



A REPORT  
TO THE  
ARIZONA LEGISLATURE

Financial Audit Division

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Management Letter

# Industrial Commission of Arizona

Year Ended June 30, 2004

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**Debra K. Davenport**  
Auditor General

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**STATE OF ARIZONA  
OFFICE OF THE  
AUDITOR GENERAL**

**DEBRA K. DAVENPORT, CPA**  
AUDITOR GENERAL

**WILLIAM THOMSON**  
DEPUTY AUDITOR GENERAL

June 21, 2005

Larry Etchechury, Director  
Industrial Commission of Arizona  
800 West Washington Street  
Phoenix, AZ 85007

Dear Mr. Etchechury:

In planning and conducting our audit of the State of Arizona for the year ended June 30, 2004, we considered the Industrial Commission's internal controls over financial reporting and tested its compliance with laws and regulations that could have a direct and material effect on the State's financial statements as required by *Government Auditing Standards*.

Specifically, we performed tests of cash; investments, including security lending transactions; revenues; receivables; expenses; capital assets; long-term debt; accrued insurance losses; related-party transactions; and financial reporting for the Commission's Special Fund.

There are no audit findings that are required to be reported by *Government Auditing Standards*. However, our audit disclosed internal control weaknesses that do not meet the reporting criteria. Management should correct these deficiencies to ensure that it fulfills its responsibility to establish and maintain adequate internal controls. Our recommendations are described in the accompanying summary.

This letter is intended solely for the information of the Commission and is not intended to be and should not be used by anyone other than the specified party. However, this letter is a matter of public record, and its distribution is not limited.

Should you have any questions concerning its contents, please let us know.

Sincerely,

Dennis L. Matheisen, CPA  
Financial Audit Director

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## The Commission needs to prepare timely financial statements

The State of Arizona must issue timely financial statements to satisfy the audit requirements imposed by federal and state laws, regulations, grant contracts and agreements, and long-term debt covenants. To help ensure that the State's financial statements are prepared and issued timely, the Department of Administration General Accounting Office (GAO) has established timelines for the individual state agencies to submit required financial information to it for inclusion in the statewide financial statements. However, the Commission did not meet GAO reporting timelines. The Commission's preliminary financial statements were not submitted to the GAO until November 11, 2004, 41 days late, and their final financial statements were not submitted to the GAO until January 27, 2005, 77 days late. These delays resulted from the Commission's not preparing timely reconciliations of financial records and not recording transactions to the general ledger in a timely manner.

To help ensure that the State's financial statements are prepared and issued in a timely manner, the Commission should implement the following procedures:

- Reconcile the financial records and post all adjustments to the general ledger within 2 weeks of the end of the month.
- Allocate the appropriate resources and monitor and enforce employee completion dates for compiling and preparing the financial statements and supporting schedules.
- Provide the GAO with complete financial statements, including notes and supporting schedules, by the deadlines established by the GAO.

## The Commission should deposit cash receipts in a timely manner

The Commission is responsible for safeguarding cash receipts. To help ensure cash receipts are safeguarded, it is essential that the Commission deposit them in a timely manner. However, the Commission did not deposit cash receipts with the State Treasurer in a timely manner. Auditors noted receipts ranging from \$1,500 to more

than \$56,000 that were deposited between 4 and 18 days after being received, with one receipt not being deposited for over 30 days.

To help ensure that cash receipts are properly controlled and safeguarded and to help maximize interest earnings, the Commission should deposit cash receipts in excess of \$500 with the State Treasurer daily.

## The Commission should develop written policies and procedures for computer operations

Written policies and procedures provide the basic framework needed for establishing employee accountability. They serve as a reference tool for employees seeking guidance on how to handle complex or infrequent transactions and offer guidance for controlling daily operations. Reliance on appropriate written policies and procedures can enhance both accountability and consistency; safeguard assets and data; and ensure continuity of services in the event of system failure. However, the Commission had not established detailed written policies and procedures over its computer operations.

The Commission should develop detailed written policies and procedures that address the following:

- Computer operations—Procedures for day-to-day operations and physical security of the computer systems to ensure that operators use the correct data, computer programs, and other resources when processing daily activity, and that computer equipment is safeguarded against theft or misuse.
- Program changes—Procedures that require proper authorization and approval of program changes, including program change requests, testing program changes, documentation of changes, and separation of responsibilities to ensure changes are not made, tested, and implemented by a single employee.
- Disaster recovery—A written plan to ensure that critical functions continue in the event of a computer system failure.



# THE INDUSTRIAL COMMISSION OF ARIZONA

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May 18, 2005

Debra K. Davenport  
Auditor General  
Office of the Auditor General  
2910 N. 44<sup>th</sup> Street, Suite 410  
Phoenix, AZ 85018

Dear Ms. Davenport:

In response to the items found in the auditor's management letter, we submit the following information.

### **Recommendation 1: The Commission needs to prepare timely financial statements.**

- The current Special Fund general ledger system has some limitations for posting monthly entries for the new State Fiscal Year while holding the previous SFY open during period the Auditor General completes the audit. With the Accounting staffing limitations, the Commission will employ a seasonal accountant to bring the Special Fund general ledger up to date by the end of the SFY.
- The Accounting Manager will put together a time schedule for completion of the various tasks related to the financial statement preparation process. The Accounting Manager will meet on a regular basis with the accounting staff working on the financial statements to be sure that the time lines are being met.
- With the additional Accounting staffing, and adherence to an incremental time schedule the Commission will be in a position to meet any deadline established by GAO for completion of the financial statements including notes and supporting schedules.



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**Recommendation 2: The Commission should deposit cash receipts in a timely manner.**

- The deposit volume varies dramatically from one week to the next especially with tax assessment checks. In the very short run, the only solution is to dedicate more staff time to deposits during peaks in activity.
- The Commission is in the process of making changes to the accounting system that in the long run will alleviate this problem. Plans are to incorporate some of the newer technologies currently used by financial institutions and merchants to clear deposits immediately.

**Recommendation 3: The Commission should develop written policies and procedures for computer operations.**

- The MIS staff is currently in the process of developing a new Special Fund accounting and information system. The plans include having comprehensive written policies and procedures for the new system. With a limited staff to develop the new system, MIS does not have the resources to develop written documentation for some of the processes of the current system mentioned below that will soon be replaced when the new system is operational.
- Computer Operations--- The batch processing jobs for the Special Fund accounting system are programmed as scripted well-defined processes. Strict control is in place so that only MIS staff has access to them and MIS staff only can execute them. They are totally restricted from any end users access. There are written MIS procedures for executing daily warrant processing.
- Physical access to the ICA Operations Center is strictly controlled. Only the MIS staff, building maintenance and security staffs have access into the Operations Center via electronic badge readers. These readers maintain a log of who entered by date and time.



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- Program Changes--- There is a defined and implemented 'Change" management procedure and documentation form that address these points. However, due to staff limitations and lack of cross training of existing staff, separation of responsibilities by different staff members to implement a required change to the system can not be done at this time.
- Disaster Recovery--- Currently, the Special Fund accounting system runs on a dedicated UNIX server, warrants and reports are generated on a line printer and laser printer respectively. The data and system software is backed-up every night and sent off site to archives. In the case of a disaster, manual accounting procedures would be the fail back option available until the hardware / software could be replaced and the system recovered. This point will be addressed in the overall Disaster Recovery plan for all ICA Computer Operations.

Sincerely,

Gary R. Norem, Manager  
Administration - Accounting

GR/sc