OPERATIONAL AUDIT

Oklahoma Workers' Compensation Commission

For the period February 1, 2014 through June 30, 2015

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

Audit Report of the Oklahoma Workers' Compensation Commission

For the Period February 1, 2014 through June 30, 2015

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Oklahoma State Auditor & Inspector

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November 18, 2015

TO GOVERNOR MARY FALLIN:

This is the audit report of the Oklahoma Workers' Compensation Commission for the period February 1, 2014 through June 30, 2015. 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,

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

Background

The Oklahoma Workers' Compensation Commission (Agency) was created by the Oklahoma Legislature in 2013 (SB 1062). By creating the commission, the workers' compensation system was moved from a judicially based system to an administrative system. The commission consists of three commissioners appointed by the Governor with advice and consent of the Oklahoma Senate.

Workers who are injured on or after February 1, 2014, may have their cases heard by an administrative law judge appointed by the commission. The commissioners also serve as an appellate body, and they perform other regulatory duties as they pertain to workers' compensation issues.

Commission members as of June 30, 2015 are:

Robert Gilliland .... Commission Chair

Mark Liotta. .... Commissioner

Dr. Leroy Young.. Commissioner

The following information illustrates the Agency's budgeted-to-actual revenues and expenditures and year-end cash balances.[1]

	FY 2015		
REVENUES	**Budgeted**	**Actual**	**Variance**
Appropriations	2,746,647	2,784,235	37,588
Taxes	1,617,038	1,078,759	(538,279)
Licenses, Permits, and Fees	-	758,370	758,370
Fines, Forfeits and Penalties	-	443,048	443,048
Income From Money and Property	-	132,104	132,104
Grants, Refunds and Reimbursements	-	11,247	11,247
Sales and Services	-	55,313	55,313
Non Revenue Receipts	-	17,735	17,735
Other Revenue Transactions	-	1,904,705	1,904,705
Total Revenues	**4,363,685**	**7,185,517**	**2,821,832**
EXPENDITURES			
Personnel Services	3,676,188	3,523,295	(152,893)
Professional Services	80,000	339,728	259,728
Travel Expenses	90,000	30,827	(59,173)
Administrative Expenses	112,981	107,227	(5,755)
Property, Furniture, Equipment, and Related Debt	404,516	315,119	(89,397)
General Assistance, Awards, Grants, and Other Program-Directed Payments		2,378	2,378
Transfers and Other Disbursements	-	550,754	550,754
Total Expenses	**4,363,685**	**4,869,329**	**505,644**
Expenditures Over (Under) Revenues		**(2,316,188)**	

Summary of Agency responses to budgeted-to-actual variances

This information is a summary of responses obtained from the Oklahoma Workers' Compensation Commission. It is for informational purposes only and has not been audited.

Revenues

- The Commission was conservative with its revenue estimations. As a new agency, it was uncertain of what to expect, making budgeting difficult.

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

Scope and Methodology

Our audit was conducted in response to Governor Fallin's request in accordance with 74 O.S. § 212.C and 213.2.B.

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.

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 February 1, 2014 through June 30, 2015.

Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of the Oklahoma Workers' Compensation Commission operations. We utilized sampling 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

Determine whether the Agency's internal controls provide reasonable assurance that revenue, expenditures (including miscellaneous expenditures and payroll expenditures), and inventory were accurately reported in the accounting records.

Conclusion

The Agency's internal controls do not provide reasonable assurance that revenues, expenditures (both miscellaneous expenditures and payroll expenditures), or inventory were accurately reported in the accounting records.

We were unable to determine whether financial operations complied with the following statutes due to lack of documentation. The risks related to this lack of documentation and related control deficiencies are detailed in the final finding of this report:

- 85A O.S. § 97 – Creation of Self-Insurance Guaranty Fund
- 85A O.S. § 98 – Self-insurance Guaranty Fund
- 85A O.S. § 99 – Impaired Self-insurer

FINDINGS AND RECOMMENDATIONS

Inadequate Segregation of Duties over Revenue

The United States Government Accountability Office's (GAO) *Standards for Internal Control in the Federal Government (2014 Revision)*[2] state, "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 of 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 not segregated key duties related to revenues. The following conflicting conditions were identified:

- The records clerk is responsible for receipting funds into the Agency's accounting system.
- The records clerk is responsible for preparing and making the deposit.
- The Agency's internal records of receipts posted to various databases are not reconciled to external records of funds deposited.

Due to lack of segregation of duties and the absence of a reconciliation of receipts posted to the Agency's internal database to deposits, the following conditions could occur and go undetected:

- The records clerk could post receipts to the internal database and misappropriate the associated payments (also due to a lack of reconciliation of Agency records to CORE records).
- When preparing the deposit, the records clerk could misappropriate payments received by excluding them from the deposit.

Recommendation

We recommend management implement a mitigating control, performed by an employee independent of the receipting and deposit process, which should provide assurance that all payments posted in Agency databases

[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.

were deposited. An example of this control would be to reconcile all payments credited to customer accounts to deposits.

Views of Responsible Officials

The Commission's duties are now properly segregated in accordance with recommendations.

Inadequate Segregation of Duties over Expenditures

The GAO's *Standards for Internal Control in the Federal Government (2014 revision)* state, "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 not segregated key duties related to miscellaneous expenditures. The following conflicting conditions were indentified:

- The HR Director is responsible for approving requisitions prior to the Office of Management and Enterprise Services, Agency Business Services (ABS), creating the purchase orders; he then approves the invoices for payment once purchased items have been received.
- The HR Director is also responsible for reviewing the monthly CORE 6-digit detailed expenditure report.

Without adequate management review, it appears someone in this position could submit an illegitimate claim for payment.

Recommendation

A member of management independent of the expenditure process should perform a detailed review of all expenditures and document this review by signing and dating the 6-digit detailed expenditure report.

Views of Responsible Officials

In agreement with the audit's recommendation, the Commission's CFO has established a procedure that properly segregated duties.

Inadequate Segregation of Duties over Payroll Expenditures

The GAO's *Standards for Internal Control in the Federal Goverment* state, "Key duties and responsibilities need to be divided or segregated amoung different people to reduce the risk of error or fraud. This should include separating the responisibilities 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 not segregated key duties relating to payroll expenditures. The HR Director is responsible for creating and approving the agency payroll information form as well as reviewing and approving the payroll claim document.

Without adequate segregation of duties, management's approval of payroll changes could be circumvented and fictitious payroll payments or improper payroll changes could be processed and concealed.

Recommendation

Management, who is independent of the payroll process, should independently obtain and review appropriate detailed payroll data, including changes made to employee's records.

Views of Responsible Officials

The Commission's procedure for payroll going forward segregates duties. The HR manager will forward email of the Payroll Register and Payroll Funding Distribution to the CFO. The CFO will review when completing monthly reconciliations; any discrepancies will be discussed with the HR Manager and/or Executive Director, Commissioners if needed.

Inadequate Segregation of Duties over Inventory

The GAO's *Standards for Internal Control in the Federal Government (2014 Revision)* state that "Management must establish physical control to secure and safeguard vulnerable assets… Management periodically counts and compares such assets to control records." Futhermore, the GAO states that "Management designs an internal control system to provide reasonable assurance regarding prevention or prompt detection and correction of unauthorized acquisition, use, or disposition of an entity's assets."

In addition, Oklahoma Administrative Code 260:110-3-1 states in part:

> a) **Report due date.** All agencies must submit an annual report of current inventory of tangible assets owned by the agency as of June 30 of the preceding fiscal year to the Office by August 15. The

> report shall include all tangible assets based upon the threshold stated in 260:110-1-3(a).

The Agency does not maintain an inventory listing of their assets and did not have a plan in place to complete inventory counts or submit required reports to the Office of Management Enterprise Services OMES.

The absence of an inventory listing and lack of controls over inventory provides an opportunity for the inventory to be mistated or misappropriated without detection.

Recommendation

We recommend management identify all assets and create an inventory listing. The individual responsible for maintaining the inventory records should not have the ability to receive purchased items or approve inventory items for surplus. In addition, we also recommend that management ensure a comprehensive annual physical inventory count is performed and documented by someone independent from purchasing assets, maintaining inventory items or inventory records, and disposing of surplus assets. Appropriate inventory should then be reported to OMES as required by Oklahoma Administrative Code 260:110-3-1.

Management should also ensure assets are appropriately safeguarded and that asset tags and inventory records are accurately maintained.

Views of Responsible Officials

The Business Office is compiling a listing of inventory items. A procedure had been created that meets the requirements set forth in recommendation prior to the audit being completed.

Failure to Comply with Laws and Regulations

As prescribed by state statute, the Self-insured Guaranty Fund operates as follows:

- The purpose of the fund is to provide continued workers' compensation benefits for eligible individuals when a self-insurer is unable to meet its compensation obligations for various reasons. Monies in the fund are also used to pay claims for related administrative fees, operating and other reasonable costs of the Self-insurance Guaranty Fund Board, and attorney fees. (**85A O.S. § 97)**

- When the Commission determines that a self-insurer has become impaired, the Commission secures release of the security the self-insurer has previously provided as required by **85A O.S. § 38** (a letter of credit or surety bond) and advises the Self-insurance Guaranty Fund Board of the impairment. Claims administration may include payment by the surety bond issuer or be otherwise contracted by the Commission. **(85A O.S. § 99)**
- Until the fund contains $2,000,000, or in the event the amount in the fund falls below $1,000,000, each private self-insurer and group self-insurance association is assessed at a rate determined by the commissioners, not exceeding one percent of actual paid losses of the self-insurer during the preceding calendar year. The assessment is paid to the Tax Commission for deposit to the fund and the rates are based on the proportion of the fund balance deficiency attributable to each class of self-insurer (private or group) for the calendar year preceding the assessment. (**85A O.S. § 98.2)**

To test for compliance with these state statutes, we selected samples of claims paid from funds 701 (Letter of Credit Fund) and 705 (Self-insured Guaranty Fund), and noted the following:

- Management was unable to locate supporting documentation for 6 of 16 claims randomly selected from *Fund 701*.
- Management was unable to locate supporting documentation for 8 of 16 claims randomly selected from *Fund 705*.

The Agency was unable to provide documentation of the calculation method used to make assessments against private or group self-insurers during the audit period. They were also unable to provide documentation of those entities who had or had not made assessment payments to the fund.

The Agency has not implemented a standardized tracking system to help identify actual paid losses during the year, though these amounts drive the annual assessments. As a result, self-insured entities not in compliance with payment obligations may not be identified, impacting the Agency's revenues and resulting in noncompliance with all other collections-related laws and regulations.

Furthermore, the GAO's *Standards for Internal Control in the Federal Government (2014 Revision)* provide that internal control should provide reasonable assurance that the objectives of the agency are being achieved in categories including compliance with applicable laws and regulations.

The Agency's internal controls do not appear to be designed to identify non-compliance with laws and regulations, and without proper controls in place and adequate supporting documentation, the Agency is at risk of non-compliance with applicable laws and regulations.

Recommendation

We recommend management consider implementing the following procedures:

- Develop a standardized tracking system for all private and group self-insurers' actual claims paid and the calculation method of the annual assessments made to ensure compliance with regulatory authority.
- Document and maintain communication with the Oklahoma Tax Commission, to ensure all self-insurers pay the assessment fee made by the Commission.
- Ensure expenditure claims, along with supporting documentation, are properly maintained.

Views of Responsible Officials

700 Funds (701 and 705) Documentation – Claims paid from a 700 fund will be filed separately from other operations' payables. The CFO completes a monthly reconciliation of the 700 funds.

705 Funds – The CFO and Insurance Services Director have discussed a new process for the next time the Self-Insured Guaranty Fund assessment is issued that is in line with the audit's recommendation. That discussion included the Oklahoma Tax Commission to ensure proper communication and documentation will take place throughout the assessment process.

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