

OPERATIONAL AUDIT

OKLAHOMA DEPARTMENT OF ENVIRONMENTAL QUALITY

For the period July 1, 2011 through June 30, 2013



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

**Audit Report of the
Oklahoma Department of
Environmental Quality**

**For the Period
July 1, 2011 through June 30, 2013**



Oklahoma State Auditor & Inspector

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December 1, 2014

**TO THE HONORABLE GOVERNOR MARY FALLIN AND
THE ENVIRONMENTAL QUALITY BOARD**

This is the audit report of the Oklahoma Department of Environmental Quality for the period July 1, 2011 through June 30, 2013. The goal of the State Auditor and Inspector is to promote accountability and fiscal integrity in state and local government. Maintaining our independence as we provide this service to the taxpayers of Oklahoma is of utmost importance.

We wish to take this opportunity to express our appreciation for the assistance and cooperation extended to our office during our engagement.

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

Sincerely,

A handwritten signature in blue ink that reads "Gary A. Jones". The signature is fluid and cursive, with the first name "Gary" being the most prominent.

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

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Background

The Oklahoma Department of Environmental Quality was established by the Legislature in 1993 to protect human health, provide quality service to Oklahomans through comprehensive environmental protection and to safeguard the natural environment: air, water and land. The agency is primarily responsible for the environmental policy of Oklahoma and management programs designed to assist citizens in sustaining a clean, sound environment and to preserve and enhance the natural surroundings.

Oversight is provided by a thirteen member Environmental Quality Board who are appointed by the Governor and confirmed by the Senate. Each member serves a term of five (5) years.

Board members as of October 2014 are:

John Wendling.....	Chair
Jan Kunze	Vice-Chair
Shannon Ferrell.	Member
Daniel Blankenship.....	Member
James Kinder.....	Member
Tracy Hammon.	Member
David Griesel.....	Member
Jerry Johnston	Member
Steve Mason.....	Member
Billy G. Simms	Member
Cheryl Vaught	Member
Loretta Turner	Member
Tim W. Munson	Member

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The following charts illustrate the Agency's primary funding sources, and where those funds are expended.¹

Chart 1 - Revenues by Category (July 1, 2011 through June 30, 2013)

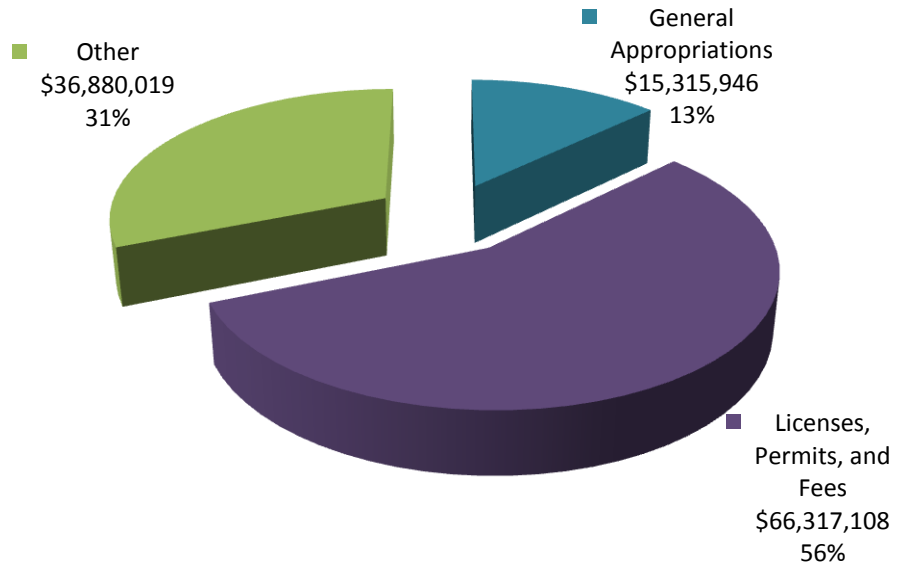
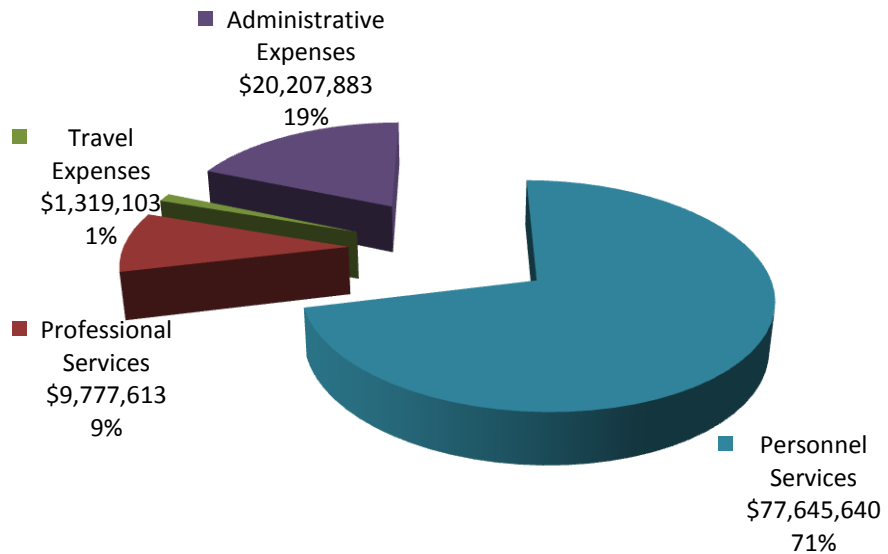


Chart 2 - Expenditures by Category (July 1, 2011 through June 30, 2013)



¹ This information was obtained from Oklahoma PeopleSoft accounting system. It is for informational purposes only and has not been audited.

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Scope and Methodology

Our audit was conducted at the request of the Governor in accordance with 74 O.S. § 212.C and 74 O.S. § 213.2.B.

We conducted this operational audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessment of materiality and risk for the period July 1, 2011 through June 30, 2013. Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of the Oklahoma Department of Environmental Quality's operations. We also tested a sample of transactions to achieve our objectives. To ensure the samples were representative of the population and provided sufficient, appropriate evidence, the random sample methodology was used. We identified specific attributes for testing each of the samples and when appropriate, we projected our results to the population.

Because of the inherent limitations of an audit, combined with the inherent limitations of internal control, errors or fraud may occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

OBJECTIVE I

Determine whether the Agency's internal controls provide reasonable assurance that revenue, expenditures (including payroll) and inventory were accurately reported in the accounting records, and financial operations complied with significant laws and regulations.

Conclusion

The Agency's internal controls provide reasonable assurance that expenditures including payroll were accurately reported in the accounting records. However, they do not provide reasonable assurance that revenues and inventory were accurately reported.

The Agency deposits 10% of fees collected from off-site hazardous waste facilities to the Northwest Oklahoma Economic Development Authority, which complies with 27A O.S. § 2-7-121 E.1.

FINDINGS AND RECOMMENDATIONS

**Control
Environment
and
Communication
Risks are High**

An effective internal control system has in place policies and procedures that reduce the risk of errors, fraud, and professional misconduct within the organization. Key factors in this system are the environment established by management, and effective information and communication to achieve the Agency's objectives. Management's ethics, integrity, attitude, and operating style become the foundation of all other internal control components. In addition, agency management needs to access relevant and reliable communication related to internal as well as external events.

As part of our control risk assessment, we surveyed and interviewed the Agency employees and the following general concerns were expressed:

- The importance of integrity and ethical values within the Agency was questioned.
- An atmosphere of mistrust and poor communication exists between division employees and upper management.
- There is a perception of gender discrimination, and that promotions and pay raises have been granted without merit.
- Employees lack the proper software, tools, and hardware to perform their job duties.

Employees' concerns, whether factual or perceived, have a negative impact on the Agency's control environment. This increases the risk of errors and misappropriation of assets.

Recommendation

We recommend the Board and the executive director recognize the risk associated with this type of environment and work towards evaluating and addressing the situation to ensure the mission of the Agency is accomplished in the most efficient manner possible. In addition, we recommend they identify the Agency's information requirements and design an appropriate method to effectively communicate this information within the organization.

Views of Responsible Officials

Since December of 2013, the following actions have taken place to address this matter.

- In December 2013, the Environmental Quality Board selected a new executive director to lead the agency. The new Executive Director is meeting frequently with a board subcommittee in order to address the cultural challenges facing the agency. The performance of employees in

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key leadership positions was evaluated and certain changes have been made. The Executive Director's office is emphasizing clear communication to the workforce. Meetings involving all agency managers are being held on a regular basis.

- In order to more effectively disseminate information and respond to relevant needs, in addition to regular staff meetings, the Executive Director's office holds a monthly meeting involving both directors and assistant directors from all divisions.
- Agency leadership is placing a special emphasis on recruiting and retaining the very best employees, and creating a work environment which improves and sustains workforce morale. True employee accountability is being emphasized.
- The executive director's office recently identified several high-priority challenges facing the agency, and formed workgroups to find solutions to those challenges. Our goal is to both solve problems and improve working conditions within the DEQ. Focus areas include: (1) enhancing our customer service culture, (2) improving workforce training and succession planning, (3) improving public relations and outreach, and (4) enhancing the agency's financial review and planning process.
- DEQ is expanding its course offerings and opening up more training to non-managers and is also pursuing a dialogue with industry representatives that are focused on training one another.
- In order to attract and retain suitable employees the DEQ is exploring options for improving its overall employment compensation package.
- An Office of External Affairs has been established, staffed by experienced individuals from the workforce. This unit is instrumental in coordinating processes that involve external customers and internal regulatory processes. The Office also includes an ombudsman function to provide a clear path of assistance to the regulated community, and to foster cooperation inside the agency. Thus far we have received many positive responses regarding the changes in culture.

No Reconciliation Between Funds Received And Licenses Issued

To protect against possible errors or irregularities in an entity's financial records, an effective internal control system should provide for accurate and reliable records and adequate review of supporting documentation.

The licensing divisions do not reconcile funds processed in the finance division to licenses and permits issued. This process would help ensure that payment has been received for all licenses and permits issued.

Lack of detailed reconciliation could allow for errors or irregularities to occur and not be detected in a timely manner.

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Recommendation

We recommend management consider designating an employee from each licensing division independent of the receipting process to reconcile licenses and permits issued with payments received.

Views of Responsible Officials

Across the agency there are several individuals who maintain records for their respective program areas to ensure that permits and licenses are not issued prior to fees being paid. The methods employed vary somewhat from program to program. For example, Air Quality Division utilizes the Finance receipt from FileMaker to issue their licenses and permits. Others check for payment at the time the application is received, in order to re-calculate the appropriate fee and make adjustments as needed. In the absence of their own recordkeeping, the permit and licensing staff members contact Finance staff to determine the status of fee payment, prior to permit or license issuance. Administrative Services staff will revisit the appropriate personnel in each division to review the processes in order to ensure compliance.

Funds Received Are Not Deposited Timely

62 O.S. § 34.57(C) states in part, "receipts of One Hundred Dollars (\$100.00) or more shall be deposited on the same banking day as received" and "receipts of less than One Hundred Dollars (\$100.00) may be held until accumulated receipts equal One Hundred Dollars (\$100.00) or for five (5) business days, whichever occurs first, and shall then be deposited no later than the next business day."

To protect against possible errors or irregularities in an entity's financial records, an effective internal control system should provide reasonable assurance that funds received are deposited timely.

Funds are not being deposited in accordance with 62 O.S. § 34.57(C).

Not depositing funds in a timely manner increases the risk of possible loss or misuse of funds.

Recommendation

We recommend management deposit funds in accordance with 62 O.S. § 34.57(C).

Views of Responsible Officials

DEQ concurs with this finding during the beginning of the audit period; however, the issues were rectified by DEQ before Calendar Year 2012 began. DEQ has a standard practice now that should keep DEQ's deposits in accordance with 62 O.S. § 34.57(C).

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Inadequate Segregation of Duties Related to Inventory

The United States Government Accountability Office's *Standards for Internal Control in the Federal Government*² states, "Key duties and responsibilities need to be divided or segregated among different people to reduce the risk of error or fraud. This should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing the transactions, and handling any related assets. No one individual should control all key aspects of a transaction or event."

The Agency has one employee who maintains inventory records and, in conjunction with the Office of Management and Enterprise Services, authorizes the disposal of surplus inventory and records transfers/surplus items in the inventory records. This individual also has the opportunity to initiate a purchase, prepare the purchase order, and receive deliveries.

This creates the risk that the employee in this position could misappropriate inventory items without detection.

Recommendation

We recommend the employee maintaining the inventory listing should not be involved in the purchasing or authorizing the disposal of surplus property.

Views of Responsible Officials

DEQ hired a new employee to work in this area on 03/17/2014. The employee left for a different job opportunity after a few months. DEQ has again posted the position. DEQ is attempting to hire another central supply manager that will not create initial purchase orders for assets but will manage the assets and be in charge of surplus. The individual must have their CPO credential prior to having certain access within the system.

However, DEQ's current standard process should still allow for segregation of duties because of the asset management software utilized by DEQ through the state of Oklahoma. The software codes an item as an asset based upon the system criteria of account code and dollar threshold, which are not criteria entered into the system by the DEQ employee maintaining the inventory. The asset requires a receiver before payment can be processed by accounts payable. Also, even if an item is surplus out, the system maintains a record of that item as an inactive asset so a documentation trail is still required.

² Although this publication addresses controls in the federal government, this criterion can be treated as best practices. The theory of controls applies uniformly to federal or state government.

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Auditor Response

We do not concur with management's interpretation of segregated duties within the inventory process. It may be DEQ's standard process to properly segregate inventory duties; however, during the audit period that policy was not functioning effectively; therefore, allowing the one individual to possibly misappropriate inventory. It is our understanding that the individual responsible for maintaining inventory records also has the responsibility of approving and handling surplus items. We agree that hiring and properly training an additional inventory staff member will help with segregating the duties. However, the surplus duties should be assigned to someone who does not have access to inventory records. This individual should also ensure at year end that all surplus items have been removed or noted as surpluses in the inventory records.



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