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LEGISLATIVE AUDITOR

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

DIRECTOR OF FINANCIAL AND COMPLIANCE AUDIT

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- *The program purchased modular furniture costing $125,201 without* taking competitive bids as required by the Louisiana Procurement Code. This furniture was originally purchased by the Louisiana Agricultural Finance Authority (LAFA), which is exempt from the procurement code and passed to SEGBP through LDAF. This practice has the effect of circumventing the procurement code.

Failure to follow adequate control policies and procedures in order to expedite payments increases the risk that errors or irregularities may occur and not be detected in a timely manner. Failure to enforce the terms of the lease agreement increases the risk that the program will incur unnecessary expenses. Failure to comply with state law regarding the solicitation of bids increases the risk that goods or services will not be obtained at the lowest possible cost.

Management should institute control procedures that require all expenditures to be supported by adequate, original documentation, that assure that payments related to the leased premises are actually the responsibility of the program, and that assure compliance with the Louisiana Procurement Code. In a letter dated October 21, 1996, Mr. James R. Plaisance, Executive Director, acknowledged that some of the charges were paid from handwritten unsigned notes but stated that these were prepared from original invoices in the possession of LDAF or LAFA. Copies of invoices for $4,875 of the questioned expenditures were subsequently obtained by the program. Mr. Plaisance does not believe the lease between LDAF and the program requires LDAF to pay for the wallpaper and paint costs because the expenses were related to remodeling rather than regular maintenance. Mr. Plaisance does not believe that obtaining furniture through LAFA was a violation of statute because R.S. 39:1702A(1) and 1703 allow any public procurement unit to sell to, acquire from, or use and supplies belonging to another public procurement unit independent of the requirements of the procurement code.

Additional Comments: Although the program subsequently obtained copies of invoices to support part of the payments that were made on handwritten, unsigned notes, at the time the disbursements were made the program had no assurance that the costs paid represented the expenses incurred by LDAF. Furthermore, LDAF should have born that portion of the costs that it would have reasonably incurred in the performance of regular maintenance agreed to in the contract. Although the program is allowed to acquire supplies from another public procurement unit without complying with the procurement code, the items in question were never intended to be for the use of either LDAF or LAFA but were clearly intended for use by the program at the time of acquisition. We continue to believe that the acquisition of equipment in this manner is a circumvention of the procurement code.

Inadequate Controls Over Purchasing

The SEGBP does not have sufficient controls over purchasing to ensure that supplies are ordered in reasonable quantities. A good system of internal controls would include appropriate review and approval to ensure that supplies in excess of need are not purchased. Our review of expenditures disclosed that the program purchased 600,000 internal requisition forms, at a cost of $41,273. Program personnel estimate that this quantity of forms would supply the needs of the program for the next 1,000 years. This condition occurred because of a clerical error in entering the quantity ordered that was not caught in the review process. Failure to detect errors in purchasing can result in unnecessary cost to the state.

The SEGBP should ensure that all purchases are properly reviewed to avoid purchases that are in excess of the program's need. In a letter dated January 10, 1997, Mr. James R. Plaisance, Executive Director, agreed that the error occurred. Mr. Plaisance stated that the program contacted the Office of State Purchasing to assist them with methods to ensure that this type of error does not recur. The Office of State Purchasing's response indicates that certain printing contracts are being restructured and these changes may assist in detecting unexpected cost overages. Mr. Plaisance further stated that the program would also implement its own procedures to ensure that it is aware of vendor cost estimates before orders are released.

Inadequate Controls Over Renovation Expenditures

The SEGBP bypassed controls for payment of certain expenditures related to the renovation of the claims processing unit. SEGBP also did not enforce the terms of its lease agreement with the Department of Agriculture and Forestry and made certain purchases in violation of the Louisiana Procurement Code. During our audit, we noted the following:

- The program made payments totaling $16,033 from handwritten unsigned notes. A good internal control structure requires that payments be made only from original invoices, receipts, or time sheets, to ensure that charges are authentic and to avoid duplicate payments.
- The program reimbursed $8,267 to the Louisiana Department of Agriculture and Forestry (LDAF), from which it leases office space, for the purchase of paint and wallpaper. However, the lease agreement requires LDAF to paint or paper the interior of the leased premises at least every three years if the program requests it.

premiums were intended to cover. Our interviews with agency personnel indicate that there were discussions among the fiscal officer, the fiscal manager, and the executive director before the decision was made not to accrue this large expenditure. Furthermore, the recognition of the revenue in one fiscal period while not recognizing the liability associated with that revenue until the subsequent fiscal period is an inconsistent application of accounting principles. We therefore believe that this condition, although corrected, is reportable.

Inadequate Controls Over Premium Revenue

The SEGBP does not have an adequate internal control structure over its premium revenues of $424,105,231. A good system of internal control would include procedures to ensure that the program receives all monies to which it is entitled and to ensure that revenue and receivables are accurately reported. During our audit, we noted the following:

- The program does not reconcile premium invoices sent to participating agencies with payments received. Currently, the program only compares change documents, sent in with payments, against the invoice exception reports generated by the program. However, no verification of the total revised invoice to the check amount is made.

- The program understated revenue and receivables by $721,830 because of poor communication between the receivables section, which determines the period in which premium revenue was earned, and the fiscal section, which prepares the financial statements. An audit adjustment correcting this error was prepared and accepted by the program.

Failure to reconcile premium invoices to payments received increases the risk that the program will not collect all amounts to which it is entitled. Failure to prepare accurate financial statements can result in inaccurate financial statements for the state of Louisiana.

The SEGBP should reconcile premium revenue to amounts billed and ensure that the financial statements contain accurate information. In a letter dated December 11, 1996, Mr. James R. Plaisance, Executive Director, concurred with the finding. Mr. Plaisance stated that invoices were reconciled to eligibility information but in the future, invoices would be reconciled to both eligibility information and payments received. Mr. Plaisance also stated that procedures have been implemented to assist in reporting revenues and receivables in the proper fiscal year.

STATE OF LOUISIANA
LEGISLATIVE AUDITOR

State Employees Group Benefits Program
State of Louisiana
Baton Rouge, Louisiana

April 16, 1997

Financial and Compliance Audit Division

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

STATE EMPLOYEES GROUP BENEFITS PROGRAM
STATE OF LOUISIANA
Baton Rouge, Louisiana

Management Letter
Dated February 18, 1997

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.

April 16, 1997

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

By provisions of state law, this report is a public document, and it has been distributed to appropriate public officials.

Respectfully submitted,

Daniel G. Kyle, CPA, CFE
Legislative Auditor

MCF:MWB:dl

[SEGBP]

that constitute a weakness in internal control. The program should take all steps possible to prevent the entering and payment of false claims.

Inadequate Controls Over Financial Reporting

The SEGBP does not have adequate controls in place to ensure compliance with financial reporting regulations and failed to record $10,960,056 of expenditures in accordance with state regulations. R.S. 39:80 requires the commissioner of administration to prepare annual financial statements for the state of Louisiana in accordance with generally accepted accounting principles. To accomplish this task, the commissioner issued Policy and Procedure Memorandum No. 68 (PPM 68) specifying that revenue should be recognized in the fiscal year in which economic activity generates the revenue. Expenditures, with the exception of payroll, should be recognized in the year in which liability for the expenditure occurs. In addition, the Division of Administration issues written instructions each year to assist agencies in preparing their annual financial report in accordance with PPM 68. Good internal controls would require review procedures to determine that these reporting requirements and instructions have been followed.

Of the unreported expenditures, $10,959,703 represents that portion of fiscal year 1996 health insurance premiums that were due to health maintenance organizations (HMOs). Although the program recorded the collection of the revenue, it failed to record the associated obligation (expenditure) to the contracting HMOs. The fiscal officer and fiscal manager were aware of the need to record the expenditure; however, the decision was made not to report the expenditure after discussion with the executive director. Had this error not been detected by the external auditor, the liabilities and expenditures on Louisiana's comprehensive annual financial report would have been understated by $10,960,056.

The SEGBP should establish and follow review procedures to ensure compliance with PPM 68 and the instructions of the Division of Administration when preparing its annual financial report. In a letter dated December 11, 1996, Mr. James R. Plaisance, Executive Director, concurred with this finding but objects to its reporting because the financial statements were corrected and resubmitted to the Division of Administration upon discovery of the error by the auditor. Mr. Plaisance also stated that the error occurred because of a misunderstanding concerning the period for which the premiums were submitted.

Additional Comments: We concur that the program corrected and resubmitted its financial statements after this error was detected by the auditor. However, we believe the matter is more complicated than a simple misunderstanding of the period of time the for the delay in processing. R.S. 22:656 requires the program to pay death claims within 60 days from the date of receipt of proof of death. Our test of paid claims disclosed the following:

- Thirty-three of 86 health claims tested totaling $18,126 were paid from 31 to 249 days after receipt. Management attributes these delays to problems experienced during the conversion to a new claims processing system and to understaffing in the claims processing section. This is the fourth consecutive year that we have reported this finding.

- Seven of 25 death claims tested totaling $83,000 were paid 68 to 95 days after receipt of proof of death. The program did not pay interest of $1,471 that was due on these claims. These delays in processing death claims are due in part to a lack of procedures requiring the timely mailing of a required Internal Revenue Service letter to the beneficiary. This is the second consecutive year that we have reported this finding.

Failure to pay claims timely can result in the assessment of penalties against the program. Management of the program should ensure that all health and death claims are processed within the time limitations imposed by state law unless the program can demonstrate just and reasonable cause for delay. The interest due on the late death claims should be remitted to the appropriate beneficiaries. In a letter dated September 24, 1996, Mr. James, R. Plaisance, Executive Director, stated that a sample of 86 from a population of 1.6 million claims paid is not sufficient to conclude that 38 percent of claims were not paid within the 30-day window allowed by law. Mr. Plaisance stated that statistics for the entire year indicate that 70 percent of total claims were paid timely and that the program's performance improved during the latter part of the fiscal year. Furthermore, Mr. Plaisance stated that the claims processing system used by the program is used throughout the insurance industry and does not allow the program to capture data which would prove that the delay in processing the claim was due to the claimant or the program. Mr. Plaisance concurred with the finding regarding death claims.

Additional Comments: R.S. 22:657(A) does not indicate that any error is acceptable. While we do concur with Mr. Plaisance's statement that the program made significant progress in reducing the error rate in the latter months of the fiscal year, this improvement did not reduce the average noncompliance rate for the year to an insignificant level. Although the computer used by the department may be widely used in the insurance industry, private insurance companies are not subject to the laws and regulations specific to State Employees Group Benefits. The program must be able to satisfy all legal requirements as well as running an efficient and effective program. The program was given the opportunity to prove that all sampled items which were not paid within 30 days were due to defects in the claims. For the 33 claims cited, the program was not able to do so.

Electronic Claims Processing Control Weaknesses

The SEGBP has not established an adequate internal control structure over the electronic claims processing system. An adequate internal control structure requires that controls be developed and maintained to ensure the integrity of the system and the information it generates. Furthermore, no one employee should be placed in a position that could both initiate and conceal errors or irregularities. The claims processing system is used to make approximately $232 million of payments annually.

During our review of the system, we noted the following:

- At the time of conversion from the prior electronic claims processing system (DataPoint) to the current system, Resource Information Management System (RIMS), plan members' claims histories were downloaded into RIMS. However, there was not a complete mapping between DataPoint claims codes and RIMS codes causing the RIMS to be unable, in some instances, to identify a claim as a duplicate if plan members or providers resubmitted claims previously paid in DataPoint. Thus, duplicate payments resulted. Management developed a computer program that identified possible duplicate payments due to the conversion. This computer program produced a report that was separated into 12 phases. Dollar amounts of duplicate payments due to the conversion were not accumulated or estimated for phases one through 6. For phases 7 through 12, the program identified conversion duplicates in the amount of $178,921. Total duplicate payments, which included conversion duplicates, totaled $1,636,747 for fiscal year 1996. This is the second consecutive year that we have reported this finding.

- The program made overpayments through RIMS, totaling $987,677, when paying Preferred Provider Organizations (PPOs). This condition occurred because SEGBP made an error in programming its computer system to compute outliers (a discount rate for PPOs).

- Claims examiners have access to the RIMS that allows them to both input and adjudicate (pay) claims. Furthermore, the plan administration manager has incompatible access that allows her to input and adjudicate claims, set up and maintain provider information, set up and modify plan parameters, and assign security levels. False claims could be input and adjudicated through this incompatible access and not be detected in a timely manner. This condition occurred because RIMS is a packaged software program that management elected not to modify to prevent inappropriate access and because the plan administration manager's access has not been properly limited. This is the second consecutive year we have reported that claims examiners have incompatible access to RIMS.

Management emphasis was not directed toward developing and implementing the necessary controls to safeguard the system. Failure to institute the necessary controls places the integrity of the system and the information generated by it at risk. In addition, if controls are weak, unauthorized individuals may have access to and the ability to read or alter information without anyone knowing the information has been accessed or altered.

Management of SEGBP should establish procedures that will identify duplicate claims so that duplicate payments can be identified and prevented, allow for the timely review and testing of outlier computations so that overpayments to PPOs can be prevented, and eliminate incompatible access currently granted to claim examiners and the plan administration manager. In a letter dated October 16, 1996, Mr. James R. Plaisance, Executive Director, stated that the program has identified approximately $423,000 of overpayments due to errors related to the conversion. This figure was obtained through October 1995 and Mr. Plaisance does not believe this finding should be repeated. Additional work was done from October 1995 through the end of the fiscal year and identified another $260,000 of overpayments. Mr. Plaisance does not believe that the overpayments due to the programming error should be reported because it was originally detected by program personnel and subsequently corrected. Mr. Plaisance believes that it is appropriate for claims examiners to both input and adjudicate claims because the program uses packaged software that is widely accepted by the insurance industry and that software allows this access. He also does not believe that the plan administration manager has inappropriate access but, nevertheless, agreed to limit her access.

Additional Comments: The finding related to overpayments due to conversions is reported as a repeat finding because only four months of the 1996 fiscal year were worked by June 30, 1996. Although the remaining eight months were subsequently worked to identify potential overpayments due to this error, we do not believe that sufficient progress had been made by the end of the fiscal year to remove this reportable condition. We agree that it is laudable that program personnel discovered the programming error which resulted in $987,677 of overpayments. However, it does not relieve our responsibility to report significant errors that occurred during the year. We continue to maintain that entering and adjudicating claims are incompatible functions

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

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

1600 NORTH THIRD STREET
POST OFFICE BOX 94397
TELEPHONE: (504) 339-3800
FACSIMILE: (504) 339-3870

February 18, 1997

STATE EMPLOYEES GROUP BENEFITS PROGRAM
STATE OF LOUISIANA
Baton Rouge, Louisiana

As part of our audit of the State of Louisiana's financial statements for the year ended June 30, 1996, we conducted certain procedures at the State Employees Group Benefits Program. Our procedures included (1) a review of the program's internal control structure; (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 year report recommendations.

The June 30, 1996, Annual Fiscal Report of the State Employees Group Benefits Program 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 program'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 selected program personnel. We also evaluated selected documents, files, reports, systems, procedures, and policies as we considered necessary. After analyzing the data, we developed recommendations for improvements. We then discussed our findings and recommendations with appropriate management personnel before submitting this written report.

In our prior audit of the State Employees Group Benefits Program for the year ended June 30, 1995, we reported findings relating to electronic claims processing controls, claim payments, and time and attendance records. The finding relating to time and attendance records has been resolved by management. The findings relating to electronic claims processing controls and claim payments are addressed again in this report.

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

Untimely Claim Payments

The State Employees Group Benefits Program (SEGBP) has not complied with the provisions of state law relating to the timely payment of health and death claims. Louisiana Revised Statutes (R.S.) 22:657(A) requires the program to pay all health claims within 30 days from the date of receipt unless just and reasonable cause exists