



INFORMATIONAL DOCUMENT FOR AUDIT COMMITTEE

Completed Closed Audits

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2011 MAR (Model Audit Rule) PAO 621

Objective/Scope

IAD was to review and test key controls, as identified by the MAR Compliance Unit, for the 2011 reporting requirements in compliance with the NAIC Model Audit Rule for financial reporting.

Methodology

Audit methodology included: 1. control walk-through and documentation; 2. control testing and identifications of deficiencies; 3. to provide advisory services regarding test plans, test results, and the remediation of controls deficiencies.

Finding:

1. Completed all assigned test plans and provided reported results to MAR Compliance Team. IAD provided 2800 hours of audit support.

Remediation: N/A

Proprietary: No

Payroll Audit PAO 637

Objective/Scope

IAD evaluated controls over payroll audit areas involving: audit review; audit selection and overrides; detecting and reporting premium fraud; field audit procedures; timeliness of audit completion and operating metrics. Reviewed policy related data for January through November 2011.

Methodology

Evaluate payroll auditing procedures, processes, roles and responsibilities, operating metrics, and recordkeeping, which ensure the consistency and adequacy of payroll auditing activities. IAD conducted compliance tests on physical audits and on policy review visits. Evaluated timeliness and process changes created by RIF.

Findings:

1. Physical audits are not completed and reviewed in a timely manner.
2. Delays to request causal cancellation (CQ) for failure to allow an audit.
3. Training in detection of premium fraud needs improvement.
4. Audit Binder reports for measuring audit resource use and effectiveness need improvements so management can prioritize policies to be audited.
5. Audit review processes and procedures for Assistant Audit Managers (AAM) needed to ensure consistency and quality of payroll audits.
6. Current procedures to waive a mandatory audit request do not take into consideration the industry risks of the policy.
7. Procedure in field auditing process is not clear: when a site inspection is required, when an auditor should speak to the insured, and what documentation is required for site inspection and contact with policyholder.
8. Policy Review Visits not performed on new policies, timely and consistently.

Remediation:

1. Field Operations has improved the audit cycle time, from policy identification to billing. Along with this, process controls, enhanced performance metric measurement and reports have been created. Finding remediated May 2012.
2. New cancellation process being created for policies that refuse an audit. Field Audit process completed Q3 and Virtual Audit process will be completed by Q4 2012.
3. Training program will be developed and implemented by Q4 2012.
4. Premium Audit Services is developing the capability to risk rank policies and to match premium audit risk with how the audit is performed. Target Q4 2012.
5. Formal procedures for audit review being developed. Implemented by Q3, 2012.
6. Field Operations has developed specific criteria to be used to support the waving of an audit. Completed May 2012.
7. Field Operations is developing business processes, the virtual audit, that will use access to EDD and FTB records to provide efficient collaboration of payroll records. Target Q4 2012.
8. SQE Tiers and Pre-coverage questionnaires reduce the need/value of this business investment. Topic will be reviewed and evaluated Q4 2012.

Proprietary: No

Dividend Payment Implementation Process PAO 676

Objective/Scope

Assess the procedures and controls, which are in place, to ensure that the objectives of the dividend payment process are met. Including:

- Verify the policies selection criteria for dividends.
- Verify that the appropriate dividend amount is assigned to qualifying policies.
- Assess the dividend exception process and identify control gaps.
- Review Dividend Results Disclosure Statements (DRDS), process and contents.

Methodology

- Reviewed Dividend Implementation Project documents and supporting material.
- Reviewed data from IT and verified accuracy on State Fund Online (SFO).
- Observed user acceptance testing (UAT) performed by the dividend project team.
- Performed an independent recalculation for dividend selection process.

Findings:

1. The Dividend Exception Selection Process lacks clarity in terms of authority, timelines, and documentation; and does not include a method to track exceptions.
2. The Dividend Disclosure Results Statement (DRDS) is misleading. The DRDS indicates that if a policy that does not complete the final audit within 18 months of inception, it will not be eligible for a dividend. The automated dividend selection process allows for these policies to be included in catch-up runs for dividend payment.
3. A notice sent to policyholders near policy inception indicates that for participating policies, the dividend calculation that will be based on a percentage of the 'earned' premium, which conflicts with DRDS.

Remediation: N/A

1. Billing and Collections has updated the Dividend Exception process to corrected noted weaknesses. Working with IT to produce an exception tracking report. Q3 2012.
2. The SFO screens were designed to elaborate on the explanation of ineligibility which the broker and State Fund employees have access too. Training was provided to State Fund Employees. Remediated. IA will verify.
3. For those policyholders that receive a dividend payment prior to the issuance of the new DRDS, they will receive a supplemental letter that explains the paid dividend as a percentage of earned premium.

Proprietary: No