



An Audit Report on

Financial Processes at the State Office of Risk Management

June 2018

Report No. 18-032



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Overall Conclusion

The State Office of Risk Management (Office) had significant weaknesses in its contracting processes and lacked key controls to ensure that it consistently performed required activities related to contract planning, procurement, and formation.

The Office processed and paid Workers' Compensation claims and calculated the annual Workers' Compensation assessments in accordance with applicable statutes, rules, and Office procedures. The Office also had processes in place to help ensure that travel expenditures complied with applicable rules and procedures, and it had adequate information technology controls for its accounting and travel systems. However, the Office should strengthen its processes to ensure proper segregation of duties for travel expenditure approvals and improve its controls over its Claims Management System.

Auditors communicated other, less significant issues to Office management separately in writing.

Table 1 on the next page presents a summary of the findings in this report and the related issue ratings. (See Appendix 2 for more information about the issue rating classifications and descriptions.)

Background Information

The State Office of Risk Management (Office) administers the State's Workers' Compensation and risk management programs. The Workers' Compensation program covers most state employees, county employees at community supervision and correction departments, and employees of the Windham School District, which operates schools at various Department of Criminal Justice facilities. The Office's risk management program includes enterprise risk management, risk transfer through insurance, and continuity of operations planning.

By statute, the Office is administratively attached to the Office of the Attorney General for administrative support services.

For fiscal years 2017 and 2018, the Office was appropriated \$51.0 million and \$50.8 million, respectively.

Source: The Office; Texas Labor Code, Chapter 412; and General Appropriations Acts (84th and 85th Legislatures).

Table 1

Summary of Chapters/Subchapters and Related Issue Ratings		
Chapter/ Subchapter	Title	Issue Rating ^a
1	The Office Had Significant Weaknesses in Its Contract Planning, Procurement, and Formation Processes for Contracts with External Vendors	High
2-A	The Office Accepted, Denied, and Paid Workers' Compensation Claims in Compliance with Applicable Statutes, Rules, and Office Policies and Procedures	Low
2-B	The Office Processed Travel Reimbursements in Compliance with Applicable Rules and Office Procedures; However, It Should Improve Controls to Ensure Proper Segregation of Duties	Medium
3	The Office Had Processes to Ensure That It Correctly Calculated Annual Workers' Compensation Assessments	Low
4	The Office Had Adequate Information Technology Controls for Its Accounting and Travel Systems; However, It Should Improve the Controls Over Its Claims Management System	Medium

^a A subchapter is rated **Priority** if the issues identified present risks or effects that if not addressed could critically affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern and reduce risks to the audited entity.

A subchapter is rated **High** if the issues identified present risks or effects that if not addressed could substantially affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern and reduce risks to the audited entity.

A subchapter is rated **Medium** if the issues identified present risks or effects that if not addressed could moderately affect the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern and reduce risks to a more desirable level.

A subchapter is rated **Low** if the audit identified strengths that support the audited entity's ability to administer the program(s)/functions(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.

Summary of Management's Response

At the end of each chapter in this report, auditors made recommendations to address the issues identified during this audit. The Office agreed with the recommendations in this report.

Audit Objective and Scope

The objective of this audit was to determine whether the Office has processes and related controls to help ensure that it administers financial transactions in accordance with applicable statutes, rules, and agency policies and procedures.

The audit scope included the Office's activities related to contracts in effect, Workers' Compensation claims, Workers' Compensation annual assessments calculated and collected, travel expenditures, and related information systems for fiscal year 2017 (September 1, 2016, through August 31, 2017) and the first five months of fiscal year 2018 (September 1, 2017, through January 31, 2018).

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Detailed Results

Chapter 1

The Office Had Significant Weaknesses in Its Contract Planning, Procurement, and Formation Processes for Contracts with External Vendors

The Office had significant weaknesses in its contracting processes and lacked key controls to ensure that it consistently performed required activities related to contract planning, procurement, and formation. (See text box for more information.)

Chapter 1
Rating:
High¹

Auditors tested three contracts totaling approximately \$4.1 million that the Office executed related to the Texas Workers' Compensation program. Those contracts were:

- A contract with Injury Management Organization, Inc. for \$1.9 million per year to provide pre-authorization and utilization reviews, a medical provider network, and medical case management services.
- A contract with Matrix Healthcare Services, Inc. (doing business as myMatrixx) for \$1.5 million per year. myMatrixx serves as the Office's pharmacy benefits manager and provides services such as a retail pharmacy network and a mail service pharmacy.
- A contract with ISG Services, LLC for \$650,000 per year for medical bill review services to determine the applicability of procedure codes and rates.

Contract Planning, Procurement, and Formation

Planning - Identify contracting objectives and contracting strategy.

Procurement - Fairly and objectively select the most qualified contractors.

Contract Formation/Rate/Price Establishment - Ensure that the contract contains provisions that hold the contractor accountable for producing desired results, including all relevant terms and conditions, and establish processes that are cost-effective and aligned with the cost of providing goods and services.

Source: *State of Texas Contract Management Guide*, version 1.12.

Auditors identified significant weaknesses in the Office's procurement of the three contracts. Specifically:

Contract Planning. The Office issued one request for proposals (RFP) related to medical cost containment services and based on that RFP, it awarded the

¹ The risk related to the issues discussed in Chapter 1 is rated as High because they present risks or results that if not addressed could substantially affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern and reduce risks to the audited entity.

three contracts tested. The services requested in that one RFP were broad and not well-defined. In addition, it did not contain 3 (30 percent) of 10 applicable statement of work components from the *State of Texas Contract Management Guide*. Specifically, in the RFP, the Office did not quantify the amount or frequency required to meet performance expectations, identify the level of quality required for acceptable performance, or clearly define criteria for determining satisfactory contract completion. In addition, when the Office executed the contracts, it did not develop performance measures or a list of deliverables within the contracts. Consistently including all statement of work components required by the *State of Texas Contract Management Guide* would help the Office include the necessary information in contracts and monitor to determine whether the contractor is performing satisfactorily.

In addition, the Department did not develop a needs assessment or cost estimate as required by the *State of Texas Contract Management Guide*. According to the *State of Texas Contract Management Guide*:

- The purpose of a needs assessment is to provide a clear definition of the contracting objectives, which should be used to develop the statement of work in a solicitation and verify the performance of a contractor.
- A cost estimate should be used to determine the type of procurement and the range of services that can be included in the statement of work in a solicitation.

Not consistently performing needs assessments and cost estimates limits the Office's ability to ensure that procurements address identified needs at the best value to the State.

Contract Procurement. The Office performed some required procurement activities for the contracts that auditors reviewed. Those activities included (1) advertising solicitations on the *Electronic State Business Daily*; (2) ensuring that purchasing staff had the required purchasing contract manager certification; (3) ensuring that evaluators and contract management personnel signed nondisclosure and conflict of interest statements; (4) using the same evaluation criteria as was published in the solicitation; and (5) reviewing vendor proposals for responsiveness. However, the Office did not consistently perform other required activities. Specifically:

- The Office scored the responses as a group rather than individually. The *State of Texas Contract Management Guide* requires that the evaluation team members evaluate and score the proposals independently.

- The Office did not assign contract managers for the three contracts reviewed as required by the *State of Texas Contract Management Guide*.

Evaluating the proposal submissions individually helps ensure that the scoring is fair and the awarded contracts are the best value to the State. In addition, assigning a contract manager would help the Office verify that contractors are complying with all contract requirements and delivering services in a timely manner.

Contract Formation. The Office did not (1) ensure that five of the clauses and provisions required by the *State of Texas Contract Management Guide* were complete or (2) incorporate all of the Contract Advisory Team's recommendations into the RFP or contracts reviewed. Specifically, for the RFP and associated three contracts reviewed:

- The scope of work, specification, and funding out provisions, and the dispute resolution and affirmation clauses were not always complete. For example:
 - ◆ Two contracts included only a brief summary, but not details, of the services being provided in the scope of work provision.
 - ◆ All three contracts did not cover all of the ways funding could be lost within the funding out provision.
- The Office included remedies and sanctions provisions in one contract as required by the *Texas Government Code*. However, the remaining two contracts included a remedies clause but did not include a sanctions schedule.
- The Office did not fully incorporate all of the State's Contract Advisory Team's recommendations into the RFP or final contracts or provide a written explanation for not including them (see text box for information about the Contract Advisory Team). Specifically:
 - ◆ The Office did not develop and include performance measures and related remedies in the RFP for two (67 percent) of the three contracts reviewed.

Contract Advisory Team

The Contract Advisory Team assists state agencies in improving contract management practices by providing recommendations and assistance throughout the contract management process.

The Contract Advisory Team is composed of one member from each of the following:

- Health and Human Services Commission.
- Office of the Comptroller of Public Accounts.
- Department of Information Resources.
- Texas Facilities Commission.
- Office of the Governor.
- A small state agency.

State agencies are required to comply with Contract Advisory Team recommendations or submit a written explanation regarding why a recommendation is not applicable to the contract under review.

Source: Texas Government Code, Chapter 2262.

- ♦ The Office did not include the essential contract clauses and general provisions identified as missing by the Contract Advisory Team in the RFP or final contracts.

Including complete, required contract clauses and terms in all contracts and complying with Contract Advisory Team recommendations or providing a written explanation for why the recommendation is not applicable to the contract would help the Office reduce the risk that the State's interests may not be protected and that the contractor may not comply with requirements.

Recommendations

The Office should:

- Ensure that all requests for proposal are well-defined and include all statement of work components required by the *State of Texas Contract Management Guide*.
- Ensure that proposal submissions are independently evaluated and scored by the members of the evaluation team as required by the *State of Texas Contract Management Guide*.
- Perform a needs assessment and cost estimate for all contracts as required by the *State of Texas Contract Management Guide*.
- Assign contract managers for all contracts as required by the *State of Texas Contract Management Guide*.
- Include all clauses, provisions, and terms and conditions required by the *State of Texas Contract Management Guide* in all contracts, and ensure that clauses and terms and conditions contain all of the required information.
- Incorporate the Contract Advisory Team's recommendations into its solicitations and contracts, or document why any recommendation is not applicable to the contract under review as required.

Management's Response

A. *Well-Defined Request for Proposal that includes State of Texas Contract Management Guide Statement of Work Components*

Management agrees with this recommendation, which has been fully implemented by General Counsel for the State Office of Risk Management

(Office) and the Office of the Attorney General, Procurement Division Director (OAG Procurement).

The Office, in conjunction with OAG Procurement, reviewed and updated procurement policies and procedures to strengthen compliance with applicable laws and the State of Texas Contract Management Guide and the State of Texas Procurement Manual.

B. *Independently Evaluate and Score Proposal Submissions*

Management agrees with this recommendation, which has been fully implemented by the Office's General Counsel and OAG Procurement.

Enhancements were made and executed related to formal solicitation scoring and the Office will continue to comply with the evaluation and scoring requirements of the State of Texas Contract Management Guide.

C. *Perform Needs Assessment and Cost Estimate for All Contracts*

Management agrees with these recommendations, which have been substantially implemented by the Office's General Counsel and OAG Procurement. Implementation of new procurement processes has strengthened compliance with the cost estimate guidance in the State of Texas Contract Management Guide. Implementation of the needs assessment recommendation will be complete when procurement planning templates and resources are utilized in future procurements.

The Office is tailoring templates created by OAG Procurement to the specific needs of the Office. The Office will use the templates and other procurement planning resources during the procurement planning phase to ensure business needs, contract objectives, and performance expectations are clearly defined. To ensure the appropriate method of procurement is used, the Office will perform and document compliance with the cost estimate recommendation.

D. *Assign Contract Manager for All Contracts*

Management agrees with this recommendation, which has been substantially implemented by the Office's Executive Director, the Division Chief of Legal Services Division, and the Director of Compliance and Practices.

Implementation will be complete when the newly created position is filled.

The Office has created and posted a Contract Administrator position within the Legal Services Division, Compliance and Practices Department. This individual will be responsible for activities related to contracts, including specifications, verification of contractor performance, monitoring compliance

with deliverable and reporting requirements, enforcement of contract terms, monitoring and reporting of vendor performance, and ensuring that contract performance and practices are consistent with applicable rules, laws and the State of Texas Procurement Manual and Contract Management Guide. The Contract Administrator will ensure the contract is satisfactorily performed and the responsibilities of both parties are properly discharged. The Contract Administrator will work directly with business users to proactively identify and address any contractor performance issues that affect the efficiency and/or effectiveness of the contracted services/goods.

E. *Include all State of Texas Contract Management Guide Required Clauses, Provisions, and Terms and Conditions*

The Office agrees with this recommendation, which has been fully implemented by the Office's General Counsel.

The Office updated and implemented new contract planning and contract maintenance processes to ensure all essential clauses and applicable recommended clauses are fully incorporated into existing contracts and future contracts.

F. *Incorporate Contract Advisory Team's Recommendations*

The Office agrees with this recommendation, which has been fully implemented by the Office's General Counsel and OAG Procurement.

The Office, in conjunction with OAG Procurement, reviewed and updated procurement policies and procedures to strengthen compliance with applicable laws and the State of Texas Contract Management Guide and the State of Texas Procurement Manual.

Chapter 2

The Office Processed and Paid Workers' Compensation Claims and Travel Reimbursements as Required; However, It Should Improve Controls Over Travel Reimbursement Approvals

The Office had adequate controls over its acceptance or denial of Workers' Compensation claims and over the processing of claims payments. The payments that auditors tested at the Office complied with state statutes and rules and Office procedures.

The Office also ensured that travel expenditures complied with applicable rules and Office procedures. However, it should improve its controls over travel reimbursement approvals.

Chapter 2-A

The Office Accepted, Denied, and Paid Workers' Compensation Claims in Compliance with Applicable Statutes, Rules, and Office Policies and Procedures

Chapter 2-A
Rating:
Low ²

The Office had adequate controls over its acceptance or denial of Workers' Compensation claims and over the processing of claims payments. The payments that auditors tested at the Office complied with state statutes and rules and Office procedures.

The Office administers the State's Workers' Compensation program. As the administrator, the Office processes payments related to Workers' Compensation claims, including medical claim payments. Those medical claims payments are processed based upon recommended amounts from the contracted medical cost containment provider. In fiscal year 2017, the Office processed a total of \$14,818,282 in medical claims payments, according to its Claims Management System. For all 25 Workers' Compensation payments tested totaling \$4,808, the Office paid the correct amounts and properly recorded them in the Uniform Statewide Accounting System.

In addition, the Office receives Workers' Compensation claims, verifies the claims, and then approves or denies the claims based on requirements defined in the Texas Labor Code, the Texas Administrative Code, and Office procedures. The Office followed its processes and complied with requirements for the claims tested. Specifically:

² The risk related to the issues discussed in Chapter 2-A is rated as Low because the audit identified strengths that support the audited entity's ability to administer the program(s)/functions(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.

- The Office accepted all 26 of the accepted Workers' Compensation claims that auditors tested within 7 days of receiving the injury report from the employer as required by Texas Labor Code, Chapter 409. Four of those 26 claims included income benefits, for which a payment must be made within 15 days as required by Texas Labor Code, Chapter 409. The Office made all 4 of those payments within that 15 day time frame, and it ensured those payments were appropriately reviewed and approved as required by the Office's procedures.
- The Office reviewed and approved as required all 25 of the denied Workers' Compensation claims tested and denied those claims within 60 days as required by Texas Labor Code, Chapter 409.

Chapter 2-B

The Office Processed Travel Reimbursements in Compliance with Applicable Rules and Office Procedures; However, It Should Improve Controls to Ensure Proper Segregation of Duties

**Chapter 2-B
Rating:**
Medium³

The Office had processes in place to ensure that its travel reimbursement payments complied with applicable rules and procedures. All 25 of the travel vouchers that auditors tested were processed from September 1, 2016, through January 31, 2018, were supported, were for official state business, were properly coded, and were approved as required.

The Office's process for travel requires a division chief or a member of executive management to approve all requests and payments. The Office configured the eTravel system to allow any of those individuals to approve all travel requests and vouchers. As a result, the automated system that processed payments after September 1, 2017, does not prohibit the same person from approving his or her own travel request or voucher (see text box for information about that system). The Department of Information Resources' *Security Controls Standards Catalog* requires adequate controls and separation of duties for tasks that are susceptible to fraudulent or other unauthorized activity. Five individuals were authorized to approve travel in the eTravel system. From September 2016 through January 2018, those individuals had a total of \$28,817 in travel expenditures.

Travel Request and Voucher Process

Prior to September 2017, the Office used paper travel request forms and reimbursement vouchers. Upon receiving required approval signatures, the Office would forward a voucher to the Office of the Attorney General for payment processing.

In September 2017, the Office of the Attorney General implemented a travel system that automated the travel request and voucher processes. All travel requests and reimbursement vouchers are entered, approved, and tracked within that system. After receiving required approvals, the documentation is routed to the Office of the Attorney General for payment processing.

Source: The Office.

³ The risk related to the issues discussed in Chapter 2-B is rated as Medium because they present risks or results that if not addressed could moderately affect the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern and reduce risks to a more desirable level.

Auditors tested expenditures totaling \$16,202 (56 percent) for those individuals and did not identify any instances in which the traveler approved the reimbursement vouchers.

Having weak controls in the eTravel system that allow an individual to approve his/her own travel reimbursement payment increases the risk that inappropriate expenditures may be approved.

Recommendation

The Office should consider strengthening controls within the eTravel system to ensure proper segregation of duties and to prevent a user from approving his/her own travel.

Management's Response

A. *Strengthen Controls Within eTravel System to Ensure Proper Segregation of Duties and Prevent a User from Approving His/Her Own Travel*

The Office agrees with this recommendation. The Office's Division Chief of Internal Operations is coordinating with applicable OAG administrative support personnel to determine the best option that would strengthen the Office's separation of duties protocol related to eTravel. Assessment and implementation of a solution is targeted for completion during fiscal year 2019.

The Office Had Processes to Ensure That It Correctly Calculated Annual Workers' Compensation Assessments

**Chapter 3
Rating:**
Low⁴

The Office had processes and controls in place to help ensure that it calculated the annual Workers' Compensation assessments in accordance with applicable rules (see text box). The Office also collected the correct annual assessment amounts from the selected participating State entities. However, the Office did not have a documented process to follow up on assessment payments not received from agencies within the required time frames.

Annual Workers' Compensation assessments accounted for 99 percent of the Office's total revenues, according to data in the Office's fiscal year 2017 annual financial report. The Office assessed \$51,717,471 for fiscal year 2017 from state entities participating in the State's Workers' Compensation program. For fiscal year 2018, the Office's assessment was \$51,719,626.⁵

Assessment Calculation. Based on the information that participating entities provided to the Office, the Office accurately calculated the participating entities' assessment amounts for fiscal years 2017 and 2018.

Assessment Collection. The Office collected the correct assessment amounts from all 14 entities tested. However, the Office did not have documented processes in place to ensure that it consistently followed up on assessment

Workers' Compensation Assessments

The Office is administered through appropriated funds, interagency contracts for insurance coverage and risk management programs, and the annual assessments for the financing of the State's Workers' Compensation benefits.

Each participating entity's assessment should be calculated using a weighted, three-year rolling average of the entity's:

- Payroll as a percentage of all participating state entities' payroll.
- Full-time equivalent employees (FTEs) as a percentage of the total of all participating state entities' FTEs.
- Injury frequency rate for all participating state entities.

In addition, the assessment calculation includes a simple three-year average of the following factors:

- Total number of accepted claims as multiplied by the state entities' injury frequency rate modifier.
- Claims costs as a percentage of all claim payments made on behalf of the participating state entities.

The due date for state entities to submit their assessment payment to the Office is no later than the third day after the entities' appropriations become available.

Sources: Title 28, Texas Administrative Code, Chapter 251; Texas Labor Code, Chapter 412; and the General Appropriations Acts (84th and 85th Legislatures).

⁴ The risk related to the issues discussed in Chapter 3 is rated as Low because the audit identified strengths that support the audited entity's ability to administer the program(s)/functions(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.

⁵ The Office calculated an initial assessment amount for fiscal year 2018 in August 2017. That initial assessment is presented in this report. To reflect actual claims expenditures incurred, the Office recalculated the assessment in May 2018 after the auditors completed testing.

payments it does not receive within the required time frame established in the Texas Administrative Code.

Recommendation

The Office should develop and document a process to consistently follow up on assessment payments that are not received within the required time frames.

Management's Response

A. *Develop and Document an Assessment Payment Follow-Up Process*

The Office agrees with the recommendation, which has been substantially implemented by the Office's Division Chief of Internal Operations. Written procedures will be developed, formalized, and implemented. The target date for full implementation is December 31, 2018.

The Office Had Adequate Information Technology Controls for Its Accounting and Travel Systems; However, It Should Improve the Controls Over Its Claims Management System

Chapter 4

Rating:

Medium⁶

The automated systems that the Office uses to administer financial transactions had controls to help ensure that the Office administered financial transactions in accordance with applicable statutes, rules, and Office policies and procedures. The selected controls were adequate for the accounting and travel systems; however, the Office should improve certain controls over its Workers' Compensation Claims Management System (CMS). The Office of the Attorney General (OAG) maintains the accounting system and has contracted with a third-party vendor to maintain the travel system. The Office maintains CMS.

Application Controls. Auditors tested selected application controls for the OAG Accounting, eTravel, and CMS systems and determined that these controls were effective to ensure the reliability of data in those systems (see text box for more information on the tested systems).

Change Management. Auditors tested change management controls over CMS. The Office did not have a documented change management policy or an adequate change management process to help ensure that it appropriately and consistently documented, tested, and approved changes to CMS as required by Title 1, Texas Administrative Code, Chapter 202. Specifically, of the 11 changes tested, 2 (18 percent) were appropriately documented, tested, and approved. However, the Office was unable to provide documentation for:

- 7 (64 percent) changes showing that they were requested and approved by management before development began.
- 4 (36 percent) changes showing that they were tested prior to being migrated into the production environment.

Office Information Systems Tested

The three information technology systems the Office used to manage its financial and Workers' Compensation processes were:

- **OAG Accounting System**, an Office of the Attorney General (OAG) application the Office used in accordance with the administrative services contract. The Office used that system to process its accounting transactions.
- **eTravel System**, a Salesforce-hosted application contracted by the OAG. The Office used that system to enter and approve travel requests and vouchers.
- **Workers' Compensation Claims Management System**, an application the Office owns and maintains but that is housed on the OAG's server and uses the OAG's enterprise database system. The Office used that system to process Workers' Compensation claims and associated payments.

Source: The Office.

⁶ The risk related to the issues discussed in Chapter 4 is rated as Medium because they present risks or results that if not addressed could moderately affect the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern and reduce risks to a more desirable level.

- 7 (64 percent) changes showing that they were reviewed and approved prior to being migrated to the production environment.

Implementing and enforcing a standardized, effective change management process would help the Office to ensure that changes to CMS do not unintentionally alter the data or promote weaknesses within the system.

User Access. The Office had restricted its user access to current employees whose jobs required access for the OAG Accounting and eTravel systems. However, the Office does not have a formal process to periodically review user access for CMS. As a result, four user accounts for CMS remained active after the users separated from the Office or other external entities that handled Workers' Compensation claims information. The Department of Information Resources' *Security Controls Standards* require state agencies to conduct periodic reviews of user access based on the agency's documented risk management decisions. Implementing effective user access controls helps to ensure that access to critical information systems is appropriately restricted to minimize the risk of unauthorized changes to data.

Recommendations

The Office should:

- Develop, document, and implement a change management policy and related procedures to help ensure that changes to its information systems comply with its change management policy.
- Develop, document, and implement a review of user access for its information systems, and conduct those reviews periodically based on the Office's documented risk management decisions for its key information systems.

Management's Response

A. *Develop, Document, and Implement an Information Systems Change Management Policy and Procedures*

The Office agrees with this recommendation, which has been substantially implemented by the Office's Information Technology (IT) Department. The target date for full implementation is December 31, 2018.

In December 2016, the Office's IT Department began to utilize Team Foundation Server (TFS) as a project management tool to describe, prioritize, and document IT projects. The IT Department is participating in a series of

meetings with stakeholders to develop written information systems change management policies and procedures.

B. Develop and Implement Information Systems User Access Review

The Office agrees with this recommendation, which has been substantially implemented by the Office's IT Department and the OAG Information Technology Services personnel. Written procedures will be developed, formalized, and implemented. The target date for full implementation is December 31, 2018.

The Office reviewed and verified all user access during the financial audit. The Office's IT Department in conjunction with OAG Information Technology Services personnel are researching options that will enhance the process currently used to provision and remove user access. The Office is also investigating possible enhancements to the process that model the Comptroller and LBB systems, which verify user access through periodic email update requests.

Appendices

Appendix 1

Objective, Scope, and Methodology

Objective

The objective of this audit was to determine whether the State Office of Risk Management (Office) has processes and related controls to help ensure that it administers financial transactions in accordance with applicable statutes, rules, and agency policies and procedures.

Scope

The audit scope included the Office's activities related to contracts in effect, Workers' Compensation claims, Workers' Compensation annual assessments calculated and collected, travel expenditures, and related information systems for fiscal year 2017 (September 1, 2016, through August 31, 2017) and the first five months of fiscal year 2018 (September 1, 2017, through January 31, 2018).

Methodology

The audit methodology included collecting information and documentation; interviewing Office staff regarding financial and operational processes; testing documentation related to contracts, travel expenditures, Workers' Compensation claims, and annual assessments; reviewing access to key financial and Workers' Compensation claims systems; and analyzing and evaluating the results of audit tests.

Data Reliability and Completeness

Auditors used Workers' Compensation accepted or denied claims and payment information from the Office's Claims Management System (CMS). To determine the reliability and completeness of the related claims and payment data, auditors (1) reviewed certain application and general controls, (2) observed the data extract and reviewed the query language used to produce the extract, and (3) performed a high-level review of data fields and their contents for appropriateness. In addition, auditors compared payment data for Workers' Compensation claims to information in the Uniform Statewide Accounting System (USAS).

Auditors used travel expenditure data from the Office of the Attorney General (OAG) accounting system. To determine the reliability and completeness of the expenditure data, auditors (1) relied on prior KPMG

audit work that tested general controls over the system, (2) observed the data extract and reviewed the parameters used to produce the extract, and (3) performed a high-level review of data fields and their contents for appropriateness. In addition, auditors compared the expenditure data to USAS.

Auditors analyzed annual assessment calculation and payment information in the Office's fiscal years 2017 and 2018 annual assessment calculation and payment spreadsheets. Auditors reviewed the related calculation and payment data for validity and completeness by comparing the spreadsheets to (1) self-reported data in third-party systems, (2) the Office's Workers' Compensation claims data in CMS, (3) Uniform Statewide Payroll/Personnel System data, and (4) USAS data.

In addition, auditors reviewed the Office's USAS user access and relied on prior State Auditor's Office audit work to determine data reliability.

Auditors determined that the data sets discussed above were sufficiently reliable for the purposes of the audit.

Auditors compared the Office's contract data, which was stored in a spreadsheet, to the contract information the Office reported to the Legislative Budget Board (LBB). Auditors identified discrepancies between the Office's list and the list it reported to the LBB. As a result of the discrepancies, the Office's contract data was of undetermined reliability for the purposes of this audit. However, that data contained the most complete population available to auditors during the course of the audit; therefore, auditors used it for testing.

Sampling Methodology

Auditors selected risk-based samples of travel vouchers and contracts for testing. The sample items generally were not representative of the populations; therefore, it would not be appropriate to project those test results to the populations.

Auditors selected nonstatistical samples of accepted Workers' Compensation claims and changes made to CMS primarily through random selection. In some cases, auditors selected additional sample items for testing based on risk. The sample items were not necessarily representative of the populations; therefore, it would not be appropriate to project the test results to the populations.

Auditors selected nonstatistical samples of denied Workers' Compensation claims and Workers' Compensation payments primarily through random selection designed to be representative of the populations. Test results may

be projected to the populations, but the accuracy of the projection cannot be measured.

Auditors selected a nonstatistical sample of agencies subject to the annual assessment primarily through random selection designed to be representative of the population and stratified by agency size. Test results may be projected to the population, but the accuracy of the projection cannot be measured.

Information collected and reviewed included the following:

- The Office's solicitation documentation, evaluation criteria and documentation, and related supporting documentation for selected contracts.
- The Office's interagency contracts with the OAG.
- The Office's expenditure data from the OAG Accounting System.
- The Office's expenditure and revenue data from USAS.
- Supporting documentation related to Workers' Compensation insurance assessment calculations.
- Supporting documentation related to travel expenditures.
- Supporting documentation for the Office's annual assessment calculation and receipt processes.
- User access data and supporting documentation related to the general controls and the application controls over the Office's financial process systems.

Procedures and tests conducted included the following:

- Interviewed Office staff to identify the Office's financial and operational processes, including financial and administrative internal controls.
- Tested documentation related to the Office's selected contracts to determine compliance with the *State of Texas Contract Management Guide* (version 1.12), state laws, and regulations.
- Tested the Office's interagency contracts with the OAG to determine whether the Office complied with the requirements in the General Appropriations Acts (84th and 85th Legislatures).

- Tested documentation related to the Office's Workers' Compensation claims and payments to determine compliance with the Office's policies and procedures and state laws and regulations.
- Tested documentation related to the Office's travel expenditures to determine compliance with the Office's policies and procedures and state laws and regulations.
- Tested documentation and calculations related to the Office's annual assessments.
- Tested documentation for annual assessment payments received to determine compliance with the Office's policies and procedures and state laws and regulations.
- Reviewed supporting documentation related to the general and application controls over the Office's financial process systems.
- Reviewed third-party reports on the suitability of design and operating effectiveness of controls over the OAG Accounting and eTravel systems.

Criteria used included the following:

- Texas Labor Code, Chapter 412.
- Title 28, Texas Administrative Code, Chapters 124 and 251.
- Texas Government Code, Chapters 771, 2261, and 2262.
- *State of Texas Contract Management Guide*, version 1.12.
- General Appropriations Acts (84th and 85th Legislatures).
- Legislative Budget Board contract reporting requirements.
- Department of Information Resources' *Security Control Standards Catalog*, version 1.3.

Project Information

Audit fieldwork was conducted from December 2017 through April 2018. 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.

The following members of the State Auditor's staff performed the audit:

- Steven Michael Summers, CPA, CISA, CFE (Project Manager)
- Jacqueline Thompson (Assistant Project Manager)
- Kirstin Adamcik
- Shaun Alvis, J.D.
- Adam Berry
- James Collins
- Annabella Rios
- Mary Ann Wise, CPA, CFE (Quality Control Reviewer)
- Cesar Saldivar, CFE, CGAP (Audit Manager)

Issue Rating Classifications and Descriptions

Auditors used professional judgement and rated the audit findings identified in this report. Those issue ratings are summarized in the report chapters/sub-chapters. The issue ratings were determined based on the degree of risk or effect of the findings in relation to the audit objective(s).

In determining the ratings of audit findings, auditors considered factors such as financial impact; potential failure to meet program/function objectives; noncompliance with state statute(s), rules, regulations, and other requirements or criteria; and the inadequacy of the design and/or operating effectiveness of internal controls. In addition, evidence of potential fraud, waste, or abuse; significant control environment issues; and little to no corrective action for issues previously identified could increase the ratings for audit findings. Auditors also identified and considered other factors when appropriate.

Table 2 provides a description of the issue ratings presented in this report.

Table 2

Summary of Issue Ratings	
Issue Rating	Description of Rating
Low	The audit identified strengths that support the audited entity's ability to administer the program(s)/function(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.
Medium	Issues identified present risks or effects that if not addressed could <u>moderately affect</u> the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern(s) and reduce risks to a more desirable level.
High	Issues identified present risks or effects that if not addressed could <u>substantially affect</u> the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern(s) and reduce risks to the audited entity.
Priority	Issues identified present risks or effects that if not addressed could <u>critically affect</u> the audited entity's ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern(s) and reduce risks to the audited entity.

Copies of this report have been distributed to the following:

Legislative Audit Committee

The Honorable Dan Patrick, Lieutenant Governor, Joint Chair
The Honorable Joe Straus III, Speaker of the House, Joint Chair
The Honorable Jane Nelson, Senate Finance Committee
The Honorable Robert Nichols, Member, Texas Senate
The Honorable John Zerwas, House Appropriations Committee
The Honorable Dennis Bonnen, House Ways and Means Committee

Office of the Governor

The Honorable Greg Abbott, Governor

State Office of Risk Management

Members of the State Office of Risk Management Board of Directors

Mr. Lloyd M. Garland, M. D., Board Chairman
Ms. Rosemary Gammon
Mr. Tomas Gonzalez
Mr. Gerald F. Ladner, Sr.
Judge John W. Youngblood
Mr. Stephen Vollbrecht, Executive Director and State Risk Manager



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