

Audit Report

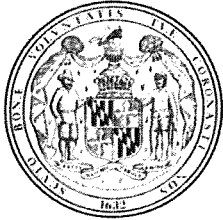
**Department of Labor, Licensing and Regulation
Division of Labor and Industry**

February 2012



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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Karl S. Aro
Executive Director

DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Bruce A. Myers, CPA
Legislative Auditor

February 1, 2012

Senator James C. Rosapepe, Co-Chair, Joint Audit Committee
Delegate Guy J. Guzzone, Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland

Ladies and Gentlemen:

We have audited the Department of Labor, Licensing and Regulation (DLLR) – Division of Labor and Industry (DLI) for the period beginning October 14, 2008 and ending May 30, 2011. DLI is responsible for safety inspections of boilers, elevators, amusement rides, and railroads. It also enforces certain protective labor laws and administers the Maryland Occupational Safety and Health Act.

Our audit disclosed that DLI continues to have a significant backlog of overdue inspections of boilers, pressure vessels, and elevators; however, the backlog has been reduced since our preceding audit. We have commented on this condition with respect to boilers and pressure vessels in each of our audit reports on DLI since 1977. In addition, comprehensive procedures were not in place to track the submission and review of certified payrolls from contractors required to pay prevailing wages under State law.

DLLR's response to this audit, on behalf of DLI, is included as an appendix to this report. We wish to acknowledge the cooperation extended to us during the course of this audit by DLI.

Respectfully submitted,

A handwritten signature in black ink that reads "Bruce A. Myers".

Bruce A. Myers, CPA
Legislative Auditor

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* Denotes item repeated in full or part from preceding audit report

Background Information

Agency Responsibilities

The Division of Labor and Industry (DLI) is a separate unit within the Department of Labor, Licensing and Regulation. The mission of DLI is to protect and promote the health, safety, and employment rights of Maryland's citizens. Specifically, DLI administers State laws that deal with employment issues, work-related safety and health issues, and prevailing wages, as well as safety inspections of amusement rides, boilers and pressure vessels, elevators, and railroads. According to the State's records, during fiscal year 2011, DLI had 199 authorized positions and operating expenditures totaling approximately \$16.6 million.

Status of Findings From Preceding Audit Report

Our audit included a review to determine the status of the four findings contained in our preceding audit report dated March 16, 2009. We determined that DLI satisfactorily addressed three of these findings. The remaining finding is repeated in this report.

Findings and Recommendations

Safety Inspections

Finding 1

Safety inspections for boilers, pressure vessels, and elevators were not performed timely in accordance with State law, although some improvement in reducing the backlog has been made to address this longstanding issue.

Analysis

According to the Division of Labor and Industry's (DLI) records, which we tested and found to be reliable, DLI did not perform safety inspections of boilers, pressure vessels, and elevators timely as required by State law. Specifically, as of June 6, 2011, inspections for 2,933 of the 52,939 boilers and pressure vessels were overdue for periods ranging from 3 months to more than 5 years. In addition, the inspections for 1,549 of 21,299 elevators were overdue for periods ranging from 3 months to 4 years.

DLI is responsible for ensuring the periodic inspection of boilers, pressure vessels, and elevators in accordance with Title 12 of the Public Safety Article of the Annotated Code of Maryland. This equipment is generally required to be inspected annually (certain boilers and pressure vessels are to be inspected bi-annually). Either DLI or authorized third-party entities, trained and certified by DLI, were responsible for conducting these inspections. The aforementioned overdue inspections are attributable to both parties.

In each of our audit reports since 1977, we have commented that DLI had not ensured that boilers and pressure vessels were inspected within the time periods specified by law. A similar condition regarding overdue elevator inspections has appeared in our audit reports since 1997. We have again been advised by DLI that inspections were not conducted in accordance with the aforementioned laws primarily because of staffing shortages. Nevertheless, DLI has been able to reduce the backlog noted in our prior report of 10,978 boilers and pressure vessels and 5,557 elevators. We were advised by DLI management that actions it had taken and certain law changes enacted since our prior audit have helped reduce the backlog.

Recommendation 1

We recommend that DLI

- a. eliminate its inspection backlog (repeat), and**
- b. maintain the inspection process on a current basis in accordance with the provisions of the law (repeat).**

Prevailing Wage

Finding 2

DLI had not established comprehensive procedures for tracking the submission and review of certified payrolls received from certain contractors to monitor compliance with the State's prevailing wages laws.

Analysis

DLI had not established comprehensive procedures for monitoring the receipt and review of required employer-prepared and certified payroll reports for certain public works projects. These reports were used by DLI to determine whether employers, who performed work on public works contracts exceeding \$500,000 for which 50 percent or more of the costs were paid with State funds, were complying with the State's prevailing wage laws.

Based on information submitted by procurement officers at State agencies, DLI initially determined whether projects were subject to the prevailing wage laws and, if so, specified the minimum wage rates to be paid on the projects for each job classification. During fiscal year 2011 (through May 30, 2011), DLI determined that projects with estimated costs totaling approximately \$772 million were subject to the State's prevailing wage laws.

Although DLI maintained a list of those projects, it had not established procedures to ensure that contractors and subcontractors on those projects submitted the required payroll reports for each pay period. Specifically, a comprehensive list of the contractors and subcontractors on each project was not maintained on a centralized basis. Furthermore, formal guidance was not established pertaining to the performance of the reviews, such as how many payrolls should be reviewed each week, the method for selecting payrolls (for example, a risk-based approach targeting contractors with higher error rates) and the method for documenting the review results. Rather, such decisions were made at the discretion of the three investigators who manually performed the reviews. According to DLI records, approximately 49,103 certified payroll reports were received during fiscal year 2011.

Our random selection of 12 employee wage payments from 10 contractors totaling \$10,714 under three open construction projects during the period July 2010 through May 2011 disclosed wage discrepancies for five employees (involving five contractors under two projects). According to the certified payrolls, these five employees were paid between 38 cents and \$6.80 less per hour than the prevailing wage rates, resulting in underpayments totaling \$101 for the applicable pay periods. DLI management was unaware of the discrepancies

because none of these certified payrolls had been selected for its review. Consequently, the wages were not adjusted by the contractors and fines for underpayment, as required by State law, had not been assessed against these contractors. Due to the lack of available records, DLI could not readily substantiate the extent of contracts reviewed by its investigators, but it estimated that the investigators reviewed about one-half of the payroll reports received each month.

Our test results suggest that reporting errors frequently occur. Many of those errors may not be detected due to the volume of payroll certifications received and the inability to manually review each payroll. Consequently, DLI should evaluate the cost-benefit of automating the submission and review of the certified payroll information to better ensure contractors and subcontractors are complying with the State prevailing wage laws.

State law regulates the hours of labor, rates of pay, conditions of employment, and obligations of employers under contracts and subcontracts for public works in Maryland. Contractors and subcontractors on State-funded construction projects covered by the law are required to submit self-certified payroll statements, indicating proper worker classification and wage for both straight time and overtime work for every pay period under their contracts. Under State law, employers found to be paying below the prevailing wage rate are required to make full restitution to the employee and can be fined \$20 per day for each worker paid less than the established rate. According to DLI, fines totaling \$390,000 were collected in fiscal year 2011. Legal remedies are available against contractors who fail to comply with the law.

Recommendation 2

We recommend that DLI

- a. establish records to centrally track the submission and review of certified payrolls from contractors required to pay prevailing wages,**
- b. establish procedures governing the selection and review of the payrolls using a risk-based approach,**
- c. investigate the aforementioned projects and take appropriate action, and**
- d. evaluate the cost-benefit of implementing automated processes for determining contractors' compliance with State prevailing wage laws.**

Cash Receipts

Finding 3

Cash receipts were not always deposited and verified in a timely manner.

Analysis

DLI did not always deposit cash receipts nor perform verifications of deposits in a timely manner. Our test of receipts collected on 20 days during fiscal years 2010 and 2011, totaling approximately \$552,067, disclosed that receipts from 7 days, totaling \$379,975, were not deposited for periods ranging from two to six business days after the dates of receipt. In addition, deposit verifications for 11 receipts totaling \$443,613 were not performed until 23 to 76 days after deposit; for 8 other receipts totaling \$95,104, there was no evidence that the collections were verified to deposit. We determined that the unverified receipts were deposited.

The Comptroller of Maryland's *Accounting Procedures Manual* requires that a reconciliation of recorded collections to amounts deposited be performed by an employee independent of the cash receipts functions. The *Manual* also requires that receipts be deposited no later than the first business day after receipt. Untimely deposits increase the possibility of loss or misappropriation and result in a loss of investment income to the State. According to DLI's records, cash receipts collected during fiscal year 2011 totaled approximately \$3.5 million.

Recommendation 3

We recommend that DLI comply with the *Accounting Procedures Manual* by

- a. depositing all cash receipts in a timely manner, and**
- b. performing timely verifications that all recorded collections were deposited.**

Audit Scope, Objectives, and Methodology

We have audited the Department of Labor, Licensing and Regulation (DLLR) – Division of Labor and Industry (DLI) for the period beginning October 14, 2008 and ending May 30, 2011. The audit was conducted 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.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine DLI's financial transactions, records and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations. We also determined the status of the findings contained in our preceding audit report.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of materiality and risk. The areas addressed by the audit included DLI's monitoring of compliance with certain laws pertaining to safety inspections (for boilers and pressure vessels, and elevators), living wages and prevailing wages, and its administration of the accounts receivable and cash receipts functions. Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of DLI's operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives. Data provided in this report for background or informational purposes were deemed reasonable, but were not independently verified.

Our audit did not include certain support services provided to DLI by the DLLR – Office of the Secretary. These support services (such as payroll, purchasing, maintenance of accounting records, and related fiscal functions) are included within the scope of our audit of the Office of the Secretary.

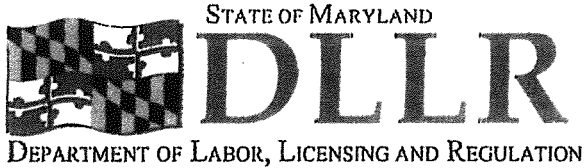
DLI's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless 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. Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect DLI's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our report also includes findings regarding significant instances of noncompliance with applicable laws, rules, or regulations. Another less significant finding was communicated to DLI that did not warrant inclusion in this report.

DLLR's response to our findings and recommendations, on behalf of DLI, is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise DLLR regarding the results of our review of its response.

APPENDIX



OFFICE OF THE SECRETARY
500 N. Calvert Street, 4th Floor
Baltimore, MD 21202

January 24, 2012

Mr. Bruce A. Myers, CPA
Legislative Auditor
Office of Legislative Audits
State Office Building, Room 1202
301 West Preston Street
Baltimore, Maryland 21201

RE: Department of Labor, Licensing and Regulation
Division of Labor and Industry
Response to Draft Legislative Audit Report
Dated January 2012

Dear Mr. Myers:

Enclosed you will find the Department of Labor, Licensing and Regulation's response to your draft report covering the examination of accounts and records of our Division of Labor and Industry. If you have any questions, please contact me or you may call Mr. Irby Cole, Director, Office of Budget and Fiscal Services at 410-230-6048.

Very truly yours,

A handwritten signature in black ink, appearing to read "Alexander M. Sanchez".

Alexander M. Sanchez
Secretary

cc: J. Ronald DeJuliis, Commissioner, Division of Labor and Industry – DLLR
Irby Cole, Director, Office of Budget and Fiscal Services – DLLR

Enclosure

AMS:ic

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MARTIN O'MALLEY, GOVERNOR • ANTHONY G. BROWN, LT. GOVERNOR • ALEXANDER M. SANCHEZ, SECRETARY

Audit Findings, Recommendations and DLI Response

Safety Inspections

Finding 1

Safety inspections for boilers, pressure vessels, and elevators were not performed timely in accordance with State law, although some improvement in reducing the backlog has been made to address this longstanding issue.

Recommendation 1

We recommend that DLI

- a. eliminate its inspection backlog (repeat), and
- b. maintain the inspection process on a current basis in accordance with the provisions of the law (repeat).

Agency Response

We concur. DLI is addressing the backlogs through legislative and policy modifications utilizing resources from the private sector to help reduce the backlog to realistic levels. DLI made significant progress over the past two years in reducing inspection backlogs and targeting resources towards safety compliance. The Commissioner initiated two plans; one for BPV and another for Elevators. These plans are providing positive results. Management staff continues to move forward by identifying new and more effective methods to leverage third-party inspection resources to decrease the population of overdue inspections. We are conducting physical inspections, and where equipment remains in operation without a certificate of inspection, posting notice prohibiting further operation. This physical inspection results in an inspection fee being charged to the owner for the inspection. Utilizing this method avoids invoking the entire citation appeal process that proved an unwanted time commitment by management and building owners.

DLI started implementing the inspection backlog plans in July, 2009, and since that time the Division has made significant progress in reducing the inspection backlog as indicated below:

Elevator Inspection Backlog

<u>Fiscal Year</u>		<u>Inspection Backlog</u>	<u>% Reduction</u>
FY-2010	July 09	6,000	
	June 10	3,452	43%
FY-2011	July 10	3452	
	June 11	1,715	50%
FY-2012	July 11	1,715	
	January	721	58%

- **Beginning inspection backlog = 28%**
- **Current inspection backlog = 3.6%**
- **Overall % backlog reduction = 88%**

Boiler & Pressure Vessel Inspection Backlog

<u>Fiscal Year</u>		<u>Inspection Backlog</u>	<u>% Reduction</u>
FY-2010	July 09	10,156	
	June 10	8,286	18%
FY-2011	July 10	8,286	
	June 11	3,375	59%
FY-12	July 11	3,375	
	January	1,817	46%

- **Beginning inspection backlog = 19%**
- **Current inspection backlog = 3.3%**
- **Overall % backlog reduction = 82%**

Prevailing Wage

Finding 2

DLI had not established comprehensive procedures for tracking the submission and review of certified payrolls received from certain contractors to monitor compliance with the State's prevailing wages laws.

Recommendation 2

We recommend that DLI

- a. establish records to centrally track the submission and review of certified payrolls from contractors required to pay prevailing wages,**
- b. establish procedures governing the selection and review of the payrolls using a risk-based approach,**
- c. investigate the aforementioned projects and take appropriate action, and**
- d. evaluate the cost-benefit of implementing automated processes for determining contractors' compliance with State prevailing wage laws.**

Agency Response

We concur. DLI is aware of the deficiencies associated with the annual review of approximately 50,000 certified payroll records. Our current process is obsolete at this volume, as the labor exceeds our staffing capabilities. DLI is in the process of investigating the aforementioned projects and will take appropriate action to ensure compliance. We will document the procedures, selection, and review with proper approvals.

The replacement system is designed by an internal DLLR design team. The first module of the system will focus on contractor input of payroll data in a web based application. The full application design features track projects and inspection activity; provide for inspection scheduling, determine and calculate late arrival of certified payroll records, determine if workers are being paid appropriate scale, and assess liquidated damages. Once project data is in the system, we are capable of targeting investigative resources to the more likely noncompliant (risk-based) projects, utilizing previous contractor history, project data and determinations, along with congruency of information on payroll records.

The payroll record module of the application is in testing time and is planned to be operational by March 31, 2012. Full functionality of the Prevailing Wage database system is anticipated by December 31, 2012.

Cash Receipts

Finding 3

Cash receipts were not always deposited and verified in a timely manner.

Recommendation 3

We recommend that DLI comply with the *Accounting Procedures Manual* by

- a. depositing all cash receipts in a timely manner, and
- b. performing timely verifications that all recorded collections were deposited.

Agency Response

We concur. This finding applied to DLI's Maryland Occupational Safety and Health (MOSH) unit. On January 19, 2012, MOSH implemented a Remote Deposit Program (RDP). In consideration of the need for separation of duties as it relates to the handling of checks while using this RDP, MOSH delegated the initial handling and receipt to an employee who is separate from the individual responsible for inputting the checks into the scanner and preparing the deposit log. The Office of the Assistant Commissioner for MOSH approves the daily deposit log once all checks are scanned for deposit. Appropriate staff was assigned as back-up to these functions should the assigned persons be unavailable to perform the task. Checks received by MOSH satellite offices (Hagerstown and Easton) will be mailed on the same day in which received; or, if received after 3:00 p.m. will be mailed on the following business day to the MOSH Hunt Valley office where they will be scanned and deposited.

DLI's Office of the Commissioner modified its verification schedule for all recorded deposits from monthly to weekly to satisfy the audit request and comply with the *Accounting Procedures Manual*.

AUDIT TEAM

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