

Audit Report

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**Subsequent Injury Fund**

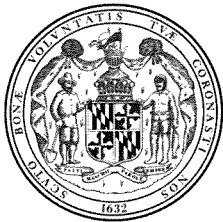
August 2014

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**OFFICE OF LEGISLATIVE AUDITS**  
DEPARTMENT OF LEGISLATIVE SERVICES  
MARYLAND GENERAL ASSEMBLY

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DEPARTMENT OF LEGISLATIVE SERVICES  
OFFICE OF LEGISLATIVE AUDITS  
MARYLAND GENERAL ASSEMBLY

August 8, 2014

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Executive Director

Thomas J. Barnickel III, CPA  
Legislative Auditor

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 conducted a fiscal compliance audit of the Subsequent Injury Fund (SIF) for the period beginning January 5, 2011 and ending October 28, 2013. SIF pays workers' compensation awards in connection with certain claims for employees' subsequent occupational injuries or deaths, and collects assessments from certain employers and insurance companies to fund these awards.

Our audit disclosed that SIF's procedures were not sufficiently comprehensive to ensure that claim payments made for injured persons were proper and that assessments were properly billed and collected. Claim payments were not independently reviewed for propriety and SIF did not always pursue recovery of payments erroneously disbursed to injured persons after their deaths. In addition, accounts receivable established for assessments to employers and insurers were not independently reviewed, and delinquent assessment accounts were not always properly pursued for collection and routinely referred to the Department of Budget and Management's Central Collection Unit. Furthermore, SIF did not properly separate the responsibilities for billing assessments and processing the related collections. Finally, sufficient password controls were not in place over the related systems, and sensitive personally identifiable information was not adequately protected.

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

Respectfully submitted,

Thomas J. Barnickel III, CPA  
Legislative Auditor



## Table of Contents

<b>Background Information</b>	4
Agency Responsibilities and Financial Activity	4
Status of Findings From Preceding Audit Report	5
<b>Findings and Recommendations</b>	6
<b>Claim Payments</b>	
*    Finding 1 – Claim Payments Were Not Independently Reviewed for Validity and Accuracy	6
Finding 2 – Payments Improperly Disbursed to Deceased Individuals Were Not Always Pursued For Recovery	6
<b>Assessment Billings and Collections</b>	
*    Finding 3 – SIF Did Not Conduct Independent Reviews of Critical Assessment Account Transactions	7
Finding 4 – Timely Action Was Not Always Taken to Collect Delinquent Accounts	8
<b>Information Systems Security and Control</b>	
Finding 5 – Controls Were Not Sufficient Over Passwords and Personally Identifiable Information	9
<b>Audit Scope, Objectives, and Methodology</b>	11
<b>Agency Response</b>	Appendix

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

## **Background Information**

### **Agency Responsibilities and Financial Activity**

The purpose of the Subsequent Injury Fund (SIF) is to encourage the employment of individuals with pre-existing health conditions by limiting an employer's liability should a subsequent occupational injury render an individual permanently disabled or result in the individual's death. The employer's liability is limited to compensation for damages from the current injury. SIF incurs the liability associated with the combined effects of all injuries.

The principal source of funding for claim payments and SIF's operating expenses is assessments collected for each award against an employer or its insurer for permanent disability or death and each amount payable by an employer or insurer under a settlement agreement approved by the Workers' Compensation Commission. SIF calculates these assessments, which are currently 6.5 percent of the aforementioned award amounts.

According to State records, during fiscal year 2013, assessment collections totaled approximately \$28.8 million, claim payments totaled approximately \$23.9 million, and operating expenses totaled approximately \$2.1 million; SIF's fund balance as of June 30, 2013, totaled approximately \$80.2 million. Claim obligations are funded on a pay-as-you-go basis, so as obligations become due in future periods, the obligations will have to be paid from future assessments collected from employers and insurance companies. In this regard, SIF's most recent actuarial study performed in June 2011 indicated that, at that time, SIF had an unfunded liability for permanent injury and death claims of approximately \$254.0 million (discounted at four percent). This amount represents a 26 percent increase from the previous actuarial study performed in November 2003. A September 8, 1992 advice of the Attorney General concluded that, should fund awards ever exceed the amount of monies in the SIF, the State would not be liable to appropriate its own funds to pay claims.

During our preceding audit, SIF provided certain support services (including processing invoices and payroll, processing collections for deposit, maintaining accounting records, and data processing services) to the Uninsured Employers' Fund (UEF). In accordance with certain established milestones detailed in a separation plan approved by the Department of Budget and Management and the Executive Directors for both SIF and UEF, effective November 1, 2011, SIF discontinued providing support services for UEF. Accordingly, the scope of our

audit included support service activities provided to UEF for the period from January 5, 2011 to October 31, 2011.

### **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 September 21, 2011. We determined that SIF satisfactorily addressed two of the findings. The remaining two findings are repeated in this report.

## Findings and Recommendations

### Claim Payments

#### **Finding 1**

**Claim payments were not independently reviewed for validity and accuracy.**

#### **Analysis**

The employee responsible for reviewing claim payments recorded in the Subsequent Injury Fund's (SIF) accounts payable system was not independent from the payment process. Although this employee reviewed supporting documentation to ensure the payments were valid and accurate, this employee had the capability to modify payment records in the accounts payable system and to approve the payments in the State's accounting system. As a result, unauthorized payments could be issued and not readily detected by SIF.

Claim payments were made for injured persons either as a lump sum or as recurring payments. Recurring biweekly payments are made indefinitely for the life of the injured person. A recurring payment is initially entered into the accounts payable system by an SIF accounting employee who enters the dollar amount of the payments and a fixed payment period (such as 100 weeks). When this fixed period ends, the accounting employee manually enters the amount due for the next period in order to prompt a manual review on a periodic basis. A similar condition was commented upon in our preceding audit report. According to SIF's records, claim payments processed by SIF during fiscal year 2013 totaled approximately \$23.9 million.

#### **Recommendation 1**

**We recommend that the employee reviewing the claim payments for propriety be independent of the payment process (repeat). We advised SIF on accomplishing the necessary separation of duties using existing personnel.**

#### **Finding 2**

**SIF did not always pursue recovery of payments improperly disbursed to deceased individuals.**

#### **Analysis**

SIF did not always pursue recovery of payments improperly disbursed to injured persons after death. SIF submits a monthly social security number query to the

U.S. Social Security Administration (SSA) to match its records of injured persons receiving (or scheduled to receive) claim payments with the death records of SSA. During the period from November 2011 to October 2013, these matches identified 32 deceased persons who were receiving payments from SIF. Our test of 15 of these cases disclosed payments totaling approximately \$22,300 were made after the individuals' reported dates of death. SIF did not actively pursue recovery of cashed payment checks totaling approximately \$16,000 for 7 individuals. According to SIF management, it was aware of these payments; however, follow-up actions were not initiated due to limited resources.

In accordance with the Labor and Employment Article of the Annotated Code of Maryland, SIF is not obligated to pay any claims after the death of the beneficiary.

## **Recommendation 2**

**We recommend that SIF**

- a. investigate the results of the monthly death matches and take appropriate follow-up actions (such as actively pursue recovery of funds in a timely manner); and**
- b. confer with the Office of the Attorney General – Criminal Division to determine what action, if any, should be taken against individuals who inappropriately cashed checks, including those identified by our tests.**

## **Assessment Billings and Collections**

### **Finding 3**

**SIF did not conduct independent reviews of the establishment of assessment accounts and adjustments to those accounts. Additionally, SIF did not properly separate the responsibilities for billing assessments and processing the related collections.**

### **Analysis**

SIF did not conduct independent reviews of the establishment of assessment accounts and any adjustments to these accounts. Additionally, SIF did not properly separate the responsibilities for billing assessments and processing the related collections. SIF records awards and settlement agreement amounts on its accounts receivable system, which automatically calculates the assessment amounts. SIF generates billings to employers and insurance companies based on these assessments.

- In March 2013, SIF stopped performing independent verifications to ensure the accuracy of Workers' Compensation Commission (WCC) awards entered in SIF's accounts receivable system. We were advised these reviews were discontinued due to limited staff resources. A similar condition was commented upon in our two preceding audit reports. According to SIF's records, during the period from April 2013 to December 2013, accounts receivable for WCC award assessments totaled approximately \$19.0 million.
- Adjustments to the accounts receivable records were not subject to independent review and approval. The employee who maintained the accounts receivable records also processed adjustments to the accounts receivable records without any oversight. Furthermore, this employee was also responsible for processing assessment collections. As a result, funds could be misappropriated without being readily detected. A similar comment regarding the need for an independent verification of the propriety of adjustments was commented upon in our three preceding reports. According to SIF' records, net adjustments totaled approximately \$2.2 million during fiscal year 2013.

### **Recommendation 3**

#### **We recommend that SIF**

- establish independent reviews, at least on a test basis, to ensure that WCC awards are accurately entered into the accounts receivable records and only properly authorized adjustments are recorded in the accounts receivable records (repeat), and**
- ensure that the assessment collection and accounts receivable functions are properly separated. We advised SIF on accomplishing the necessary separation of duties using existing personnel.**

#### **Finding 4**

**SIF did not always take timely action to collect delinquent assessment accounts.**

#### **Analysis**

Timely action was not always taken to pursue collection of delinquent assessment accounts. Although SIF had a significant number of delinquent assessment accounts, it did not consistently make monthly written demands for payment and generally did not refer delinquent assessments accounts to the Department of Budget and Management's Central Collection Unit (CCU). Specifically, no accounts were referred to CCU in fiscal year 2012 and only one delinquent account was referred in fiscal year 2013. As of December 31, 2013, according to

SIF's records, there were 1,891 assessment accounts receivable totaled approximately \$3.1 million, of which 720 of these accounts had balances totaling \$1.3 million that were older than 90 days.

Our test of ten delinquent assessment accounts totaling approximately \$209,000, which had not been referred to CCU as of November 2013, disclosed that SIF did not properly pursue collection for six accounts totaling approximately \$121,600. Specifically, written demands for payment were not made every 30 days, as required for four accounts and no written demands for payment were made for two accounts. The delays in issuing written demands ranged from 60 to 330 days from the date of the prior notice. Delays in the pursuit of outstanding debts may decrease the likelihood of collecting the funds.

State regulations generally require that three written demands for payment be made on accounts at 30-day intervals and, if no payments are received, the accounts be considered delinquent and immediately referred to CCU for collection assistance.

#### **Recommendation 4**

**We recommend that written demands for payment be made at 30-day intervals and that all delinquent accounts be referred to CCU for collection assistance, as required.**

## **Information Systems Security and Control**

### **Finding 5**

**Controls were not sufficient over passwords and sensitive personally identifiable information (PII).**

#### **Analysis**

Password controls and controls over claimants' sensitive personal identifiable information were not sufficient. We noted the following conditions:

- SIF did not fully use the available capabilities in its accounts receivable and accounts payable application with respect to enforcing password age, length, complexity, and history. This was not in accordance with the password provisions of the Department of Information Technology's (DoIT) *Information Security Policy*.

- The database used to record claims information contained unencrypted sensitive personally identifiable information (PII). Specifically, as of January 9, 2014, we determined that this database contained 636,651 unique social security numbers with associated names and dates of birth in clear text. Furthermore, eight active accounts (used by eight individuals) had unnecessary read access to the aforementioned social security numbers in this database. This sensitive PII, which is commonly sought by criminals for use in identity theft, should be protected by appropriate information system security controls. Also, DoIT's *Information Security Policy* requires that confidential information be protected with administrative, technical, and physical safeguards to ensure its confidentiality, integrity, and availability and to prevent unauthorized or inappropriate access, use, or disclosure.

### **Recommendation 5**

#### **We recommend that SIF**

- a. enforce the available password controls that are in accordance with the provisions of the DoIT's *Information Security Policy*,**
- b. encrypt sensitive PII in its database, and**
- c. ensure that read access to sensitive PII is restricted to only personnel who require such access for their job responsibilities.**

## **Audit Scope, Objectives, and Methodology**

We have conducted a fiscal compliance audit of the Subsequent Injury Fund (SIF) for the period beginning January 5, 2011 and ending October 28, 2013. 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 SIF's financial transactions, records and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of significance and risk. The areas addressed by the audit included assessment collections, assessment billings, claim payments, and information systems security and control. We also determined the status of the findings contained in our preceding audit report.

To accomplish our audit objectives, our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of SIF's operations and test of transactions. We also performed various data extracts of pertinent information from the State's Financial Management Information System (such as revenue and expenditure data). The extracts are performed as part of ongoing internal processes established by the Office of Legislative Audits and were subject to various tests to determine data reliability. We determined that the data extracted from this source were sufficiently reliable for the purposes the data were used during this audit. We also extracted data from SIF's automated accounts receivable and accounts payable system for the purpose of testing assessment accounts receivable and claim payment monitoring. We performed various tests of the relevant data and determined that the data were sufficiently reliable for the purposes the data were used during the audit. Finally, we performed other auditing procedures that we considered necessary to achieve our audit objectives. The reliability of data used in this report for background or informational purposes was not assessed.

SIF'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 findings relating to conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect SIF'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. Other less significant findings were communicated to SIF that did not warrant inclusion in this report.

SIF's response to our findings and recommendations 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 SIF regarding the results of our review of its response.



MARTIN O'MALLEY  
Governor

JOHN L. ULRICH, JR.  
Director

JENNIFER ROWE  
Fiscal Administrator

MARK MONDOR  
Information Technology  
Director

**Subsequent Injury Fund  
Responses to DRAFT Audit Report**

**Audit Period: January 5, 2011 to October 28, 2013  
Findings and Recommendations**

**Claim Payments**

**Finding 1**

**Claim payments were not independently reviewed for validity and accuracy.**

*Recommendation 1*

*We recommend that the employee reviewing the claim payments for propriety be independent of the payment process (repeat). We advised SIF on accomplishing the necessary separation of duties using existing personnel.*

**SIF Response 1**

**SIF concurs and as of February 12, 2014 SIF has been in compliance with OLA's Recommendation. An independent review of all weekly non-recurring payments, recurring payment account payment setup requests, and recurring payment removal requests are verified for accuracy and validity. In addition, SIF has reinstated the use of the bi-weekly reconciliation summary sheets to independently review recurring benefit payments (on a test basis) to ensure payments are valid and accurate.**

**Finding 2**

**SIF did not always pursue recovery of payments improperly disbursed to deceased individuals.**

*Recommendation 2*

*We recommend that SIF*

- a. investigate the results of the monthly death matches and take appropriate follow-up actions (such as actively pursue recovery of funds in a timely manner); and*

## Subsequent Injury Fund

### Responses to DRAFT Audit Report

- b. *confer with the Office of the Attorney General – Criminal Division to determine what action, if any, should be taken against individuals who inappropriately cashed checks, including those identified by our tests.*

#### **SIF Response 2**

- a. **SIF agrees with OLA’s recommendations. Current practice once notified of claimant’s death is to immediately cease further payments and recover any outstanding payments that have not been presented for payment. SIF will actively pursue recovery of funds disbursed to deceased beneficiaries in a timely manner; and**
- b. **Further pursuit to recover improper payments made to deceased beneficiaries will be pursued diligently including referral to the Attorney General - Criminal Division when appropriate.**

#### **Assessment Billings and Collections**

##### **Finding 3**

**SIF did not conduct independent reviews of the establishment of assessment accounts and adjustments to those accounts. Additionally, SIF did not properly separate the responsibilities for billing assessments and processing the related collections.**

##### *Recommendation 3*

*We recommend that SIF*

- a. *establish independent reviews, at least on a test basis, to ensure that WCC awards are accurately entered into the accounts receivable records and only properly authorized adjustments are recorded in the accounts receivable records (repeat), and*
- b. *ensure that the assessment collection and accounts receivable functions are properly separated. We advised SIF on accomplishing the necessary separation of duties using existing personnel.*

#### **SIF Response 3**

- a. **SIF concurs and will conduct independent reviews, on a test basis, to ensure that WCC awards are accurately entered into the accounts receivable records and only properly authorized adjustments are recorded into the accounts receivable records. Tested assessments and adjustments will be marked ‘reviewed’ date/time stamped by reviewer in QuickBooks.**
- b. **SIF concurs and is in the process of complying with OLA’s recommendation to separate all accounts receivable functions now that the third fiscal position has been filled and becoming fully functional.**

Subsequent Injury Fund  
Responses to DRAFT Audit Report

**Finding 4**

**SIF did not always take timely action to collect delinquent assessment accounts.**

*Recommendation 4*

*We recommend that written demands for payment be made at 30-day intervals and that all delinquent accounts be referred to CCU for collection assistance, as required.*

**SIF Response 4**

**SIF concurs and will comply with OLA's Recommendation to pursue accounts for collection in accordance with State regulations.**

**Information Systems Security and Control**

**Finding 5**

**Controls were not sufficient over passwords and sensitive personally identifiable information (PII).**

*Recommendation 5*

*We recommend that SIF*

- a. enforce the available password controls that are in accordance with the provisions of the DoIT's Information Security Policy,*
- b. encrypt sensitive PII in its database, and*
- c. ensure that read access to sensitive PII is restricted to only personnel who require such access for their job responsibilities.*

**SIF Response 5**

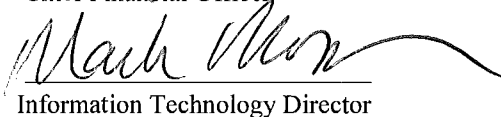
- a. SIF agrees. On 4/18/14 SIF enabled the highest level of password controls available in the application which is PCI DSS level protection.**
- b. SIF agrees, and on 2/12/14 SIF implemented a revised database and application that encrypts and decrypts the SSN both at rest and in transit to state and federal encryption standards.**
- c. SIF agrees. The version implemented 2/12/14 provides a masked version only of the SSN in tabular form to all users and in the detail level to personnel without a specific need.**

  
Agency Director

August 5, 2014  
Date

  
Chief Financial Officer

August 5, 2014  
Date

  
Information Technology Director

August 5, 2014  
Date

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