

MUNICIPAL POLICE EMPLOYEES' RETIREMENT SYSTEM



COMPLIANCE AUDIT
ISSUED AUGUST 18, 2010

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LOUISIANA LEGISLATIVE AUDITOR
DARYL G. PURPERA, CPA, CFE

August 18, 2010

**MS. KATHY BOURQUE, DIRECTOR,
AND BOARD OF TRUSTEES
MUNICIPAL POLICE EMPLOYEES' RETIREMENT SYSTEM**
Baton Rouge, Louisiana

We have audited certain transactions of Olde Oaks Development, LLC, a wholly owned subsidiary of the Municipal Police Employees' Retirement System. Our audit was conducted in accordance with Title 24 of the Louisiana Revised Statutes to determine the propriety of certain financial transactions of Olde Oaks Development.

Our audit consisted primarily of inquiries and the examination of selected financial records and other documentation. The scope of our audit was significantly less than that required by *Government Auditing Standards*; therefore, we are not offering an opinion on the Municipal Police Employees' Retirement System's financial statements or system of internal control nor assurance as to compliance with laws and regulations.

The accompanying report presents our findings and recommendations as well as management's response. This correspondence is intended primarily for the information and use of management of the Municipal Police Employees' Retirement System. Copies of this report have been delivered to the District Attorney for the Nineteenth Judicial District of Louisiana and others as required by law.

Respectfully submitted,

Daryl G. Purpera, CPA, CFE
Legislative Auditor

DGP:GD:DD:dl

MPERS 2010

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Report Summary

Between January 6, 2004, and October 12, 2009, Randy Zinna, a contract attorney for the Municipal Police Employees' Retirement System (MPERS), either diverted or held approximately \$5,137,802 of Olde Oaks Development, LLC (real estate investment owned by MPERS) and other MPERS-owned entity funds into his private law office escrow account in possible violation of state law.¹ By handling client funds in this manner, Mr. Zinna may also have violated the Louisiana Rules of Professional Conduct.² The breakdown of these funds is as follows:

1. Olde Oaks Development lot sale proceeds totaling \$815,189 of which \$635,565 was later repaid by Mr. Zinna leaving a balance of \$179,624;
2. Other checks payable to Olde Oaks Development and other MPERS-owned entities totaling \$354,779 for timber sales, gas well leasing rights, options on lots, insurance claim payments, the repayment of an appeals bond, real estate closings, and other unknown purposes. Of this amount, funds totaling \$158,029 were remitted back to Olde Oaks Development and MPERS leaving a balance of \$196,750;
3. \$2,201,145 paid by Boot Ranch, LLC to MPERS as part of the severance agreement between MPERS and Boot Ranch, LLC.; of this amount, funds totaling \$1,814,090 were forwarded to MPERS by Mr. Zinna leaving a balance of \$387,055; and
4. Olde Oaks Development and MPERS checks made payable to vendors totaling \$1,766,690. Of this amount, checks totaling \$1,595,414 were subsequently issued from Mr. Zinna's account to pay vendors leaving a balance of \$171,276 that was not forwarded to the appropriate vendor.

Because Mr. Zinna deposited Olde Oaks Development and other MPERS-owned entity funds into his private law office escrow account, system funds were commingled with Mr. Zinna's private funds. As a result, Mr. Zinna may have used system funds for private

¹ **R.S. 14:67** provides, in part, that theft is the misappropriation or taking of anything of value which belongs to another, either without the consent of the other to the misappropriation or taking, or by means of fraudulent conduct, practices, or representations.

R.S. 14:68 provides, in part, that unauthorized use of a movable is the intentional taking or use of a movable which belongs to another, either without the other's consent, or by means of fraudulent conduct, practices, or representations, but without any intention to deprive the other of the movable permanently.

² (a) A lawyer shall hold property of clients or third persons that is in a lawyer's possession in connection with a representation separate from the lawyer's own property. Except as provided in (g) and the IOLTA Rules below, funds shall be kept in one or more separate interest-bearing client trust accounts maintained in a bank or savings and loan association...No earnings on a client trust account may be made available to or utilized by a lawyer or law firm. Other property shall be identified as such and appropriately safeguarded. Complete records of such account funds and other property shall be kept by the lawyer and shall be preserved for a period of five years after termination of the representation.

(b) A lawyer may deposit the lawyer's own funds in a client trust account for the sole purpose of paying bank service charges on that account or obtaining a waiver of those charges, but only in an amount necessary for that purpose.

(c) A lawyer shall deposit into a client trust account legal fees and expenses that have been paid in advance, to be withdrawn by the lawyer only as fees are earned or expenses incurred. The lawyer shall deposit legal fees and expenses into the client trust account consistent with Rule 1.5(f).

(d) Upon receiving funds or other property in which a client or third person has an interest, a lawyer shall promptly notify the client or third person. For purposes of this rule, the third person's interest shall be one of which the lawyer has actual knowledge, and shall be limited to a statutory lien or privilege, a final judgment addressing disposition of those funds or property, or a written agreement by the client or the lawyer on behalf of the client guaranteeing payment out of those funds or property. Except as stated in this rule or otherwise permitted by law or by agreement with the client, a lawyer shall promptly deliver to the client or third person any funds or other property that the client or third person is entitled to receive and, upon request by the client or third person, shall promptly render a full accounting regarding such property.

purposes including the general operations of his private law firm. In addition, because system funds were either diverted to or held in Mr. Zinna's private law office escrow account for extended periods of time, Mr. Zinna temporarily deprived Olde Oaks Development, MPERS, and other MPERS-owned entities of funds needed for their general operations. Of the amounts diverted to or held in Mr. Zinna's private law office escrow account, funds totaling \$934,705 plus interest were not repaid as of the date of this report.

During our audit, we identified significant deficiencies in the management of Olde Oaks Development which increased the potential for misappropriation of assets to occur and not be detected in a timely manner. These deficiencies included a lack of adherence to written procedures, poor segregation of duties, and a failure to maintain public records. In addition, because Olde Oaks Development offered incentives to developers, including zero-interest notes and discounts, these incentives effectively lowered the purchase price of the lots and may constitute an improper donation.³ Finally, some MPERS board members and staff appear to have improperly accepted gifts from Mr. Zinna in possible violation of state law.⁴

Background

MPERS is one of nine statewide retirement systems. Included in its investment portfolio are two golf courses (Olde Oaks Golf Course and Stonebridge Golf Course) and a land development (Olde Oaks Development) all located near Shreveport, Louisiana. Before June 22, 2007, MPERS owned part of the Boot Ranch Development, LP (a residential development and golf course) in Texas. The real estate developments and golf courses are wholly owned subsidiaries of MPERS and are included in its consolidated financial statements.

On January 1, 2004, Olde Oaks Development, LLC was created. MPERS entered into a contract with Twin Peaks, a local land development company in the Shreveport area to develop the property of the Olde Oaks Development and perform real estate services including the selling of lots. On February 13, 2004, Olde Oaks Development purchased land adjacent to the Olde Oaks Golf Course, one of the golf courses owned by MPERS. Between May 11, 2004, and December 16, 2009, there were 102 lot sales in the development totaling \$5,219,133.

The manager for the Olde Oaks Development was Mr. Zinna. Although his contract with MPERS did not specify specific responsibilities regarding Olde Oaks Development, the MPERS board appears to have relied on Mr. Zinna to manage the Olde Oaks Development operations. Based on our review, it appears that Mr. Zinna assumed numerous responsibilities for Olde Oaks Development that are incompatible with proper segregation of duties. In addition, both MPERS staff and management of Twin Peaks claim to have accepted direction from Mr. Zinna regarding the operation of Olde Oaks Development.

³ **Article 7, Section 14 of the Louisiana Constitution** provides, in part, that except as otherwise provided by this constitution, the funds, credit, property, or things of value of the state or of any political subdivision shall not be loaned, pledged, or donated to or for any person, association, or corporation, public or private.

⁴ **R.S. 42:1115** provides, in part, that no public servant shall solicit or accept, directly or indirectly, anything of economic value as a gift or gratuity from any person or employee of any person who has or is seeking to obtain contractual or other business or financial relationships with the public servant's agency.

During the MPERS financial audit for the fiscal year ended 2009, auditors (external CPAs) determined that approximately \$567,000 of lot sale revenue for Olde Oaks Development was not deposited into system accounts. Those auditors requested supporting documentation for these lot sales including closing checks, validated deposit slips, and bank statements showing the deposited funds. MPERS officials notified the auditors that these records were not in their possession and they were unable to obtain them from their contractor. On September 29, 2009, Mr. Zinna supplied a check to MPERS made payable to Olde Oaks Development for approximately \$545,939 along with a supporting schedule indicating that the funds were from 13 lot sales in the development.

Given the length of time between the lot sales and their eventual deposit into the Olde Oaks Development operating account and the lack of supporting documentation for these lot sales, the Louisiana Legislative Auditor initiated an audit of MPERS performed in conjunction with the Louisiana Attorney General's Office and the Louisiana Office of Inspector General. The findings of the audit are described on the following pages.

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Improper Use of Client Trust Account

Rule 1.15 of the Louisiana Rules of Professional Conduct, as amended through January 6, 2010, establishes the rules that all attorneys licensed to practice in the State of Louisiana must follow in regards to the safekeeping of property or funds belonging to clients or third parties.

Rule 1.15 provides for two types of accounts in the possession of an attorney in which all funds of clients or third persons in connection with their representation must be kept separate from the property of the attorney; a general Interest on Lawyers Trust Accounts (IOLTA) or one or more separate attorney created client trust accounts (non-IOLTA). Both types of accounts (IOLTA and non-IOLTA) are required to be interest-bearing accounts and must be held separately from the attorney's personal/operating funds. The attorney is, however, permitted to place his/her own personal money into the non-IOLTA account for the sole purpose of paying bank service charges on the trust account or obtaining a waiver of the charges but only in an amount necessary for that purpose. No earnings on either IOLTA or non-IOLTA accounts may be made available to or used by a lawyer or law firm. Attorneys shall deposit any legal fees and expenses that have been paid in advance and may only withdraw the funds as fees are earned or expenses are incurred.

Upon receipt of any funds or other property in which a client or third person has an interest, an attorney shall promptly notify the client or third person. Except as otherwise permitted by law or by agreement with the client, an attorney shall promptly deliver to the client or third person any funds or other property that the client or third person is entitled to receive and upon request by the client or third person, promptly render a full accounting regarding such property. If two or more persons claim interest in property (including the attorney) held by the attorney, the attorney shall keep the property separate until the dispute is resolved and promptly distribute all portions of the property for interests that are not in dispute.

During our review of Mr. Zinna's client trust account (escrow account), we noted the following which appear to violate the Louisiana Rules of Professional Conduct:

1. Mr. Zinna's escrow account was not an interest-bearing account.
2. From January 6, 2004, to October 12, 2009, Mr. Zinna either diverted or held approximately \$5,137,802 of Olde Oaks Development, MPERS, and other MPERS-owned entity funds into his private law office escrow account. Because Olde Oaks Development and/or MPERS were entitled to a majority of these funds, the funds should have been promptly delivered to the entity or third party to which they were entitled. Our analysis of these funds indicates that a majority of the funds were either not remitted or not promptly remitted.
3. Mr. Zinna deposited multiple client funds into one client trust account.

4. Mr. Zinna appears to have used client funds for personal/operating purposes as he did not account for these funds separately. In addition, we noted several instances in which automatic withdrawals were made from the account to pay credit card bills.

As a result of these actions, Mr. Zinna appears to have violated the Louisiana Rules of Professional Conduct and used client funds for personal/operational purposes.

Lot Sale Proceeds

From November 2, 2004, to October 12, 2009, a total of 22 Olde Oaks Development lot sale proceed checks totaling \$815,189 were deposited into Mr. Zinna's private law firm escrow account. According to deposit records, each of the checks appears to be endorsed by Mr. Zinna in the name of Olde Oaks Development. With the exception of two checks totaling \$89,626, none of these funds were remitted to Olde Oaks Development until September 2009 when auditors determined that lot sale proceeds were not deposited into Olde Oaks Development's bank account. After questions arose about missing funds, Mr. Zinna supplied a check to MPERS made payable to Olde Oaks Development in the amount of \$545,939.

The Olde Oaks Development was domiciled at Mr. Zinna's law office and correspondence including settlement checks from the sale of Olde Oaks Development lots was mailed to Mr. Zinna. Mr. Zinna was not the attorney responsible for closing on the real estate sales and therefore there was no apparent reason for the sales proceeds to be deposited into his private law firm escrow account. In fact, Olde Oaks Development had its own operating account where approximately 80% of these settlement checks were deposited by either Mr. Zinna or MPERS accounting staff.

During the period in which these checks were deposited to Mr. Zinna's private law firm escrow account, two checks, one in the amount of \$33,388 and the other in the amount of \$56,238, were later remitted to Olde Oaks Development. The \$33,388 and \$56,238 checks were initially deposited into Mr. Zinna's private law firm escrow account on November 2, 2004, and May 19, 2009, respectively. According to account records, Mr. Zinna issued checks to Olde Oaks Development in these same amounts on June 27, 2005, and September 11, 2009, respectively. None of the other lot sale proceeds checks that were deposited into Mr. Zinna's account were remitted to Olde Oaks Development until September 29, 2009, when Mr. Zinna provided MPERS with a check for \$545,939.

According to documentation provided by Mr. Zinna at the time of the repayment, the \$545,939 included revenue from 13 lot sales made between August 4, 2005, and June 13, 2008. However, a review of Mr. Zinna's private law firm escrow account indicates that just before issuing the check to MPERS, Mr. Zinna deposited a \$450,000 check from an unrelated third party into the account. Without depositing this check, there were insufficient funds in the account to repay MPERS. Repayment was only made after auditors identified missing lot sale revenue and requested documentation of lot sales from Mr. Zinna.

As a result of these transactions, it appears that proceeds from lot sales remained in the possession of Mr. Zinna for as long as four years before repayment. In addition, lot sale proceeds appear to have been commingled with private funds in Mr. Zinna’s private law firm escrow account. Mr. Zinna stated that revenues from lot sales were to be used for development expenses but when asked why lot sale proceeds were deposited into his private law firm escrow account rather than the Olde Oaks Development operating account, Mr. Zinna stated that he “had no acceptable audit explanation.” The repayment of \$635,565 leaves a balance owed by Mr. Zinna of \$179,624. To date these proceeds have not been remitted to Olde Oaks Development.

Other Olde Oaks Development and MPERS Funds

From March 1, 2004, to August 29, 2007, nine additional checks made payable to Olde Oaks Development, MPERS, and other MPERS-owned entities were deposited into the private law firm escrow account of Mr. Zinna. These nine checks totaled \$354,779 and included timber sales, gas well leasing rights, options on lots, insurance claim payments, the repayment of an appeals bond, and other unknown purposes. Descriptions of these payments are provided in the following table.

Date	Payor	Payee	Amount	Purpose
3/1/04	The Hays County Abstract Co.	MPERS	\$155,434	MPERS refund on Boot Ranch land purchase
5/17/04	CitiCapital	MPERS	46,200	Unknown
11/17/04	Red Oak Timber Co.	MPERS	45,485	Purchase of timber
10/26/05	Chesapeake Operating Inc.	Olde Oaks Development	10,000	Gas leasing rights
10/26/05	Chesapeake Operating Inc.	Olde Oaks Development	3,147	Gas leasing rights
11/21/05	Olde Oaks Development	Olde Oaks Development	5,529	Unknown
10/2/06	The Hanover Insurance Co.	Olde Oaks Golf Club LLC	10,000	Claim payment
7/30/07	MKH Properties LLC	Olde Oaks Development	42,000	Lot options
8/29/07	Bossier Parish Clerk of Court	Stonebridge Enterprises LLC	36,984	Appeals bond repayment
		Total	\$354,779	
		Reimbursements from Mr. Zinna to OOD/MPERS	(158,029)	
		Amount Outstanding	\$196,750	

Records from Mr. Zinna’s private law firm escrow account indicate that Mr. Zinna reimbursed the Olde Oaks Development and MPERS funds totaling \$158,029. These funds included three checks: a \$2,500 check dated September, 10, 2004, made payable to Olde Oaks Development; a \$150,000 check dated November 2, 2004, made payable to MPERS; and a \$5,529 cashier’s check dated December 30, 2005, made payable to Olde Oaks Development.

Mr. Zinna could not give a definitive purpose for the \$2,500 and \$150,000 checks. However, he suggested that the \$150,000 check made payable to MPERS may have been a partial repayment of the \$155,434 check from the The Hays County Abstract Company. The \$5,529 cashier’s check to Olde Oaks Development appears to be a repayment of the \$5,529

check deposited into the escrow account. The repayment of \$158,029 leaves a balance owed by Mr. Zinna of \$196,750. As of the date of this report, these funds have not been remitted to MPERS or Olde Oaks Development.

Because the checks received by Mr. Zinna were made payable to Olde Oaks Development, MPERS, and other MPERS-owned entities, there appears to be no legitimate business justification for the deposit of these checks into Mr. Zinna's private law firm escrow account. When asked about these funds being deposited into his bank account, Mr. Zinna was unable to provide auditors with an explanation.

Boot Ranch Funds

On June 22, 2007, funds totaling \$2,201,145 were wire transferred from the Boot Ranch Real Estate, LLC, into the private law firm escrow account of Randy Zinna. Boot Ranch was a development owned by MPERS located in eastern Texas. Account records indicate that from June 25, 2007, to June 24, 2008, three wire transfers totaling \$1,814,090 were made from Mr. Zinna's escrow account to MPERS leaving a balance of \$387,055 of funds not remitted to MPERS. In addition, because system funds were held in a private account for extended periods of time, Mr. Zinna appears to have deprived MPERS, at least temporarily, of the use of funds for general operations. Furthermore, MPERS was deprived of the opportunity to earn interest income on the funds held in Mr. Zinna's private law firm escrow account.

After receiving the wire transfer described above from Boot Ranch on June 22, 2007, two wire transfers totaling \$1,467,630 were made from the law firm escrow account of Randy Zinna to MPERS on June 25, 2007. The balance of the funds totaling \$733,515 remained in Mr. Zinna's escrow account until June 24, 2008, when a third transfer of \$346,460 was wired from Mr. Zinna's escrow account to an MPERS account. These transactions left a balance of system funds totaling \$387,055 in Mr. Zinna's escrow account. According to an MPERS official, the three wire transfers to MPERS were funds owed to MPERS as part of the termination of the partnership agreement between MPERS and Boot Ranch. However, MPERS could not provide any documentation to indicate why system funds were transferred to Mr. Zinna's account instead of going directly to MPERS.

Mr. Zinna stated that the initial transfer from Boot Ranch consisted of funds owed to MPERS as part of the conversion of the Boot Ranch partnership into a debt instrument. He added that the funds included interest reimbursement, lot sale revenues, letter of credit funds, and other funds that he negotiated during the conversion. Mr. Zinna could not provide an explanation as to why all funds were not immediately transferred to MPERS. Mr. Zinna indicated that he would research the three payments and follow up with the auditors. He has not responded to date.

Vendor Payments

From January 6, 2004, to April 15, 2009, a total of 51 Olde Oaks Development and MPERS checks made payable to various vendors totaling \$1,766,690 were improperly deposited into the private law firm escrow account of Mr. Zinna. These 51 checks were issued to pay vendors for services provided to Olde Oaks Development such as landscaping, engineering, and development work. All the checks were made out to vendors of the Olde Oaks Development or MPERS. Consequently, there does not appear to be any legitimate business purpose for depositing the checks into the private law firm escrow account of Randy Zinna.

During an analysis of Mr. Zinna's bank account, we were able to identify transactions totaling \$1,595,414 in which Mr. Zinna appears to have remitted the Olde Oaks Development and MPERS funds to these vendors. We were unable to find support for the \$171,276 balance owed to these vendors. Payments to vendors from Mr. Zinna's escrow account were made through cashier's checks purchased by Mr. Zinna or checks drawn on Mr. Zinna's escrow account and made payable to the vendors. Although most of the funds appear to have been remitted to the appropriate vendors, the disbursements to vendors from Mr. Zinna's account were made anywhere from several weeks to over a year after Mr. Zinna initially received the funds. Because system funds were diverted to and held in Mr. Zinna's private law firm escrow account for extended periods of time, Mr. Zinna temporarily deprived Olde Oaks Development and MPERS of funds needed for general operations.

For example, on August 9, 2006, an Olde Oaks Development check made payable to a vendor in the amount of \$18,596 was deposited into Mr. Zinna's escrow account. Over a year later on September 25, 2007, a check was drawn on Mr. Zinna's escrow account for this same amount and made payable to this same vendor. Similarly, on October 17, 2008, an Olde Oaks Development check for \$24,990 was deposited into Mr. Zinna's escrow account. Approximately ten months later on August 21, 2009, a check was drawn on Mr. Zinna's escrow account for this same amount and made payable to this same vendor.

Lack of Management Control

During our audit, we identified significant deficiencies in the management of Olde Oaks Development which increased the potential for misappropriation of assets to occur and not be detected in a timely manner. These included a lack of adherence to written procedures, poor segregation of duties, and failure to maintain public records. These deficiencies are described in the following paragraphs.

Lack of Adherence to Written Procedures

During the first year and a half of its operations, Olde Oaks Development appears to have operated without any written procedures. In May 2005, auditors noted the deficiency and recommended written procedures including detailed procedures governing cash disbursements and receipts. These procedures included requirements that checks for lot sales be forwarded directly to the system's office with original acts of sale and that approved invoices be sent to the system for payment.

Although these recommendations were brought to the attention of the MPERS Board and Mr. Zinna, audits for fiscal years ended in 2005, 2006, and 2007 included an internal control finding stating the majority of these procedures had not been implemented. In response to the audit findings, MPERS management asserted that it had complied with these procedures; however, based on our audit, it appears that these procedures were not fully implemented. Had these procedures been fully implemented, management could have prevented the diversion of these funds.

Poor Segregation of Duties

Based on our audit, it appears that control over Olde Oaks Development operations was concentrated in one individual--Randy Zinna. Mr. Zinna appears to have received invoices, signed checks, mailed payments to vendors, participated in determining lot sale prices, received lot sale closing checks, received other checks made payable to the Olde Oaks Development, made disbursements from the Olde Oaks Development line of credit, maintained custody of the bank account, and provided regular updates to the MPERS Board on Olde Oaks Development operations.

Good business practices and proper internal control dictate that duties be segregated so that no individual performs or controls all duties related to a financial area or function. The lack of proper segregation of duties created an environment where a diversion of funds was possible. For example, the lot sale proceeds checks were sent to Mr. Zinna's law office (which is the registered office address for Olde Oaks Development) rather than MPERS accounting staff. MPERS accounting staff was only aware of lot sale proceeds forwarded to them by Mr. Zinna. As a result, Olde Oaks Development accounting records did not accurately reflect the income from the lot sales. The responsibility to receive lot sale proceeds should have been assigned to MPERS accounting staff and lot sale proceeds should have been received directly from the closing attorneys as recommended by the external auditors.

Failure to Maintain Public Records

During the current audit, MPERS staff was unable to provide complete business records for the Olde Oaks Development, including complete documentation of lot sales and contracts even though Louisiana law requires public records be maintained for three years.⁵ Mr. Zinna claims that he provided MPERS with complete documentation for Olde Oaks Development including contracts, bid documents, invoices, budgets, etc. He claims to have only kept copies of these documents at his office.

⁵ R.S. 44:36(A) states, in part, "All persons and public bodies having custody or control of any public record, other than conveyance, probate, mortgage, or other permanent records required by existing law to be kept for all time, shall exercise diligence and care in preserving the public record for the period or periods of time specified for such public records in formal records retention schedules developed and approved by the state archivist and director of the division of archives, records management, and history of the Department of State. However, in all instances in which a formal retention schedule has not been executed, such public records shall be preserved and maintained for a period of at least three years from the date on which the public record was made."

Management of MPERS and its external auditor assert that Mr. Zinna maintained many of the Olde Oaks Development business records at his private law firm offices. During our audit, we observed that the operating account for Olde Oaks Development was maintained by Mr. Zinna for a period of time outside the MPERS offices; invoices to and payments for Olde Oaks Development were routinely sent to Mr. Zinna's law offices; and audits of MPERS repeatedly cited the failure to "maintain copies of legal documents relating to its subsidiary entities at its principle location" as an internal control issue.

The failure of MPERS management to maintain adequate business records for Olde Oaks Development hindered its ability to adequately manage and monitor activities of Olde Oaks Development and increased the potential for misappropriation of assets to occur and not be detected in timely manner.

We recommend that MPERS management implement the following procedures to strengthen controls, improve operations, and comply with state law:

1. Ensure that all business records for the Olde Oaks Development, including corporate documents, correspondence, bank statements, contracts, and closing documents are housed at the MPERS system office.
2. Change the address for Olde Oaks Development from the Law Offices of Randy Zinna to the MPERS domicile address to ensure that correspondence, including invoices and payments, is routed to the appropriate individual reducing the likelihood of unauthorized diversion of funds.
3. Require that all Olde Oaks Development expenditures be authorized, paid, and mailed by MPERS accounting staff and that all payments to the Olde Oaks Development be routed to MPERS. In addition, policies and procedures should be implemented for handling payments received by mail to ensure that all checks received by mail are logged, restrictively endorsed, recorded in the accounting system, and deposited into the appropriate bank account.
4. Require MPERS staff to periodically reconcile payments received on individual lots with the amounts recorded on the signed HUD Settlement Sheet to ensure that all payments owed from lot sales including deposits have been received.
5. Clearly document in writing the management responsibilities for Olde Oaks Development and the persons they have been assigned to.
6. Recover all funds held in Mr. Zinna's private law firm escrow account that have not been remitted to date.

Lot Sale Incentives

Olde Oaks Development offered incentives to developers to purchase lots. These incentives included allowing developers to pay with zero-interest notes, facilitating developer credit through the use of subordination agreements, and discounts. The rationale for the use of these incentives was not documented by MPERS; therefore, we cannot determine whether their use was appropriate given the real estate market at the time.

Zero Interest Notes/Subordination Agreements

The terms of the zero-interest notes allowed the developers to pay back the notes upon the resale of the lot or two years, whichever came first. Interest revenue did not accrue to Olde Oaks Development during this interval. The notes were secured by mortgages on the lots held by Olde Oaks Development. Based on our audit, developers purchased 15 lots that were paid in part with zero-interest notes. The notes ranged in price from \$16,950 to \$45,000.

Olde Oaks Development subordinated its interest in all 15 lots to various financial institutions. Under subordination agreements, Olde Oaks Development gave up its interest in the lots to financial institutions that in turn provided financing for the developers to develop the lots for resale. The use of subordination agreements meant that if the developer defaulted on the obligation to pay the note, the financing company would have right of first possession on the lot.

The use of both these incentives was of benefit to the developers. The use of zero-interest notes enabled the developers to pay for their lots with funds borrowed at no interest. The use of subordination agreements allowed developers to borrow through the use of collateral (i.e., the lots) still owned by Olde Oaks Development until the zero-interest note was paid. The use of zero-interest notes and the accompanying subordination agreements may, therefore, constitute the donation of Olde Oaks Development assets and thus violate the Louisiana Constitution.⁶

We recommend that MPERS management obtain an Attorney General opinion to determine if the practice of accepting payment in the form of zero-interest notes from developers is lawful. The acceptance of these notes in conjunction with subordination agreements puts Olde Oaks Development at risk of nonpayment, limits cash flow to Olde Oaks Development restricting its ability to pay expenses, and may violate Louisiana law.

Discounts on Lot Sales

Based on our review of HUD Settlement Sheets, Olde Oaks Development gave discounts on 53 of the 102 lot sales reviewed during our audit. The total value of the discounts on these 53 lot sales was \$865,575. The value of discounts on individual lot sales ranged from \$2,500 to \$43,750. These discounts represent the difference between the sale price and the amount paid by the purchaser.

⁶ Article 7, Section 14 of the Louisiana Constitution provides, in part, that except as otherwise provided by this constitution, the funds, credit, property, or things of value of the state or of any political subdivision shall not be loaned, pledged, or donated to or for any person, association, or corporation, public or private.

According to management of Twin Peaks, discounts were used to keep the listed sale price on lots high to maximize lot sale revenue. Since discounts do not affect the listed sales price, they result in listed sale prices higher than the amount actually paid by the purchaser. The effect is to increase the recorded sale prices for lots in the development, enabling Olde Oaks Development to list lots for higher prices. Mr. Zinna stated that discounts were used if sales were slow. He added that if the selling price with the discount was above the cost of the lot he felt okay with the sale.

MPERS was unable to supply documentation of the calculations supporting the discounts. Therefore, we were unable to determine how the discounts were calculated and whether the use of discounts resulted in sale prices less than fair market value. According to Mr. Zinna, he calculated the land and development cost for the lots and ensured the sale price including discounts was sufficient to cover these costs and provide a profit.

We recommend that MPERS management obtain an Attorney General opinion to determine if the practice of offering discounts is lawful. Although common in private sector dealings, the use of discounts in public sector real estate transactions is problematic. Unless fully documented and justified by market conditions, the use of discounts can create an impression of favoritism. In addition, the use of discounts may be viewed as a donation and therefore may be a violation of the Louisiana Constitution.⁷

Gifts to MPERS Board Members and Staff

During our audit, we spoke to several board members concerning the operation and management of the Olde Oaks Development. Some board members and an MPERS staff member indicated to us that they had accepted sporting event tickets from Mr. Zinna. Mr. Zinna stated that he did not give gifts to board members or MPERS staff. Acceptance of sporting event tickets by MPERS staff and board members from a contracted service provider may be prohibited under the Louisiana Code of Governmental Ethics.⁸

We recommend the board implement training to ensure that all board members and office staff are aware of the prohibition against acceptance of gifts from individuals doing business with the agency.

⁷ **Article 7, Section 14 of the Louisiana Constitution** provides, in part, that except as otherwise provided by this constitution, the funds, credit, property, or things of value of the state or of any political subdivision shall not be loaned, pledged, or donated to or for any person, association, or corporation, public or private.

⁸ **R.S. 42:1115** provides, in part, that no public servant shall solicit or accept, directly or indirectly, anything of economic value as a gift or gratuity from any person or employee of any person who has or is seeking to obtain contractual or other business or financial relationships with the public servant's agency.

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The Municipal Police Employees' Retirement System (MPERS) is one of nine statewide retirement systems and was established by Act 189 in 1973. MPERS was created to provide retirement allowances and other benefits for full-time municipal police officers and employees in the state of Louisiana, secretaries to chiefs of police, and employees of this retirement system. MPERS is governed by a Board of Trustees including a representative of the Retirement Committee of the House of Representatives and the Chairman of the Senate Finance Committee as ex-officio members of the board.

The procedures performed during this audit include:

- (1) interviewing employees of MPERS;
- (2) interviewing other persons as appropriate;
- (3) examining selected documents and records of Olde Oaks Development;
- (4) gathering documents from external parties; and
- (5) reviewing applicable state laws and regulations.

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Management's Response

MUNICIPAL POLICE EMPLOYEES' RETIREMENT SYSTEM

7722 OFFICE PARK BOULEVARD - SUITE 200 BATON ROUGE, LOUISIANA 70809-7601
 TELEPHONE 1-800-443-4248 OR (225) 929-7411 - FAX (225) 929-6542
 www.lampers.org



June 21, 2010

KATHY BOURQUE
 DIRECTOR

Charles G. Hall
 Actuary

R. Randall Roche
 General Counsel

BOARD OF TRUSTEES:

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 Chairman
 Non-Chief District II
 Lafayette P.D.

Larry D. Reech
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EX-OFFICIO:

D.A. Butch Gautreaux
 Senator
 Chairman
 Senate Retirement Committee

Joel C. Robideaux
 Representative
 Chairman
 House Retirement Committee

Mr. Daryl G. Purpera, CPA, CFE
 Louisiana Legislative Auditor
 P.O. Box 94397
 Baton Rouge, LA 70804-9397

Dear Mr. Purpera:

The following is in response to the compliance audit report on the Municipal Police Employees' Retirement System.

After having reviewed in detail the compliance audit report including the background and various items addressed including the report summary, the staff and the Board Chairman have no dispute with the report findings.

With regard to the recommendations that should be implemented to strengthen controls, improve operations, and to comply with state law, MPERS reports that the following have been implemented:


1. MPERS has implemented a policy requiring that all business records for Olde Oaks Development, including corporate documents, correspondence, bank statements, contracts, and closing documents are maintained at the MPERS system office.
2. The domically address for Olde Oaks Development has been changed to the MPERS domicile address. Mr. Zinna has been removed from all corporate documents.
3. Procedures have been implemented requiring that all Olde Oaks Development expenditures are authorized, paid, and mailed by MPERS accounting staff and that all payments to Olde Oaks Development are routed directly to MPERS. Additionally all payments and expenditures are logged and recorded in the accounting system and all checks are restrictively endorsed and deposited into the appropriate bank account.
4. MPERS staff reconciles payment amounts received on lot sales with the amounts recorded on the signed HUD settlement sheet upon receipt.
5. Management responsibility for Olde Oaks Development and the persons to whom they have been assigned is documented in writing.

Mr. Daryl G. Purpera
June 21, 2010
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6. Proceedings to recover funds held in Mr. Zinna's law office escrow account have been instituted.
7. Incentives on lot purchases have ceased.
8. Proper training will be provided to MPERS staff and board members regarding the acceptance of gifts from individuals doing business with MPERS.

In the event that further response is needed on these matters, please advise.

Sincerely,



Kathy Bourque
Director

Response from Mr. Randy Zinna

In a letter dated June 21, 2010, we asked Mr. Zinna to respond, in writing to this report. As of the date of this report, Mr. Zinna has chosen not to respond.