



STATE OF ILLINOIS  
**OFFICE OF THE  
 AUDITOR GENERAL**

William G. Holland, Auditor General

**SUMMARY REPORT DIGEST**

**DEPARTMENT OF INSURANCE**

Compliance Examination  
 For the Two Years Ended June 30, 2014

Release Date: March 26, 2015

FINDINGS THIS AUDIT: 9				AGING SCHEDULE OF REPEATED FINDINGS			
	New	Repeat	Total	Repeated Since	Category 1	Category 2	Category 3
<b>Category 1:</b>	<b>0</b>	<b>0</b>	<b>0</b>	2012		14-1, 14-2, 14-5	
Category 2:	4	5	9	2010		14-3*, 14-4	
Category 3:	<u>0</u>	<u>0</u>	<u>0</u>				
<b>TOTAL</b>	<b>4</b>	<b>5</b>	<b>9</b>				
<b>FINDINGS LAST AUDIT: 10</b>							

\*Prior to becoming a separate agency, issues associated with this finding had been previously reported in the Department of Financial and Professional Regulation's reports back to 2006.

**SYNOPSIS**

- (14-1) The Department did not fully comply with the requirements of the Workers' Compensation Act.
- (14-2) The Department did not fully comply with the requirements of the Illinois Pension Code.
- (14-5) The Department did not have proper segregation of duties over processing of insurance privilege tax refunds.
- (14-8) The procurement of the Illinois Health Insurance Marketplace marketing and outreach campaign had several issues during the scoring of the proposals.
- (14-9) The Department did not exercise adequate controls over expenditures for the contract of the Illinois Health Insurance Marketplace marketing and outreach campaign.

**Category 1:** Findings that are **material weaknesses** in internal control and/or a **qualification** on compliance with State laws and regulations (material noncompliance).

**Category 2:** Findings that are **significant deficiencies** in internal control and **noncompliance** with State laws and regulations.

**Category 3:** Findings that have **no internal control issues but are in noncompliance** with State laws and regulations.

{Expenditures and Activity Measures are summarized on next page.}

**DEPARTMENT OF INSURANCE  
COMPLIANCE EXAMINATION  
For the Two Years Ended June 30, 2014**

EXPENDITURE STATISTICS	FY 2014	FY 2013	FY 2012
<b>Total Expenditures.....</b>	<b>\$ 83,661,422</b>	<b>\$ 48,030,772</b>	<b>\$ 42,113,703</b>
OPERATIONS TOTAL.....	\$ 81,337,479	\$ 45,956,693	\$ 39,306,232
% of Total Expenditures.....	97.2%	95.7%	93.3%
Personal Services.....	20,797,817	19,183,102	20,020,641
Other Payroll Costs (FICA, Retirement, Insurance)	15,108,955	14,053,381	12,616,566
Contractual Services.....	44,559,787	11,839,750	5,267,088
Telecommunications.....	490,639	413,697	446,771
Transfers.....	-	-	483,241
All Other Operating Expenditures.....	380,281	466,763	471,925
AWARDS AND GRANTS.....	254,299	753,298	1,179,552
% of Total Expenditures.....	0.3%	1.6%	2.8%
REFUNDS.....	\$ 2,069,644	\$ 1,320,781	\$ 1,627,919
% of Total Expenditures.....	2.5%	2.7%	3.9%
<b>Total Receipts.....</b>	<b>\$ 471,708,458</b>	<b>\$ 451,189,184</b>	<b>\$ 453,009,821</b>
<b>Average Number of Employees (not examined).....</b>	<b>255</b>	<b>250</b>	<b>263</b>
SELECTED ACTIVITY MEASURES (not examined)	2014	2013	2012
<b>Consumer Market Division</b>			
New/Renewal Licenses Processed	89,563	88,588	112,486
Market Conduct Examinations completed	46	32	19
Closed Consumer Complaint Files	8,965	7,715	8,788
<b>Financial-Corporate Regulatory Division</b>			
Financial Statement Analysis Annual	357	362	369
Field Financial Examinations	119	62	71
Pension Fund Examinations completed	71	76	89
AGENCY DIRECTOR			
During Examination Period: Andrew Boron (through 1-11-2015), James Stephens, Acting (beginning 1-12-2015)			
Currently: James Stephens, Acting			

**FINDINGS, CONCLUSIONS, AND  
RECOMMENDATIONS**

**NONCOMPLIANCE WITH THE REQUIREMENTS OF  
THE WORKERS' COMPENSATION ACT**

**Failure to implement a system for  
the detection and prevention of  
fraud, waste, and abuse**

The Workers' Compensation Fraud Unit has not procured and implemented a system utilizing advanced analytics inclusive of predictive modeling, data mining, social network analysis, and scoring algorithms for the detection and prevention of fraud, waste, and abuse.

**Documentation retention policy  
needs to be established**

In addition, the Department has not established a document retention policy regarding reports of workers' compensation fraud specifically requiring the Department to destroy any investigations that are not referred for prosecution upon the expiration of the statute of limitations for the acts under investigation.

The Workers' Compensation Act (Act) requires the fraud and insurance non-compliance unit to procure and implement a system utilizing advanced analytics inclusive of predictive modeling, data mining, social network analysis, and scoring algorithms for the detection and prevention of fraud, waste, and abuse on or before January 1, 2012.

The Act also requires that investigations that are not referred for prosecution shall be destroyed upon the expiration of the statute of limitations for the acts under investigation and shall not be disclosed except that the person making the report shall be notified that the investigation is being closed.

Department management stated that no system for the detection and prevention of fraud waste and abuse has been procured due to the following: (1) no appropriation has been made specifically for this purpose, (2) the Department did not have data regarding individual claims, and (3) the Act did not contemplate available, accurate data for use with such a system. The failure to establish a document retention policy is due to oversight. (Finding 1, pages 11-12)

We recommended the Department (1) either procure and implement a system utilizing advanced analytics or seek a legislative change, and (2) establish procedures and develop a document retention policy related to workers' compensation investigations for submission with the State Records Commission to ensure compliance with the Act.

**Department concurred with the  
recommendation**

The Department concurred with this finding. The Department issued a Request for Information (RFI) regarding a system utilizing advanced analytics inclusive of predictive modeling, data mining, social network analysis, and scoring algorithms for the detection and prevention of fraud, waste, and abuse

(advanced analytics system) in 2012. The responses to the RFI did not assist the Department in procuring the advanced analytics system. The Department is again analyzing the viability of such a system given the near complete lack of information available to the Department for analysis by such an advanced analytics system. Moreover, the Department has recommended in the Workers' Compensation Fraud Unit's 2013 and 2014 Annual Reports that were submitted to the Governor, General Assembly, Attorney General, and others, that the advanced analytics system requirement be removed from Section 25.5(e-5) of the Illinois Workers' Compensation Act.

The Department is currently working with the Secretary of State Archives Division to establish an approved records retention policy that complies with Section 25.5(e) of the Illinois Workers' Compensation Act.

### **NONCOMPLIANCE WITH THE REQUIREMENTS OF THE ILLINOIS PENSION CODE**

During testing, auditors noted the Public Pension Division did not perform required examinations of the 657 police and firefighters pension funds that are required to be examined once every three years. As a result of testing auditors noted:

- 128 (19%) have been examined on two occasions since 2004. The second examination occurred between 4 and 10 years after the first examination.
- 480 (73%) have been examined on one occasion since 2004.
- 23 (4%) pension funds were currently under examination as of the audit period. Twenty-two of the 23 were second examinations since 2004.
- 18 (3%) pension funds eligible for an examination have never been examined. The 18 pension funds were formed between 2007 and June 30, 2011.

**Required examinations of police and firefighter pensions not performed as required**

Failure to perform the required examination of a pension fund every three years results in the Department not being able to fully monitor that pension funds are in compliance with the Code. (Finding 2, pages 13-14)

We recommended the Department allocate sufficient resources to perform the pension fund examinations every three years as required by the Pension Code.

**Department concurred with the recommendation**

The Department concurred with the finding and will continue to seek legislation to either provide the resources needed to fully implement the three year compliance audit cycle or to modify the examination requirement as contained in 40 ILCS 5/1A-104(b).

## **LACK OF SEGREGATION OF DUTIES OVER PROCESSING OF INSURANCE PRIVILEGE TAX REFUNDS**

### **Lack of segregation of duties identified in processing refunds**

During testing of 23 vouchers representing insurance privilege tax refunds, auditors noted there is only one employee who: 1) receives the requests for insurance privilege tax refunds, 2) reviews and prepares the refund authorization memo, and 3) approves the refund for payment. The same employee also maintains and updates the Department records on insurance privilege taxes. The individual amounts of insurance privilege tax refunds vouchers tested during the current examination ranged from \$6,753 to \$250,000.

Department management stated a new staff person added to process the privilege tax refunds was not informed of the additional approval levels during their training for the position. (Finding 5, pages 19-20)

We recommended the Department ensure there is proper segregation of duties by allocating sufficient staff to process, review, approve and record tax refunds.

### **Department concurred with the recommendation**

The Department concurred with this finding and the recommendation regarding the segregation of duties and has implemented an additional level of approval authority to the privilege tax refund process.

## **ISSUES DURING SCORING OF PROPOSALS**

### **Issues with scoring proposals for the Illinois Health Insurance Marketplace marketing and outreach campaign**

In April 2013, the Department issued a Request for Proposals for the Illinois Health Insurance Marketplace marketing and outreach campaign. Proposals were opened May 8, 2013 and there were 12 responsive proposers. A five-person evaluation team scored the technical proposals, which included the written proposals and oral presentations, while a sixth individual conducted reference checks. The \$33 million contract was awarded in July 2013.

During testing of the procurement, auditors found several issues with the scoring of the proposals. Specifically the auditors noted the following:

### **Evaluation committee meeting member attendance not documented**

- Evaluation committee meetings – The procurement file did not contain adequate documentation of who attended evaluation committee meetings. The procurement file did not document attendance. Documenting evaluation committee meetings would provide evidence that committee members complied with the Department’s requirement that members attend all evaluation committee meetings.

- Reference checks – Reference checks were not completed for six of 11 vendors because references failed to respond when contacted. (One of the 12 vendors did not provide references.) Each vendor was required to provide four references.

**Reference checks were not completed for six of 11 vendors because references failed to respond when contacted**

While proposals were opened May 8, 2013, reference checks did not begin until May 28. Because of the late start date and the timing of vendor presentations, reference checks were only given one week for completion.

In six instances, reference checks for all four of a vendor's references were unable to be completed. For one vendor, only one of the vendor's four reference checks was completed. There were notes in the file indicating that contact was attempted for the incomplete reference checks but the notes were not always conclusive. Vendors were penalized when the Department was unable to complete the reference checks.

**Five of the 12 scoring summaries contained minor errors**

- Scoring tabulation – Five of the 12 scoring summaries contained minor errors in tabulating the scoring of technical proposals. While none of the errors had a material effect on the final rankings or on other decisions to eliminate vendors, the failure to detect the errors is indicative of a breakdown in the internal controls over final scoring tabulation.
- Pricing Component – The points for the media buying commission portion of the pricing score were calculated incorrectly. The Department averaged the commission rate percentages instead of the media buying fees. This resulted in slightly different scores.

**The points for the media buying commission portion of the pricing score were calculated incorrectly**

In addition, the points assigned to the two pricing components in the Request for Proposal were not reflective of the total cost to the State represented by each component (i.e. the component with most cost to the State was assigned less points than the component that had the least cost to the State.) Officials stated that the media buying commission (155 points) was weighted higher than hourly rates (95 points) because the media buy was going to be the bigger part of the contract. As a result of the point structure contained in the Request for Proposals, the vendor with the highest hourly rates but lowest media buying commission was awarded the contract. Based on the winning vendor's commission rate, auditors calculated the cost of commissions to be approximately \$0.6 million. Comparatively, the hourly rates section included a total of 39,845 hours for a total cost of \$9.1 million

The Department stated it conducted this procurement under the oversight of the Chief Procurement Office (CPO) and followed the policies and procedures outlined by the CPO's Office, State Purchasing Officer, and Procurement Compliance Monitor. The Department further stated there was no violation of the Procurement Code or procurement rules in awarding the contract to the awardee. (Finding 8, pages 25-28)

We recommended the Department and the Chief Procurement Office for General Services closely examine and adequately test the scoring elements in Request for Proposals to ensure the winning proposal will be the most advantageous to the State. We also recommended the Department and Chief Procurement Office for General Services examine their procedures for scoring proposals and make any needed additions or changes to improve the controls over the scoring process.

**Department concurred with the recommendation**

The Department concurred and welcomed the auditor's recommendations noted in the finding. Department officials stated that this procurement was conducted under the oversight of the Chief Procurement Office (CPO) and followed the policies and procedures outlined by the CPO's Office, State Purchasing Officer and Procurement Compliance Monitor. There was no violation of the Procurement Code or procurement rules and the recommendations noted did not compromise the outcome of the awarding of this contract. The Department will continue to strive to adequately ensure DOI procurements are conducted with the utmost integrity.

**CPO agreed with the recommendation**

The CPO agreed the scoring elements in the Requests for Proposals should be closely examined and tested to ensure winning proposals are most advantageous to the State. The CPO further agreed to examine the procedures it establishes for scoring proposals and to determine whether additions or changes to improve the controls over the scoring process are necessary.

**LACK OF CONTROLS OVER EXPENDITURES**

The Department did not exercise adequate controls over expenditures for the contract of the Illinois Health Insurance Marketplace marketing and outreach campaign. The contract totaled \$33.3 million for a one year term beginning August 16, 2013. According to the Department, the total amount expended was \$28.9 million.

Auditors examined expenditures incurred during fiscal year 2014 related to the contract and noted the following issues:

- Travel and other expenditures – The Department allowed the vendor to bill for travel and other related expenditures even though the request for proposals (RFP) specified bills for those expenses were not allowed. This point was made clear by the Department in responding to two different questions from vendors prior to the submission of proposals. Answers to vendor questions were published as addendums to the RFP.

**Vendor was allowed to bill for travel and other related expenditures when RFP specified bills for those expenses were not allowed**

The resulting contract contained the same section that was in the RFP. However, a different section of the contract conflicted with the Department’s stated position on allowing expenses. Appendix A of the contract, which contained the pricing schedule, stated the vendor would be allowed to bill the State for reasonable out of pocket and incidental expenses.

According to the Department, the State reimbursed the vendor for travel and other related expenses totaling \$11,628.

- Direct Costs – Auditors noted there was no supporting documentation to indicate that all direct costs were pre-approved as required in the contract. Auditors asked the Department to provide supporting documentation to show direct costs were pre-approved for nine specific examples from the expenditure testing.

**Lack of supporting documentation that all direct costs were pre-approved as required in the contract**

The Department was able to provide supporting documentation showing pre-approval for 1 of the 9 examples. For three of the direct costs, the Department’s response stated that the approval was done verbally. For an additional three items, the Department’s response stated that the expenses were included as a subcontractor in the original contract. For those six examples, as well as the remaining two examples, the Department was unable to provide any supporting documentation.

- Hourly Rates – The contract lacked controls over which individuals could charge at the various hourly rates. The contract did not contain a requirement to get formal approval for team members which would have ensured only approved individuals could bill at the various hourly rate levels. The Department stated billing rates were based on roles, not individual’s names.



**The contract lacked controls over which individuals could charge at the various hourly rates**

Auditors identified 19 individuals that billed at different hourly rates in November 2013 compared to January 2014. In 15 instances, the individuals' titles were the same in both monthly reports while in 4 instances, the titles were different. In 18 of the 19 instances, the individuals charged at a lower rate in January compared to November. The Department stated the 18 individuals noted were moved to a lower billing category because their core duties had changed while the remaining individual took on a more senior role due to the departure of another employee.

The Department further stated that individuals were not allowed to bill at multiple rates unless the Department and the vendor mutually agreed that an individual's core duties had changed significantly enough to warrant his or her move from one billing category to another category. However, the Department did not provide supporting documentation showing that the Department and the vendor had mutually agreed that the core duties had changed.

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires all State agencies to establish and maintain a system or systems, of internal fiscal and administrative controls, which shall provide assurance that funds, property, and other assets and resources are safeguarded against waste, loss, unauthorized use and misappropriation. (Finding 9, pages 29-33)

We recommended the Department exercise adequate controls over expenditures for the Illinois Health Insurance Marketplace marketing and outreach contract to ensure all expenditures are appropriate.

**Department concurred with the recommendation**

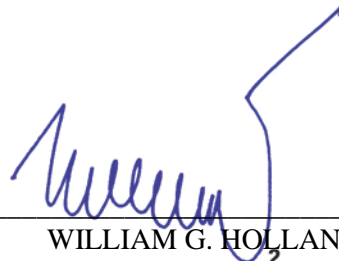
The Department concurred with the finding and will continue to closely monitor expenditures to ensure that they are appropriate and allowed within the contractual agreement. The review process for expenditures in Year 2 of the contract has been enhanced and direct cost forms have been added to the expenditure review process to ensure the Director of Get Covered Illinois is aware of and clearly approves specific items and services ordered under the Contract. The Department has also developed and retained a tracking document to ensure hourly rates charged by the vendor are included within the contractual agreement.

## **OTHER FINDINGS**

The remaining findings are reportedly being given attention by the Department. Auditors will review the Department's progress towards the implementation of all the recommendations in the next engagement.

## **ACCOUNTANTS' REPORT**

The auditors conducted a compliance attestation examination of the Department for the two years ended June 30, 2014 as required by the Illinois State Auditing Act. The accountants' report does not contain any scope limitations, disclaimers or other significant non-standard language.

A handwritten signature in blue ink, appearing to read 'William G. Holland', is written over a horizontal line. The signature is stylized and cursive.

WILLIAM G. HOLLAND  
Auditor General

WGH:RPU

## **AUDITORS**

E.C. Ortiz & Co., LLP were the Special Assistant Auditors for this examination.