, when Prime Contractor representatives consulted with the Software Developer, the Software Developer stated that it was reluctant to characterize it as such. Obviously, the fact that this discrepancy was unexplained for over 18 months is indicative of the weak control environment allowed to exist at the warehouse. As for the eight return shipments classified as lost or missing, PennDOT investigated the discrepancy but could provide no further explanation. The backlog of return shipments was explained by the Warehouse Operator's employee as due to inadequate staffing.

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FINDINGS AND RECOMMENDATIONS

Finding No. 2

Effect: A lack of segregation of duties and supervisory oversight by PennDOT over the receiving, shipping, tracking, printing and mailing of duplicate PA driver licenses and ID cards, and destruction of high security inventory creates the potential for fraud and abuse, including producing PA driver licenses and ID cards for illegal use.

Recommendations: We recommend that PennDOT remedy the lack of segregation of duties at the warehouse as soon as possible in order to have better controls in place over high security inventory. In addition, PennDOT should include appropriate language in contracts and subcontracts to ensure that adequate oversight and segregation of duties are in place.

PennDOT Response:

Recommendations:

- 1. PennDOT remedy the lack of segregation of duties at the warehouse as soon as possible in order to have better controls in place over high security inventory.**

Response: Since October 2005, no single employee has had sole responsibility for receiving, shipping, tracking, destroying inventory and the same is true for production of the central duplicating procedures ensuring that voided PA driver licenses and ID cards and used laminate received from the field locations are properly destroyed.

The Prime Contractor currently maintains two (2) employees at the warehouse facility and their Warehouse Operator maintains three (3) employees each with varied starting dates (October 3, 2005, September 8, 2005 and April 13, 2006). The Prime Contractor's employees consist of a full-time, on-site State Program Manager and a full-time employee hired October 23, 2006. The State Program Manager is tasked with full-time oversight and responsibility over all aspects of the PennDOT program and the Prime Contractor Harrisburg facility. The second employee is utilized to assist in the PennDOT tasks. The assignment of daily "duties" each staff member performs is done with the approval and oversight of the State Program Manager.

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The discrepancy in one (1) sleeve of blank cards (500 cards) as noted in the findings was identified and reported in a timely manner. The sleeve of blank cards was not physically missing but SIMS showed one more sleeve than what was physically on hand at the warehouse. This was displayed on the Inventory Levels sheet under Quantity Available. The oversight of the system actually enabled the Warehouse Operator employee to pick up the difference between SIMS and the on hand count at the warehouse. The cause of this problem could not be ascertained by the SIMS Software Developer as it could not be replicated. As such, the Software Developer could not characterize this one-time system occurrence as an end-user action. The Software Developer adjusted this discrepancy in SIMS after an exhaustive investigation and this problem has not been evidenced since this first and only occurrence.

- 2. PennDOT should include appropriate language in contracts and subcontracts to ensure that adequate oversight and segregation of duties are in place.**

Response: The prime contract was extended for seven years prior to the issuance of this report. As shown above, segregation of duties does exist. PennDOT will pursue amending the contract to explicitly include such language. In addition, PennDOT has developed procedures for the PennDOT Field Audit Manager to audit the warehouse twice a year. The first audit was conducted in January 2007 and no issues were found.

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Auditors' Conclusion: We applaud PennDOT's efforts to include segregation of duties language within the extended prime contract, as well as to add the warehouse to the PennDOT Field Audit Manager's audit sites.

With respect to a lack of segregation of duties at the warehouse, PennDOT's response not only acknowledges that a segregation of duties concern existed during much of the audit period (January 2003 through September 2005) but also implies that, as of October 2005, the segregation of duties problem no longer exists. Although we were aware that there are now three Warehouse Operator employees at the warehouse, when we inquired about each employee's duties, it was explained to us that the warehouse maintained driver license supplies for several other states and only one of these employees had full responsibility for all aspects of PennDOT's inventory. It was noted that the three employees will fill in for each other, but only during extended periods of leave by one of the employees. As a result, it appears that the segregation of duties problems still exist even though more Warehouse Operator employees have been hired.

Additionally, it appears that oversight provided by the Prime Contractor continues to be limited to when a problem is found rather than regular on-going oversight of warehouse operations. However, because the hiring of an additional Prime Contractor employee in October 2006 was subsequent to the audit period and on-site fieldwork, no audit procedures were performed with regard to this new employee and the related effect on the segregation of duties weakness.

Finally, with respect to the missing sleeve of blank cards, although we acknowledge that this problem was timely identified we do not understand why it took until the auditors made inquiry, 18 months later, for PennDOT to fully investigate the problem and finally correct the inventory count.



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Finding No. 3 - Weaknesses Noted in PennDOT's Oversight of High Security Inventory Used to Produce PA Driver Licenses and ID Cards

Condition: As part of our audit, we evaluated the effectiveness of PennDOT's monitoring of high security inventory. We found a number of weaknesses, including individuals accessing SIMS do not have unique user IDs and passwords, reconciliations not performed between the number of driver licenses and ID cards issued per the SIMS' data file and the number issued per the Prime Contractor's invoices; and analytical reviews comparing the usage of blank cards to the usage of laminate overlays not performed. Following is an explanation of these monitoring weaknesses:

- Many of the individuals who access SIMS, including PIBH management and photo license technicians, Prime Contractor management and help desk representatives, Warehouse Operator employees, and PennDOT management and driver license center employees, have access and ability to make entries and adjustments to the SIMS high security inventory records. However, these individuals do not have unique user IDs and passwords. Instead, all entries into SIMS are identified by site only. As a result, individual accountability for entries to SIMS records is not recorded. Also, PennDOT management does not monitor all adjusting entries to SIMS inventory to ensure the integrity and reliability of reported inventory amounts because SIMS does not have the capability of producing edit reports.
- Monthly Prime Contractor invoices sent to PennDOT for reimbursement for the number of PA driver licenses and ID cards produced at the 97 photo license centers are not consistent with the number in SIMS' data file. We compared these invoices to a SIMS' data file for the 21-month period of April 2004 through December 2005 and found that the number of PA driver licenses and ID cards invoiced was 1,610 more than what was on the data file. Although all 21 months showed differences, the largest occurred in October 2005, when the Prime Contractor overbilled PennDOT \$3,442 for producing 2,095 more PA driver licenses and ID cards than what was on the data file. Although the dollar value effect for the entire 21-month period is over \$2,600, Prime Contractor's management could not explain the differences.

In October 2005, PennDOT officials began to use an internal Time Sharing Option (TSO) report to validate the Prime Contractor's invoices. For the three-month period of October through December 2005, we found differences between the TSO report and the Prime Contractor's invoices. PennDOT management did not follow up on these differences and represented to us that there are no established thresholds for pursuing differences between the TSO report and the Prime Contractor's invoices.

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- Analytical comparisons of the number of laminate overlays used to the number of blank cards used revealed nine photo license centers, during the 21-month period of April 2004 to December 2005, used greater than a 3:1 ratio of laminate to blank cards. PennDOT management stated it does not perform any analytical reviews to track the usage of laminate to the usage of blank cards.

Also, as a result of certain weaknesses noted in Finding No. 1 that we brought to the attention of management, PennDOT implemented procedures to have district managers perform quarterly reviews of internal controls, including the handling of high security inventory, proper completion and accuracy of paperwork, procedures for defacing voided cards, and procedures for returning voids and used laminate rolls to the warehouse for destruction. These procedures covered each of the 52 driver license centers with over-the-counter duplicate license production capabilities. We selected four driver license centers for the fourth quarter of calendar year 2005 and requested the standard review form implemented as part of these procedures. We reviewed the three forms provided and noted no unusual items. However, PennDOT was unable to locate a form for one location and, therefore, it does not appear that this oversight control is functioning as intended.

Criteria: To deter fraud, waste and abuse, PennDOT management should have controls in place to ensure individual access to SIMS is available only by unique user IDs and passwords. Also, thresholds for comparing invoices to a data file should be well defined, reconciled, and subject to review for accuracy. In addition, analytical reviews should be performed to track the usage of high security inventory. As for the district manager quarterly reviews, checks and balances should be in place to ensure that controls implemented are functioning as designed.

Cause: PennDOT and the Prime Contractor's management stated that reports, identifying who made adjustments to high security inventory records, as well as user ID and password functionality, are not supported by SIMS because they were not required in the original prime contract.

The current control procedures in place to compare the monthly Prime Contractor's invoices to PennDOT's TSO report were not adequately designed, as evidenced by the fact that there are no documented thresholds for following up on discrepancies noted and no secondary review procedures in place.

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As for the analytical comparisons of the number of laminate overlays used to the number of blank cards used PennDOT management stated that, at times, laminate overlays do not properly adhere to PA driver licenses and ID cards and printer hardware problems can also contribute to unusable laminate overlays, making analytical procedures difficult to analyze. Considering management's response, we still consider the 3:1 ratio of laminate overlays to blank cards used at the nine photo license centers to be excessive because, ideally, this ratio should be 1:1. As for quarterly district manager reviews, PennDOT management could provide no explanation for the missing forms we requested.

Effect: The accuracy and reliability of the high security inventory are diminished due to the lack of controls in place. As a result, fraud, waste and abuse can occur with the issuance of PA driver licenses and ID cards. In addition, failure to properly review invoices gives PennDOT little assurance that the Prime Contractor's invoices are accurate.

Recommendations: We recommend that PennDOT management contractually require the Prime Contractor to enhance SIMS functionality to enable the production of edit reports and to identify individual users responsible for making adjustments to high security inventory records through the use of unique user IDs and passwords. PennDOT management should also review these entries to identify unauthorized and unusual adjusting entries to ensure the accuracy and reliability of high security inventory. Also, PennDOT should have well defined thresholds in place for reviewing the Prime Contractor's invoices for accuracy as well as secondary review procedures to ensure that these invoices are accurate.

In addition, PennDOT should consider the use of analytical comparisons of laminate and card usage by photo license center in order to gauge the reasonableness of card and laminate usage, as well as to identify potential problems or irregularities in a timely manner. Furthermore, a system of checks and balances should be developed to ensure that all quarterly district manager reviews are performed and maintained.

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PennDOT Response:

Recommendations:

- 1. PennDOT management contractually require the Prime Contractor to enhance SIMS functionality to enable the production of edit reports and to identify individual users responsible for making adjustments to consumable supplies inventory records through the use of unique user IDs and passwords.**

Response: In July 2007, PennDOT will roll out new photo license equipment at all locations. At that time, upgrades to SIMS will be made. These upgrades will include a unique log-in for each individual which will allow auditors to track who creates a request for supplies, who acknowledges receipt of supplies and who initiates and acknowledges product transfers. In addition, the unique user IDs and passwords will provide the ability to track all edits.

- 2. PennDOT management should also review these entries to identify unauthorized and unusual adjusting entries to ensure the accuracy and reliability of consumable supplies inventory.**

Response: Reviewing entries will be incorporated into the PennDOT's Field Audit Manager procedures when the SIMS upgrade is completed in July 2007.

- 3. PennDOT should have well defined thresholds in place for reviewing the Prime Contractor's invoices for accuracy as well as secondary review procedures to ensure that these invoices are accurately stated.**

Response: During the time span indicated in the audit report, April 2004 through December 2005, PennDOT issued over 5 million driver's licenses/identification cards. A difference of 1,610 between the Prime Contractor's invoices and PennDOT's reports equates to .03%. In many cases, the Prime Contractor's monthly invoice was less than the PennDOT report. PennDOT has established thresholds for pursuing differences between the Time Sharing Option (TSO) Reports and the Prime Contractor's invoices. In addition, we will continue to review both reporting mechanisms to document the cause of the discrepancies and how they can be eliminated.

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- 4. PennDOT should consider the use of analytical comparisons of laminate and card usage by photo license centers in order to gauge the reasonableness of card and laminate usage, as well as to identify potential problems or irregularities in a timely manner. Furthermore, a system of checks and balances should be developed to ensure that all quarterly District Manager reviews are performed and that copies are maintained.**

Response: For security reasons, at the end of each day all secure materials are removed from the printer and locked in a safe. Each morning, the secure materials are placed back into the printers and the printers are turned on. Each time the printer is started the roll of laminate advances and utilizes a patch of laminate. In addition, any time there is a printer issue, restarting the printer is necessary. For this reason, it is difficult to establish a standard laminate/card usage rate because printer performance varies. In July 2007, new photo license equipment will be deployed statewide. After implementation, PennDOT will establish a standard laminate/card usage rate and investigate anomalies.

PennDOT does have a process in place to ensure that all quarterly District Manager reviews are performed and that copies are maintained. The summary report used to track these audits indicated that the audit referenced in the report had been completed; however the documentation could not be located. At that time, an additional audit was completed (which included comments that the original audit could not be located) and that report was provided to the auditors. PennDOT did review the audit process and in January 2007 a reminder was sent to all managers regarding their audit responsibilities.

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Auditors' Conclusion: We acknowledge PennDOT's corrective action plans noted in its response. However, we do not agree with the reason as to why analytical comparisons of the number of laminate overlays used to the number of blank cards used had not been previously implemented. Although we understand that laminate overlays may not all be used as PennDOT explains, due to the high security nature of these supplies and the fact that cards and laminate overlays are not individually tracked in SIMS, sufficient oversight, including various analytical reviews, is necessary to increase the likelihood of detecting possible fraud, waste, and abuse. As noted in the finding, the 3:1 ratio of the number of laminate overlays used to the number of blank cards used at certain locations is excessive and should have been timely investigated by PennDOT.

With regard to PennDOT's comments on District Managers' quarterly reviews, these reviews were implemented in 2005 as a result of PennDOT realizing, through the results of our audit testwork, that insufficient oversight existed at the 52 Driver License Examiners sites in producing duplicate licenses and ID cards. Although we applaud PennDOT's efforts to increase these oversight controls, we noted during our limited review of these new procedures that forms for one of the four reviews we requested could not be located. The issue that PennDOT does not address is that these District Managers' quarterly reviews are conducted and maintained by the District Managers. There is no one centrally at PennDOT obtaining and reviewing these reviews, even though, as PennDOT indicates in its response, there does exist a summary report for District Managers to note when each review took place and whether any problems were noted. PennDOT needs to ensure through sufficient oversight that reviews are properly conducted and documentation is maintained.

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Finding No. 4 - Weakness in PennDOT Management's Oversight of Service Organizations Used to Manage the Operation of the Driver Licensing Program

Condition: PennDOT contracted with the Prime Contractor, which is a service organization as defined by Statement on Auditing Standards No. 70 (SAS 70), to provide the digital photo technology, including the central image server and database used by photo license centers across the state for producing high security PA driver licenses and ID cards, generally known as the driver licensing program.

SAS 70, entitled *Service Organizations*, developed by the American Institute of Certified Public Accountants, provides guidance to independent auditors (service auditor) who issue reports on the processing of transactions by a service organization for use by other auditors. The SAS 70 report, which includes the service auditor's opinion, would signify that the service organization's internal controls as related to an audit of financial statements were suitably designed to achieve specified control objectives. This report allows service organizations to uniformly disclose their control activities and processes to their customers.

To perform these services, the Prime Contractor subcontracted with a Software Developer to develop, provide, and maintain the SIMS software application, and to track PA driver licenses and ID cards used in conjunction with the driver licensing program. The Prime Contractor also subcontracted with a Warehouse Operator for all warehousing functions and for central duplicating (i.e. online customer orders) of PA driver licenses and ID cards. We found that PennDOT did not contractually require these service organizations to provide an independent audit/review of their respective control policies and procedures and operating effectiveness. As a result, an independent audit/review of these service organizations' controls, including general and application computer controls over the highly automated SIMS system, the central image server database, and photo license center workstations was not obtained.

Criteria: PennDOT's controls over the driver licensing program should include contractual provisions for service organizations and sub-service organizations to require an independent audit/review to evaluate controls. This will give PennDOT better assurance that controls are in place and operating effectively to properly safeguard high security PA driver licenses and ID cards and laminate overlay, as well as having appropriate computer controls in place over automated systems.

Cause: PennDOT failed to include contract provisions requiring an independent audit/review of each service organizations' internal control structures to ensure that the service organizations' controls relevant to the driver licensing program are suitably designed, operational, and sufficiently effective to support the security objectives of the driver licensing program. When we brought this matter to the attention of PennDOT management, it appeared to be unaware of SAS 70 requirements and did not review the adequacy of contractor controls.

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Effect: PennDOT's objectives to secure high security inventory for producing PA driver licenses and ID cards and protect personal identities are jeopardized by its failure to require an independent audit/review engagement in their contracts with service organizations. As a result, PennDOT has limited assurance as to the effectiveness of each service organization's control structure policy and procedures and ability to meet the driver licensing program security objectives.

Recommendation: We recommend that PennDOT contractually require each service organization to obtain a SAS 70 independent audit/review engagement of its control structure policy and procedures relevant to the security objectives of the driver licensing program. This should include whether such policies and procedures are suitably designed, operating, and effective to provide reasonable assurance that program control objectives are achieved.

PennDOT Response:

Recommendation:

- 1. PennDOT contractually require each service organization to obtain a SAS 70 audit or agreed upon procedures engagement of its control structure policy and procedures relevant to the security objectives of the driver licensing program. This should include whether such policies and procedures are suitably designed, operating and effective to provide reasonable assurance that program control objectives are achieved.**

Response: Since PennDOT will be installing new photo license equipment and software in July 2007, we will pursue having a SAS 70 audit completed for Fiscal Year 07/08.

Auditors' Conclusion: We commend PennDOT's plans to pursue a SAS 70 audit for each service organization used in the driver licensing program.

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