



**Department of Legislative Services
Office of Legislative Audits**

Maryland Insurance Administration

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Presentation to the Joint Audit Committee

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Audit Overview

- MIA licenses and regulates insurers, insurance agents, and brokers who conduct business in the State, and monitors the financial solvency of licensed insurers. As of June 30, 2014, 1,723 insurers were authorized to conduct business in the State.
 - MIA also collects taxes levied on all premiums collected by insurance companies within the State.
 - In FY 2014, MIA revenues totaled \$489 million, including \$458 million of premium taxes and transferred \$338 million to the General Fund, \$123 million to the Health Care Rate Stabilization Fund, and \$28 million to the Insurance Regulation Fund.
 - The report included 14 findings, 4 of which were repeated from the preceding audit report. OLA determined that MIA's accountability and compliance level was unsatisfactory, in accordance with the rating system OLA established in conformity with State law.
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Key Audit Issues

- A new automated premium tax system was installed without being competitively procured or properly planned.
 - Certain capabilities available under the old system were lost, adversely impacting the administration of premium tax filings.
 - One employee exercised excessive control over the procurement, system implementation, and invoice payment.
 - Security over the new system was inadequate.
- Proper controls were not established over desk audits of premium tax filings and resulting tax refunds.
 - Tax audits were not always performed properly.
 - Penalties and interest were not always properly assessed.
 - Duplicate account credit and tax refunds were issued.



Premium Tax System

MIA's procurement of a new automated premium tax system did not comply with State procurement regulations and was implemented without adequate planning (**Finding 1**).

- MIA's request for proposals to create an online payment feature for a new premium tax system that MIA was developing did not identify the technical requirements and their relative importance for bid evaluation purposes, as required by regulations. The basis for the contract award decision and amount was not documented.
 - MIA decided to significantly change the contract scope for the contractor hired to develop the online payment feature, instead of soliciting a new procurement. The contractor was directed to implement a new premium tax system using an insurance tax program developed and owned by the contractor and implemented in one other state. Total system cost at April 2014 was \$210,300.
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Premium Tax System (cont'd)

- A comprehensive development and implementation plan was not prepared for this new premium tax system, which became operational in February 2012 with basic functionality. Consequently, MIA lacked assurance that the product would meet functionality requirements, including DoIT security requirements, and would facilitate its existing business operations.

While the new system provided certain new capabilities, other capabilities that were available in the former system were lost, which had adversely impacted operations, including premium tax auditing and refunds.

- MIA did not always justify and/or obtain appropriate approvals for related contract modifications. For example, three subsequent modifications totaling \$73,040 were executed without justification and/or seeking required DoIT approval.
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Premium Tax System (cont'd)

An MIA management employee exercised excessive control over virtually all aspects of the procurement and implementation of the new premium tax system. Due to past familiarity with the successful bidder, a potential conflict of interest was created (**Finding 2**). This employee

- communicated with the eventual successful bidder to obtain rates, prior to MIA's decision to solicit for services to create an online payment feature;
 - served on a 3-member evaluation committee and although no bidders were deemed qualified by the other members, recommended to the procurement officer (a subordinate) that the contract be awarded to the aforementioned contractor;
 - recommended that the contractor install its proprietary premium tax system after the internal system development was abandoned; and
 - monitored the contractor's work, approved invoices for payment, and initiated modifications to the scope of work.
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Premium Tax System (cont'd)

- The premium tax system was not properly secured to restrict and control access and the system contractor had complete control over the system and unnecessary access to the remainder of the MIA network (**Finding 3**). The contractor was
 - responsible for program code development and placing code into production without independent review or testing,
 - defined as the primary administrator for a 3rd party online payment system, and,
 - improperly granted unrestricted access to the entire MIA internal network.

 - MIA lacked assurance that the premium tax system was properly secured and configured to protect it from external threats and unauthorized changes. For example, certain vulnerability assessments had not been performed and the tax system database and host server had not been updated for numerous security-related patches (**Finding 4**).
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Premium Tax Filings

- MIA had not established proper controls over audits of premium tax filings, and test results disclosed a number of errors (**Finding 5**).
 - Audit results were not always subject to independent review.
 - OLA tests of premium tax audits found a duplicate account credit of \$403,000, the failure to assess penalties and interest of \$283,000, and tax underpayments by two companies of \$70,200.
 - MIA had not established procedures to ensure certain premium tax payments were received by the dues dates established in law (**Finding 6**).
 - Tax payments are to be postmarked by the required filing dates, but MIA did not have a process for recording the postmark date of payments received in the mail. FY 2013 mail payments totaled \$154 million.
 - Based on available records, OLA tests identified \$156,000 of penalties and interest that could have been assessed.
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Premium Tax Filings (cont'd)

- MIA had not established proper controls over premium tax refunds (**Finding 7**).
 - Certain refunds were approved and released for payment by the same supervisory employee.
 - MIA procedures did not ensure that all refund requests were subject to an independent review and approval.
 - Five refunds totaling \$146,000 appeared to be duplicates of previously issued refunds.
 - MIA did not reconcile its records of premium tax payments with the corresponding revenues in the State's accounting records (**Finding 8**).
 - OLA tests found 33 tax payments totaling \$15.7 million received between June 2012 and July 2013 per the State's records that were not recorded in MIA's premium tax system.
 - MIA also did not reconcile the receipt of electronic checks from its online payment system to State records.
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Cash Receipts

MIA lacked accountability and control over cash receipts received at its office that totaled \$154 million during fiscal year 2013 (**Finding 10**).

- Checks received in the mail were not always immediately recorded by the individual opening the mail, but forwarded to a second individual to be logged. Furthermore, OLA tests disclosed that not all checks were logged.
- Checks were not always deposited timely.
- Independent deposit verifications were not performed and alternate procedures subsequently developed by MIA were not adequate for this purpose.



Producer Licensing

MIA issues licenses to qualified resident and nonresident individuals and business entities to act as insurance producers, who sell, solicit, or negotiate insurance contracts and contract renewals for persons issuing such contracts for compensation.

- Sufficient controls were not established for the issuance of producer licenses (**Finding 11**).
 - An independent reconciliation of receipts posted to State accounting records with transactions posted in the MIA producer licensing system was not performed.
 - Five employees could process and approve certain on-line license applications without supervisory review.
 - MIA lacked assurance that 3rd party producer licensing and pre-licensing services systems were protected against operational and security risks (**Finding 12**). For example, MIA had not performed security reviews of the service providers' operations.
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Other Issues

- The MIA project manager who monitored financial examination services' contract activity and authorized vendor payments exercised excessive control over these processes. The manager was primarily responsible for evaluating vendor proposals, compiling the related evaluation results, recommending awards to vendors, and requesting any subsequent contract modifications. Vendor payments from September 2011 to April 2014, totaled \$4.7 million (**Finding 9**).
 - Proper internal controls were not established over purchases and disbursement transactions and did not always comply with State procurement regulations (**Finding 13**). For example, certain purchases could be processed without supervisory approval and temporary personnel services totaling \$390,000 were not competitively procured.
 - Administrative access to MIA's network was excessive as six accounts were improperly classified as domain administrators (**Finding 14**).
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Conclusions

MIA should ensure that

- future procurements comply with State procurement regulations; a comprehensive plan is developed prior to system development; and the procurement, contract monitoring, and invoice approval functions are separated;
 - access to the premium tax system, including contractor access, is restricted and that its servers and applications are securely configured;
 - premium tax audits are properly completed and that penalties and interest are assessed, as applicable;
 - independent supervisory personnel are responsible for approving refunds and that premium tax records are reconciled with the corresponding State records;
 - transactions recorded in the producer licensing system are proper and that third-party systems and internal networks are properly secured; and,
 - appropriate controls are established and in effect.
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