

LEGISLATIVE AUDIT COMMISSION



Review of
Department of Insurance
Two Years Ended June 30, 2014

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DEPARTMENT OF INSURANCE
TWO YEARS ENDED JUNE 30, 2014

FINDINGS/RECOMMENDATIONS - 9
IMPLEMENTED - 5
ACCEPTED - 4

REPEATED RECOMMENDATIONS - 5

PRIOR AUDIT FINDINGS/RECOMMENDATIONS - 10

This review summarizes the auditors' report of the Illinois Department of Insurance for the two years ended June 30, 2014, filed with the Legislative Audit Commission March 26, 2015. The auditors performed a compliance examination in accordance with *Government Auditing Standards* and State law.

The Department of Insurance was re-established on June 1, 2009 by Executive Order 2009-04. The Department was previously a part of the Department of Financial and Professional Regulation. The mission of the Department is to protect consumers by providing assistance and information, by efficiently regulating the insurance industry's market behavior and financial solvency, and by fostering a competitive insurance marketplace. The Department carries out this mission through effective administration and enforcement of the Illinois Insurance Code, the Illinois Pension Code and related laws and regulations. The Department is divided into ten Divisions as follows:

- Office of Legal Affairs
- Workers' Compensation Fraud
- Financial/Corporate Regulatory
- Public Pension Regulation
- Consumer Education and Protection
- Finance and Administration
- Information Technology
- Producer Regulatory Services/Property and Casualty Products
- Life and Annuities Products and Health Insurance Products and Regulation

The Department has three associated organizations as follows:

- The Office of the Special Deputy (OSD) assists the Director in carrying out the statutory responsibilities of conservator, rehabilitator or liquidator of insurance companies declared insolvent or otherwise impaired from managing their own affairs.
- The Comprehensive Health Insurance Plan (CHIP) offers health insurance to a limited number of Illinois residents who can afford but cannot find adequate health insurance coverage because of their medical or physical condition.

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- The National Association of Insurance Commissioners (NAIC) is a central organization of nationwide chief insurance regulator officials who strengthen and improve State regulation.

Andrew Boron was Director during the audit period, serving from June 2011 until January 2015 when James Stephens became Acting Director. Anne Melissa Dowling was appointed Acting Director on July 1, 2015 and she continues in that position. Ms. Dowling previously served in the Connecticut Department of Insurance after 25 years in the private sector. The average number of employees for fiscal years ended June 30 was:

2014 - 255; 2013 - 250; 2012 – 263.

Appendix A indicates service efforts by the Consumer Market Division and the Financial/Corporate Division.

Expenditures From Appropriations

The General Assembly appropriated a total of \$53.6 million to the Department of Insurance during FY14 compared to \$52.6 million in FY13. The Department received appropriations from four funds in FY14: the Insurance Financial Regulation Fund, the Insurance Producers' Administration Fund, the Public Pension Regulation Trust Fund, and the Illinois Workers' Compensation Commission Operations Fund. Appendix B summarizes the appropriations and expenditures by the Department.

Total expenditures from appropriations increased from \$37,479,995 in FY13 to \$38,581,267 in FY14, an increase of \$1.1 million, or 2.9%. The increase of \$2.6 million in expenditures from the Insurance Producers Administration Fund was due to increased personal services costs for additional personnel and increased contractual services costs. Total expenditures, including expenditures from non-appropriated funds, increased from \$48 million in FY13 to \$83.6 million in FY14 due to a \$34 million increase in expenditures from the Federal Trust Fund for the expansion of activities associated with implementing the Illinois Health Insurance Marketplace.

Lapse period expenditures for appropriated funds were \$2,365,866 in FY14, or about 6.1%.

Cash Receipts

Appendix C summarizes the Department's cash receipts during FY12-14. Total cash receipts were \$453 million in FY12, \$451 million in FY13 and \$471 million in FY14. Some of the significant changes in receipts are as follows:

- \$22 million increase in federal grant for Health Insurance Exchange Project;
- \$5.7 million decrease in fines; and
- \$2.4 million decrease in the Senior Health Insurance Program due to the transfer of SHIP to the Department on Aging.

Property and Equipment

Appendix D contains a summary of the Department of Insurance's property and equipment for the two-year period under review. The Department's property balance decreased from \$2,522,095 as of July 1, 2012 to \$2,339,693 as of June 30, 2014. These balances consist of equipment and capital lease equipment.

Accountants' Findings and Recommendations

Condensed below are the nine findings and recommendations presented in the audit report. Five of the recommendations from the prior audit were repeated. The following recommendations are classified on the basis of information provided by Tad Huskey, Chief Internal Auditor, Illinois Department of Insurance, via email received February 26, 2015.

Accepted or Implemented

- 1. Procure and implement a system utilizing advanced analytics or seek a legislative change, and 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. (Repeated-2012)**

Finding: The Department did not fully comply with the requirements of the Workers' Compensation Act.

The Workers' Compensation Fraud Unit (WCFU) 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.

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.

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.

Updated Response: Accepted, but not implemented; requires legislative remedy. The Department accepts this finding. The deficiencies noted in this finding are the result of amendments to the Workers' Compensation Act (Act) in 2011, which added Section 25.5(e-5) to the Act.

Accepted or Implemented – continued

The Department issued a Request for Information (RFI) in March 2012 to obtain information on how to draft a Request for Proposal (RFP) to obtain the advanced analytics system required by the Act. Through independent confirmations with two large workers' compensation carriers who are at the forefront of using advanced analytics to combat fraud, the Department concluded that neither the Workers' Compensation Fraud Unit nor any other division of the Department collects the type of claims and medical data necessary to perform data mining or predictive modeling required by the Act.

The Department has drafted legislation to repeal Section 25.5(e-5) of the Act and will pursue the repeal of this mandate as a means to resolve the deficiencies noted in the finding. The legislation has been proposed to the Governor's Office for consideration. The Department will also continue to recommend that the General Assembly consider whether requiring the Illinois Workers Compensation Commission, CMS, or CMS' third party administrator to procure the system required under Section 25.5(e-5) of the Act might better serve the State as CMS possesses the medical records, employment history, and other data related to the claims filed by State employees, which could be mined and analyzed by the system.

Further, the Department has developed a records retention schedule which has been approved by the Secretary of State Archives Division.

2. Allocate sufficient resources to perform the pension fund examinations every three years as required by the Pension Code. (Repeated-2012)

Finding: The Department did not fully comply 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 once every three years as required. As a result of testing auditors noted:

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

Department management indicated the Legislature did not provide an increase in the compliance fee to meet the three-year examination cycle when Public Act 95-0950 became law on August 29, 2008. Department management noted the Division has a headcount allocation for eight examiners and estimates 17 field auditors would be required to examine all 657 pension funds every three years, at a cost of \$1.6 million. To provide sufficient resources to meet the mandate, the Department indicated it would, at a minimum, need to double the current compliance fee or establish an examination assessment during the examination year.

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Further, Department management indicated they sought to include an increase in the public pension compliance fee as part of their 2013 and 2014 legislative agenda.

Updated Response: Accepted, but not implemented; requires legislative remedy. This requirement was enacted as a result of P.A. 95-0950, which was passed without an associated funding increase. Despite requests from the Department, no legislation was passed to increase the compliance fee and budget of the Public Pension Division (Division) to hire additional resources or audit staff. Therefore, the Division was required to increase its audit productivity without any additional resources. The Division is currently operating on a seven year audit cycle (down from a 12 year cycle) and is working toward the three year audit cycle.

The Division employs six field auditors and one audit manager. The Division has increased its threshold for performing desk audits (which are less time consuming than field audits, although field audits are necessary for certain larger funds) from funds with less than 30 participants to funds with less than 40 participants. This will enable the Division to complete audits on smaller funds more quickly, which will get the Division closer to the three year audit cycle.

Additionally, the Division currently has one audit manager position and one field auditor position in the process of being posted and/or filled through the CMS hiring process. Once these positions are filled and the new hires are trained, this will increase our audit staff to seven field examiners and two audit managers, which will help get the Division closer to the three year audit cycle.

Further, the Division has established procedures for review of audits and their final submission, streamlining the process from the previous procedure. We have also reduced the amount of extensions granted to funds for their response to the draft audit report in order to shorten the length of time an audit is open (after the field work is complete and the draft audit is sent to the funds), in spirit with the statute (which only gives the funds two weeks to respond). This will enable the Division to close audits more timely and perform audits more frequently.

Finally, the Division has proposed amending the language of the statute to require that the audits be performed periodically based on a risk-review of the audits, in order to utilize standard auditing procedures to performing audits on funds based on their assessed risk. This will also address the unfunded mandate in the statute requiring the three year audit cycle. The legislation has been proposed to the Governor's Office for consideration.

3. Comply with the statutory requirements of the Insurance Code. (Repeated-2006)

Finding: The Department did not fully comply with the requirements of the Illinois Insurance Code. Specifically auditors noted the following:

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- During testing of life, accident and health policy forms filed with the Department through the System for Electronic Rate and Form Filing as of June 30, 2014, auditors noted 34 of 242 filings were pending Department review or awaiting final approval or denial beyond the 60 day requirement. The policies were waiting for approval or disapproval between one to 1,434 days later than the required 60 day timeline.
- The Illinois Insurance Code requires the Director to approve or disapprove life, accident and health policy forms within 60 days after submission unless the Director extends by not more than additional 30 days the period to approve or disapprove any such form by giving written notice to the insurer of such extension before expiration of the initial 60 day period.
- During testing of 25 surplus line producer semi-annual tax statements, the auditors noted the following:
 - The Department did not correctly assess the penalty for four tax returns. The penalties for two of the returns were underpaid by \$3,604 and the other two were still outstanding for a total of \$3,600.
 - The Department failed to issue the penalty invoice for non-filing for one surplus line producer semi-annual tax statement amounting to \$2,000.
- In testing refunds, auditors noted that written requests for the refund of overpayment for two of 25 companies tested were not paid within 120 days after receipt of the request. These refunds were paid 23 and 27 days after the 120 day requirement of the statute.

Department management stated due to staffing issues, policy forms were not being approved or disapproved within the required timeframe and deadlines for payment of requests for refunds of overpayment have not been met. Department management further stated the failure to correctly assess the penalty was a result of human error and current cash receipts computer program that requires manually inserting additional penalty and/or interest charges on an existing invoice as the charges accrue.

Updated Response:

Bullet 1: Accepted, but not implemented; requires legislative remedy. The Department accepts this bullet and has made improvements in approving forms timely. It is common for most filings to involve communication back and forth between the Department and the companies submitting the filings. These communications primarily consist of the Department submitting objection notices for filings which requires the filing company to review the objection, compare with their filing, statutes, and other criteria and then respond to the objection. It is very common for the Department to have multiple objections on a filing due to the companies not responding sufficiently to the original objection, which again involves waiting on a response from the filing company for each objection. When a filing has multiple objections it is nearly impossible to approve the filing within the 60 day requirement prescribed by the statute.

It is the Department's position that when a company submits a filing, if an objection is submitted, the filing is not fit for the Illinois Marketplace, so it is put on hold until the company

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corrects the objection or clarifies the issue to the Department's satisfaction. Rather than simply disapproving the filing entirely and asking the companies to start over and pay another filing fee, the Department continues dialogue with the companies to efficiently and cost-effectively move the filings through the process.

To remedy this issue, the Department plans to involve the insurance industry in the discussion and planning to develop alternative statutory language to amend the Illinois Insurance Code (215 ILCS 5/143(1)) to allow additional time to approve filings when objections notices are filed.

Bullet 2: Accepted and partially implemented. Penalty calculations need to be automated to fully rectify this bullet. The Department accepts this bullet and has moved forward with implementing the Account Management System (AMS), which went live on October 1, 2015. All transactions are being processed through AMS and the old cash receipts system with monthly reconciliations being performed to reconcile discrepancies between the two programs.

AMS will be able to perform the function of inserting additional charges of interest and penalties; however, as of December 2015, the penalty calculations are not automated due to additional priorities that take precedence in the implementation of AMS. As a result of this process not being automated, it is possible that this bullet could be repeated during the Auditor General's FY15/16 compliance examination. As a compensating control for the lack of an automated penalty calculation process, the Department has implemented a second layer of approval to ensure the correct penalty amounts are assessed. The Department hopes to begin looking into automating this process in the first quarter of calendar year 2016, which should resolve this bullet going forward.

Bullet 3: Accepted. The Department accepts this bullet and has replaced retired staff to correct this issue going forward.

4. Comply with the Administrative Code and perform annual performance evaluations for all employees in a timely manner. (Repeated-2010)

Finding: The Department did not perform employee performance evaluations in a timely manner. During testing of the performance evaluations for 40 employees during FY13 and FY14, the following exceptions were noted:

- Two performance evaluations for the period tested were not performed.
- Fifteen (38%) performance evaluations were performed and submitted after the due dates. The time elapsed from the due date to the performance review approval ranged from three to 370 days.

During the prior examination, 19 performance evaluations were not performed and eight performance evaluations were submitted late. In the prior finding response, management stated the Department would work with the Administrative and Regulatory Shared Services Center to develop an evaluation system which will provide notifications to Department

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supervisors for evaluations due. Although the Department implemented a corrective action plan, current testing showed the Department did not complete performance evaluations for all employees in a timely manner.

Department management stated that it is always the intent of the Department to comply with the performance evaluation timeframes by continually stressing to the supervisors the importance of the evaluations being completed in a timely manner. In late FY14, a new system for tracking evaluations was put into place and the supervisor of the field staff was pulled out of the field into the office to complete all late evaluations. However, Department management stated the exceptions noted above were due to oversight.

Updated Response: Accepted, but not fully implemented due to turnover in management and supervisors. The turnover resulted in subordinate staff not having supervisors to complete their performance evaluations. The Department accepts this finding and has implemented monthly reminders sent to supervisors regarding evaluations that are due.

5. Ensure proper segregation of duties by allocating sufficient staff to process, review, approve and record tax refunds. (Repeated-2012)

Finding: The Department did not have proper segregation of duties over processing of insurance privilege tax refunds.

During testing of 23 vouchers representing insurance privilege tax refunds, auditors noted there is only one employee who receives the requests for insurance privilege tax refunds, reviews and prepares the refund authorization memo, and 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.

In the prior finding response, management stated the Department added another employee to be involved with the processing of insurance privilege tax refunds which would provide additional segregation of duties and also had implemented an additional approval level for the issuance of these refunds.

Department management stated the new staff person processing the privilege tax refunds was not informed of the additional approval level during their training for the position.

Updated Response: Accepted and fully implemented. The Department accepts this finding and has fully implemented the auditor's recommendation by implementing a process for the Deputy Director of Finance and Administration to review and approve tax refund requests prior to the refund being processed for payment.

6. Strengthen controls over submission of required Agency reports by ensuring reports are accurate and filed in a timely manner.

Finding: For two statutorily required reports the Department did not timely file one report and included inaccurate information in another report.

During testing, the following exceptions were noted:

- The amount of fees reported on the Agency Fee Imposition Reports did not agree with the Department's records. For the FY13 Agency Fee Imposition Report, 12 of 14 fees reported did not agree with Department's records. The effect of the differences resulted in the Department overstating reported fees for FY13 by \$48.6 million. For FY14, after filing of the report with the Office of the Comptroller, the Department was advised of discrepancies in the report. The Department subsequently revised its FY14 report.
- The Department did not timely submit the Agency Workforce Report for FY12 with the Office of the Governor and Secretary of State. The Agency Workforce Report is due by January 1 each year. The FY12 Agency Workforce Report was submitted to the Office of the Governor on January 14, 2013, and to the Secretary of State on January 16, 2013, 13 days and 15 days late, respectively. In addition, the Department did not accurately report the information on persons employed within the agency workforce as professionals in the FY13 and FY12 Agency Workforce Reports. The Department reported 187 of 246 (76%) employees as professional in its FY12 Agency Workforce Report and 180 of 241 (75%) employees in its FY13 report.

Department management stated the exceptions noted above were due to the following: a) inaccuracies in the Agency Imposition Fee reports were due to oversight; and b) the Department is under the Administrative and Regulatory (A&R) Shared Services and relies upon them to fill out the Agency Workforce Report. A&R Shared Services fills out the workforce report consistently among all the agencies that are part of A&R Shared Services and the method used to classify employees is consistent with the Department of Central Management Services job classification system.

Updated Response: Accepted and fully implemented.

Bullet 1: The Department agrees with the finding and has ensured the reports filed after Fiscal Year 2013 have been accurate. This issue should not be a problem going forward.

Bullet 2: The Department agrees with the finding and will ensure that Agency Workforce Reports are timely submitted going forward. Further, the Department will comply with the definition of "professional" employees established in the State Employment Records Act to ensure that the Reports are accurate.

Accepted or Implemented – continued

- 7. Ensure compliance with Fiscal Control and Internal Auditing Act (FCIAA) by allocating sufficient staff to complete audits of major system of internal accounting and administrative control to be conducted on a periodic basis so that all major systems are reviewed at least once every two years.**

Finding: The Department's internal auditing program did not fully comply with the Fiscal Control and Internal Auditing Act (FCIAA).

During testing, auditors noted there was no formal approved internal audit plan in FY13, thus no audits were performed. The Department hired a Chief Internal Auditor in February 2013 who developed a two-year internal audit plan covering the period FY14 - FY15. During FY14, there were nine specific internal operational and program audits and reviews included in the audit plan. Testing of the completed audits disclosed that the internal audit plan was not fully implemented. Only three of the nine proposed audits were completed during FY14. In addition, auditors also noted there were no audits relating to internal accounting and administrative controls for grants received or made by the Agency completed during the last two years and there were also no reviews of the design of major new electronic data processing systems and major modifications of those systems completed.

Department management stated the condition noted above was due to staffing issues in the Department.

Updated Response: Accepted and fully implemented. The Department accepts this finding and has taken appropriate corrective action to address the deficiencies noted. The Department's internal audit division has developed a two-year audit plan the past three fiscal years; however, limited resources and competing priorities have kept the internal audit division from fully implementing the audit plans. Most recently, the Department was without a Chief Internal Auditor from December of 2014 through November 15, 2015 leaving the internal audit division functioning with one staff auditor. It took additional time to fill the position due to the change in administration when positions were not being filled.

The internal audit division is in the process of completing a risk-assessment and amending the two-year audit plan for FY16 and FY17 to ensure that the requirements in the Fiscal Control and Internal Auditing Act are met given the limited personnel resources and time left in FY16. The amended audit plan will include an audit related to the internal accounting and administrative controls for grants received or made by the Department and also a pre-implementation review of the Department's new cash receipt system, Account Management System (AMS).

As of December 2015, with adequate staff and leadership in the Department's internal audit division, we do not anticipate this finding to be repeated going forward.

8. **Ensure 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. Also, ensure 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.**

Finding: The procurement of the Illinois Health Insurance Marketplace marketing and outreach campaign had several issues during the scoring of the proposals.

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.

- **Evaluation committee meetings** – The procurement file did not contain adequate documentation of who attended evaluation committee meetings. The evaluation committee was established to analyze and score the vendors' technical proposals. Instructions provided to the evaluation team required team members to attend all meetings. Officials at both the Department and the Chief Procurement Office for General Services (CPO) stated that all members of the evaluation committee attended all meetings. However, 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. References were worth 35 points of the 600 points available for the written proposals.

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.

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Vendors were penalized when the Department was unable to complete the reference checks. In the above example, the one completed reference received a perfect score of 35. However, scores of zero were used for the three uncompleted reference checks which resulted in an average score of 8.75.

The Department indicated there was no policy in place on how to handle reference checks when references fail to respond. Officials stated they relied on advice from the State Purchasing Officer at the Chief Procurement Office for General Services (CPO).

CPO officials stated that while no policy is in place, some procurements are more specific on the reference check requirements making the vendor responsible for ensuring the references will be available and responsive. Officials stated ignoring unresponsive references could penalize vendors that provided four responsive vendors compared to a vendor that was unable to do so.

- **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 ranking or on other decision to eliminate vendors, the failure to detect the errors indicates a breakdown in the internal controls over 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 which resulted in slightly different scores.

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 RFP, the vendor with the highest hourly rates but lowest media buying commission was awarded the contract. 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 and followed the policies and procedures outlined by the CPO's Office, State Purchasing Officer, and Procurement Compliance

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Monitor. The Department further stated there was no violation of the Procurement Code or procurement rules in awarding the contract to the awardee.

Response: The Chief Procurement Office agrees the scoring elements in Requests for Proposals should be closely examined and tested to ensure winning proposals are most advantageous to the State. The CPO further agrees 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.

Updated Response: Accepted and fully implemented. The Department accepts this finding. The procurement noted in the finding was for the Illinois Health Insurance Marketplace marketing and outreach campaign. The contract was procured under extreme time constraints due to the necessity to establish the exchange by open enrollment on November 1, 2013. Due to Department staff being unfamiliar with procurements for this type of service and the significant dollar amount of this procurement, the Department worked closely with the Chief Procurement Office – General Services (CPO) throughout the RFP and award process of this contract and followed the procurement policies established by the CPO. 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 welcomes the recommendations and will work to implement these recommendations going forward to ensure the Department's procurements are conducted with the utmost integrity.

9. Exercise adequate controls over expenditures for the Illinois Health Insurance Marketplace marketing and outreach contract to ensure all expenditures are appropriate.

Finding: The Department did not exercise adequate controls over expenditures for the contract of the Illinois Health Insurance Marketplace marketing and outreach campaign.

On July 12, 2013, the Department awarded a contract to implement the Illinois Health Insurance Marketplace marketing and outreach campaign. The purpose of the contract was to educate and prepare Illinois consumers for the new coverage opportunities available under the Affordable Care Act. The contract totaled \$33 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 FY14 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

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the submission of proposals. Answers to vendor questions were published as addendums to the RFP.

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 stated the vendor would be allowed to bill the state for reasonable out of pocket and incidental expenses. The State reimbursed the vendor 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.

The Department was able to provide supporting documentation showing pre-approval for one of the nine 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.

Auditors identified 19 individuals that billed at different hourly rates in November compared to January. In 15 instances, the individuals' titles were the same in both monthly reports while in four 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.

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Department management stated they interpreted the “unless otherwise agreed upon” to permit the parties to bill the expenses detailed in Appendix A. The Department also stated the contract expressly anticipated that the parties would further develop and approve a detailed Work Plan that identified the vendor’s services and the necessarily resulting Direct Costs that would be required for their implementation. After significant joint development, the parties mutually agreed on the text of a 46-page Work Plan on or about October 1, 2013, after the execution of the Contract and its Section 2.1.2 requirement that the State approve Direct Costs. Department staff indicated all costs charged by the vendor were in compliance with the descriptions and budgeted amounts established within the Work Plan. However, auditors noted that the Work Plan contained just four large budgeted amounts and no other detailed dollar amounts for direct costs. In the second year of this contract, the Department has added Direct Cost Forms to add another check on costs associated with the Contract. Finally, the Department stated individuals were not allowed to bill at multiple rates unless Get Covered Illinois 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. As the Get Covered Illinois outreach efforts evolved, some individuals’ core duties changed from project planning to project execution. Such was the case with the 18 individuals sampled in this audit that were moved to a lower billing category.

Updated Response: Accepted and fully implemented. The Department accepts this finding and will continue to closely monitor expenditures to ensure that they are appropriate and allowed within the associated contractual agreement. The review process for expenditures in Year 2 of the contract was 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 implemented a tracking document to ensure hourly rates charged by the vendor are included within the contractual agreement.

Emergency Purchases

The Illinois Procurement Code (30 ILCS 500/) states, “It is declared to be the policy of the State that the principles of competitive bidding and economical procurement practices shall be applicable to all purchases and contracts....” The law also recognizes that there will be emergency situations when it will be impossible to conduct bidding. It provides a general exemption when there exists a threat to public health or public safety, or when immediate expenditure is necessary for repairs to State property in order to protect against further loss of or damage to State Property, to prevent or minimize serious disruption in critical State services that affect health, safety, or collection of substantial State revenues, or to ensure the integrity of State records; provided, however that the term of the emergency purchase shall not exceed 90 days. A contract may be extended beyond 90 days if the chief procurement officer determines additional time is necessary and that the contract scope and duration are limited to the emergency. Prior to the execution of the extension, the chief procurement officer must hold a public hearing and provide written justification for all emergency contracts. Members of the public may present testimony.

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Notice of all emergency procurement shall be provided to the Procurement Policy Board and published in the online electronic Bulletin no later than 3 business days after the contract is awarded. Notice of intent to extend an emergency contract shall be provided to the Procurement Policy Board and published in the online electronic Bulletin at least 14 days before the public hearing.

A chief procurement officer making such emergency purchases is required to file an affidavit with the Procurement Policy Board and the Auditor General. The affidavit is to set forth the circumstance requiring the emergency purchase. The Legislative Audit Commission receives quarterly reports of all emergency purchases from the Office of the Auditor General. The Legislative Audit Commission is directed to review the purchases and to comment on abuses of the exemption.

The Department filed no emergency purchase affidavits in FY13. The audit report states that during FY14 the Department of Insurance filed one affidavit for \$306,827 for IT support for the continuation of time sensitive projects. However, this affidavit was filed with the Office of the Auditor General in the fourth quarter of FY12.

Headquarters Designations

The State Finance Act requires all State agencies to make semiannual headquarters reports to the Legislative Audit Commission. Each State agency is required to file reports of all of its officers and employees for whom official headquarters have been designated at any location other than that at which their official duties require them to spend the largest part of their working time.

The Department indicated in July 2014 that the official headquarters for 65 employees had been designated at a location other than that at which their official duties required them to spend the largest part of their working time.