



Johnson County Auditor  
Johnson County, Kansas  
**PERFORMANCE AUDIT**

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May 28, 2009

**Risk Management Audit**

*The Division is well managed. Some improvements would enhance operations.*





## Executive Summary

The County's Risk Management Division positioned in the Office of Financial Management was generally well managed as determined by our audit. We found staff to be dedicated to the services they provide and generally receptive to our recommendations for improvements. We noted areas that could be enhanced with adjustments to policies, procedures and practices.

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Financial Management Strategy	The current practice of financing the Risk Management Fund is not consistent with the language contained in the adopting resolution. <i>(See Page 1)</i>
Workers Compensation Fund Balance Operated Without a Target	County management has not set policy or sought Board approval for the fund balance retained in Risk Management. <i>(See Page 2)</i>
Written Policies and Procedures Are Needed	Without a target fund balance, the fund grew to over \$5 million. Risk Management staff recognized that reductions were warranted and needed to develop policies and procedures <i>(See Page 5)</i>
Contractor Monitoring Needs Improvement	Knowledge lost will be difficult if not impossible to regain. Without proper documentation, succeeding managers and staff will have to fend for themselves in accomplishing program tasks. <i>(See Page 7)</i>
Ergonomic Program Can Be Better Defined	Contracts with the County's third party administrator did not specify deliverables; audits of claims processed by the administrator did not provide representative coverage of all claims processed; and, reviews of payments made by the administrator were lacking. <i>(See Page 9)</i>
Ergonomic Program Can Be Better Defined	The program has not clearly identified the type of workplace to be reviewed and has not identified the universe of employees to be reviewed. Consequently, program benefits do not reach many of the intended beneficiaries and program results cannot be effectively measured. <i>(See Page 17)</i>

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## Johnson County Audit Services

May 28, 2009

To: The Johnson County Board of County Commissioners  
Michael Press, Johnson County Manager  
Tom Franzen, Director, Financial Management

In accordance with the approved audit plan, we performed an audit of the Risk Management and Workers Compensation Funds. The audit included a review of selected program operations within the Risk Management Division and the budgeting and accounting for the Risk Management and Workers Compensation Funds. The audit reviewed practices and procedures for compliance with laws, rules, and regulations as well as County policy. We reviewed transactions for the 2006-2007 periods.

Risk Management program operations were organized and well managed. We found the Risk Manager to be receptive to the audit results and on many occasions, she initiated corrective measures during the audit. Our audit identified the need to establish stronger internal controls for managing third party administration activities. We also noted financial policies and procedures were needed for managing the Risk Management and Workers Compensation Funds reserve balances.

The audit was conducted according to applicable standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, except that a Peer Review has not been performed, and included such tests of the procedures and records as considered appropriate.

I appreciate the cooperation received from the staff during this audit.

William D. Miller, CIA, CGFM  
County Auditor

The following auditors contributed to this report:

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# Risk Management Audit

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## **RESULTS AND RECOMMENDATIONS**

### **1. Risk Management Fund Program Operations Need to be Reassessed**

Operating procedures necessary to guide and manage the Risk Management Fund have not kept pace with the maturity level of the Risk Management program. Our audit disclosed the following:

- Current day financing of the Risk Management Fund is not consistent with the language contained in the original Board Resolution authorizing establishment of the fund
- A Reserve Policy has not been developed for the Risk Management Fund
- Current level of self-insured retained amounts and commercially procured insurance may not be established at optimal levels

These actions are the result of not developing a comprehensive financial strategy necessary for program operations. Consequently, Risk Management Fund program results may not be as effective as they could be.

### **Recommendations**

We recommend the County Manager:

- 1.1 Evaluate the operational language in BOCC Resolution No. 89-96 and modify the language to the extent needed to meet the current operational needs of the fund. Develop a new resolution for Board discussion and consideration.
- 1.2 Develop a Reserve Policy for the Risk Management Fund that reflects:
  - programmatic and cash flow requirements
  - emergent situations and unpredictable events and
  - an evaluation of self-insured retention levels to they are established at optimum levels

### **Management Comments**

- 1.1 *Staff will work with Chief Legal Counsel on developing a new resolution that will include formulation of a Risk Management Reserve Fund policy.*
- 1.2 *Staff has reviewed the language in BOCC resolution No. 89-96 with Chief Legal Counsel. The internal auditor states that annual funding has exceeded the original intended amount of funding. It is the opinion of the Chief Legal Counsel that the resolution was not intended to set a maximum amount and that the Board could provide funding in addition to that specified in the resolution. It is also Chief Counsel's opinion that the actions of the staff in maintaining funding in the Fund are consistent with the intent of the resolution. However, staff acknowledges that the resolution should be reviewed and updated and a Reserve Fund Policy be established with a target fund balance as the goal. The existing procedure*

*reflects, at a minimum, the funding amount per the resolution, and it also considers actuarially projected losses for the coming budget year.*

*The Risk Management Fund, collectively, consists of funding for administrative costs, and insurance premiums and losses, both liability (tort) and property (non-tort). The Risk Management Reserve Fund (established per BOCC resolution 89-86) is included in the Risk Management Fund, but retains only those funds required for the purpose of paying claims or losses incurred by the County which are within the retention or deductible amounts or for which no insurance is procured.*

## Discussion

### Background

Board Resolution No. 89-86, dated August 14, 1986, authorized the establishment of a Risk Management Reserve Fund for the purpose of: "...providing moneys to reimburse the County, in whole or in part, from insurable losses not otherwise insured." The Board of County Commissioners (BOCC) used the authority granted to them by K.S.A. 12-2615 in establishing this fund. This resolution authorizes a specific dollar amount, \$208,000.00, be contributed each year to the fund. In addition, a fund "ceiling" was established which is based on one percent (1%) of the "...gross revenues of the general, special, capital and enterprise funds, plus Two Hundred Eight Thousand Dollars (\$208,000.00)..." Table 1.1 identifies activity occurring in the Risk Management Reserve Fund during FY 2006 & 2007.

**Table 1.1 – Risk Management Reserve Fund**

Activity	FY 2006	FY 2007
Beginning Fund Bal	\$2,634,482	\$2,735,939
+ Revenues	\$2,639,885	\$2,818,556
- Expenses	\$2,538,428	\$2,507,034
= Ending Fund Bal	\$2,735,939	\$3,047,461

Source: Oracle Detail Trial Balance for adjusted fiscal years ending 12/31/06 & 12/31/07

The "Revenue" line in Table 1.1 primarily represents the amounts contributed to the fund that originate from each County department and agency. Programmatic activity has evolved over the years. Today the fund receives contributions from each department and agency exceeding the original intended amount. Although the fund has never reached the authorized ceiling, the current practice of financing the Risk Management Fund is not consistent with the language contained in the adopting resolution. Resolution language should be evaluated and modified to the extent needed to meet the current needs of the fund.

The County is self-insured and retains liability for \$350,000 of each occurrence for losses related to automobile and general liability. Coverage in excess of the retained limits is provided by excess insurance procured through the commercial insurance industry. The County's loss history of settled claims has never exceeded the self insured (retention) amount. The County contracts with a third party claims administrator to provide claims administration and payment services on the County's behalf.

The County's Financial Policies for "Reserves" has a section reserved for the Risk Management Fund. However, a specific policy identifying operating guidelines and a targeted position has not been developed, recommended to and adopted by the Board of County Commissioners. A Risk Management Fund Balance policy should be developed for BOCC review and approval.

Risk Management's strategy for financing program operations has the following components: fund balance, self-insured retained amounts and insurance procured commercially for excess insurance needs. These components are interdependent of each other as action taken on one will influence the other. Developing a Reserve Policy for the Risk Management Fund must also consider the impact on the other financing components, self-insured retained amounts and excess insurance, and whether or not they are established at appropriate levels.

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## **2. Workers Compensation Fund Reserve Does Not Have a Target Balance**

Since the Division had not established a target fund balance or established policies and procedures for determining such a balance, the Workers Compensation Fund just grew over the years. As of December 31, 2007, the reserve balance was \$5,460,904. At least \$2.9 million of that balance was excess based on closed claim amounts for the years 1990-1997. Risk Management and Office of Financial Management staff recognized the fund was too high when compared to historic claims information and began reducing the fund balance (\$1,000,000 for 2009) through lesser rate charges to county departments and agencies. However, to gain better knowledge and management of the fund, a target fund balance should be set, and procedures for determining appropriate fund balances should be developed. Once an appropriate fund balance is created, departments and agencies will be properly charged.

### **Recommendation**

We recommend the County Manager:

- 2.1 Develop a Reserve Policy for the Workers Compensation Fund that reflects programmatic and cash flow requirements, emergent situations and unpredictable events and adjust the reserve balance to comply with the policy.

### **Management Comments**

*Staff will draft a reserve policy for the workers compensation portion of the Risk Management Fund and present it to the BOCC for consideration.*

*Staff works with a third party administrator (TPA) and has an established methodology in place for the development of estimated annual costs for workers compensation claims and the corresponding annual funding. Staff agrees that a policy should be developed to consider the annual funding requirement and govern the use of funds associated with prior claim years. Workers compensation claims are actuarially projected based on historic losses, however, these claims are volatile and unpredictable and the ultimate outcome is dependent on statutory requirements and litigation activity. Workers compensation claims may take in excess of eight years to close, and based on the new stimulus legislation, may be subject to Medicare expenses, which could extend the open status of the claims*

### **Discussion**

Board Resolution No. 107-90, dated October 25, 1990, authorized the establishment of a Workers Compensation self-insurance account for payment of workers compensation claims, judgments and expenses related to administering self-insurance under the Workers Compensation Act. The BOCC used the authority granted to them by K.S.A. 44-505b in establishing this fund. Since November 1990, the County has qualified as a self-insurer for workers compensation benefits. The Workers Compensation Fund receives its financing from other County funds through an allocation system. The fund is available to pay claims and administrative costs of the program. The County retains liability for \$350,000 per accident with

commercial insurance coverage purchased to provide protection from losses in excess of that amount. No claim has ever exceeded the self insured amount. The County contracts with a third party claims administrator to provide claims administration and payment services on the County's behalf.

The County's Workers Compensation Program is managed by claim year. Programmatic actions during a claim year include revenue that has been paid into the fund during that year and the expenses incurred associated with the administrative costs and payment of claims. Table 2.1 identifies activity occurring in the Workers Compensation Fund during FY 2006 & 2007.

**Table 2.1 – Workers Compensation Fund**

Activity	FY 2006	FY 2007
Beginning Fund Bal	\$3,628,651	\$4,504,041
+ Revenues	\$2,522,912	\$2,679,458
- Expenses	\$1,647,522	\$1,722,595
= Ending Fund Bal	\$4,504,041	\$5,460,904

Source: Oracle Detail Trial Balance for adjusted fiscal years ending 12/31/06 & 12/31/07

The Risk Manager concluded there was very little likelihood of incurring additional costs for claims applicable to the 1990 through 1997 claim years and considered these years to be closed. Excess Fund Balance attributed to those closed years was determined to be \$2,934,682 (54%), as of December 31, 2007.

Recognizing the Workers Compensation Fund balance was building more reserve than required to meet operating needs, management initiated action to use \$1,000,000 of the fund balance, specifically targeted to the closed years, to lower future workers compensation fees assessed County departments and agencies. FY 2009 was the first year in which the County's budget reflected this approach. If budget results meet expectations and other assumptions remain unchanged, this approach will be repeated again in years 2010 and 2011, essentially, drawing down the reserve applicable to the closed claim years.

Planned reduction  
of excess fund  
balance

The County's Financial Policies for "Reserves" do not address the Workers Compensation Fund. A targeted fund position for the Workers Compensation Fund has not been developed, recommended to, and adopted by the Board of County Commissioners. Nonetheless, budgetary action was taken to reduce the Fund balance applicable to the excess calculated for the closed claim years. In light of economic events facing the County, a Workers Compensation Fund Balance policy should be developed for BOCC review and approval.

### **3. Written Policies and Procedures Would Enhance Personnel Transitions**

The County could be better prepared for the succession of staff in Risk Management. Key Risk Management staff account for more than 50 years of experience all within the Risk Management Division. Some written policies and procedures outlining the duties and nature of the work to be performed exist, but not all functions are properly documented. Management acknowledged the need for these policies and procedures and stated the development of them lagged behind the priorities of providing required services to the agencies and departments of the County. Lack of documentation detailing processes and work objectives leads to future risks when employees are absent, retire or leave. Written policies and procedures defining employee responsibilities, guidance on accomplishing tasks, and accountability for work completed ensure smooth and efficient transition of personnel.

#### **Recommendation**

3.1 We recommend the Director of Financial Management develop a written policy and procedures manual for the Risk Management Division, addressing:

- Significant activities, nature of work to be performed, and detailed instructions of how these accomplishments are to be met
- Employee responsibilities, including limits to authority and reporting relationships
- Control procedures

#### **Management Comments**

*Staff agrees that documentation of Risk Management division processes needs to be improved. Risk Management staff's highest priority is to perform the functions within the activities stated with a limited staff of 5.5 FTE. The complexity and extensive workload associated with our duties in serving the County's departments and agencies and their programs leaves little time to fully detail job duties. Management will reallocate Risk Management staff resources from current service level provision to the organization in order to fully document all current processes and compile those into a procedural manual.*

### **Discussion**

#### **Risk Management Activities**

Risk Management is responsible for a variety of programs that benefit and protect the County and its employees. These activities include:

- Managing the County-wide property and casualty insurance and self-funded program
- Managing the property and liability losses that result from operations
- Managing the self-funded workers compensation program
- Conducting safety audits
- Conducting loss control and property conservation inspections
- Conducting risk management and safety training
- Providing workplace crisis management services

Risk Management has 5.5 FTE employees; a Risk Manager, Safety Officer, Risk Management Specialist, Crisis Management Specialist, Administrative Assistant, and Risk Management Coordinator, who are responsible for the day to day operations of the Risk Management Division. The Risk Management Division has benefited from low staff turnover over the past 20 years. Of these positions, the Risk Manager, Risk Management Specialist, and Risk Management Coordinator are responsible for the administration of the general liability and workers compensation programs. Cumulatively, they account for over 50 years of experience.

### **County financial policy and procedures**

Johnson County Financial Policy 100.4 states “...the County Manager shall establish and maintain financial procedures....” and further “...these procedures shall apply to all departments in the performance of their official duties.” The management of each County Department is responsible for defining processes and providing written documentation within its department.

Written policies and procedures are needed

### **Risk Management needs to document policies and procedures to ensure smooth transitions**

Risk Management, as a Division of OFM, has limited written procedures documenting employee duties and responsibilities. The Risk Manager stated approximately 50 percent of her duties were documented in the form of written procedures. Formal, written procedures should provide information pertaining to the overall scope of Risk Management Division, as well as, basic “how-to” guidance for individual positions. This documentation will mitigate risk when planned or unplanned absences occur. During the course of the audit, the Risk Manager proactively initiated a comprehensive effort to document business processes and develop policies and procedures in accordance with our recommendations.

#### **4. Program `Oversight of Third Party Administrator (TPA) Needs Improvement**

Risk Management's internal controls related to managing the TPA contracts were weak. The following issues were found:

- Contracts for the Workers Compensation and Automobile/General Liability Programs did not contain specific deliverables and measurement and timeliness criteria
- Independent audit procedures do not ensure a representative review of Workers Compensation and General and Automobile Liability claims processed
- There were no written procedures for reviewing payments made by the TPA
- The Risk Management Information System, RiskMaster, was not secure because TPA personnel received permission levels and access privileges beyond that needed to accomplish tasks

These actions are the result of Risk Management staff not devoting sufficient attention to the activities of the TPA to ensure proper controls were in place. Without adequate internal controls, the program is at risk.

#### **Recommendations**

We recommend the Director of Financial Management:

- 4.1 Identify key contract deliverables and appropriate measurement and timeliness criteria and incorporate these requirements into the contract.
- 4.2 Require the independent auditor review a representative sample of claims processed by the TPA in addition to other specific claims considered necessary.
- 4.3 Transfer the responsibility of updating and maintaining RiskMaster's Entity Table from the TPA to the County's Risk Management Office.
- 4.4 Develop and establish a recurring Quality Control Review of payments made by the TPA to ensure they are accurate, complete, and for valid claims.
- 4.5 Within RiskMaster, review system assignments and responsibilities by position, what capabilities are granted, and make appropriate adjustments to reflect the individual's duties and responsibilities.

#### **Management Comments**

- 4.1 *The Scopes of Service are being modified to the degree that measurable deliverables are appropriate.*
- 4.2 *Staff will direct the independent auditor to randomly sample the claims processed by the TPA, however Risk Management staff will still select additional claims that we believe require auditor oversight and evaluation.*

4.3 *This recommendation has been completed.*

4.4 *This recommendation has been completed.*

4.5 *This recommendation has been completed.*

## Discussion

### **TPA contract language**

Johnson County entered into two separate contracts on January 1, 2004, to provide a full range of third party administration and claims management services for the County's Workers Compensation and Automobile and General Liability Programs. Both contracts have exhibits defining the scope of services required to administer these programs. The Scope of Services lack contract language identifying *how*, *when* and the *time frames* services are to be performed and in some limited instances, the product or deliverable. The following examples are provided:

- Workers Compensation Contract, Scope of Services item #5 requires the TPA to "Make immediate on-site investigations of serious injuries at the County's request." Scope of services does not identify specific time frame investigations should be initiated or completed nor does it require a product or deliverable reporting the outcome of the investigation.
- Workers Compensation Contract, Scope of Services item #25 requires the TPA to "Prepare federal form 1099's on the County's behalf." Scope of Services does not require the TPA to file with the Internal Revenue Service or issue the recipient a copy of the 1099. The Scope of Services is silent regarding a specific timeframe to prepare and report the federal form 1099.

The contracts, in their current form and content, leave the County vulnerable and would make it difficult to hold the contractor accountable in case of nonperformance. Incorporating key contract deliverables and appropriate measurement and timeliness criteria into the contract would mitigate this risk.

### **Independent audit of TPA**

On a biennial basis, an independent auditor reviews open and closed claims processed by the TPA to assess whether or not the TPA is doing an effective job administering the County's Workers Compensation and General and Automobile Liability claims. The Risk Manager determines which claims the independent auditor should review using first-hand knowledge of all claims and focusing on a specific claim profile(s). The profile can target claims that are:

- Severe, both dollar and extent of injury
- Significant in number of lost days
- Significant as to the extent of medical or rehabilitative treatment provided

Opinions expressed by the independent auditor are only representative of the claim profile and do not provide a basis for evaluating the overall performance of the TPA. Expanding the claim selection criteria to include a statistically representative sample of all claims, in addition to a predetermined profile, would provide the County a more comprehensive assessment of the TPA's performance and whether or not it is administering the claims management process efficiently and effectively.

### **TPA payment processing**

On a weekly basis, the TPA forwards to Risk Management a schedule of payments being issued for expenses related to the County's Workers Compensation and Auto and General Liability Programs. Typically, this schedule is representative of the TPA's previous week's processing. The schedule is forwarded to Risk Management so the County can process a wire transfer to the TPA's bank account prior to the payments being issued.

Our audit noted two concerns with this process. First, Risk Management did not have a formal process in place to review payments being generated by the TPA. Second, some TPA staff supporting the County, because of their access to RiskMaster, had too much control of the financial aspects related to managing the claim. For example, they could:

- Add/delete payees
- Input the payment transaction
- Approve the payment
- Print the check
- Process the check with facsimile signature
- Prepare the check for mailing
- Mail the check

Both conditions create an environment susceptible to fraud. While many of the above tasks would remain with the TPA, Risk Management should institute a quality control review of payments generated by the TPA and eliminate the TPA's ability to add and delete payees to mitigate this risk.

### **Risk Management's automated information system "RiskMaster"**

The TPA, by means of electronic interfacing, works and processes data within the County's Risk Management Information System, RiskMaster. The TPA has four personnel who have access to and operate certain aspects of the system. One individual is assigned to the County's Auto/General Liability program. Two individuals have been assigned to the County's Workers Compensation program, one of which can support the Auto/General Liability side if needed. These individuals have been assigned an "adjuster" password allowing extensive read and write capabilities and, in one instance, access to information not required by their position. The fourth individual, the supervisor, has been assigned a "supervisor" password allowing him to review and modify the work of the other three, delete records, and print checks. System privileges granted to TPA personnel were too broad, allowed privileges beyond the scope

System  
access  
increases risk

of their positions and access to confidential information when their position did not require it. The Risk Manager should review system assignments and privileges along with a TPA representative to strengthen system access controls and to more accurately reflect system assignments and responsibilities.

## **5. Policy Requires Competition in Acquiring Excess Workers Compensation Insurance**

Risk Management staff should comply with the County's policy requiring either formal and publicly advertised competition, or obtaining an exemption or exception from competition, in obtaining the County's Excess Workers Compensation insurance policy. Staff requested the County's Workers Compensation third party administrator to privately obtain bids for this coverage. The staff believed this procurement method, which had been in use for many years, was appropriate. The total cost for this insurance policy exceeded \$100,000, which, according to Purchasing Policy and Procedures, required formal and publicly advertised competition. Without formal and public competition, the County does not have the assurance of achieving the best available price for this product.

### **Recommendation**

We recommend the Director of Financial Management:

5.1 Comply with County Purchasing Policy and Procedures in acquiring excess workers compensation insurance.

### **Management Comments**

*Staff has complied and will continue to comply with County Purchasing policy. Staff would like to provide the following clarification:*

- *The firm providing the TPA services is also an insurance broker. We are utilizing two distinct services from one firm.*
- *The excess workers' compensation is obtained using the services of an insurance broker, not a TPA.*
- *Staff did not violate the Purchasing Policy in utilizing the broker services. Competitive quotes were obtained by the broker and reviewed by Risk Management. The broker discussed each renewal and the markets to be approached for the excess coverage with Risk Management.*

*Because excess workers compensation insurance coverage and the method by which it is procured in the corresponding markets are unique, management will be updating the Purchasing Procedures to identify procurement of insurance coverages as an eligible exception from competition.*

*Fair and open competition for insurance coverages will be obtained by brokers. Also, the County will continue to compete the services for brokers in a fair and open manner.*

### **Audit Comment:**

At issue is whether or not procedures used to acquire the excess workers compensation insurance satisfy County Purchasing Policy. The Purchasing Policy is clear "...formal, publicly advertised competition...." is required for this type of purchase and dollar amount. The procurement

method used by Risk Management staff does not bring about a formal or public competitive process. Further, Risk Management staff did not seek a waiver from the competitive process which is allowed in certain circumstances by the Purchasing Policy.

### Discussion

The County's workers compensation program retains liability and self-insures for \$350,000 per accident and procures specific coverage, commercially, to provide protection in excess of that amount. The commercial coverage, hereafter referred to as excess workers compensation insurance, is obtained using the services of the County's third party administrator (TPA) for the workers compensation claims management as a procurement manager and insurance broker. In this capacity the TPA provides bid management and insurance brokerage service for the County's excess workers compensation insurance.

Competition  
needed for  
insurance  
purchase

In performing the procurement management services on the County's behalf, the TPA conducted a private solicitation by contacting insurers they believed would be able and willing to provide the type of coverage needed. The TPA provided a listing of the bids to County staff for their review and final selection but did not provide the full details of the solicitation process. Once the final selection had been made, the TPA acted as an insurance broker in dealing with the selected insurance provider. The TPA was paid a brokerage commission by the selected insurance carrier which amounted to approximately 15 percent of the insurance premium paid by the County. This brokerage fee was in addition to the fee paid to the TPA under the TPA contract for services.

#### County Purchasing Policy # 110.135 Authority to Purchase, Contract

Purchases of less than \$10,000.00 may be made, without competition, on the open market upon the authorization of the appropriate agency, department or office director. Purchases of goods and services with a cost exceeding \$10,000.00 but not over \$100,000.00 shall require competitive procurement practices, and the County Manager shall establish Purchasing Procedures consistent with this Policy, to ensure the proper and effective procurement.

#### County Purchasing Procedure # 110.135 Authority to Purchase, Contract

F. Purchases of goods, and general services in an amount of \$50,000.00 or more, but less than \$100,000.00, shall require formal, publicly advertised competition and approval by the appropriate department head and the Purchasing Manager.

G. Purchases of goods, professional services and general services in an amount of \$100,000.00 or more shall require formal, publicly advertised competition and approval by the Board of County Commissioners or the appropriate governing board.

## County Purchasing Procedure # 110.165 Competitive Procurements

B.3. FORMAL BIDS are written documents issued by the Purchasing Office, inviting potential contractors to submit sealed, written pricing for specific goods and services in conformance with specifications, terms, conditions and other requirements described in the bid invitation documents. Formal bids require public notice (legal publication), public bid opening at a time and place designated in the bid document, and a minimum of ten (10) working days between publication of the bid invitation and bid opening. Formal bids shall be utilized to document procurements of goods and contractual services with an estimated project cost of \$50,000.00 or more.

The brokerage and TPA services are unrelated services and paid for separately. The County pays the TPA more than \$100,000.00 annually for the cost of the Excess Workers Compensation Insurance policy and brokerage fees. County Purchasing Policy and Procedures require formal and publicly advertised competition as a means to obtain best value for the County. Conducting a private telephone solicitation to obtain bids is not allowed unless the purchase is less than \$50,000. Staff believed the method used to solicit and obtain bids, which has been in use since the County became self-insured in 1990, satisfied the requirement for formal competition and was appropriate.

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## **6. Ergonomic Program Can Achieve Enhanced Outcomes**

The worksite evaluation portion of the County's ergonomic program is not reaching a majority of the program's target population of new employees and employees who have changed positions within the County. The Safety Officer is performing worksite assessments only at the employee's or their supervisor's request and is not informed of all potential participants of the program. Better coverage of the County's workforce is achievable through implementation of a few program enhancements.

### **Recommendations**

We recommend the Director of Financial Management:

- 6.1 Correct the point of contact on Risk Management's website (30-day assessment request) to the current Safety Officer.
- 6.2 Collaborate with Human Resources and develop a recurring automated reporting tool that identifies new employees and employees changing positions to provide the Safety Officer with information to initiate inspections.
- 6.3 Refine program outcomes identifying quantifiable goals of acceptable employee participation and timeframes.
- 6.4 Take measures to increase employee awareness of the ergonomic program benefits.

### **Management Comments**

- 6.1 *This recommendation has been completed.*
- 6.2 *This recommendation has been completed. We began obtaining a monthly new hire report from HR in February, and although it provides countywide information, its use is limited primarily because it is not a goal of the Program to assess all work areas. Plus all areas, including many workstations, do not require assessments, and time does not allow the assessment of all jobs or work areas.*
- 6.3 *The existing goals are set based on a targeted group and approach. We appreciate the auditor's comment to clarify program terminology regarding "work area", and we will better define it. However, we do not see the need to change the existing performance measure.*
- 6.4 *Our approach is to utilize managers, supervisors and individual employees to identify the need for an ergonomic assessment. We have assessed this element of the program and have determined that we do need to increase the training frequency. We are scheduling, and will be conducting, training classes specific for supervisors and informational sessions for employees. In addition, staff will update information regarding this program and*

*continue communicating it to the organization at various levels (e.g. E-Team, A-Team) and in various processes (e.g. new employee orientation).*

*The Ergonomics Program was originally developed due to a growing trend we were seeing in upper extremity workers compensation claims and its target population was never intended to be all new employees and employees who have changed positions. Although there were a minimal number of claims from other jobs, duties, work areas and functions, the focus was and continues to be workstations and computer usage. This does not preclude the need for assessments for other jobs that require repetitive use of tools and equipment. We are not staffed to assess the work areas of all new hires.*

*We prefer to use a collaborative approach with managers, supervisors and employees to assist in identifying assessment needs and to concentrate on informational training.*

*On average, the Safety Officer spends 2.0-2.5 hours from start to finish performing an ergonomic assessment. This includes travel to and from a site, assessment, discussion with the supervisor and employee, writing a work order for physical modification of the workstation, and writing a report with recommendations to the supervisor. Using an average of 2 hours per assessment and considering that the auditor wants us to assess all new hires (which per below was 657 in 2007), the time devoted just to ergonomics would be 1,314 hours per year or 63% of the Safety Officer's work time. This is not feasible given the significant other responsibilities of the Safety Officer, such as safety audits, accident investigations, workplace environmental issues, and other types of training. Expanding this program will require additional staff.*

*We feel that two of the comments and recommendations are of value: 1) redefining the Program terminology and focus, and 2) improving employee awareness of the Program and the resource available to assist in creating a more comfortable work area. We will reassess those elements of our program.*

## **Discussion**

### **The Ergonomics Program**

Johnson County's Safety Manual states:

The purpose of the program is to provide a safe and comfortable work area for those employees whose job duties require repetitive motions, forced or awkward positions. We will apply the principles of ergonomics to the workplace in an effort to reduce the number and severity of Musculoskeletal Disorders (MSDs) thus making employees more comfortable in their work areas, increasing productivity, quality and efficiency where possible, and decreasing workers compensation claims.

Risk Management/Safety Division is committed to the ergonomics process. Management supports the efforts by assisting in the identification and control of

ergonomic risk factors and regularly communicating to employees the benefits of the program.

### **Requesting a worksite evaluation**

At each *New Hire Orientation Meeting*, Risk Management provides attendees with a wealth of information concerning Risk Management and Safety, Accident Reporting, Emergency Planning and Ergonomics. Included in the ergonomics portion of the presentation is information regarding the worksite evaluation process. New employees are instructed at this session that they, or their supervisor, may request an evaluation be performed by the Safety Officer. New employees may also request an evaluation be performed by accessing OFM Risk Management & Safety “Ergonomics” Intranet Site. Risk Management’s procedures for requesting evaluations need to be reviewed. The Safety Officer’s email address on the Intranet website is not correct and needs to be updated to reflect the current Safety Officer as the point of contact.

### **Collaborate with Human Resources to identify potential employees needing evaluations**

In 2007, the County hired 658<sup>1</sup> new employees and had 377<sup>2</sup> employees change positions. The Safety Officer conducted a total of 188 ergonomic workstation evaluations in 2007, 60<sup>3</sup> of which, were for new hires. Worksite evaluations, as stated in the Safety Manual “...will be done to assess the work areas of new hires and transferees within 30 days of their employment or job change, or when an employee reports a Musculoskeletal Disorder (MSDs) sign or symptom. Evaluations will also be done for employees that have moved to another work area, location or new facility.”

Successful program can be improved

Risk Management should partner with Human Resources to develop a reporting tool that would identify employees qualifying for a workstation assessment to be conducted by the Safety Officer. Human Resources can extract lists of new employees, employees changing positions, and other potential groups of employees from the employee database. This information is available for the Safety Officer to initiate worksite assessments and enable Risk Management to take a proactive approach to the assessment process. This would result in a better opportunity for County employees to have their worksite evaluated.

### **Redefine Ergonomic Program Goals**

Risk Management has defined ergonomic program success levels as they relate to workers compensation claims. Reduced numbers of workers compensation MSD claims, in terms of frequency, severity, and cost have been attributed to the ergonomics program. However, stated ancillary goals of the program, i.e., provide a safe and comfortable work area for employees, are left unmeasured.

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<sup>1</sup>2007 New Hire information provided by the Human Resources Department.

<sup>2</sup> 2007 Employees Changing Positions information provided by the Human Resources Department.

<sup>3</sup> Number provided by Risk Management.

Program terminology used, such as, “worksites”, “work area” or “workstation assessments” tend to be used interchangeably which leads to confusion that may be impacting program outcomes. The intended audience, those employees eligible for a worksite evaluation, is not well defined. It is not clear if worksite evaluations are limited to employees occupying sedentary positions in a workstation environment. Or, does it include all individuals regardless of type of position held? In a broad sense, “Ergonomics is the science of fitting workplace conditions and job demands to the capabilities of employees.”<sup>4</sup> A practical approach would consider the match between the person, the equipment he or she uses, the work processes and the work environment.

Risk Management should determine if the assessments are to be offered to all employees, just those employees occupying a sedentary position working at a workstation, or apply other relevant criteria. They should also define program goals and outcomes based on these new criteria so that program success can be accurately measured.

Risk Management staff takes some measures to make some employees aware of the ergonomic program. This includes orientation for new employees, employees who change jobs and responses to requests for assessments. After the initial orientation, the program is reactive rather than proactive. More outreach is needed to ensure broad coverage of the program throughout the County.

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<sup>4</sup> University of Alabama at Huntsville, Center for Modeling, Simulation and Analysis, Office of Environmental Health & Safety presentation dated 4/20/06.

## **7. Purchase Card Documentation Retention Practices Need Improvement**

OFM staff was unable to locate a significant number (6.5%) of purchase card (P-card) transactions selected for our review and verification. Weak adherence to the P-card documentation retention guidelines, as set forth in OFM's Procurement Card Administrative Guidelines, is the reason for not being able to locate documentation in support of these transactions. As a result, OFM is not in compliance with the County's Purchase Card Policies and Procedures.

### **Recommendations**

We recommend the Director of Financial Management:

- 7.1 Ensure all 2006 and 2007 P-Card documentation is accounted for and in compliance with OFM's Procurement Card Administrative Guidelines.
- 7.2 Review current P-card retention system practices and institute changes to maintain accountability of purchases made using the P-card.

### **Management Comments**

*7.1-7.2 Staff has been notified of this problem and reminded of their responsibilities in properly filing and retaining these documents. Although we strive for no errors, as a matter of course, documents can be misfiled or misplaced.*

### **Discussion**

Our audit reviewed P-card transactions made in support of Risk Management operations. To test the internal controls established for purchases made using the County's P-card, we randomly selected 153 transactions for review out of a total population of 347 transactions which occurred from January 1, 2006, through, September 4, 2008. Expanding the scope of our review to include 2008 purchase card transactions allowed us to review P-card purchases made by Risk Management personnel. Prior to 2008, the Risk Management Division received P-card support from cardholders outside Risk Management. This sample size allowed us to project our results to the full population with 90 percent certainty (at +/- 5% margin of error). Our audit revealed substantiation for 10 of the 153 transactions, or 6.5 percent, could not be located and was not available for our review. The missing transactions were made by two separate cardholders, one of whom is no longer employed by the County. Based on our sampling methodology, we project with 90 percent certainty that 21 to 24 transactions out of the 347 total transactions do not have supporting documentation.

When asked about the probable whereabouts of the documentation, OFM's P-card Office Program Coordinator responded that it never occurred to her that documentation for a P-card transaction was not being filed. The County's Procurement Card Administrative Guidelines require records, i.e., invoices, receipts and transaction approval reports be retained for a period of

3 years. Retaining all public records for this length of time is a requirement of the Kansas Open Records Act.

Action should be initiated to obtain the missing documentation and, more importantly, institute changes to the P-card documentation retention system to ensure accountability of purchases made using the P-card.

## **8. Processing Claims Internally Should Be Reconsidered**

Risk Management staff process a limited number of general and automobile claims internally as opposed to forwarding to the third party administrator for processing. The Risk Manager believes internal processing, in limited circumstances, is the most effective way to process these claims. Concerns noted with internal claims processing were:

- Cost associated with in-house processing, i.e., check generation, labor, etc., may prove to be more costly to perform when compared to the costs of using the third party administrator
- County checks returned to Risk Management staff awaiting disposition to the claimant lack adequate security and accountability controls

Perceived benefit of in-house processing may be more costly to the County and the lack of security and accountability control procedures expose the County to an increased risk of fraud, theft or loss.

### **Recommendations**

We recommend the Director of Financial Management:

- 8.1 Perform a cost benefit analysis to determine which alternative, internal claims processing or forwarding claims to the third party administrator, is more advantageous to the County.
- 8.2 If this practice is continued:
  - County checks should not be returned to Risk Management for distribution. The checks should be mailed to the recipient using standard County practices and procedures
  - The TPA contract should be modified to reflect this activity

### **Management Comments**

- 8.1 *Risk Management will perform a high level cost-benefit analysis to evaluate the cost-effectiveness of the current claims processing methodology. Risk Management will also rely on advice of the Legal Services Department as to which claims they prefer to handle in-house as opposed to referring to the TPA.*
- 8.2 *We will revise our current procedure to request checks when the final release is received, at which point the checks will be mailed directly to the claimant by Accounts Payable staff. This will not preclude us from making an exception to this procedure as a matter of customer service to our citizens and in a good faith effort to resolve outstanding claims.*

**Audit Comment:**

Regarding the response for recommendation 8.2, recommend OFM address lack of adequate security and accountability controls before any exception processing is authorized.

**Discussion**

The County entered into a contract with the TPA to provide a full range of third party administration and claims management services for their automobile and general liability programs. The TPA administers, processes, investigates, adjusts and manages automobile and property loss claims filed against Johnson County and are reimbursed on a per claim basis. The Risk Manager has determined certain claims filed against the County will not be forwarded to the TPA for processing and will be processed internally. Criteria used to determine whether or not the claim will be processed internally include the following:

- Liability is not in question
- Claim does not include injury and/or medical costs
- Overall loss is not significant

Internal claims processing requires accomplishing specific steps that would not normally be required to be performed had the claim been forwarded to the TPA for processing. These steps include but are not limited to:

- Coordinating with County agencies and departments
- Coordinating with claimant to obtain documentation in support of damages incurred
- Using Oracle's *Accounts Payable Check Request* process to produce a County check to reimburse claimant for loss
- Coordinating with claimant to obtain a "Release of Claims"
- Mailing or personally delivering check to claimant
- Updating Risk Management's RiskMaster information system to reflect action and events taken
- Maintaining files

The cumulative costs associated with performing the above steps have not been determined and it is possible processing claims internally may be more costly than forwarding to the TPA for processing.

When reviewing Risk Management's procedures for processing claims internally, our audit disclosed specific practices that expose the County to a risk of fraud, theft or loss. Risk Management staff use Oracle's *Accounts Payable Check Request* process to produce a County check to reimburse a claimant for their loss. These checks are produced by Accounts Payable and hand delivered to Risk Management. A control procedure is not in place requiring Risk Management to sign for these checks immediately upon receipt. Accountability of the check is compromised at this point in the process. Our audit also disclosed checks delivered to Risk Management may not be delivered to the claimant on the same day they were hand delivered to

Internal processing may increase costs

Risk Management. When this occurred, Risk Management would store these checks in a locked overhead compartment within an employee's work station or in a locking file cabinet along with other files and records. Security concerns related to this practice include the following:

- Location of overhead compartment and file cabinet is accessible to other individuals
- Physical security of the locking mechanism can easily be compromised with little effort
- Multiple individuals have access to the keys which operate the lock

Management should assess whether or not it is cost effective to continue processing automobile and general liability claims in-house. The assessment should consider all costs involved with internal processing compared to the cost of forwarding the claim to the TPA for processing. If the cost benefit analysis concludes it is financially advantageous for Risk Management to continue this practice and the decision is made to continue processing some claims internally, County checks should not be returned to Risk Management for disposition. Checks should be mailed to the claimant using standard County practices and procedures.

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## **9. Management of User Licenses Could be Improved**

Risk Management Division grants licenses to non-County municipalities and governments to use Johnson County Airport Commission property – a practice that may violate the lease agreement between Risk Management Division and the Airport Commission. User licenses are granted for a 12-month period and users are assessed a daily license fee which was developed years ago based on what activities were willing to pay and does not reflect the current cost of administering this program for County and non-County activities. We attribute these conditions to a lack of management attention and oversight.

### **Recommendations**

We recommend the Director of Financial Management:

- 9.1 Coordinate with the Legal Department to determine if usage is restricted to municipalities and local governments located within Johnson County. If usage:
  - Is restricted to Johnson County municipalities and local governments, discontinue issuing licenses to non-county activities
  - Can be expanded to municipalities and local governments beyond Johnson County, seek approval from the Airport Commission to modify the basic lease agreement expanding usage
- 9.2 Discontinue the practice of issuing User Licenses on an annual basis and limit the term of the license to the actual dates in use.
- 9.3 Develop a pricing schedule that more accurately reflects the cost of administering this program and assess to all County and non-County activities

### **Management Comments**

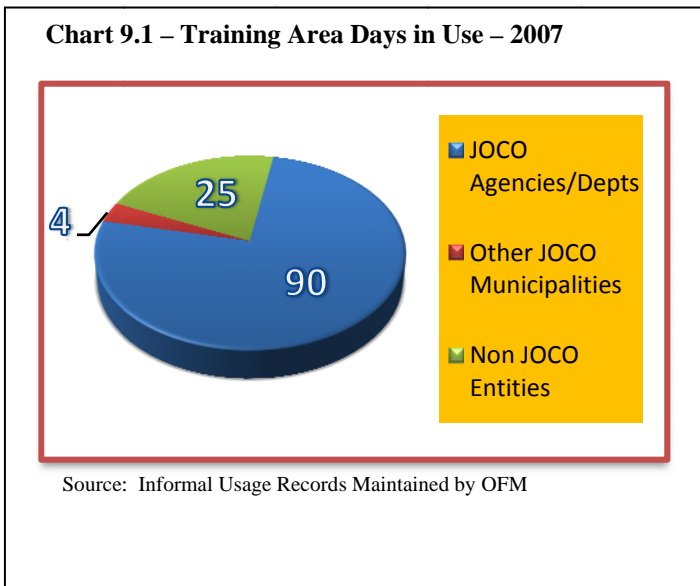
- 9.1 *The lease agreement is being amended to include any public entity.*
- 9.2 *The user license is being amended and each will be limited to the term of the dates reserved.*
- 9.3 *In accordance with County Financial Policy Section 120.5, staff will assess the full cost of administering the program and recommend a pricing schedule for Board consideration.*

*The Airport Commission decided to renovate and make available an abandoned runway to serve the County and a community of public users who had no access to other facilities. There was never any intent, when this area was renovated and opened, to charge County department users. The per diem rate was set based on user input as to the amount that would be acceptable to generate and maintain usage. Several years later, we examined the possibility of increasing the per diem rate. Input from user entities indicated that an increase would bar their usage.*

Legal staff has advised there is no need to restrict use of the facility to Johnson County municipalities. The Airport Commission is in agreement. The lease agreement is being amended to include any public entity. The user license is being amended and each will be limited to the term of the dates reserved.

### Discussion

Risk Management Division leases property from the Johnson County Airport Commission located at New Century AirCenter, New Century, Kansas. The property being leased is a portion of an abandoned runway used to conduct driver's safety training. The lease agreement between the Airport Commission and Risk Management Division acknowledges further assignment or subleasing of the property (hereafter referred to as training area) to municipalities and other governmental agencies located in Johnson County, Kansas. The lease stipulates payment of rent in the amount of \$7,200 per year and any repairs and maintenance of the training area to be at the Tenant's expense.



**Chart 9.1** illustrates the number of days in use during 2007. Risk Management issues non-County activities a user license, in lieu of a sub-lease, to use the property when not in use by County agencies and departments. User Licenses have a 12-month term. In 2007, the training area was used a total of 119 days by County agencies and departments, Johnson County governmental entities and non-Johnson County governmental entities. Issuing a user license to non-Johnson County entities may be in violation of the lease agreement between Risk Management and the Airport Commission.

Johnson County municipalities and government agencies and non-Johnson County entities were assessed a daily user license fee of \$50 to use the training area. This fee was determined many years ago based on a survey conducted to determine what entities were willing to pay. The daily user license fee does not reflect the actual costs associated with operating the training area. For example, in 2007, the cost of leasing the training area was \$60.50<sup>5</sup> per day used. Our audit also disclosed County agencies and departments were not required to reimburse Risk Management for use of the training area. Risk Management can improve the overall management of user licenses by adopting a pricing schedule that more accurately reflects the costs of operations and ensuring all users, County and non-County entities, are assessed a fee when they use the training area.

<sup>5</sup> This computation only considers the fixed cost of operating the training area, i.e., annual lease amount, and does not consider other fixed and overhead costs. (\$7,200 divided by 119 days used.)

## **OTHER MATTERS**

The Risk Management Fund as reported in the Comprehensive Annual Financial Report, *Internal Service Funds, Combining Statement of Cash Flows* exhibit, for the year ended December 31, 2006, identified (\$42,356) as “Acquisition and Construction of Capital Assets” under the category of “Cash Flows from Capital Financing Activities.” Our audit determined this specific category was overstated in the amount of \$37,653. The error is attributed to the workpapers used as supporting documentation for this exhibit being incorrectly prepared.

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## **OBJECTIVES, SCOPE AND METHODOLOGY**

### **Objectives**

The objectives of the audit were to determine if Risk Management's operations were in compliance with all relevant laws, regulations and County policies. In addition to reviewing financial and program management, the audit reviewed the Risk Management Fund and the Workers Compensation Fund. The audit reviewed a limited number of Risk Management programs for efficiency and effectiveness.

Specific objectives for this audit included:

- Determine nature of Accounts Receivable reported within Risk Management Division and applicability to GAAP reporting requirements. We determined the Accounts Receivable amounts to be insignificant and exempted from GAAP reporting requirements.
- Review the department's internal controls and determine if sufficient internal controls were in place to effectively reduce risks. This objective included a review of the security/application controls for Risk Management's automated information system, RiskMaster, and the controls established for payments issued on behalf of the County by the Third Party Administrator.
- Review contract management and vendors to determine if appropriate safeguards were included in contracts to protect the county and ensure that vendor selection was done in accordance with county policy and procedures.
- Review the management of employee expenses and AP checks to determine if the department was utilizing the most efficient county resources (iExpense) for payment of employee reimbursement.
- Review purchases made using the County's Purchase Card procedures to determine program usage and validity of payments.
- Review the Risk Management Fund and the Workers Compensation Fund fund balances to determine if they were being managed effectively. This included a review of the fund balance history for the period under review, trend analysis and comparison with budget projections.

### **Background**

The Risk Management Program is responsible for managing the county-wide property and casualty insurance and self funded program, managing the property losses that result from operations, managing the self funded workers compensation program, conducting safety audits, loss control and property conservation inspections, conducting risk management and safety

training, and providing workplace crisis management services. The 2006 & 2007 Risk Management budget indentified three major services as follows:

- Risk Management and Safety
- Risk Financing
- Claims Management

In accomplishing these programs on behalf of the County, the Risk Management Division operates two funds, the Risk Management Fund and the Workers Compensation Fund. Risk Management contracts with a third party administrator who performs a full range of third party administration and claims management for the Workers Compensation and Auto/General Liability programs.

### **Scope and Methodology**

In order to accomplish the objectives we reviewed:

- County wide financial and purchasing policies and procedures
- Information Technology security controls and procedures
- Limited department written procedures for the processing and handling of receipts
- Statistical sample of purchases made using the Purchase Card
- Statistical sample of purchases made using the Accounts Payable system
- Comprehensive Annual Financial Reporting for fiscal years ending 2006 & 2007
- Risk Management budgets for 2006 & 2007
- Contracts established with the third party administrator (TPA)
- Board of County Commissioners (BOCC) resolutions authorizing the establishment of the Risk Management Fund and the Workers Compensation Fund
- Background data and management reports establishing budget goals and measures
- Independent audit results of the TPA
- Actuarial Studies of the County's Self-Insured Auto/General Liability program and Workers Compensation program
- Lease Agreement between the Johnson County Airport Commission and the BOCC
- User License agreements between the BOCC and various local governments and municipalities
- Johnson County Treasurer's procedures for allocating interest to the Risk Management Fund (#3070) and the Workers Compensation Fund (#3080)
- Risk Management's Ergonomic Program results for 2007
- Interviewed select County personnel who were directly and indirectly with Risk Management

### Scope Limitations

Our scope for the review of billing/collection activities related to issuing User Licenses was limited to FY 2007 only. Substantiation for FY 2006 activity had been mistakenly purged from the files and was not available for our review.

Risk Management procures a significant number of auto/general liability insurance policies to provide coverage beyond the self insured amount. Our audit scope did not include a review of the competitive procedures used to acquire those insurance policies.

Actuarial studies are performed of the County's Workers Compensation and General and Automobile Liability Programs. Risk Management uses these studies to estimate and project losses and for financial reporting and program management purposes. Our audit scope did not include a review of these studies to determine their accuracy or validity. Audit scope was limited to determine the extent to which these studies were being used for financial reporting and program management purposes.

Our audit did not include a review of the third party administrator's (TPA) timeliness in claims administration and accuracy in making payments. On a biennial basis, an independent audit is conducted of the TPA in these specific areas and we referred to those results.

The audit period included transactions from January 1, 2006, through December 31, 2007 with the exception of P-card transactions. Our review of purchases using the P-card included some 2008 transactions. We interviewed management and staff members to obtain an understanding of management and internal controls.

Our audit did not include a review of Risk Management Division's Crisis Management or Violence in the Workplace Programs.

### Computer Data

We used data from various computer systems in performing this audit including, but not limited to: The County's financial and human resources system (Oracle); Risk Management's information system, RiskMaster X; and other systems used to gather information and report on operations.

The Oracle system data has been validated by others as part of the annual audit process. We did not test the information residing in RiskMaster X but did not find anything to indicate that the data in that system was unreliable. We did not rely on any other systems other than to make selections for testing purposes.

### Statistical Sampling

We used statistical and judgment sampling to select items for review. We used statistical sampling to select testing samples in a number of audit steps. Where statistical sampling was used, we designed our samples to provide 90 percent assurance with a 5 percent margin of error.

Both sample sizes and items to be reviewed were generated by commercial statistical software. Judgment sampling was used primarily for attribute testing – procedural compliance.

We did not use statistical sampling in the review of employee expenses. We based our examination on the entire population of checks written during our audit period.