PERFORMANCE AUDIT

Corporation Commission

For the period July 1, 2008 through December 31, 2011

Oklahoma State
Auditor & Inspector
Gary A. Jones, CPA, CFE

Audit Report of the Corporation Commission

For the Period July 1, 2008 through December 31, 2011

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Oklahoma State Auditor & Inspector

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TO THE OKLAHOMA CORPORATION COMMISSIONERS:

The Corporation Commission's recent public announcement of plans to pursue a strategically oriented approach to regulation, and the appointment of a new director of administration, place the agency in a fortuitous position to maximize the benefits of the recommendations provided in this report. From a planning perspective, the goals of developing an agency-wide strategic plan and of continuing modernization efforts are particularly relevant to our observations, as accomplishment of these worthy objectives will be difficult, if not impossible, without a deliberate approach to the agency's communication and information systems and a continuing external auditing presence to monitor and facilitate their effective execution.

The OCC exercises a unique combination of executive, legislative, and judicial powers, with broad authority over several critical sectors of Oklahoma's economy as varied as telecommunications, transportation and transmission of electricity and natural gas, and natural resource extraction. This vast and diverse regulatory authority lends itself to multi-faceted, complex operations that require specific expertise, resulting in isolated regulatory jurisdictions. Our observations also suggest that barriers to effective communication at the executive level persist among agency division directors. The challenge is in developing communication and information systems that successfully integrate the regulatory and adjudicatory functions of the agency to ensure the efficient and effective regulation of industries representing, directly or indirectly, roughly half of the state's gross state product.

Specifically, the Commission is advised to continue pursuit of a new case management system to electronically integrate agency divisions and provide user friendly access to industry and the public. Similarly, our audit considers development and application of an IFTA/IRP electronic system to be a priority because Oklahoma remains the only contiguous state that is electronically incompatible with the national clearinghouses, posing a serious risk to this substantial state revenue stream and the OCC's internal information systems.

Perhaps the most cost effective audit recommendation that will provide the most long-term benefit to the OCC, regulated industries, and the general public is the creation of an agency-wide communication plan. Our proposal includes a "top down" and "bottom up" approach to communication and the integration of strategic planning across divisions and regulatory jurisdictions with an on-going external audit function to realize the established plan's continued success. This integrated communication and information network is the key to the future effective exercise of the Commission's vast regulatory and unique adjudicatory authority.

Gary A. Jones

GARY A. JONES, CPA, CFE
OKLAHOMA STATE AUDITOR & INSPECTOR

Audit Purpose and Objectives

This audit was conducted at the request of the Oklahoma Corporation Commission (OCC or "agency") in accordance with 74 O.S. § 213.2.B.

Objectives

- Evaluate the status of prior period audit findings.
- Evaluate OCC's International Fuel Tax Agreement (IFTA) and International Registration Plan (IRP) programs and, as applicable, provide recommendations for increased efficiencies that may include cost savings or elimination of overlapping duties.
- Evaluate OCC's remaining programs on a limited basis and identify, as applicable, areas of risk that may warrant audit procedures in the future.

Audit Scope and Methodology

This performance audit was conducted in accordance with generally accepted government auditing standards. These standards require that the audit is planned and performed to obtain sufficient, appropriate evidence to provide a reasonable basis for findings and conclusions based the audit objectives. The auditors believe that the evidence obtained provides a reasonable basis for the findings and conclusions based on the audit objectives.

The audit period covered July 1, 2008 through December 31, 2011, unless otherwise noted in the report.

This report is a public document pursuant to the Oklahoma Open Records Act (51 O.S. § 24.A.1 et seq.), and shall be open to any person for inspection and copying.

Prior Period Methodology

Management was interviewed and limited procedures were performed related to the status of prior period findings.

IFTA/IRP Methodology

An understanding of the receipting and expenditure processes was obtained through discussion with agency employees, observation, and review of documents. Procedures were performed on certain receipts and expenditures to ensure that receipts were deposited and sufficiently supported. A detailed description of this methodology is contained in Appendix A.

In order to gain an understanding of the IFTA/IRP program history, of efforts toward electronic system development, and of potential participation in the IFTA and IRP national clearinghouses, discussions were held with agency employees and contractors.

Remaining Programs Methodology

Auditors reviewed agency and division websites, rules, applicable statutes, constitutional provisions, budget work programs and budget requests, quarterly and annual reports, strategic plans, and performance measures. In addition, interviews and discussions were held with division directors.

The program evaluation was conducted at the divisional level based on time and budget limitations of the defined objective and diversity, complexity, and number of OCC programs.

A complete assessment of agency-wide controls was not performed. Any comments related to the information and communication component of the internal control framework are primarily derived from observation of certain processes, interviews, discussions, and professional judgment.

Agency Overview

Established in 1907 by Article IX of the Oklahoma Constitution, the First Legislature granted the OCC authority to regulate public service corporations, businesses whose services are considered essential to the public welfare.[1] Numerous changes in state and federal laws over the years have altered and expanded the OCC's regulatory authority, but the basic rate-making and anti-monopoly authority mandated under Article IX has remained intact. OCC continues as one of the few constitutionally empowered state ratemaking, permitting, and regulatory agencies having combined authority over telecommunications, transportation and transmission of electricity and natural gas, and natural resource extraction.

As the primary regulatory authority over several sectors of the state's economy, the OCC regulates railroads, public utilities and public service corporations including electricity and natural gas rates and delivery, telecommunications and transmission, rural water utilities and cotton gins; oil and gas conservation including exploration, production, gathering, abandonment, waste disposal, and pollution abatement, prevention, and remediation; transportation and motor carriers including pipeline and motor carrier safety; and aboveground and underground tank storage and delivery of petroleum-based motor fuels. The OCC also has the power of a court of record with respect to adjudicatory authority over its jurisdictional areas.

The multifaceted nature of OCC's vast regulatory and adjudicatory authority is further illustrated in Appendix B, where descriptions of each division's responsibilities and relevant economic and industry information are presented.

Unique Powers

Deriving and retaining its basic ratemaking and anti-monopoly authority from Article IX of the Oklahoma Constitution and other enabling legislation[2], the OCC possesses wide discretion to implement and enforce authority over specified jurisdictional areas through a unique combination of executive, legislative, and judicial powers.

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[1] The legal principle for such regulation was established in 1877 when the United States Supreme Court ruled in *Munn v. Illinois*, 94 U.S. 113 (1877), that when a private company's business affects the community at large, it becomes a public entity subject to state regulation.

[2]Since the establishment of its general constitutional power, the OCC has been granted statutory authority by subsequent Oklahoma Legislatures through omnibus provisions in the Oklahoma Statutes, Title 17, chapters 1 through 5, and various enabling acts covering specific areas of OCC jurisdiction in Oklahoma Statute, Titles 17, 27A, 29, 47, 52, 68 and 82.

The OCC exercises statewide legislative privileges through constitutional ratemaking powers and rulemaking statutes; enforces requirements using executive and police power through orders, citations, subpoenas and other legal processes; and functions as a court of record when it adjudicates matters by hearing and order in a proceeding. A commission of three statewide elected officials makes the final decisions on all regulatory matters within the OCC's jurisdiction. Most orders of the Commission can be appealed only to the Oklahoma Supreme Court, although some appeals are taken to federal district court pursuant to federal statute.

Limited Dialogue Venue

In 2011, over 24,000 applications for an order of the Commission, spanning all jurisdictional areas, were filed with the OCC, resulting in issuance of over 10,000 orders.[3] The commissioners typically meet on a daily basis to sign orders in accordance with the daily signing docket. Except when matters under consideration are judicial in nature[4], these meetings are subject to provisions of the Open Meeting Act, (25 O.S. § 301 et seq.), which defines "meeting" as the conduct of business of a public body by a majority of its members being personally together or together pursuant to a videoconference.

Commissioners' limited dialogue venues pose an inherent communication barrier at the executive level.

A majority of the Commission constitutes a quorum, and the concurrence of the majority of the Commission is necessary to decide any question.[5] Commissioners are unable to discuss agency business unless meeting at specified times and places that are open to the public and that meet the notice and recordkeeping requirements of the Open Meeting Act. For example, commissioners would be in violation of the Act if they met for lunch at a restaurant to discuss the agency's strategic business plan or if two commissioners met with the director of administration in one of the commissioners' offices to discuss the status of an electronic case management development project. Such limited dialogue venues appear to pose an inherent barrier to effective communication at the executive level of the agency.

This innate obstacle to communication at the executive level, coupled with the OCC's aforementioned diverse regulatory authority and multi-faceted, complex operations, appear to call for an integrated communications system that spans all agency divisions.

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[3] Corporation Commission FY-13 Budget Request.

[4] Actions of a commissioner made in performance of the quasi-judicial authority of the Commission granted under Article IX, Section 19 of the Oklahoma Constitution are exempted from the application of the Open Meeting Act (Monson v. State ex rel. Oklahoma Corporation Commission, 1983 OK 115, 673 P.2d 839).

[5] Crawford v. Corporation Commission, 1940 OK 432, 106 P.2d 806.

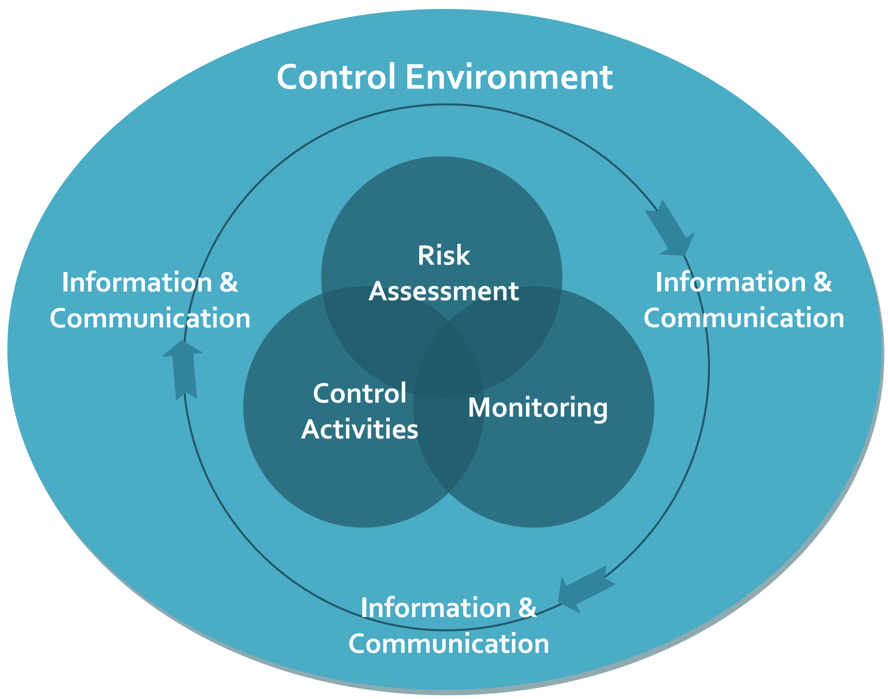
Organization Communications

Experts on organizations, management, and leadership assert that effective communications is the foundation for overall effectiveness in any type of organization. Well-functioning information and communications systems generate better decision making by managers, more engaged employees and fewer obstacles.[6]

Many organizations take a deliberate, formal approach to ensuring sound communications by developing a communications plan.

Communications: An Internal Control Perspective[7]

Effective communication of relevant, accurate, and timely information is required to meet business objectives including reliable financial reporting, efficient and effective operations, and compliance with statutes, regulations, and rules. The framework presented below illustrates this internal control standard.



The information and communication component does not stand alone, but rather is involved in every aspect of the internal control framework. No other component within the model is effective without an appropriate flow of information and communication.

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[6] Adapted from *The Field Guide to Leadership and Supervision*, Carter McNamara, MBA, Ph.D., Authenticity Consulting LLC, 2010.

[7] *COSO Internal Control Integrated Framework*, 1994. For more in-depth discussion of the framework and its components, see http://www.coso.org/guidance.htm.

Review of information and communication improves the effectiveness of internal controls and assists with the achievement of agency objectives.

Overall Observation

A formal and deliberate approach to ensuring sound communication is critical given the inherent communication barrier at the executive level of the OCC, the complexity of jurisdictional regulation, and the unique judicial function affecting most agency divisions.

Development of an agency communication plan could improve information sharing and integration of divisional efforts.

As this communication and information concern is likely a causal factor to some of the disparate issues discussed in the remainder of the report, fundamental improvements in the agency's overarching communication and information systems must occur for management to effectively address many of the following observations.

Evaluating the status of prior period findings

Auditors determined that the following prior period recommendations[8] were addressed by the agency:

- Reconciling interstate trucking account data with the State Treasurer's Office;
- Reconciling agency funds with the Office of State Finance;
- Tracking voided transactions in the receipting system;
- Review of daily deposits before delivery to the bank;
- Posting deposits to the PeopleSoft accounting system in a timely manner;
- Segregation of duties related to miscellaneous expenditures;
- Configuration of ChkEFT system passwords.

One recommendation was partially addressed:

- The agency has updated its inventory reporting system. However, a 100% inventory count has yet to occur, and the locations of field inventory items do not appear to be accurately tracked. These deficiencies could lead to misappropriation of assets.

[8] The prior period report with full findings and recommendations is available on the State Auditor's website at *http://www.sai.ok.gov/Search%20Reports/AuditSearch.shtml?audits.php?action=search&searchtext=corporation Commission*

Three prior period recommendations were not addressed:

- Highly complex Mineral Owners Escrow Account (MOEA) and clearing account reconciliations are not independently reviewed. Lack of independent review could result in misstatements which are not detected in a timely manner.
- Receipting functions have not been centralized, thus increasing the risk of receipt theft or misappropriation.
- Inadequate approval of IFTA and IRP expenditures was identified, potentially resulting in the issuance of unauthorized checks. It appears a mitigating control for this issue was developed after the conclusion of our audit period. See recommendations in the next report section.

The fact that several audit recommendations had not been addressed and the inability of the former director of administration to discuss prior year observations at the initial planning meeting appear to be further indications of an ineffective agency communication system.

Failure to address audit recommendations and management unawareness of audit results indicate ineffective communication.

Recommendations

In order to address these repeat observations, auditors recommend the following:

- Conduct a full inventory assessment and develop procedures to ensure proper tracking.
- An employee, independent of the MOEA reconciliation and clearing account reconciliation preparation, should perform a detailed review of these documents. This review eventually could be performed on a random basis at the reviewer's discretion.
- All funds should be initially received through the finance division, specifically the cashier's cage. The cashier should then forward the appropriate documentation to the various agency divisions. At month's end, each division should ensure the appropriate amount of funds was deposited to agree with the division's processed documentation. If these procedures are not feasible, management should consider alternative measures to reduce receipting risks.

Views of Responsible Officials

- *The Commission has almost completed the full inventory assessment of IT fixed assets and will conduct a full inventory assessment of other fixed assets. Management will review the current procedures for tracking fixed assets, especially those assigned to field personnel,* *to ensure that proper tracking procedures are in place and being followed.*

- *The finance director has started work on a more formalized approach to review of the MOEA and the clearing account reconciliations. Reviews will be performed monthly by an employee independent of those employees who do the initial reconciliation.*
- *Management agrees that centralized receipting procedures would organize the function and provide better control of funds. The agency will start by preparing a step-by-step plan to implement such procedures. The following issues will need to be addressed in the development of this plan: FTE duty reassignments; secure space requirements; establishment of central controls; a system to ensure receipts are correctly matched with their intended application; and cost.*

Evaluating IFTA and IRP programs

Program Overview

The International Fuel Tax Agreement (IFTA) and the International Registration Plan (IRP) are federally mandated programs that allow:

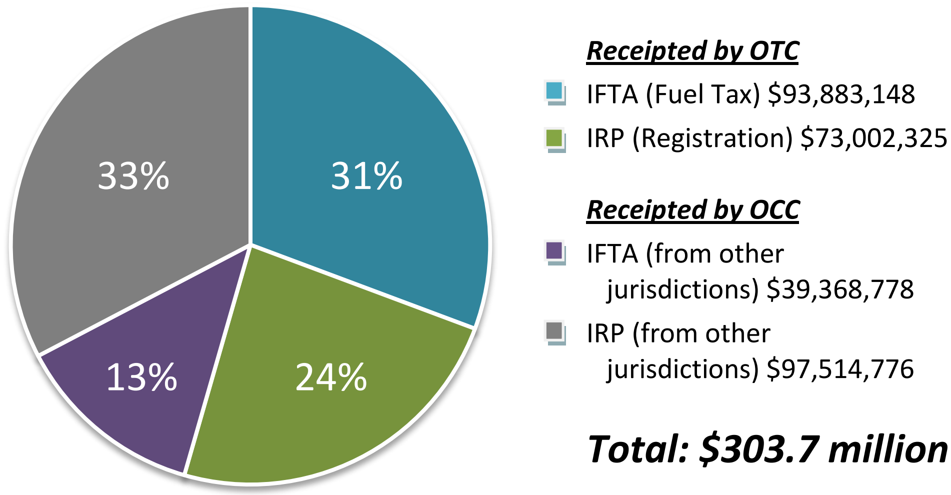
- A motor carrier to file quarterly fuel tax reports with a base jurisdiction (state or Canadian province), which then must apportion the fuel taxes paid to each state based on the mileage traveled in each jurisdiction.
- A vehicle to be registered and tagged in one jurisdiction and pay "apportioned" fees for the registration based on the mileage traveled in each jurisdiction. These fees are also redistributed by the base jurisdiction.

Each jurisdiction is required to administer the programs in a uniform manner as set forth by IFTA, Inc. and IRP, Inc. respectively.

Responsibility for administering the IFTA and IRP programs was transferred from the Oklahoma Tax Commission (OTC) to OCC in 2005 by legislation. A memorandum of understanding was developed between OCC and OTC outlining the responsibilities of each agency and including a monthly service charge of $5,000 for mainframe services provided by OTC. Between fiscal years 2009 and 2010, OTC increased this monthly service charge to $10,000.

Revenue

Revenue for both programs is received from 58 jurisdictions and totals over $303.7 million for the audit period. These revenue totals are unaudited amounts and were obtained from the OCC IFTA accountant and used only for planning purposes:



National Clearinghouse Compatibility

Oklahoma is the only participating state that is not electronically compatible with the national IFTA and IRP clearinghouses, which offer information sharing and jurisdictional payment netting.[9]

Oklahoma is the only state not compatible with national clearinghouses, posing significant risk to state revenues.

To avoid reliance on the OTC mainframe system and save monthly service charges, the OCC contracted with an automation consultant, LSG, in 2005 to create a customized and improved system that subsequently would allow Oklahoma to participate in the national clearinghouses. The decision to use a contractor was based on management's belief that in-house IT resources were inadequate to successfully create the desired system. The original project scope and cost were listed as four years at a total of $2,386,476 respectively.

Over the course of five years, OCC spent approximately $3.9 million, in addition to actual OTC service charges and an indeterminate amount of internal staff resources, to develop the customized system.

[9] According to staff, one or more Canadian provinces may not be compatible with the electronic clearinghouses; the other 47 contiguous United States are all compatible.

In 2010, the contract was cancelled without documented justification prior to cancelation and without the general counsel's knowledge.[10]

The electronic system remains incomplete and incompatible with the national clearinghouses. Disagreement also exists between the contractor and OCC IT management with regard to the rate of system completion. IT management asserts the project was 33% complete while LSG claims the system was approximately 80% complete when the contract was cancelled. Further, IT management has determined to complete the project using in-house resources which appears to be in direct contradiction to the initial rationale for selection of an outside contractor.

Observations

The auditors' evaluation of the financial processes related to IFTA and IRP funds resulted in the following observations:

- No controls are in place to ensure payments received from other jurisdictions are deposited (inadequate segregation of duties). In addition, a $38,000 jurisdictional payment was made payable to the OCC IFTA accountant[11] as well as the OTC.
- No independent review of supporting documents for expenditures was performed during the audit period.
- 8 of 60 IFTA/IRP expenditures reviewed had inadequate supporting documentation.
- Over $300,000 in outstanding jurisdictional payments that had not been received by Oklahoma were identified, and $1,500 was paid out to another state when it was actually due to Oklahoma.

National clearinghouse compatibility would reduce risk to the internal information network.

Management's responsibility is to maintain an effective internal control system to ensure that segregation of duties is maintained and an appropriate level of review is performed. Based on the auditors' observations, management has no assurance that funds received are deposited. It appears opportunities exist for jurisdictional payments

[10] The agency has contracted for IT projects with Aldos LLC, an electronic automation consultant, founded by a former LSG employee. An Aldos employee, while employed with LSG, worked as project manager for both oil and gas IT projects and the IFTA/IRP system project. Aldos continues to work for the agency on various projects as a sole source contractor following cancellation of the original LSG contract, receiving over $942,000 in payments between September 29, 2010 and the end of March 2012.
[11] The IFTA/IRP accountant is responsible for receiving and verifying jurisdictional payments and forwarding payments to the cashiers for deposit; no independent review of these jurisdictional receipts is performed.

received to be misappropriated and for unauthorized payments to be made.

The uncertainty surrounding Oklahoma's future compatibility with the national clearinghouses also appears to represent a significant risk to the agency's ability to effectively process IFTA and IRP jurisdictional revenues and payments, potentially impacting this substantial state revenue stream and posing additional risk within the agency's overall information network.

Recommendations

Management should complete and implement the electronic system in a timely and efficient manner to establish compatibility with the national clearinghouses, to reduce the risk of fraud, and to decrease risk to the agency's information network.

Temporarily, management should develop a centralized receipting system and the IFTA/IRP accountants should reconcile the jurisdictional payments receipted to the clearinghouse each month. Alternately, an employee, independent of the IFTA/IRP jurisdictional receipting process, should compare amounts reported to the clearinghouse to amounts receipted and deposited by the agency each month. The amount of transactions confirmed and the approach for performing this procedure should be at the reviewer's discretion.
As of January, management adopted an independent review process for expenditures that appears to reduce the segregation of duties deficiency. This process should be continued.

At the discretion of OCC management, engagement of an external audit presence and execution of future audit procedures could reduce identified risk.

Views of Responsible Officials

Management is keenly aware of the critical need for a new IFTA/IRP processing system. After determining in early 2010 that the system development project was not progressing satisfactorily and that additional contract funds would not be available, the director of administration made the decision to allow the contract with outside consultants to expire and tasked Commission staff to complete the project. By that time, the IT division had recruited staff with the necessary project management, systems analysis, and programming skills to successfully complete the project.

Every effort is being made by the Commission's IT and transportation divisions to complete the IFTA/IRP system as soon as possible. The system is currently on track for completion in 2013. Once implemented, this system will be compatible with the national clearinghouses and will remedy the need to manually process jurisdiction warrants, which will ensure better control.

An interim procedure is being developed in the finance department to route incoming jurisdictional receipts to one staff member and transmittal information to another staff member for review. Currently, the finance department has one employee that works IFTA receipts and another to process IRP. In the future, one employee will handle all paper warrants, and the other will look at transmittal data and reconcile it with the clearinghouse information.

A formalized method to reconcile to both the IFTA and IRP clearinghouses is also being established. This method will involve gathering information from the IFTA and IRP clearinghouses' online data, placing it in a worksheet, and matching receipted payments against this independent source. The finance department will coordinate with the transportation division and other jurisdictions during this change. Currently, the transportation division receives all transmittals and warrants initially. Many jurisdictions send warrants separately from transmittals, but not all. All jurisdictions will be requested to send warrants separately to the finance department while continuing to send the transmittal data to the transportation division.

Evaluating remaining agency programs

Communication & Information Systems

The following observations related to the OCC's existing communication and information networks are based upon an evaluation conducted at the division level:

- Perceived overall operational self-containment within divisions, particularly those that are self-funded, and insufficient communication among division directors.

- Inconsistency in successful development and application of internal information systems:
    - An original in-house IT design concept for a revised Consumer Services database was abandoned in 2011 because numerous errors occurred during the testing phase and the overall design was not user friendly.
    - The IFTA/IRP electronic system project has run over budget in terms of cost and time estimates and remains incomplete. IT management and Transportation Division management believe that an obstacle to the project's successful development and application was inadequate project oversight.
    - The Petroleum Storage Tank Division applied a system designed by an outside contractor that allows inspectors to electronically transmit data from inspection sites to the division's main database. Later phases of this project will involve online registration. Division management believes

active "hands on" project management by division staff is the basis for current and continued project success.
    - The Oil and Gas Division is successfully applying a newly developed electronic database system with assistance of an outside automation contractor and attentive oil and gas management oversight.

- Reliance on antiquated internal and integrated electronic information systems:
    - The IFTA/IRP electronic processing system is incompatible with the national clearinghouses and the agency continues to rely on OTC mainframe services.
    - The agency requested $500,000 in increased funds for a professional services contract to replace the antiquated Oracle system that serves as the Transportation Division's primary database.
    - The OCC requested $880,000 in additional appropriations to replace the Office of Administrative Proceedings' case management system with lower cost Microsoft technology, allowing scalable and web enabled case tracking to further the agency's goal of modernization. The system will be designed to integrate many division systems into one docket system for purposes of financial tracking and case management.

Modern, integrated case management system could decrease risk and improve communication.

The Office of Administrative Proceedings (OAP) is the central repository for a considerable percentage of the material either filed with the OCC by regulated industry and the public or generated by the agency as a result of its adjudicatory and regulatory authority. OAP management believes improvement in public access and use of this data is a fundamental duty of the OCC as a constitutional court of record and regulatory agency asserting both legislative and executive authority under state law.

As OAP is a central hub of document filing, retention, and public dissemination, the present case management, tracking, and processing system appears to represent a critical component of OCC's integrated information system, and therefore is paramount to the agency's future successful management of and integration of information across all divisions.

The agency seems to risk significant opportunity cost by failing to take advantage of the technology available to establish a modernized version of this case management system. Such a system could create an information network spanning across divisions to more effectively and efficiently fulfill OCC's constitutional and statutory mandate through the sharing and integration of information with a more user friendly interface.

General Observations

Legislative Policy

Evident risk to the state's environment and quality of ground and surface water exists as funds are redirected from assessment and remediation of contaminated sites to other priorities based on legislative policy. HB 2391 modifies apportionment of the $0.01 per gallon on the sale of each gallon of motor fuel by increasing the total amount deposited into the Weigh Station Improvement Revolving Fund from $51 million to $81 million at a prescribed rate of $500,000 per month. This apportionment must occur before any funds are deposited into the Indemnity Fund, thus delaying remediation efforts for eligible projects over the next five years.

Unreliable or Insufficient Funding

Funding from a potentially volatile revenue source, such as the oil and gas excise tax, creates a future recurrent risk to the oil and gas industry, surface owners, and environment[12]. Fluctuation in the oil and gas markets affects the level of excise tax revenue, so the agency does not have any assurance that these funds will be consistently available to support the expenses associated with industry regulation. According to division directors, without sufficient outside funding, internal revenue sources such as petroleum storage tank fees and court filing fees are insufficient to recover actual regulatory and adjudicatory costs.

Indirect Cost Allocation

The OCC's indirect cost allocation methodology is not tied to studies of actual time spent on support activities. The absence of a reasonable allocation method may lead to imprecise cost assignment, including costs passed on directly to consumers, and in inaccurate funding requests by the agency. In addition, the division directors, including finance, appear to exhibit a general lack of understanding of the agency's long established indirect cost allocation methodology.

[12] SB 1434, effective July 1, 2013, redirects a maximum of $2.7 million in excise taxes on oil and natural gas from the General Revenue Fund to the Oil and Gas Division Revolving Fund.

Compliance and Controls

The following areas could derive benefits from an ongoing external audit presence and audit procedures based on the divisional level assessment:

External audit presence could address risk issues in many divisions.

- Oklahoma Universal Service Fund (OUSF): FY-13 estimated funding requirement of $48 million is substantial and continues to increase. As OCC assumes a greater role in evaluating and granting OUSF funding requests through provisions of HB 2738, as the process to select a third party fund administrator currently is under Supreme Court review, and as associated costs are recoverable by public utilities through a direct charge to customers, there appears to be an emerging need to ensure compliance with statutory mandates.
- Mineral Owners Escrow Account (MOEA): Based on the manner in which funds are received and deposited into the MOEA, the ending FY-11 MOEA balance of almost $45.6 million, and inadequate oversight of MOEA processes and procedures, there appears to be an opportunity to ensure that appropriate controls and reviews are in place that protect mineral owner interests.
- Inspections: Non-compliance with inspection criteria, particularly with regard to petroleum storage tanks and pipeline safety, could have devastating consequences to the public's health and safety. Ensuring proper compliance with an on-going external audit presence could reduce associated risk.

Recommendations

- Capitalize on the opportunity to establish effective internal and integrated information and communication systems through the commitment to and oversight of strong director of administration leadership fully supported by the commissioners.

Views of Responsible Officials

The Commission is fully committed to the continual improvement of its information and communication systems. The agency will include an assessment of the effectiveness of these systems and the opportunities for their improvement as a critical component of the strategic planning process upon which the agency is about to embark.

- Establish a formal and deliberate approach to communication by developing a communication plan. The OCC communication plan should be designed to minimize inherent communication risk at the executive level and to maximize integrated communication and information sharing through agency-wide participation. For example, the plan could include:
  - A "Top Down" Communication Network: Form an Executive Management Team consisting of division directors to routinely meet with the director of administration;
  - Scheduling regular briefings by the director of administration, the "Executive Management Team," or other designated team members as directed by the commissioners or director of administration;
  - A "Bottom Up" Communication Network: Provide opportunities for information sharing by creating work teams consisting of various division representatives to monitor processes and adherence to policies and procedures, and to offer suggestions for improvements and new approaches to processes within and across divisions;
  - Incorporating the strategic planning and budget planning process in the development and implementation of the communication plan.

Views of Responsible Officials

Management will work to address this recommendation by formalizing and strengthening certain aspects of the agency's communication strategy, such as the frequency and structure of meetings of the leadership team. The Commission already uses a number of both formal and informal communication mechanisms effectively. Following are a few examples:

- *Our Commissioners meet on a daily basis to consider pending matters and discuss issues of concern to the agency, and they meet at least once a month with staff to receive updates on*

agency operations, including reports from the director of administration and the finance director.
- *The Commission receives regular updates from the divisions on various program activities and quarterly reports on performance measures and current trends, as well as immediate briefings on urgent matters and emergency situations.*
- *We employ a public information officer who plays a key role in disseminating information throughout the agency using various communication methods, including a daily report on industry news and a monthly newsletter for Commission employees.*
- *In recent years, the Commission has broadened both formal and informal communication channels by deploying computers with email and Internet capabilities to all Commission employees.*
- *The Commission and staff make regular use of ad hoc workgroups to address issues of policy and procedure.*

These examples clearly demonstrate the importance the Commission places on effective communications.

- Develop an indirect cost allocation process based on methods such as actual time management studies and ensure that division directors have a clear understanding of the adopted methodology. Division director input should be considered when developing the methodology.

Views of Responsible Officials

The director of administration is currently reviewing and adjusting the indirect cost allocation methodology. The director and fiscal staff of each division are participating in the review, which involves a survey of support staff to define actual time spent on different agency programs.

- Evaluate in-house expertise and ability to develop the necessary programs or oversee electronic conversion projects relating to data base management, case management, or web based licensing and registration. Although not specifically evaluated by the auditors, it appears reasonable to contract for, develop, and apply the OAP case management system as timely as possible to avoid opportunity cost and electronically integrate divisional information when appropriate. Designate an established work group, potentially including the general counsel or designated representative, to assist and advise the selected contractor with system development, testing, and implementation. The work group could also assist in contractor selection.

Views of Responsible Officials

The Commission will complete a comprehensive assessment of IT needs and project management capabilities and approaches as part of the upcoming strategic planning process. Work on the case management system will begin in the second half of FY-2013. The Commission's FY-2014 budget request seeks funding needed to complete the development *and implementation of this system. The existing case processing planning committee will be expanded to include representatives of all affected divisions.*

- Commit to carrying out audit recommendations through the communication plan, and follow up on recommendations to evaluate the plan's effectiveness and to assess agency efforts toward realizing audit recommendations.

Views of Responsible Officials

The Commission's leadership team will be responsible for evaluating the audit recommendations and ensuring they are appropriately addressed. The leadership team will also play a key role in the development and implementation of the Commission's strategic plan.

- Employ an external ongoing audit presence to perform audit procedures, as determined by agency management and based on a risk assessment, in identified areas such as the Mineral Owners Escrow Account, Oklahoma Universal Service Fund, petroleum storage tank inspections, and pipeline safety. This would include conducting a detailed risk assessment within each division including an agency-wide internal controls assessment.

Views of Responsible Officials

The Commission has directed the director of administration (the agency's appointing authority) to take necessary actions to engage auditors, and the director of administration has initiated discussions with the state auditor's office concerning the possible engagement of embedded auditors. The Commission's FY-2014 budget request includes a request for additional funding to support an ongoing auditor presence.

Conclusion

Effective communication and information systems are essential to the attainment of an organization's objectives. The OCC's unique powers, diverse regulatory authority, complex operations, and tendencies toward isolated regulatory jurisdictions appear to call for an integrated and deliberate approach to communication and the appropriate expertise and oversight to ensure the successful development and application of electronic information systems.

The OCC is advised to formulate a communication plan that involves agency-wide strategic planning and to continue pursuit of a modernized case management system that facilitates effective communication and information sharing across agency divisions and regulatory jurisdictions.

Prospective Areas for Further Study

During the course of the engagement, the following issues came to our attention. While further procedures related to these issues were not performed, the issues could merit future consideration.

- Evaluate current agency strategic planning and implementation efforts with an emphasis on integrated divisional planning.
- Assess statutes and constitutional provisions impacting commissioners' ability to meet in alternative venues and develop alternative communication strategies based on assessment.
- Review the cost effectiveness of the Consumer Services Division.
- Consider initiatives to cross-train inspectors across divisional lines to realize potential cost savings and efficiencies.
- Evaluate the feasibility of conducting a compensation study to obtain information for improving recruiting efforts, attaining optimal staffing levels, and retaining professional and institutional expertise.
- Assess options to prohibit use of Indemnity Fund proceeds other than those originally intended in the relevant enabling legislation.
- Evaluate current fee structure with a focus on functional self-sufficiency at the division and program level.
- Evaluate cost effectiveness of the Tulsa office.
- Assess current and potential training initiatives designed to reduce agency liability in employee issue-related litigation.

APPENDIX A:

Objective 1 Detailed Methodology

IFTA/IRP Revenues:

Auditors judgmentally selected 12 months from the audit period (January, February, March, October, November, December 2009; July, August, September 2010; and September, October, and November 2011) to ensure IFTA and IRP jurisdictional payments were receipted into the agency's internal accounting system. From these months, auditors agreed 136 IFTA amounts and 696 of 2,436 IRP amounts reported as paid to Oklahoma through the IFTA and IRP clearinghouses to internal agency documentation. (Note that due to the limitations of the agency's internal system, there was not a feasible manner by which to determine the total population of IFTA amounts due to Oklahoma each month.)

IFTA/IRP Expenditures:

Auditors judgmentally selected (by payee name and/or leading digit) 60 of 8,166 expenditure claims (totaling $123,582 of $1,097,471) to ensure the expenditure was allowable. (Note that there were 6,412 warrants totaling $698,746,122 that were not considered in these procedures because they were payments to other jurisdictions and were considered low risk.)

APPENDIX B:

Division Scope of Regulation and Responsibility (amounts are unaudited)

- **Oil & Gas Division** provides information, permitting, investigation, and compliance services to the oil and gas industry, mineral interests, landowners, and the general public to develop the oil and gas resources of the state while protecting the environment and ensuring public safety through regulation for all activities associated with the exploration and production of oil and natural gas. Oil and Gas also assists the Oklahoma Tax Commission with the identification of production and operators to ensure accurate accounting of Gross Production Tax proceeds. Gross Production Tax revenue deposited into the General Revenue Fund in FY-11 totaled almost $878 million (*Oklahoma's Oil and Natural Gas Industry Economic Impact and Jobs Report,* May 2012).

  Presently, there are about 2,660 active operators, 137,800 active wells (43,600 gas, 83,700 oil, and 10,500 injection/disposal), and thousands of miles of gathering and transmission pipelines. There are approximately 320,000 plugged and abandoned wells in Oklahoma (*Oklahoma Hydraulic Fracturing State Review,* January 2011). Annual operations from the state's oil and natural gas industry generate nearly $52 billion in goods and services or one-third of the Oklahoma's gross state product **(***Oklahoma's Oil and Natural Gas Industry Economic Impact and Jobs Report,* May 2012).

- **Public Utilities Division** provides analysis, research, technical support and recommendations to the OCC to fulfill the constitutional and statutory mandates related to public utility regulation. This division administers and enforces agency rules, regulations, and orders involving electric, gas, water, cotton gin, and telecommunications service providers. Much of the regulation involves ratemaking, auditing fuel costs, and rulemaking. In FY-10, the division was responsible for regulating 529 public utilities *(FY-2012 Executive Budget, Energy, B-66).*

- **Transportation Division** licenses and certifies motor carriers operating within and through Oklahoma; enforces motor carrier licensing requirements, special permit requirements, and commercial motor vehicle requirements; administers the International Fuel Tax Agreement (IFTA), the International Registration Plan (IRP), and the Unified Carrier Registration program (UCR); and enforces certain state nonconsensual towing, railroad crossing, and pipeline safety regulations.

  Oklahoma presently has approximately 7,600 for-hire and private motor carriers licensed to operate in intrastate commerce, 24 operating railroads, and about 40,000 miles of natural gas and hazardous liquid pipeline within state boarders (*FY-2012 Executive Budget, Energy, B-66).*

- **Petroleum Storage Tank Division** (PSTD) administers and enforces state and federal regulations pertaining to the storage, quality, and delivery of refined petroleum products such as motor fuel, gasohol, ethanol, and fuel grade ethanol and administers the Petroleum Storage Tank Release Indemnity Fund, or Indemnity Fund, designed to support remediation of contaminated sites due to releases of petroleum from storage tank systems into the environment.

  The division conducted approximately 5,500 tank inspections and 97,300 pump inspections in FY-10. For the previous twelve months, the Indemnity Fund averaged $1.74 million in assessments and $1.18 million in claims per month following the designated apportionments. As of December 31, 2011, $288.2 million has been spent to close 2,916 Indemnity Fund cases. Cost to complete clean-up of the currently active 446 Indemnity Fund cases is projected to be $111.0 million. The cost to assess and/or remediate these sites has already reached $98.2 million. *(PSTD Presentation 2-15-12).*

- **Consumer Services Division** serves as the OCC's liaison to the public on regulatory issues. The division investigates and mediates public utility and oil and natural gas complaints, provides education and community outreach services, and maintains the Mineral Owners Escrow Account (MOEA).

  The funds collected by the division, on the behalf of unknown or unlocated mineral owners as a result of oil and gas forced pooling, are held in escrow until these owners are found or for a maximum of five years before transfer into the Unclaimed Properties Fund which is managed by the Oklahoma State Treasurer. The MOEA ending fund balance totaled $45,595,776 for FY-11 *(Consumer Services Division annual Report, FY 2011).*

- **The Office of General Counsel** represents the OCC in causes to develop public policy and assists in the implementation through enforcement or adversarial proceedings, and through continuing advisory legal service. These services include representing the OCC and its employees in matters before the state and federal courts and administrative agencies and advising the agency regarding legislation, rules, and contracts while striving to balance the rights and needs of Oklahoma citizens with those of public utilities. In FY-11, the office conducted over 550 representations (*Office of General Counsel Annual Report FY 11*).

- **Office of Administrative Proceedings** (OAP) serves as the judicial branch of the OCC by ensuring the opportunity for fair and open hearings, after proper notice, in all jurisdictional areas; by processing and maintaining all public records pertaining to hearing applications, notices, and orders through the Court Clerk's Office; and by providing public access to all docket information, public records of applications, notices and affidavits, hearing transcripts or recordings, exhibits, administrative law judge reports and recommendations, OCC decisions, and interlocutory (interim) and final orders. The office issued over 10,000 reports in FY-11 (*Corporation Commission FY-13 Budget Request*).

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