DEPARTMENT OF LABOR

FOR THE PERIOD
JANUARY 1, 2007 THROUGH
DECEMBER 31, 2008

OPERATIONAL AUDIT

OFFICE OF THE STATE AUDITOR AND INSPECTOR
OKLAHOMA

Oklahoma State Auditor
& Inspector

Audit Report of the Department of Labor

For the Period January 1, 2007 through December 31, 2008

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September 3, 2009

TO THE COMMISSIONER OF LABOR

This is the audit report of the Department of Labor for the period January 1, 2007 through December 31, 2008. The Office of the State Auditor and Inspector is committed to serving the public interest by providing independent oversight and by issuing reports that serve as a management tool to the State. Our goal is to ensure a government that is accountable to the people of the State of Oklahoma.

We wish to take this opportunity to express our appreciation to the agency's staff for the assistance and cooperation extended to our office during the course of our engagement.

Sincerely,

STEVE BURRAGE, CPA
STATE AUDITOR & INSPECTOR

Background

The Department of Labor (Agency) is responsible for the enforcement of labor laws that promote fairness and equity in the workforce, including state wage laws, workers' compensation compliance, state occupation and safety health administration laws for public employers, asbestos compliance, child labor laws as well as various other duties.

Table 1 summarizes the Agency's sources and uses of funds for fiscal years 2007 and 2008 (July 1, 2006 through June 30, 2008).

Table 1 - Sources and Uses of Funds for FY 2007 and FY 2008

	2007	2008
Sources:		
State Appropriations	$ 3,760,271.58	$ 3,613,883.95
Worker's Compensation Assessement	$ 1,275,000.00	$ 1,221,940.76
Worker's Compensation Fines	$ 423,015.97	$ 499,218.00
Federal Reimbursements	$ 1,703,196.46	$ 1,533,855.15
Other	$ 77,300.85	$ 287,005.74
Total Sources	$ 7,238,784.86	$ 7,155,903.60
Uses:		
Personnel Services	$ 6,006,129.81	$ 6,074,801.24
Professional Services	$ 109,879.75	$ 56,194.49
Travel	$ 156,696.05	$ 112,529.32
Miscellaneous Administrative	$ 199,467.51	$ 252,005.34
General Operating Expenses	$ 45,773.65	$ 39,828.85
Other	$ 739,222.64	$ 735,116.20
Total Uses	$ 7,257,169.41	$ 7,270,475.44

Source: Oklahoma PeopleSoft Accounting System (unaudited - for informational purposes only)

Purpose, Scope, and Sample Methodology

This audit was conducted in response to 74 O.S. § 212, which requires the State Auditor and Inspector's Office to audit the books and accounts of state officers whose duty it is to collect, disburse or manage funds of the state.

The audit period covered was January 1, 2007 through December 31, 2008.

We selected our samples in such a way that whenever possible, the samples are representative of the populations and provide sufficient evidential matter. Sample methodologies can vary and are selected based on the audit objective and whether the total population of data was available. Random sampling is the preferred method; however, we may also use haphazard sampling (a methodology that produces a representative selection for non-statistical sampling), or judgmental selection when data limitation prevents the use of the other two methods. We identified specific attributes for testing each of the samples. When appropriate, we projected our results to that population.

We conducted this performance 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. 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.

Objective 1 - To determine if the Agency's internal controls provide reasonable assurance that revenues, expenditures, and inventory were accurately reported in the accounting records, and financial operations complied with 74 O.S. § 250.4.

Conclusion

The Agency's internal controls:

- Generally provide reasonable assurance that revenues and expenditures were accurately reported in the accounting records; however, two areas could be strengthened; and
- Do not provide reasonable assurance that inventory was accurately reported in the accounting records.

Financial operations complied with 74 O.S. § 250.4 (limitations related to the Commissioner of Labor's salary).

Methodology

To accomplish our objective, we performed the following:

- Documented internal controls related to the receipting, expenditure, and inventory processes which included discussions with Agency personnel, observation, and review of documents;
- Tested controls which included:
    - Determining if the person preparing the deposit is independent of the receipting process;
    - Determining if the person receiving the processed deposit slip from the bank and reconciling it to the deposit ledger is independent of the receipting process;
    - Randomly selecting 40 deposits to ensure the deposit slip was initialed by the chief financial officer as well as agreed to the edit report and the deposit ledger. Additionally, we ensured the date on the processed deposit slip was within one day of the date on the deposit ledger;
    - Determining the Agency's clearing account was reconciled on a monthly basis to the State Treasurer's Office by someone independent of the receipting process;
    - Reviewing a random sample of eight Office of State Finance (OSF) Form 11 reconciliations to ensure the reconciliations were mathematically accurate, were performed in a timely manner, agreed to supporting documentation, and reconciling items appeared reasonable;
    - Reviewing a random sample of 40 expenditure claims to ensure they were properly authorized. This included ensuring the invoice supported the payment, the invoice was mathematically accurate, the correct account code was used, and the expenditure was reasonable given the Agency's mission.

- Reviewed 74 O.S. § 250.4 (states the Commissioner of Labor's salary is equal to a special judge's salary), 20 O.S. § 92.1A (sets a special judge's salary), 20 O.S. § 3.4 (authorizes the Board on Judicial Compensation to set judicial salaries), and the report issued by the Board on Judicial Compensation[1];

- Reviewed the HR Actions report from the PeopleSoft accounting system's for the audit period to determine the Commissioner of Labor's salary was in compliance with 74 O.S. § 250.4.

Observation **Inadequate Segregation of Duties Related to Expenditures**

An effective internal control system provides for adequate segregation of duties.

The accounts payable clerk is responsible for posting expenditures into the PeopleSoft accounting system as well as receiving warrants from OSF. Management has designed a control to reduce this risk. The chief financial officer reconciles the Agency's internal records with PeopleSoft on a monthly basis which he feels would detect an unauthorized expenditure. However, the reconciliations and portions of the Agency's records from the audit period were not retained.

Management was unaware that the retention of the records was necessary. Misappropriation of assets could occur and not be detected in a timely manner.

Recommendation If management wishes to continue having the accounts payable clerk post expenditures into the PeopleSoft accounting system as well as receive warrants from OSF, the reconciliation between the Agency's records and PeopleSoft as described by management should continue. However, since this information would be used to mitigate the segregation of duties risk, we recommend management formalize this process which would include the chief financial officer signing and dating the reconciliation as well as retaining all pertinent data related to the reconciliation.

Since the reconciliation is not required by law, management could elect to design procedures to ensure the employee responsible for posting expenditures in the accounting system is not the same employee responsible for receiving warrants from OSF or develop other mitigating controls.

Views of Responsible Officials This recommendation is consistent with current practice and will require only slightly increased administrative action. The Oklahoma Department of Labor concurs with the audit recommendation.

Observation **Inadequate Segregation of Duties Related to the Inventory Process**

An effective internal control system provides for accurate and reliable records.

The procurement officer is responsible for:

- Surplusing items no longer needed by completing the DCS Form 001 as well as deleting items from the inventory listing; and
- Participating in the physical inventory count process.

[1] This report was issued in accordance with 20 O.S. § 3.4 and revised the salary amounts identified in 20 O.S. § 92.1A.

The inventory count is conducted by multiple employees who may not be independent. For example, an administrative assistant is given a listing of items in their department to verify. If the supervisor has lost or stolen a digital camera, they could notify the procurement officer the camera was accounted for.

Management was unaware of the risks created by not ensuring there was an adequate segregation of duties. Deficiencies such as these increase the risk that misappropriations of assets may occur.

Recommendation

We recommend:

- An employee without the ability to update inventory records be responsible for completing the DCS Form 001; and
- Physical inventory counts performed by the administrative assistants should be discontinued. A designated employee(s) (excluding the procurement officer) should perform this duty. If discrepancies are noted, the Commissioner of Labor or designee, other than the personnel involved in the physical count, should investigate and resolve. The Agency should also retain documentation to support who performed the actual count, when the count was performed, and any discrepancies noted during the count.

Views of Responsible Officials

ODOL will segregate the conduct of inventory and certification to an appropriate staff member. This staff person will be an administrative assistant and will report all findings to the Commissioner with recommendations for action as deemed necessary.

Observation

Inadequate Segregation of Duties and Procedures Related to Petty Cash Fund

An effective internal control system provides for adequate segregation of duties and restricts access to assets that are susceptible to misappropriation. In order to preserve proper safeguarding of assets and establish proper asset accountability, it is vital that access to assets be limited to the fewest number of people reasonably possible.

The Agency has not established an adequate system of internal control over its petty cash fund. The following was noted:

- The employee who is primarily responsible for managing the petty cash fund is also performing daily petty cash reconciliations; and
- Four additional employees have access to the petty cash fund as backup roles.

Management was unaware of the risks created by not ensuring there was an adequate segregation of duties and allowing multiple employees access to the petty cash. Misappropriation of assets could occur and not be detected in a timely manner.

Recommendation

We recommend management segregate the duties related to the petty cash fund so the person primarily responsible for managing the fund is independent of the person reconciling the fund. Furthermore, we recommend that access to the petty cash fund be limited to the fewest number of employees possible that would allow for operations to carry on in the absence of the person primarily responsible for managing the fund.

Views of Responsible Officials

The primary custodian of the petty cash fund will count and certify fund contents each morning. The fund contents will be counted and certified by a person from a different division at the close of business each day. This will give dual review of daily activity.

Since the window is open all day, every day, having back up personnel is necessary. A minimum of two available personnel is necessary to ensure full coverage during days off, lunch breaks, etc.

The Oklahoma Department of Labor will keep additional personnel at a minimum and they will be required to do the same as the permanent custodians.

Observation

Agency Should Develop Formal Policy Related to Ethical Behavior

An effective internal control system has in place policies and procedures that reduce the risk of errors, fraud, and professional misconduct within an organization. A key factor in this system is the environment established by management. Management's ethics, integrity, attitude, and operating style become the foundation of all other internal control components.

As part of our control risk assessment, we surveyed Agency employees based on their relationship to our objective and other employees which were haphazardly selected. We also conducted follow–up interviews. The following was noted:

- The Agency has not developed and implemented an official written policy addressing ethical behavior in the workplace. Without a written policy and procedure in place, employees may not be aware of management's expectations regarding ethical behavior thus affecting the Agency's control environment risks; and
- Communication challenges exist between management and staff. These challenges could negatively impact any efforts at communicating ethical expectations.

Recommendation

We recommend the Agency develop a written policy regarding ethical behavior in an effort to reduce the possibility of unethical behavior occurring. Once developed, the policy should be distributed to all current employees and procedures should be implemented to provide the policy to all new employees.

Views of Responsible Officials

We concur with the finding that an additional section in the employee handbook would be beneficial. The Deputy Commissioner, Human Resources Director, and General Counsel have been directed to prepare a section to be distributed to all current employees and new hires of ODOL regarding ethical behavior including conflicts of interests, gifts, gratuities, relationships between state employees, and overall professionalism.

Recommendation

We recommend executive management be cognizant of the risks associated with ineffective communication within an entity and work to eliminate any such barriers in an impartial manner. Clear communication channels should flow in both an upstream and downstream direction within the Agency.

Views of Responsible Officials

We concur this is an ongoing problem, not only in this agency, but in every organization. We agree if communications are not well maintained, there may be undesirable outcomes.

Communications have been dramatically improved by moving to a single story building on June 1, 2009. This had a positive effect in enhancing interoffice communications between not only divisions, but administration and staff.

Communications planning is ongoing and will include: regularly issue-oriented staff meetings with directors, requirements that directors inform staff of appropriate information from meetings, and an enhancement of the responsibility of all levels of staffing to conform to the chain of command. Employees need to be assured of no retaliation when items of program effectiveness and management are brought to the attention of administration. This will be a major goal of the Oklahoma Department of Labor during the upcoming year.

Additional Procedures Performed

Methodology

As a result of the control deficiencies identified under objective 1 of this report, the following procedures were performed:

- Agreed 30 high-appeal assets from the inventory listing to the floor to ensure they existed. No exceptions were noted as a result of the procedures.

Other Items Noted

Although not considered significant to the audit objective, we feel the following issue should be communicated to management.

Observation

<u>Questions Related to Compensatory Time Requirements Regarding Employees Exempt Under the Fair Labor Standards Act</u>

Oklahoma Administrative Code (OAC) 530: 10-7-12 (d) (2) states in part, “An employee shall be permitted to use accrued compensatory time within 180 days following the pay period in which it was accrued…”

OAC 530: 10-7-12 (e) Appointing Authorities may provide compensatory time off to FLSA Exempt…employees with the following stipulations:

(1) The compensatory time off shall be taken within time periods and policy outlined in 530:10-7-12(c) (2)[2]. Unused compensatory time shall be taken off the books if not taken by the end of the time periods and policy outlined in 530:10-7-12(c) (2)…

(3) Payments shall not be made for compensatory time accrued by an employee on FLSA Exempt status for any reason, except as provided for in (e) of this Section.

Based on unaudited Agency records, as of June 30, 2008, two employees exempt from the Fair Labor Standards Act (FSLA) had compensatory (comp) time balances of approximately 115 hours and 300 hours, respectively. Based on management’s

[2] This reference appears to be incorrect as there is not a 530:10-7-12(c) (2). For the reference to make sense, it appears it should read 530:10-7-12(d) (2).

understanding of these employees' status with respect to the FSLA, they did not consider their comp time subject to the above mentioned requirements. It is possible a portion of the hours presented may have been accrued more than 180 days prior to June 30, 2008.

Recommendation

We recommend management and legal staff consult with the Office of Personnel Management to determine the appropriate course of action with regards to OAC 530:10-7-12, specifically those outlined in (d) and (e) with regards to exempt personnel.

Views of Responsible Officials

A review of comp time records indicate that, in fact, some employees had an excessive amount of comp time which may have exceeded 180 days. The agency has reviewed the recommendation, and after appropriate consultation with OPM, have erased all comp time past 180 days. Further, the Commissioner has determined that no unclassified, exempt employee will accrue comp time without prior written approval effective July 1, 2009. All affected agency employees have been notified of this change.

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