



Arizona Department of Insurance and Financial Institutions
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Katie Hobbs
Governor

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Lindsey Perry, CPA, CFE
Auditor General
2910 N. 44th Street, Suite 410
Phoenix, Arizona 85018-7571

RE: Auditor General's report, *Arizona Department of Insurance and Financial Institutions - Performance audit and sunset review*

Dear Ms. Perry:

The Arizona Department of Insurance and Financial Institutions (DIFI) has reviewed the Auditor General's report, *Arizona Department of Insurance and Financial Institutions - Performance audit and sunset review*. Attached please find DIFI's responses to the report's recommendations.

DIFI staff appreciate the opportunity to have participated in the audit process with members of your team and look forward to implementing changes to enhance the efficiency and effectiveness of carrying out DIFI's mission.

Sincerely,

Barbara D. Richardson

Barbara Richardson
Director

Finding 1: Department did not consistently consider licensee history or determine if violations were corrected and lacked a documented explanation for some enforcement actions, increasing risk of harm to public welfare and unequal treatment of licensees

Recommendation 1: The Department should ensure its enforcement actions address the violations identified by developing and implementing policies and procedures for all license types that are consistent with recommended practices, including:

Recommendation 1a: Establishing a graduated and equitable system of enforcement actions, such as civil money penalties, corrective education, monitoring, license suspension, and license revocation, to address any legal or regulatory requirements, and ensuring the enforcement actions are set sufficiently high to help compel the licensee to comply or stop operating.

Department response: The finding of the Auditor General is agreed to and a different method of dealing with the finding will be implemented.

Response explanation: DIFI will establish procedures where department staff will fully document each factor it considered in assessing an administrative penalty or action, including factors like license history, severity of the cited conduct and all mitigating and aggravating factors. Through establishing these new procedures, the Department will ensure that all enforcement actions are decided on an equitable system that maintains uniformity and consistently documents how each factor contributed to the ultimate enforcement action.

Recommendation 1b: Specifying and requiring consideration of the number or severity of violations that should trigger each level of enforcement action(s) including whether the licensee has had prior violations.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI currently considers all factors relating to a case prior to imposing an administrative action, however, as discussed in 1a, DIFI will establish a process under which any reviewing party will be required to document all factors that were considered relating to an enforcement action, including the number and severity of violations.

Recommendation 1c: Working with licensees who have committed violations as needed—such as through written reports or examinations—to determine whether the problem has been corrected or whether additional enforcement action is needed.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will revise its current processes to incorporate the use of corrective action plans aimed at ensuring that licensees have corrected their actions and ensure compliance with the law. Under this process, DIFI, at its discretion, will place certain licensees on an agreed upon corrective action plan. Under the plan, the licensee might have to provide quarterly submissions of compliance, and attest to all actions the licensee has taken in order to remedy the cited violations.

Recommendation 1d: Documenting an explanation for how it determined enforcement actions, including its consideration of the number or severity of violations and aggravating and/or mitigating factors.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: As discussed in 1a, DIFI will implement a process under which all reviewing parties will provide better documentation and explanation in support of the recommended administrative action.

Finding 2: Department did not comply with some State conflict-of-interest requirements, increasing risk that employees and board/committee members did not disclose substantial interests that might influence or could affect their official conduct

Recommendation 2: The Department should revise its conflict-of-interest disclosure form to include the disclosure of substantial decision-making interests to help ensure employees and board/committee members comply with conflict-of-interest statutes.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI is currently updating its conflict of interest procedures and forms. DIFI will further implement more training opportunities for employees and board members to better educate them on their duties under Arizona's conflict of interest laws.

Recommendation 3: The Department should revise and implement its conflict-of-interest policies to include all State conflict-of-interest requirements and further align them with recommended practices, including:

Recommendation 3a: Storing all substantial interest disclosures, including disclosure forms and meeting minutes, in a special disclosure file available for public inspection.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI's revised policies will comply with all applicable conflict of interest laws.

Recommendation 3b: Establishing a process to review and remediate disclosed conflicts by board/committee members.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI's revised policies will include board member specific procedures relating to conflict of interest review and remediation.

Recommendation 3c: Developing guidance for board/committee members to fully disclose substantial interests related to meeting agenda items either through a signed document or during public meetings and documenting these disclosures in the board/committee's meeting minutes,

including the name of the person with an interest (i.e., board/committee member or board/committee member's relative), the interest's description, and the reason the board/committee member is refraining from discussing or otherwise participating.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI's revised policies will include board member specific procedures relating to the disclosure of potential conflict of interests.

Recommendation 3d: Establishing a centralized process to track and monitor whether each board/committee member has annually completed a disclosure form in line with Department policy.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI's new policy will establish a process to track and monitor whether each board member has completed their conflict of interest disclosure or updated disclosure form.

Recommendation 4: The Department should continue to implement its policies and procedures requiring Department staff to review and verify that the IRO's individual reviewers have signed the Department form attesting that they have met the statutory requirement of not having a conflict of interest with the healthcare appeal case reviewed.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will continue to consistently follow its policies in reviewing IRO applications.

Sunset Factor 2: The Department's effectiveness and efficiency in fulfilling its key statutory objectives and purposes.

Recommendation 5: The Department should continue to prioritize, assign, and investigate all high-priority fraud referrals.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: In April 1, 2023 the Department made changes to its referral processes. The new process defines high priority cases and ensures that such cases are timely reviewed and assigned for further investigation. The Department will continue to prioritize, assign and investigate all high-priority fraud referrals.

Recommendation 6: The Department should revise and implement its collection agency initial licensing policies and procedures to include a process for obtaining documentation from initial collection agency licensing applicants to determine they have not defaulted on any payments collected or received for a customer.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will revise and implement its collection agency initial licensing procedures to obtain documents relating to the entity's active manager defaulting on any payments collected or received for another.

Recommendation 7: The Department should implement its policies and procedures for conducting quarterly reviews of all workers' compensation claims handled by its contracted third party, including documenting the results of its quarterly reviews.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI currently conducts quarterly reviews, however, it will revise its current policies to include proper documentation of the results of each quarterly review.

Recommendation 8: The Department should work with DPS to determine what information it can collect to ensure that monies appropriated to the Task Force are used to pay for 75 percent of the personal services and employee-related expenses for city, town, and county sworn officers participating on the Task Force and implement a process for reviewing the information it collects from DPS.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: AATA staff met with Department of Public Safety budget staff on July 25th, 2024, to discuss this expected recommendation. DPS committed to provide an annual summary that will include the total cost of each outside agency detective's salary and ERE and the amount reimbursed to the agency to ensure the 75% reimbursement requirement was met. AATA staff will determine a location to archive this DPS attestation.

Recommendation 9: The Department should ensure ATA vertical prosecution grant monies are used consistent with grant and statutory requirements by:

Recommendation 9a: Requiring Department staff to document their review of vertical prosecution grant information it receives, ensuring all grant expenditure information it receives is accurate, complete, and that discrepancies are investigated and resolved.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: AATA staff will ensure recent revisions to Contract Compliance Review (CCR) policy and procedure adequately promote accuracy, completeness, and allow for discrepancies to be investigated and resolved. This recommendation will be accomplished through the development of enhanced checklists.

Recommendation 9b: Implementing a supervisory review process to review staff's documentation of its review of vertical prosecution grant information received, ensuring any noted discrepancies were investigated and resolved, and information was consistent with grant and statutory requirements.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The AATA staff practice has been to have the grant administrator, budget administrator, and the AATA director present for the Contract Compliance Review process. AATA staff routinely reviews the relevant agencies to determine the level of contract compliance. If documents or other information were found to be deficient, the grants administrator would request follow-up from the agency and the additional information would be reviewed when submitted, until staff was satisfied with the agency response. To satisfy this recommendation, AATA staff will separate this review into two phases: a staff review consisting of the grant and budget administrators, and a supervisory review of the documentation and findings by the AATA director.

Recommendation 10: The Department should ensure ATA law enforcement grant monies are used consistent with grant and statutory requirements by developing and implementing written procedures for reviewing grantee expenditure reports, invoices, and other documents provided by law enforcement agencies to demonstrate how grant monies were used and ensuring law enforcement grant monies were spent in accordance with grant requirements.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: AATA staff met on May 16, 2024 to review and revise the Contract Compliance Review policy and procedures to ensure all grants, not just Vertical Prosecution, are reviewed using the same criteria previously outlined in the Vertical Prosecution CCR policy and procedures. While AATA staff believes the Law Enforcement grants have been reviewed in this manner in practice, the development of written procedures within the policy and procedure documents is in process of being accomplished.

Recommendation 11: The Department should review long-term care insurance rate filings within 60 days, as required by statute.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department's procedures and policies have been revised for the review of LTC rate filings. The new processes have been implemented for several months which has led to an immediate decrease in filings that were dated over the 60 days, as defined in statute.

Recommendation 12: The Department should revise and implement its policies and procedures to include all aspects of its revised process for reviewing and approving long-term care insurance rates, including:

Recommendation 12a: Procedures for tracking its progress for all key review steps, such as contracted actuary review completion date, recommended outcome, date routed to staff actuary for review, and final outcome.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department's new policies for tracking all LTC rate filings with a shared tracking system ensures that the senior analyst, in-house actuary and the life and health oversight manager can be updated in real time to more accurately reflect the specific location of the file during the review process.

Recommendation 12b: Procedures requiring a supervisory review of information recorded on its tracking spreadsheet to ensure information is complete and accurate so it can accurately monitor the status of the filings it receives.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department's life and health manager currently reviews the division's tracking spreadsheet for accuracy on a weekly basis under the Department's new process.

Recommendation 13: The Department should evaluate whether its new process for reviewing long-term care insurance rate filings has facilitated its ability to review and approve long-term care insurance rate filings within its statutory time frame of 60 days, and determine what changes to its process, if any, are needed to ensure filings are reviewed within its statutory time frame. The Department should make corresponding changes to its policies and procedures, as needed.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: Recommendation 13 was initiated about 8 months ago and continued to develop over the last few months. The Department's policies and procedures system has now been updated with its new process. Recommendation 13 implementation has yielded significant progress since changes to the LTC rate filing process were implemented.

Recommendation 14: The Department should require its Chief Information Officer to develop and implement a written plan that outlines key steps it will take to develop and implement all required IT security procedures in line with ADOHS requirements, including outlining associated completion deadlines and assigned staff responsibilities. The plan should include steps for further revising the Department's incident response plan and account management procedures to include:

Recommendation 14a: Incident response plan testing requirements to allow the Department to make applicable modifications to its plan based on the testing results and providing training to those individuals responsible for carrying out the plan when an incident occurs.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will review its current policies and expand upon its payment card industry incident response plan testing to incorporate testing of all areas, including the use of the results of such testing to improve its preparedness.

Recommendation 14b: Specific procedures for restricting access to IT systems, including steps for identifying user responsibilities when granting user access to Department-used systems to help

ensure proper segregation of duties, limiting privileged/super-user accounts, and steps for monitoring the use of agency system accounts, including those granted to vendors.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will work on designing processes and procedures to provide greater definition of access level for on boarding and role assignments.

Recommendation 15: The Department should hold the Chief Information Officer accountable to the written plan outlined in recommendation 14, including requiring the Chief Information Officer to provide quarterly written progress reports to the Department director.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will implement processes that ensure all responsible personnel provide updates on compliance with all internal policies.

Recommendation 16: The Department should, once it has developed all required IT policies and procedures, provide training to its employees on these policies and procedures.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will provide training to its employees on any new policies relating to the Department's IT functions and procedures.

Recommendation 17: The Department should work with ASET to define and document the scope of IT security services ASET provides to the Department and ensure that ASET provides these services.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI has been working with ASET on an ongoing basis and will continue to improve ASET provided services.

Recommendation 18: The Department should develop and implement written policies and procedures for verifying whether initial licensing applicants applying for a licensing fee waiver meet statutory eligibility requirements for a licensure fee waiver.

Department response: The finding of the Auditor General is not agreed to, but the recommendation will be implemented.

Response explanation: DIFI currently uses attestation forms but will review other available options to ensure applicants meet the requirements for licensee fee waiver. DIFI will start to require applicants to submit a copy of their most recent tax filings, on top of the applicant's attestation.

Recommendation 19: The Department should revise and implement its collection agency renewal policies and procedures to include steps for verifying collection agency applicants' surety bond amounts comply with statute beginning with its next annual renewal application review.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will review all possible options and determine whether a statutory change is necessary in order to ensure that applicants maintain a sufficient surety bond throughout their license period, including whether licensees should provide, on an ongoing basis, reports including information that ensures compliance with the law.

Recommendation 20: The Department should continue its efforts to develop and implement a process to track and monitor that collection agency licensees have submit fictitious names reports by both July 1 and December 31 each year, as required by rule, and to follow up with licensees that do not submit the reports as required by rule.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI's new backend system, Thentia, was created with a more robust tracking system for filings. DIFI staff is now able to run reports that will show which filings have not been submitted. Once the new system is fully functional, DIFI will be able to more efficiently review missing filings and add notes to a licensee's record to ensure any missing information is submitted at renewal.

Recommendation 21: The Department should continue its efforts to address the recommendations received from CSBS and NASCUS through the accreditation reviews of its bank and credit union regulatory programs.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI is committed to addressing and implementing recommendations from CSBS and NASCUS.

Sunset Factor 4: The extent to which rules adopted by the Department are consistent with the legislative mandate.

Recommendation 22: The Department should conduct and document an assessment of the need for rules related to A.R.S. §§6-1203, 20-108.01(C), 20-211(B), and 20-235(A). Based on this assessment, the Department should adopt the required rules or work with the Legislature to revise statute(s) to remove the requirements to adopt rules.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department continues to evaluate the need for updates to its enabling statutes to address deficiencies, redundancies, and modernization efforts as necessary. The Department will continue to work with the Arizona Legislature in the future to fulfill its mission and purpose.

Sunset Factor 5: The extent to which the Department has provided appropriate public access to records, meetings, and rulemakings, including soliciting public input in making rules and decisions.

Recommendation 23: The Department should continue to revise and implement its public records policies and procedures to help it comply with the State's public records law and recommended practices, including procedures and guidance for:

Recommendation 23a: Providing requests promptly, including developing internal time frames.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will revise its public records policies and procedures to provide the requesting party with a timeframe for fulfilling a request. DIFI revised policies will aim to better inform the requestor that their request is being worked on and provide approximate timeframe by which the request might be completed, barring any unforeseen circumstances.

Recommendation 23b: Providing requestors with an anticipated time frame for providing requested records, based on the Department's resources, nature of the request, content of the records, and location of the records, and notifying the requestor of any delays, as necessary.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: As discussed in 23a, DIFI will review and revise its current policies to better inform requestors of anticipated timeframe of completion and of any unexpected delays in producing the requested records.

Recommendation 23c: Tracking and monitoring the group email inbox to ensure all records requests are recorded and responded to in line with the internal time frames or that the requestor is notified of any delays.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI is currently tracking all public record requests and will work to implement processes to notify requestors of any unexpected delays.

Recommendation 24: The Department should ensure its meeting agendas for its Mental Health Parity Advisory Committee include a notice to the public of the statutory section authorizing the executive session and provide an agenda for the executive session that states a general description of the matters to be considered.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will review the Committee's public notice and ensure that it provides all information that is required under Arizona's open meeting laws.

Recommendation 25: The Department should develop and implement policies and procedures for the Mental Health Parity Advisory Committee to ensure it complies with all open meeting law requirements, including those related to executive sessions.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will implement policies that ensure the Committee's meetings comply with all applicable open meeting laws.

Recommendation 26: The Department should revise and implement the ATA Board's policies and procedures to include the specific open meeting law requirements that need to be followed during meetings.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: AATA staff will incorporate specific open meeting law requirements into AATA policy and procedures that pertain to Board meetings.

Sunset Factor 6: The extent to which the Department timely investigated and resolved complaints that are within its jurisdiction.

Recommendation 27: The Department should investigate and resolve insurance complaints within the time frames established through its goals and policies.

Department response: The finding of the Auditor General is agreed to and a different method of dealing with the finding will be implemented.

Response explanation: DIFI consistently strives to handle all cases within the specified timeframes. However, certain extenuating circumstances may exist, such as 1) unexpected events or company system failures that result in sudden increased requests for assistance to the MRCS Division, 2) complex cases that may require a longer time to handle, 3) staff shortages, etc. DIFI will remain committed to meeting all internal time frames, barring any unexpected circumstances that could lead to reasonable delays.

Recommendation 28: The Department should revise and implement its complaint handling procedures to include time frames for:

Recommendation 28a: Following up with nonresponsive licensees that miss the deadline for responding to the complaint allegations.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will review its existing policies that address non-responsive parties, and will determine the most efficient process by which to address such instances.

Recommendation 28b: Initiating and finalizing the review of licensee responses, including documenting instances where the final review may need to exceed the established time frame based on the circumstances of the case.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will review existing policies and determine an efficient process of documenting instances where the final review may go beyond the established time frames based on circumstances.

Recommendation 29: The Department should revise and implement its case management procedures to include time frames for its investigators and supervisors to generate open complaint reports, including implementing steps for supervisors to track and monitor the timeliness of its open complaints and follow up with investigators to inquire about delays in investigating open complaints to facilitate complaint resolution.

Department response: The finding of the Auditor General is not agreed to and the recommendation will not be implemented.

Response explanation: DIFI currently tracks team member performance, which is reviewed weekly, and has sufficient case management tools and procedures in place. DIFI will review its current processes and determine if there are more efficient tools and processes to improve its case management.

Recommendation 30: The Department should revise and implement its secondary review processes to include correcting errors in its complaint tracking systems when identified.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI will review its current processes to determine if there are more efficient practices to improve its secondary review.

Recommendation 31: The Department should investigate and assess the extent of missing and incorrect dates in its complaint tracking data, such as identifying missing dates or dates that are inconsistent with the sequence of case numbers and correct any errors it identifies. Once it corrects the errors, the Department should analyze its complaint-tracking data to determine the timeliness of its open complaints, and for any open complaints that are untimely, follow up with investigators to facilitate complaint resolution.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: DIFI has already adopted this recommendation and will continue to address the recommendation under its new revised policies.

Sunset Factor 9: The extent to which changes are necessary for the Department to more efficiently and effectively fulfill its key statutory objectives and purposes or to eliminate statutory responsibilities that are no longer necessary.

Recommendation 32: The Department should work with the Legislature to make necessary statutory changes to more efficiently and effectively fulfill its key statutory objectives and purpose.

Department response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department is always ready to provide the Legislature information to identify and discuss suggestions for statutory changes. The Department has worked with the Legislature in the past and will continue to provide information.