

Schedule of Audit Findings and Responses

State of Washington Office of Administrative Hearings

1. **The Office of Administrative Hearings does not have adequate internal controls over payroll which resulted in a misappropriation of \$55,360.**

Background

In December, 2005, an official of the Agency informed us that management, during a review of payroll records, found the Accounting Manager was regularly generating extra payroll warrants and then cancelling them in the payroll system. We were also informed of several instances in which the Accountant Manager had been paid twice for the same payroll period.

Description of Condition

Our review of the Agency's payroll found the Accounting Manager had been misappropriating payroll payments from 1999 through 2004 and, on a regular basis, during 2005. We also found several internal control weaknesses. The Accounting Manager had incompatible duties and system capabilities. These duties included input capability in the payroll system; review and approval of all entries into the payroll system; certification of the payroll register and performance of the monthly reconciliation of the payroll system to the state's accounting system. These internal control weaknesses allowed the Accounting Manager to generate extra payments to herself and conceal the activity by cancelling the amounts in the payroll system. However, the amounts were not cancelled in the state's accounting system.

We acknowledge the Agency acted quickly to correct these weaknesses by strengthening internal controls and procedures. However, we believe the Agency's previous lack of adequate internal controls placed public resources at risk for misappropriation.

Cause of Condition

The Agency did not have adequate segregation of duties in place to ensure all payroll payments were properly authorized and independently reviewed.

Effect of Condition

The lack of segregation of duties allowed the Accounting Manager to misappropriate payroll payments totaling \$55,360 over a seven-year period.

Recommendation

We recommend the Agency establish payroll procedures that include adequate segregation of duties to protect public resources.

We recommend the Agency seek recovery of \$55,360 in misappropriated funds and \$15,825 in related audit costs from the former Accounting Manager.

We refer this matter to the Thurston County Prosecuting Attorney for any action deemed appropriate.

Any compromise or settlement of this claim must be approved in writing by the Attorney General and State Auditor as directed by state law (RCW 43.09.330).

Insurance coverage for Office employees is as follows:

Insurance Company:	Travel Casualty and Surety Insurance Company
Policy Type:	Fidelity Bond
Policy Number:	104238506
Amount of Coverage:	\$10,000,000 limit/\$500,000 deductible
Coverage Period:	August 1, 2006 to August 1, 2007

Agency's Response

The Office of Administrative Hearings (OAH) agrees with the auditor's findings and has taken the following action to strengthen internal controls and expand separation of duties for payroll processing in the agency.

The Financial Manager reviews and approves payroll reports to ensure that employees are receiving the correct salary amount each pay period. This certification of the payroll register strengthens the internal controls and allows the independent review of the payroll.

The payroll functions have been separated to help strengthen the internal controls. The Accounting Manager verifies changes in the payroll system and a Fiscal Analyst inputs the leave and attendance into the payroll system. The Financial Manager certifies the amounts listed in each payroll are true and correct charges.

A payroll cancellation report is run each pay period to ensure that no warrants are canceled without the approval of the Financial Manager.

To further segregate the duties of the Accounting Manager, the incoming mail is now distributed to each section of the fiscal unit by a designated mail person. The Accounting Manager previously received and distributed all incoming mail. The payroll checks are distributed by a Fiscal Analyst. These internal controls and segregation of duties ensure payroll payments are properly authorized.

OAH is committed to conducting an internal audit to ensure continued compliance with the recommendations of the State Auditor's Office.

Finally, the new state payroll system only allows one check per pay period for each employee. Duplicate payroll checks cannot be input into the system.

Auditor's Remarks

We appreciate the Agency's willingness to take the necessary action to improve internal controls over their payroll system.

We will review the Agency's progress implementing these controls during our next audit.

Applicable Laws and Regulations

Section 20.20.20.a of the *State Administrative and Accounting Manual* states in part:

Each agency director is responsible for establishing and maintaining an effective system of internal control throughout the agency.