

PRELIMINARY ANALYSIS
PERFORMANCE AUDIT
OF
WORKERS' COMPENSATION ADMINISTRATION

EMPLOYEE HEALTH MANAGEMENT DIVISION
DEPARTMENT OF MANAGEMENT AND BUDGET

EXECUTIVE DIGEST

WORKERS' COMPENSATION ADMINISTRATION

INTRODUCTION

This report, issued in June 1997, contains the results of our performance audit* of Workers' Compensation Administration, Employee Health Management, Department of Management and Budget (DMB).

AUDIT PURPOSE

This performance audit was conducted as part of the constitutional responsibility of the Office of the Auditor General. Performance audits are conducted on a priority basis related to the potential for improving effectiveness* and efficiency*.

BACKGROUND

The State has self-insured* its claims for workers' compensation* since the adoption of the Workers' Compensation Act of 1912 and has always contracted with a third party administrator* (TPA) to administer its workers' compensation claims. Since 1987, DMB has been responsible for the centralized management of the State's workers' compensation program. The Risk Management Division was responsible for these functions; however, the Division became a unit of Employee Health Management (EHM) beginning in fiscal year 1996-97.

EHM was established to improve the State's risk control policies and procedures and is responsible for the centralized purchasing of certain insurance coverage* . EHM processes monthly billings to each of the State's

* See glossary on page 31 for definition.

departments, remits payment to the TPA, and maintains and also provides summary claims information to each of the departments. EHM bills the departments for actual expenses plus administrative fees charged by the TPA and EHM.

The claims management responsibilities are coordinated between the TPA and personnel from each department or, in some cases, from each agency within a department. The departments work with the TPA to ensure that employees are eligible for the benefits they receive, receive the benefits they are due, and do not abuse the system.

According to the TPA's data, State of Michigan employees filed 7,961 injury reports during fiscal year 1994-95, with 1,232 of these injuries resulting in lost work time and compensatory payments.

In fiscal year 1995-96, EHM paid \$41.9 million to the TPA for State of Michigan workers' compensation benefits.

**AUDIT OBJECTIVES
AND CONCLUSIONS**

Audit Objective: To assess the effectiveness of the State in ensuring the accuracy of the State's workers' compensation claims.

Conclusion: Our assessment concluded that the State was generally effective in ensuring the accuracy of its workers' compensation claims. However, we noted reportable conditions* related to the removal of names from employment listings* , the addition of comment lines* to employee history files*, and the consistency of terminology in redemption* legal documents (Findings 1 through 3).

* See glossary on page 31 for definition.
07-145-96

Audit Objective: To assess the effectiveness of the State's internal control structure* over workers' compensation claims.

Conclusion: Our assessment concluded that the State's internal control structure over workers' compensation claims was generally effective. However, we noted reportable conditions related to the development of procedures for computing benefits, strengthening of the internal control structure over assault claims*, coordination of data matches with the Michigan Employment Security Commission (MESC), and the timely submission of accident reports (Finding 4 through 7).

**AUDIT SCOPE AND
METHODOLOGY**

Our audit scope was to examine the program and other records of the State of Michigan's workers' compensation administration. Our audit was conducted in accordance with generally accepted auditing standards and *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

We interviewed staff and management from EHM, the State's TPA, and six State departments to gain an understanding of the purpose and responsibilities of the State's workers' compensation program.

We reviewed EHM's oversight responsibilities for the State's workers' compensation program. We evaluated the reasonableness of the tests and monitoring performed by the State and the TPA. We examined the internal control structure.

* See glossary on page 31 for definition.
07-145-96

For our testing population, we considered all employee injuries occurring during the period October 1, 1991 through June 30, 1996. We verified the accuracy of the TPA's compensation payments, the State's 2/3 supplement* payments, and the State's assault claim payments. We reviewed legal documents for redemption settlements* for consistency in the terms and conditions. We matched employees who had waived rights to future State employment against subsequent State payroll records, the Department of Civil Service employment lists, and Michigan Employment Security Commission records. We also reviewed selected employee history files to determine if the history file identified that the employee had had a workers' compensation claim or a redemption settlement or had signed a waiver of future employment* with the State.

AGENCY RESPONSES

Our audit report includes 7 findings and 10 corresponding recommendations. DMB agreed with the recommendations.

Mr. Mark A. Murray, Director

* See glossary on page 31 for definition.

Department of Management and Budget
Lewis Cass Building
Lansing, Michigan

Dear Mr. Murray:

This is our report on the performance audit of Workers' Compensation Administration, Employee Health Management, Department of Management and Budget.

This report contains our executive digest; description of agency; audit objectives, scope, and methodology and agency responses; background; comments, findings, recommendations, and agency preliminary responses; a summary of workers' compensation claims reported, presented as supplemental information; and a glossary of acronyms and terms.

Our comments, findings, and recommendations are organized by audit objective. The agency preliminary responses were taken from the agency's responses subsequent to our audit fieldwork. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a formal response within 60 days after release of the audit report.

We appreciate the courtesy and cooperation extended to us during this audit.

AUDITOR GENERAL

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Description of Agency

The State has self-insured its claims for workers' compensation since the adoption of the Workers' Compensation Act of 1912 and has always contracted with a third party administrator (TPA) to administer its workers' compensation claims. Since 1987, the Department of Management and Budget has been responsible for the centralized management of the State's workers' compensation program. The Risk Management Division was responsible for these functions; however, the Division became a unit of Employee Health Management (EHM) beginning in fiscal year 1996-97.

EHM is responsible for processing monthly billings to each of the State's departments, remitting payment to the TPA, and maintaining and also providing summary claims information to each of the departments. EHM bills the departments for actual expenses plus administrative fees charged by the TPA and EHM.

The claims management responsibilities are coordinated between the TPA and personnel from each department or, in some cases, from each agency within a department. The departments work with the TPA to ensure that employees are eligible for the benefits they receive, receive the benefits they are due, and do not abuse the system.

According to the TPA's data, State of Michigan employees filed 7,961 injury reports during fiscal year 1994-95, with 1,232 of these injuries resulting in lost work time and compensatory payments.

In fiscal year 1995-96, EHM paid \$41.9 million to the TPA for State of Michigan workers' compensation benefits.

Audit Objectives, Scope, and Methodology and Agency Responses

Audit Objectives

Our performance audit of Workers' Compensation Administration, Employee Health Management (EHM), Department of Management and Budget (DMB), had the following objectives:

1. To assess the effectiveness of the State in ensuring the accuracy of the State's workers' compensation claims.
2. To assess the effectiveness of the State's internal control structure over workers' compensation claims.

Audit Scope

Our audit scope was to examine the State of Michigan's workers' compensation administration. Our audit was conducted in accordance with generally accepted auditing standards and *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

Audit Methodology

Our work was performed between July and December 1996. To accomplish our audit objectives, we interviewed staff and management from EHM, the State's third party administrator (TPA), and six State departments (the Departments of Community Health, Corrections, Military Affairs, and State; the Michigan Department of State Police; and the Family Independence Agency). We reviewed the Workers' Compensation Act; other statutory requirements; and policies and procedures of DMB, the Department of Civil Service, and the Department of Corrections to gain an understanding of the purpose and responsibilities of the State's workers' compensation program.

We reviewed and tested the internal control structure related to the administration of the workers' compensation program. We identified control strengths and weaknesses and then developed our detailed analysis and testing.

We reviewed EHM's oversight responsibilities for the State's workers' compensation program. We evaluated the reasonableness of the tests and monitoring performed by the State and the TPA. Also, we reviewed audit reports of other states' workers' compensation programs to identify the other states' practices for managing workers' compensation claims.

For our testing population, we considered all employee injuries occurring during the period October 1, 1991 through June 30, 1996. We tested accuracy of payroll and tax status information in the State's claims. We verified the accuracy of the TPA's compensation payments, the State's 2/3 supplement payments, the State's assault claim payments, and the State's provisions permitting employees to remain in full pay status*. We reviewed redemption agreements; redemption orders* ; and resignation, waiver, and release documents for redemption settlements for consistency in the terms and conditions. We matched employees who had received redemption settlements against subsequent State payroll records; the Department of Civil Service lay-off, rehire, and employment lists; and Michigan Employment Security Commission records. We also reviewed employee history files of selected workers' compensation claims with redemption settlements to determine if the history file identified that the employee had had a workers' compensation claim or a redemption settlement or had signed a waiver of future employment with the State.

Agency Responses

Our audit report includes 7 findings and 10 corresponding recommendations. DMB agreed with the recommendations.

The agency preliminary response which follows each recommendation in our report was taken from the agency's written comments and oral discussion subsequent to our audit fieldwork. Section 18.1462 of the *Michigan Compiled Laws* and DMB Administrative Guide procedure 1280.02 require DMB to develop a formal response to our audit findings and recommendations within 60 days after release of the audit report.

* See glossary on page 31 for definition.

Background

The Workers' Compensation Act (Sections 418.101 - 418.941 of the *Michigan Compiled Laws*) established workers' compensation benefits for employees who suffer temporary or permanent disabilities from work-related injuries and diseases. Benefits for injured employees include payments for loss of wages, medical care, vocational rehabilitation, scheduled awards* for loss of body parts, and death benefits for surviving family members. Employees are paid weekly compensation benefits* for the duration of the disability or until death.

Employees' weekly compensation benefits are based on their average weekly wages*, marital status, number of dependents, and the year the injury occurred. Tables to compute weekly compensation benefits and maximum allowed benefits are developed annually by the Department of Consumer and Industry Services. Weekly compensation benefits are based on the year of the accident and are not adjusted annually. For calendar year 1996, the maximum weekly compensation benefits was \$524. Weekly compensation benefits are offset by other disability benefits, social security, pensions, and unemployment benefits but are not offset by duty or nonduty disability retirement benefits. State employees electing to remain in full pay status while collecting workers' compensation benefits use 26.7 hours of leave credits each pay period and continue to accrue sick and annual leave credits.

Injured State employees are also entitled to a 2/3 supplement payment from their department if their weekly workers' compensation benefit is less than 2/3 of their regular gross wages including any premiums, shift differentials, etc. The employee's department personnel office is responsible for making the determination and for computing and paying the supplement. This supplement is initially authorized for 50 weeks, but it may be extended to 100 weeks with approval by the Department of Civil Service.

* See glossary on page 31 for definition.
07-145-96

Several State departments have special workers' compensation provisions for employees who have been assaulted on the job. Unlike other workers' compensation claims, the employee remains in full pay status without using sick or annual leave credits. The Departments of Corrections, Military Affairs, Community Health, and State and the Family Independence Agency each have statutory provisions for workers' compensation injuries arising from specific types of assaults. The Michigan Department of State Police has similar provisions included in the State troopers union contract. For assault claims (also referred to as 100% claims), the employee remains on the department's payroll and receives weekly compensation benefits from the third party administrator (TPA). The employee also receives a biweekly check initiated by his/her department for the difference between the employee's net wages* and the employee's weekly compensation benefits from the TPA. The employee's personnel office is responsible for computing the amount of the employee's biweekly check.

The claims processing functions begin when an employee (or supervisor) reports a work-related injury, disease, or death to the employer or the TPA. When the TPA receives the claim, it is assigned to a claims examiner. The claims examiner reviews the claim, determines the weekly compensation benefit amount, and continues to monitor the medical and compensatory benefits over the life of the claim. The employee's personnel office determines the employee's average weekly wage and whether any other State payments (for the 2/3 supplements and the assault claims) are due the employee. The personnel office is also responsible for charging the correct amount of sick or annual leave against the employee's leave balances if the employee elects to remain in full pay status.

The Workers' Compensation Act also authorizes death benefits to the surviving spouse and children of an employee who dies as the result of a job-related injury or illness. Workers' compensation death benefits are paid to the employee's spouse for 500 weeks or until remarriage. Death benefits are also paid to the employee's children until age 18.

An employee collecting workers' compensation benefits may negotiate a lump sum settlement* instead of collecting weekly benefits. There are two types of lump sum settlements: voluntary payments* and redemption settlements. With a voluntary

* See glossary on page 31 for definition.

payment, the employer and employee agree to a dollar settlement for the existing compensatory payments and medical expenses of the employee and the employee keeps his/her right to re-open the claim if there are additional related medical problems in the future. With a redemption settlement, the employee receives a single, lump sum payment from the employer for all current and future compensatory payments and medical expenses of the employee. In return the employee gives up his/her rights to any future workers' compensation benefits related to the specific claim. In many redemption settlements, the employee waives his/her rights to future employment with the State.

For the period October 1, 1991 through June 30, 1996, the TPA received 38,310 injury reports from State employees. A summary of total claims reported for the period October 1, 1991 through June 30, 1996 is presented in the supplemental information section of this report.

COMMENTS, FINDINGS, RECOMMENDATIONS, AND AGENCY PRELIMINARY RESPONSES

EFFECTIVENESS IN ENSURING CLAIMS ACCURACY

COMMENT

Audit Objective: To assess the effectiveness of the State in ensuring the accuracy of the State's workers' compensation claims.

Conclusion: Our assessment concluded that the State was generally effective in ensuring the accuracy of its workers' compensation claims. However, we noted reportable conditions related to the removal of names from employment listings, the addition of comment lines to employee history files, and the consistency of terminology in redemption legal documents. The effectiveness of the State in ensuring the accuracy of its workers' compensation claims will also be enhanced by findings included under our second audit objective.

FINDING

1. Removal of Names From Employment Listings

The Department of Management and Budget (DMB) was not effective in enforcing the terms of negotiated waivers of employment because the State had not developed controls to ensure that the names of all employees who signed waivers of employment with the State were removed from the Department of Civil Service employment listings.

The third party administrator (TPA), the Department of Attorney General, and the employee's department negotiate a redemption settlement with the employee. During the negotiations, these entities determine whether it would be in the State's best interest to redeem the case and have the employee sign a waiver of future employment with the State. The TPA and the employer take into consideration the employee's willingness to sign a waiver when determining the amount of the settlement.

Requesting an employee to waive rights* to future employment with the State is common practice when settling a workers' compensation claim.

We examined the Department of Civil Service employment listings for 79 employees who had settled their workers' compensation claims during the period October 1, 1992 through June 30, 1996. As a condition of the settlements, 60 employees received redemption settlements and waived their rights to current and future State employment. Our examination disclosed 21 employees who, as a condition of the redemption, agreed to waive their rights to re-employment with the State of Michigan but were still listed on one or two Department of Civil Service employment listings. Of the 21 employees identified in our testing:

- a. Three employees had signed waivers relinquishing their rights to future State employment but were still included in the Department of Civil Service Layoff/Recall Register. These 3 employees had received redemptions totaling \$185,000.

Departments seeking to hire employees from outside their own department must hire from the Layoff/Recall Register if there are names on this Register before they can consider persons on other employment lists. Failure to remove employees from the Layoff/Recall Register after the employees have waived their rights to future State employment almost ensures subsequent re-hiring by another department.

- b. Sixteen employees had signed waivers relinquishing their rights to future State employment but were still included in the Department of Civil Service Standard Certification and Referral List. These 16 employees had received redemptions totaling \$713,500.
- c. Two employees were on both the Department of Civil Service Layoff/Recall Register and the Standard Certification and Referral List. The 2 employees had received redemptions totaling \$188,500.

* See glossary on page 31 for definition.

If an employee's name remains on the Standard Certification and Referral List after the employee signs a waiver of employment, there is a reasonable probability that the employee may be re-hired by another department. Departments seeking to fill positions do not have knowledge that persons on either the Layoff/Recall Register or the Standard Certification and Referral List had previously signed a waiver of employment with the State.

The Department of Civil Service did not have written procedures to ensure that, after an employee signs a waiver of employment, the employee's name is removed from the Layoff/Recall Register and the Standard Certification and Referral List. DMB did not have procedures requiring the employee's department to contact the Department of Civil Service when an employee signed a waiver of future State employment.

The process of negotiating a redemption and obtaining a waiver of re-employment with the State is ineffective when there are no procedures to ensure that the names of employees who have waived their rights to future State employment are removed from the Layoff/Recall Register and the Standard Certification and Referral List. Allowing ineligible names to remain on the employment lists hampers the State's efforts to protect other departments from hiring potentially problem employees.

RECOMMENDATION

We recommend that DMB improve its effectiveness in enforcing the terms of the negotiated waivers of employment by developing controls to ensure that the names of all employees who sign waivers of employment with the State are removed from the Department of Civil Service employment listings.

AGENCY PRELIMINARY RESPONSE

DMB informed us that it will comply with this recommendation by December 31, 1997.

FINDING

2. Addition of Comment Lines to Employee History Files

DMB did not have procedures which require departments to add comment lines to an employee's history file when the department negotiated a workers' compensation redemption settlement or a voluntary payment or when an employee resigned and waived his/her rights to future State employment.

Comment lines summarize an employee's work history information (promotions, step increases, leaves of absence, transfers, etc.) which is available to all State departments. Comment lines can be a useful tool to identify previous workers' compensation activity, including employees who have received a redemption payment or a voluntary payment or who have signed a waiver of future employment with the State.

We reviewed the employee history files of 79 employees who had received either a redemption settlement or a voluntary payment to settle their workers' compensation claims during the period October 1, 1992 through June 30, 1996. The 79 employees had collected workers' compensation settlements of \$2.7 million. Our review of employee history files disclosed that only 17 (22%) of the employee history files included comments identifying a previous workers' compensation claim, a redemption settlement, or a voluntary settlement.

We also reviewed the legal files for these employees and determined that 60 of the 79 employees had agreed to resign and waive their rights to future employment with the State. In matching this information with the employee history file information, we determined that only 10 (17%) of the 60 employee history files included a comment indicating the employee's resignation and waiver of subsequent State employment. In addition, 6 (10%) of the 60 employees were still employed with the State. These 6 employees had collected redemption settlements ranging from \$5,000 to \$85,000, with a total value of \$251,900.

DMB had not developed procedures identifying when it would be appropriate for a department to add comment lines to an employee's history file. As a result, departments did not always add comment lines to employee history files after negotiating workers' compensation settlements with the employees. DMB's internal control structure for workers' compensation claims would be more effective if the

State had procedures for identifying when to add comment lines to an employee's history file. All departments review the employee history files prior to hiring employees; therefore, this information would be useful to departments considering the hiring of employees who have previous work experience with the State. This information would also help prevent departments from hiring employees who have waived their rights to future employment with the State.

RECOMMENDATION

We recommend that DMB develop procedures which require departments to add comment lines to an employee's history file when the department negotiates a workers' compensation redemption settlement or voluntary payment with the employee and also when the employee resigns and waives his/her rights to future State employment.

AGENCY PRELIMINARY RESPONSE

DMB informed us that it will comply with this recommendation by December 31, 1997.

FINDING

3. Consistency of Terminology in Redemption Legal Documents

DMB did not provide specific instructions to help ensure that redemption legal documents prepared by the Department of Attorney General consistently identified the employee's employer as the State of Michigan.

The Department of Attorney General negotiates worker's compensation claims settlements and either assigns cases to its staff or hires outside legal counsel to handle cases. The Department had developed some general procedures for handling workers' compensation settlements. However, the Department's procedures did not provide specific instructions to ensure that consistent terminology is used in each of the documents for a settlement.

The legal files for each redemption settlement include two legal documents: the redemption agreement and the redemption order. The redemption agreement is signed by the employee, the employer, and the attorneys and identifies when the injury occurred, the settlement amount, and the agreement to close the claim for

all past, present, and future claims expenses. The terms of the agreement also usually include a paragraph indicating that the employee has resigned employment, has waived all seniority rights, and agrees not to apply for re-employment. The redemption order is signed by the magistrate after approving the terms of the redemption agreement. The redemption order identifies the parties and the amount of the settlement.

The legal files may also include a resignation, waiver, and release document. This document includes wording similar to the resignation wording found in the redemption agreement. In the resignation, waiver, and release document, the employee agrees to resign employment, to waive all seniority, to release the employer from any claims, and to not apply for re-employment with the employer. As part of the settlement negotiations, both the employee and the employer may agree to waive some or all of these provisions.

DMB's ability to effectively enforce the terms of the negotiated workers' compensation settlements may be jeopardized because DMB did not have specific instructions for ensuring that standard terminology was used to identify the employer in the legal documents. We determined in our review of legal files for redemption settlements that the employer was not always properly identified as the State of Michigan.

In our review of legal files for 25 redemption settlements, we noted:

- a. In 11 files, at least one of the legal documents (redemption agreement; redemption order; or resignation, waiver and release document) did not identify the State of Michigan as the employer. Instead, the employer was identified as the department, the facility, or both.
- b. The legal documents for 7 redemption settlements did not include consistent terminology to identify the employer. For example, in 1 settlement, the redemption agreement identified the employer as the State, the department, and the facility; the redemption order identified the employer as the State and the department; and the resignation, waiver, and release document identified the employer as the facility.

- c. Fifteen files included wording in either the redemption agreement or the resignation, waiver, and release document indicating that the employee agreed to resign and not seek re-employment with the State. However, we determined that 6 of the 15 employees had returned to work for either another department or the same department.

Although the Department of Attorney General informed us that it has interpreted the employer as the State of Michigan (and all of its departments), it had not developed standard terminology to ensure that the State was always identified as the employer in the redemption legal documents. The Department also informed us that, during the settlement negotiations, employees are informed that they are expected to resign from and not seek future State employment. However, the employee may negotiate to retain rights to State employment.

DMB could strengthen the effectiveness of the claims negotiations and its ability to enforce the terms of the legal documents by developing policies and procedures with specific instructions to help ensure that the necessary legal documents are prepared with consistent terminology identifying the employer as the State of Michigan.

RECOMMENDATION

We recommend that DMB provide specific instructions to help ensure that redemption legal documents prepared by the Department of Attorney General consistently identify the employee's employer as the State of Michigan.

AGENCY PRELIMINARY RESPONSE

DMB informed us that it has complied with this recommendation and that procedures and a training guide were developed with the Department of Attorney General and disseminated to all Attorney General Workers' Compensation Attorneys. Further information will be provided to department personnel offices by December 31, 1997.

EFFECTIVENESS OF INTERNAL CONTROL STRUCTURE

COMMENT

Audit Objective: To assess the effectiveness of the State's internal control structure over workers' compensation claims.

Conclusion: Our assessment concluded that the State's internal control structure over workers' compensation claims was generally effective. However, we noted reportable conditions related to the development of procedures for computing benefits, strengthening of the internal control structure over assault claims, coordination of data matches with the Michigan Employment Security Commission (MESC), and the timely submission of accident reports. The effectiveness of the State's internal control structure over workers' compensation claims will also be enhanced by findings included under our first audit objective.

FINDING

4. Procedures for Computing Benefits

DMB had not developed detailed procedures to help ensure the consistent and accurate computation of employees' average weekly wages and weekly compensation benefits. As a result, personnel staff from five departments (the Departments of Corrections, Military Affairs, and State; the Michigan Department of State Police; and the Family Independence Agency) did not always accurately determine employees' wage and other information used to compute employees' weekly compensation benefits.

Employees' weekly compensation benefits are based on the employees' marital status, number of dependents, and average weekly wages. Section 418.371 of the *Michigan Compiled Laws* states that the average weekly wage computation is based on the employee's total wages paid in the highest 39 of the 52 weeks immediately preceding the date of injury divided by 39. The employee's department is responsible for ensuring the accuracy of the average weekly wage computation. The department provides this information along with the employee's marital status and number of dependents to the TPA. Using compensation tables developed by the State, the TPA determines the employee's weekly compensation benefit.

In 57 claims we reviewed, we found 15 errors in the computation of either the weekly compensation benefits or the average weekly wages. Individually, these errors were immaterial; however, they indicate a weakness in the internal control structure and a potential for larger errors. These included:

- a. Four departments (the Departments of Corrections, Military Affairs, and State and the Family Independence Agency) and the TPA made 15 errors in the computation of the employees' average weekly wages or the weekly compensation benefits. These errors included:
 - (1) Seven claims had errors in the average weekly wage computation because the departments did not use the correct 52-week time period. In 2 instances, these errors created additional errors in the employees' 2/3 supplement calculations. The average weekly wage is used in determining whether the employee is eligible for the 2/3 supplement.
 - (2) Three claims included computational errors in either the average weekly wage or the weekly compensation benefits.
 - (3) One claim did not include the employee's hourly premium payments in the average weekly wage computation.
 - (4) Three claims had errors because the TPA was provided an incorrect number of dependents for the employees. The number of dependents is used in calculating employees' weekly compensation benefits. One of these errors caused an offsetting error in the employee's 2/3 supplement computation.
- b. The departments and the TPA computed the 39th week of the average weekly wage computation by dividing a biweekly pay period by two instead of determining the actual weekly earnings from the time and attendance records.

If the employee's biweekly wages for the 52-week period were the same each pay period, the computation for the 39th week would have no effect. However, the biweekly earnings of most of the employees in our testing varied

from pay period to pay period because of the amount of overtime hours worked.

DMB did not have written procedures for computing the 39th week of average weekly wage computation. Departments used the State's payroll records, which record payroll information on a biweekly basis, instead of using other information which was summarized on a weekly basis.

The errors we identified were immaterial in relation to the \$2 million of workers' compensation payments we tested. The initial workers' compensation computations are calculated by staff within each State department and by TPA staff. With so many employees responsible for computing the workers' compensation calculations, it is important for DMB to develop procedures to ensure that each of the State departments correctly computes workers' compensation employee wage information and accurately reports this information to the TPA. Written procedures serve as a tool to help departments establish and maintain an effective internal control structure.

RECOMMENDATION

We recommend that DMB develop detailed procedures to help ensure the consistent and accurate computation of employees' average weekly wages and weekly compensation benefits.

AGENCY PRELIMINARY RESPONSE

DMB informed us that detailed procedures currently exist within the Personnel-Payroll Information System procedures manual. DMB will revise these procedures and redistribute them to department personnel office by December 31, 1997.

FINDING

5. Assault Claims Controls

DMB's and the departments' internal control structure over assault claims had several weaknesses.

Six State departments have provisions for employees to receive up to 100 weeks of full net pay* from the employer if the employee's workers' compensation injury was the result of an assault. The Departments of Community Health, Corrections, Military Affairs, and State and the Family Independence Agency have statutory provisions for on-the-job assaultive injuries. In addition, the Michigan Department of State Police has similar provisions within its union contract.

Employees with assault claims collect their weekly compensation benefits from the TPA. The employees also remain on their department's payroll and receive biweekly checks initiated by his/her department for the difference between their net wages and their weekly compensation benefits. Unlike other workers' compensation claims, employees with assault claims do not use sick or annual leave credits. The provisions for assault claims were established to restore the injured employee to his/her full net pay.

Our review of 25 assault claims at four departments (the Departments of Community Health and Corrections, the Michigan Department of State Police, and the Family Independence Agency) disclosed the following deficiencies:

- a. Neither DMB nor the departments had developed procedures identifying what records should be kept to document the computations for assault claims. We noted:
 - (1) Two departments (Community Health and Corrections) had not retained sufficient supporting documentation to determine the accuracy of computations for net wages paid to three employees for assault claims. Without supporting documentation, we could not determine the accuracy of the computations for assault claims.
 - (2) The Family Independence Agency had not developed controls to ensure the accuracy of assault claims computations. The department did not correctly compute the net wages paid to an employee for an assault claim. As a result, this employee was overpaid \$1,081. The department had not requested repayment of this overpayment.

* See glossary on page 31 for definition.

- b. Neither DMB nor the Department of Corrections had developed procedures to ensure that employees did not collect more compensation than was permitted by statute. The Department of Corrections permitted employees to collect more benefits than were provided for by statute and also permitted the employees to repay overpayments with deductions from their sick, annual, compensatory, and deferred leave balances.

Our testing identified two instances in which the Department allowed employees to repay overpayments of \$1,448 and \$2,425 with leave credits. By permitting the employees to use leave credits in addition to collecting their full net pay, the Department of Corrections did not comply with the statutory provisions limiting assault claims benefits to the employee's net wages. While collecting benefits on their assault claims, the two employees earned more than they would have earned while working.

When an assault injury occurs, the department places the employee on administrative leave (which does not require the employee to use personal leave credits). This allows the employee to remain in full net pay status while waiting for the weekly compensation payments to begin. When the employee's workers' compensation benefits begin, the benefits are retroactive to the date of injury. After the workers' compensation benefits begin, the department determines the gross and net wages that the employee received since the injury occurred, the amount of workers' compensation benefits that the employee collected, the difference between the two (which is the amount of net wages that the employee is entitled to), and any overpayment or underpayment to the employee. Because of this process, most employees must reimburse the department for overpayments.

RECOMMENDATIONS

We recommend that DMB strengthen its internal control structure over assault claims by:

- (a) Developing procedures to help ensure that departments retain sufficient supporting documentation for assault claims.
- (b) Working with the Family Independence Agency to develop controls to help ensure the accuracy of department assault claim computations.

- (c) Working with the Department of Corrections to develop procedures to help ensure that employees do not collect more compensation than permitted by statute.

We also recommend that DMB request that those departments with overpayments or other errors in the assault claims computations take steps to collect money from the employees.

AGENCY PRELIMINARY RESPONSE

DMB will ensure that procedures are in place regarding these areas and contact individual departments to ensure compliance. This will be accomplished by December 31, 1997.

FINDING

6. Coordination of Data Matches With MESC

DMB did not perform any periodic matches of workers' compensation claims data with Michigan Employment Security Commission (MESC) records to ensure that employees receiving both workers' compensation and MESC benefits had their benefits coordinated.

The Workers' Compensation Act and TPA procedures require that all sources of income be identified and considered in the computation of an individual's weekly workers' compensation benefits. Certain sources of income, including unemployment benefits, must be coordinated with the individual's workers' compensation benefits. TPA staff informed us that they do not perform any separate and independent verification of income with MESC, although this information is available through MESC. TPA staff informed us that they rely on the employee to identify all sources of his/her income.

By relying on information provided by the employee, the TPA was not assured that it had identified all sources of income received by the employee. Without an independent verification, it would be possible for an employee to have additional sources of income that were not identified and considered in any coordination of benefits.

MESC provided us with a computer tape of all employees collecting unemployment benefits for the test period. We developed a computer match and identified 3,095 State employees receiving workers' compensation benefits and collecting unemployment benefits during the same period. We tested 93 employees to determine whether these employees had informed the TPA of their MESC income. We identified 1 employee who had not informed the TPA of the additional source of income.

The effectiveness of DMB's internal control structure over workers' compensation payments could be strengthened if the State developed and periodically performed a computer match to identify employees receiving both workers' compensation benefits and MESC benefits. This computer match would help ensure that all employees are accurately reporting other sources of income.

RECOMMENDATION

We recommend that DMB perform periodic matches of workers' compensation claims data with MESC records to ensure that employees receiving both workers' compensation and MESC benefits have their benefits coordinated.

AGENCY PRELIMINARY RESPONSE

DMB informed us that it will work with the State's TPA to ensure compliance by December 31, 1997.

FINDING

7. Timely Submission of Accident Reports

DMB had not taken steps to ensure that State departments complied with procedures and submitted employee injury reports* in a timely manner to the State's TPA.

* See glossary on page 31 for definition.
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Employee Health Management procedures require departments to file a formal notice with the TPA as soon as possible, but no later than 10 (business) days from the date of occurrence. The TPA has 30 days from the date of injury to begin compensation payments to the employee. Section 418.801 of the *Michigan Compiled Laws* requires an employer who has notice or knowledge of an employee's injury and who fails to give notice to the insurance carrier within 30 days to pay a penalty of \$50 per day beginning on the 31st day with the total penalty not to exceed \$1,500.

In our review of claims files, we tested the timeliness of submitting claims to the TPA. Nineteen of the 56 claims were not submitted to the TPA within 14 calendar days. For these 19 claims, the departments' averaged 61 days from the date of injury until the department submitted an accident report to the TPA. The TPA did not assess the departments with penalty provisions for any of the 19 claims.

Delays in filing can unduly delay determination of compensation benefits and may incur a financial penalty to the department.

RECOMMENDATION

We recommend that DMB take steps to help ensure that State departments comply with procedures and submit employee injury reports in a timely manner to the State's TPA.

AGENCY PRELIMINARY RESPONSE

DMB informed us that steps have been taken to address this issue. In October 1996, DMB and the TPA instituted a toll-free claim reporting system for all State agencies which reduced time delays by over 40% in the first six months of operation. In addition, educational programs are being conducted by DMB to further enhance timely claim reporting. Further, DMB is collecting claim reporting data on a quarterly basis to monitor current and future compliance with claim reporting guidelines.

SUPPLEMENTAL INFORMATION

STATE OF MICHIGAN

Summary of Total Workers' Compensation Claims Reported

For the Period October 1, 1991 through June 30, 1996

<u>Department/Agency</u>	<u>Claims Reported</u>
Agriculture	151
Attorney General	56
Civil Rights	22
Civil Service	39
Commerce (1)	557
Corrections	13,255
Education	299
Environmental Quality	54
Family Independence Agency	4,634
Judicial	321
Labor (1)	776
Legislature	188
Management and Budget	578
Mental Health (2)	9,074
Military Affairs	1,016
Natural Resources	1,194
Public Health (2)	199
Secretary of State	465
State Police	1,789
Transportation	1,521
Treasury	606
Unknown (3)	<u>1,516</u>
Total	<u>38,310</u>

- (1) The Departments of Commerce and Labor became the Department of Consumer and Industry Services on May 15, 1996.
- (2) The Departments of Mental Health and Public Health became the Department of Community Health on April 1, 1996.
- (3) The Michigan Jobs Commission received department status on December 16, 1994. Its claims are primarily presented in the "Unknown" category.

Glossary of Acronyms and Terms

assault claims	Claims from specific departments (the Departments of Community Health, Corrections, Military Affairs, and State; the Michigan Department of State Police; and the Family Independence Agency) for employees who are assaulted on the job. Unlike other workers' compensation claims, the employee remains in full pay status without using sick or annual leave credits if the injury meets the statutory or contractual provisions for assault claims. These are also referred to as 100% claims.
Average weekly wage	The employee's total wages paid in the highest 39 of the 52 weeks immediately preceding the date of the injury divided by 39. Total wages include premium and overtime wages.
Comment lines	Information included in an employee's history file which is available to all departments. Comment lines summarize the employee's work history, including promotions, step increases, leaves of absence, transfers, etc.
DMB	Department of Management and Budget.
Effectiveness	Program success in achieving mission and goals.
Efficiency	Achieving the most outputs and outcomes practical for the amount of resources applied or minimizing the amount of resources required to attain a certain level of outputs or outcomes.
EMH	Employee Health Management.
Employee history files	The State's historical record of an employee's personnel information (promotions, step increases, leaves of absence, transfers, etc.).

employee injury reports	Reports used to inform the employer and TPA of a workers' compensation injury.
Employment listings	Department of Civil Service lists used by departments for hiring employees. These listings include the Layoff/Recall Register and the Standard Certification and Referral List.
Full net pay	An employee's after-tax earnings for 80 regular hours at his/her hourly wage.
Full pay status	A condition when the employee is allowed to accrue leave credits and continuous service hours although not working.
Insurance coverage	A contract for a specific time period to protect an entity against financial losses arising from accident, injury, theft, etc., which involves transferring risk from an entity to a group for a set premium.
Internal control structure	The management control environment, management information system, and control policies and procedures established by management to provide reasonable assurance that goals are met; that resources are used in compliance with laws and regulations; and that valid and reliable performance related information is obtained and reported.
Lump sum settlement	The fixed amount agreed to close all existing liability on a claim.
MESC	Michigan Employment Security Commission.
Net wages	An employee's after tax earnings.
Performance audit	An economy and efficiency audit or a program that is designed to provide an independent assessment of the performance of a governmental entity, program, activity, or function to improve public accountability and to facilitate decision making by parties responsible for overseeing or

initiating corrective action.

Redemption	A claim that has been canceled and settled for a fixed amount to cover any current or future expenses.
Redemption orders	The legal orders approving a redemption settlement.
Redemption settlement	The fixed amount that the injured party and the employer have agreed to for any current or future expenses related to the injury.
Reportable condition	A matter coming to the auditor's attention that, in his/her judgment, should be communicated because it represents either an opportunity for improvement or a significant deficiency in management's ability to operate a program in an effective and efficient manner.
Scheduled awards	Financial awards based on statute that specify the number of weeks' compensation that will be awarded to employees for the permanent loss, or loss of use, of a specific body part (e.g., hand, arm, leg, or finger).
Self-insurance	An entity's retention of risk of loss, rather than transferring that risk to an independent third party through the purchase of an insurance policy. The retention of risk is sometimes accompanied by the setting aside of assets to fund any related losses. The entity's staff or a third party administrator may handle all claims, legal, and administrative responsibilities.
Third party administrator (TPA)	An insurance company or other entity separate from the State hired to administer the insurance claims expenses.
Voluntary payment	To settle a claim for a fixed amount to cover any current expenses without canceling rights to any potential future expenses.

Waived rights	Voluntarily giving up one's opportunity for employment with an employer.
Waiver of future employment	A legal document whereby the employee relinquishes his/her rights to future employment with the employer (e.g., the State) for a specific monetary settlement.
Weekly compensation benefits	The employee's weekly payment from the TPA while collecting compensation for a work-related injury. An employee's weekly compensation benefit amount is dependent on the employee's average weekly wage and tax filing status.
Workers' compensation	A statutorily required insurance to cover job-related accidental injury, disease, or death to covered employees. The insurance provides compensation for lost wages and for medical and legal expenses.
2/3 supplement	When an employee's weekly compensation benefits are less than 2/3 of the employee's regular gross wages, the employee may be eligible for a Department of Civil Service supplemental payment. The 2/3 supplement, when added to the weekly compensation benefit, will bring the employee up to 2/3 of the regular gross wages.

