

STATE OF LOUISIANA LEGISLATIVE AUDITOR

Office of Risk Management
Executive Department
State of Louisiana
Baton Rouge, Louisiana

November 3, 1999



Financial and Compliance Audit Division

***Daniel G. Kyle, Ph.D., CPA, CFE
Legislative Auditor***

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LEGISLATIVE AUDITOR

Daniel G. Kyle, Ph.D., CPA, CFE

DIRECTOR OF FINANCIAL AND COMPLIANCE AUDIT

Albert J. Robinson, Jr., CPA

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**OFFICE OF RISK MANAGEMENT
EXECUTIVE DEPARTMENT
STATE OF LOUISIANA
Baton Rouge, Louisiana**

**Management Letter
Dated October 20, 1999**

Under the provisions of state law, this report is a public document. A copy of this report has been submitted to the Governor, to the Attorney General, and to other public officials as required by state law. A copy of this report has been made available for public inspection at the Baton Rouge office of the Legislative Auditor.

November 3, 1999



OFFICE OF
LEGISLATIVE AUDITOR
STATE OF LOUISIANA
BATON ROUGE, LOUISIANA 70804-9397

DANIEL G. KYLE, PH.D., CPA, CFE
LEGISLATIVE AUDITOR

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October 20, 1999

**OFFICE OF RISK MANAGEMENT
EXECUTIVE DEPARTMENT
STATE OF LOUISIANA**
Baton Rouge, Louisiana

As a part of our audit of the State of Louisiana's financial statements for the year ended June 30, 1999, we conducted certain procedures at the Office of Risk Management. Our procedures included (1) a review of the office's internal controls; (2) tests of financial transactions; (3) tests of adherence to applicable laws, regulations, policies, and procedures governing financial activities; and (4) a review of compliance with prior report recommendations.

The Annual Fiscal Report of the Office of Risk Management was not audited or reviewed by us, and, accordingly, we do not express an opinion or any other form of assurance on that report. The office's accounts are an integral part of the State of Louisiana's financial statements, upon which the Louisiana Legislative Auditor expresses an opinion.

Our procedures included interviews with management personnel and other selected office personnel. We also evaluated selected documents, files, reports, systems, procedures, and policies as we considered necessary. After analyzing the data, we developed recommendations for improvement. We then discussed our findings and recommendations with appropriate management personnel before submitting this written report.

In our prior report on the Office of Risk Management for the year ended June 30, 1998, we reported findings concerning the lack of an internal audit function, the lack of review of original documentation, the overstatement of reserves for claim payments, and inadequate controls over claim payments. Management has resolved the findings relating to the review of original documentation and controls over claim payments. The findings relating to the internal audit function and overstatement of reserves for claim payments are addressed again in this report.

Based on the application of the procedures referred to previously, all significant findings are included in this report for management's consideration.

Ineffective Internal Audit Function

For the sixth consecutive year, the Office of Risk Management (ORM) did not have an effective internal audit function to examine, evaluate, and report on its internal controls and to evaluate its compliance with the policies and procedures of the control system. Considering the size of ORM's reported assets (\$177,201,678) and revenues (\$155,622,985), an effective internal audit function is needed to ensure that ORM's assets are safeguarded and that ORM's policies and procedures are uniformly applied.

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OFFICE OF RISK MANAGEMENT EXECUTIVE DEPARTMENT STATE OF LOUISIANA

Management Letter, Dated October 20, 1999

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ORM did have an employee assigned to the internal audit function for 10 months during the fiscal year. ORM hired the internal auditor on May 25, 1998. She terminated her employment on January 10, 1999, and was replaced on February 25, 1999. The second internal auditor did not function as a full-time internal auditor because on May 10, 1999, he was detailed into another position. Management does not anticipate filling this position before November 1999.

The internal auditor performed office and field reviews of payments to contract attorneys, reviews of second injury payments, reviews for duplicate payments in Corporate Systems, and reviews for Year 2000 compliance. The significant portion of the work performed resulted from Legislative Auditor findings from the June 30, 1998 audit.

While an internal auditor was present for most of the fiscal year, no formal reports were issued at the conclusion of each audit. Also, there was insufficient written documentation of audit goals, policies and procedures, work schedules, workpaper format, and risk assessment. In addition, ORM did not adequately consider training requirements for the internal auditors to ensure that the auditors were aware of current auditing standards and practices.

ORM should continue in its efforts to establish the internal audit function as an effective part of the office's control system. In addition, the office should ensure that its audits are properly planned, performed, and documented; that formal reports are issued; and that the internal auditor is adequately trained. Management did not concur with the finding. The state risk director outlined the qualifications of both internal auditors who held this position for nine months of the 1999 fiscal year. In addition, the director stated that five field audits and seven in-house audits relating to billings by contract attorneys and payroll system audits were performed during the fiscal year. Also, the director indicated that our office, in the 1998 fiscal year exit conference, told him that ORM would be in compliance with the internal audit function if two field audits were conducted during the year. Finally, the director did not agree that this was the sixth consecutive year that the internal audit function was ineffective (see Appendix A, page 1).

Additional Comments: This is the sixth consecutive year that ORM has had a finding relating to the internal audit function. Whether there are no internal auditors or ineffective internal auditors, the function remains ineffective. In addition, although finding resolution was discussed during the fiscal year 1998 exit conference, the auditors did not state that two field audits during the next year would suffice for an effective internal audit function.

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OFFICE OF RISK MANAGEMENT
EXECUTIVE DEPARTMENT
STATE OF LOUISIANA

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Overstatement of Reserves for Claim Payments

For the third consecutive year, ORM has overstated reserves for second injury claims and has not requested timely reimbursements from the Second Injury Fund. The Second Injury Fund exists to encourage the employment of physically handicapped employees who have a permanent, partial disability by protecting employers and their insurers from excess liability when a subsequent injury to such an employee merges with his preexisting disability. Louisiana Revised Statute 23:1378 divides the financial responsibility for paying second injury claims between the insurer (ORM) and the Second Injury Fund. In addition, it sets limits for insurer reserves for future payments and states that no reimbursement will be made to the insurer unless the insurer certifies compliance with those limits on reserves.

In a test of 148 open second injury claims, reserves were overstated beyond the legal limit in four claims, for a total of \$122,450. In addition, two claims were closed within the fiscal year even though reimbursements of \$10,566 were still due from the Second Injury Fund. These errors occurred because some claim adjusters did not adhere to established procedures. Failure to set reserves at the proper amount and failure to bill the Second Injury Fund timely places the office at risk of losing reimbursements from the Second Injury Fund. In addition, errors in reserves cause misstatements on the financial statements of the state of Louisiana.

ORM should comply with legal limits on reserves for second injury claim payments. Furthermore, ORM should request timely reimbursements from the Second Injury Fund. Management concurred with the finding and outlined a plan of corrective action (see Appendix A, page 3).

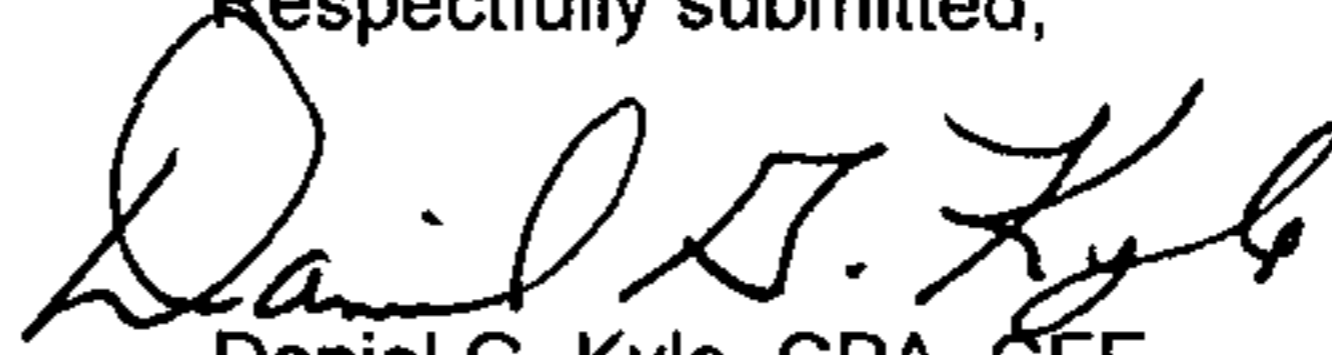
The recommendations in this report represent, in our judgment, those most likely to bring about beneficial improvements to the operations of the office. The varying nature of the recommendations, their implementation costs, and their potential impact on the operations of the office should be considered in reaching decisions on courses of action. The finding relating to the office's compliance with applicable laws and regulations should be addressed immediately by management.

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OFFICE OF RISK MANAGEMENT
EXECUTIVE DEPARTMENT
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This report is intended for the information and use of the office and its management. By provisions of state law, this report is a public document, and it has been distributed to appropriate public officials.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Daniel G. Kyle". The signature is fluid and cursive, with a large initial "D" and "K".

Daniel G. Kyle, CPA, CFE
Legislative Auditor

ALE:BJJ:PEP:dl

[ORM]

Appendix A

Management's Corrective Action Plans and Responses to the Findings and Recommendations



M. J. "MIKE" FOSTER, JR.
GOVERNOR

State of Louisiana
DIVISION OF ADMINISTRATION
OFFICE OF RISK MANAGEMENT

MARK C. DRENNEN
COMMISSIONER OF ADMINISTRATION

September 16, 1999

Dr. Daniel G. Kyle, CPA, CFE
Legislative Auditor
Office of the Legislative Auditor
State of Louisiana
Baton Rouge, LA 70804-9397

RE: Response to Legislative Audit Findings

Dear Dr. Kyle:

This is to thank you for the recent comprehensive legislative audit we received conducted by your capable staff. Since it is our desire at ORM to operate this agency effectively and efficiently, we appreciate outside review and recommendations.

Response to the finding detailed in your audit

1. Ineffective Internal Audit Function

I do **not** concur with this finding. The Office of Risk Management hired a qualified Certified Internal Auditor on May 25, 1998. She worked until her resignation date of January 10, 1999. She was replaced on February 25, 1999 by a Certified Public Accountant who was approved by Civil Service to fill the position and did so until May 10, 1999.

Both of these two individuals were well qualified for their positions. During the period of their employment, which encompassed one month in 1998 and nine months and several days in 1999, they accomplished quite a lot. They conducted five field audits and seven office audits (in-house). In addition, payroll system audits were performed in-house.

I have attached to this letter a memo from our auditor to Evon Wise wherein he outlines the audit work that has been done.

Dr. Daniel G. Kyle
September 16, 1999
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In meeting with the legislative auditors during 1998 exit conference, I was told that if we conducted two field audits in the year, the legislative auditors would be satisfied with compliance. Now we are being told that we are **not** being cited for not **having** an internal auditor (although the finding says **for the sixth consecutive year**). We are being cited because our internal audit program is ineffective.

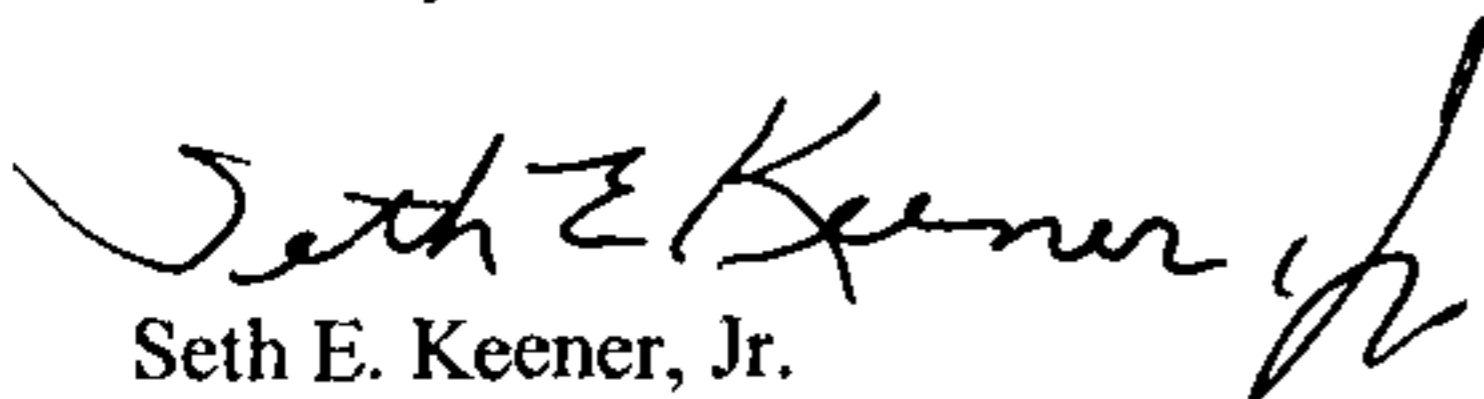
I believe the way the finding is written is contradictory. In 1998, the finding stated "Lack of Internal Audit Function". In 1999, the citation is not "Lack of Internal Audit Function" but "*Internal Audit Function is Ineffective*". And then the description is added – *For the sixth consecutive year*.

As to your comments about the format of the reports and sufficient documentation, we take your comments under advisement and will change the reports as you outlined but I do not believe the finding is properly stated.

I am attaching to this memo, a copy of a letter dated September 14, 1999 from Kiefer and Kiefer indicating that they were refunding the dollar amount we were questioning without further research.

Should you have any further questions, please advise.

Sincerely,



Seth E. Keener, Jr.
State Risk Director

SEK/ELW/tb

Attachments



M. J. "MIKE" FOSTER, JR.
GOVERNOR

State of Louisiana
DIVISION OF ADMINISTRATION
OFFICE OF RISK MANAGEMENT

MARK C. DRENNEN
COMMISSIONER OF ADMINISTRATION

September 16, 1999

Dr. Daniel G. Kyle, CPA, CFE
Legislative Auditor
Office of the Legislative Auditor
State of Louisiana
Baton Rouge, LA 70804-9397

RE: Response to Legislative Audit Findings

Dear Dr. Kyle:

This is to thank you for the recent comprehensive legislative audit we received conducted by your capable staff. Since it is our desire at ORM to operate this agency effectively and efficiently, we appreciate outside review and recommendations.

Response to the finding detailed in your audit

1. Overstatement of Reserves for Claim Payments

Although the finding is a surprise to me because I thought this issue had been taken care of last year, I do concur with the finding. Of the claims audited (148) only 2.7% were found to be overstated. Although the percentage is low, the dollar amount \$122,450 is certainly significant.

The adjusters have already been instructed to set the Second Injury Claims at the statute level for Second Injury, which is \$7,500. In order to insure that reserves are properly set, a procedure will be developed whereby the supervisor will conduct a quarterly review of Second Injury claims to determine that these reserves are set properly. A report on the review will be sent to the Director and Assistant Director.

ORM has already added a 13th factor to every employee's Performance Evaluation that grades on whether or not an employee is the cause of a Finding being rendered against the agency.

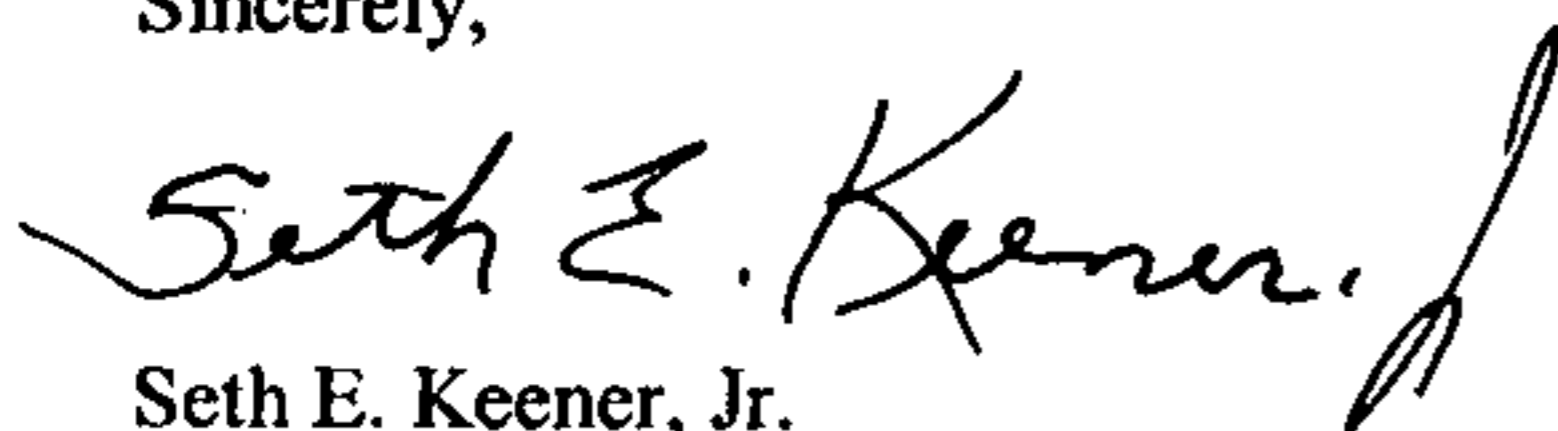
Dr. Daniel G. Kyle
September 16, 1999
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This review will be ongoing on a quarterly basis and will be conducted by the following supervisors:

Page Feller
Bertha Meisner

Should you have any further questions, please advise.

Sincerely,

A handwritten signature in cursive script that reads "Seth E. Keener, Jr." with a long, sweeping flourish at the end.

Seth E. Keener, Jr.
State Risk Director

SEK/ELW/tb