

STATE OF LOUISIANA LEGISLATIVE AUDITOR

**New Orleans Home and
Rehabilitation Center
Department of Health and Hospitals
State of Louisiana
New Orleans, Louisiana**

March 19, 1997



Financial and Compliance Audit Division

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

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**NEW ORLEANS HOME AND
REHABILITATION CENTER
DEPARTMENT OF HEALTH AND HOSPITALS
STATE OF LOUISIANA
New Orleans, 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 and New Orleans offices of the Legislative Auditor.

March 19, 1997



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February 18, 1997

**NEW ORLEANS HOME AND
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DEPARTMENT OF HEALTH AND HOSPITALS
STATE OF LOUISIANA
New Orleans, Louisiana**

As part of our audit of the State of Louisiana's financial statements for the year ended June 30, 1997, we conducted certain procedures at the New Orleans Home and Rehabilitation Center. Our procedures included (1) a review of the rehabilitation center's internal control structure; (2) tests of financial transactions for the years ended June 30, 1997, and June 30, 1996; (3) tests of adherence to applicable laws, regulations, policies, and procedures governing financial activities for the years ended June 30, 1997, and June 30, 1996; and (4) a review of compliance with prior year report recommendations.

The June 30, 1997, Annual Fiscal Report of the New Orleans Home and Rehabilitation Center was not within the scope of our work, and, accordingly, we offer no form of assurance on that report upon its issuance. The rehabilitation center'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 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 improvements. We then discussed our recommendations with appropriate management personnel before submitting this written report.

In our prior management letter dated April 13, 1994, we reported compliance and internal control findings concerning the patient recreation fund - vending machines, daily census reports, cash collections, and controls over medical and office supplies inventory. These findings have been resolved by management, except for the finding relating to the medical and office supplies inventory, which is addressed 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.

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Controls Over Consumable Inventory

As previously reported in our management letter dated April 13, 1994, the New Orleans Home and Rehabilitation Center (NOHRC) has not maintained adequate internal controls over its inventory of medical and office supplies. An adequate internal control structure would provide management with the basis to accurately account for the receipt, issuance, validation, and disposition of inventory items.

During our review of the NOHRC's inventory controls, we noted the following weaknesses:

1. Stock requisition forms are not prenumbered. Therefore, the NOHRC cannot determine that all inventory items issued are recorded in the *perpetual inventory system*.
2. The perpetual records are not reconciled to the balance in the Government Financial System (GFS), until an annual physical inventory count is performed. As a result, errors may not be detected in a timely manner.
3. Journal entries made to record usage of inventory in GFS are not reviewed by a supervisor before electronic approval.
4. The NOHRC's physical inventory count performed at June 28, 1996, resulted in differences between the perpetual inventory records and the quantity on hand. The net value of the perpetual inventory was adjusted from \$87,182 to \$81,961, a change of \$5,221, or 5 percent.
5. Of 17 different inventory categories tested by us during fiscal year 1997, there were differences between the perpetual inventory records and the quantity on hand for 16 inventory categories (94 percent).

Because of these control weaknesses, the NOHRC cannot adequately track and report its inventory of medical and office supplies. Furthermore, there is an increased risk that errors and/or irregularities may occur in the future and not be detected in a timely manner.

The NOHRC should implement procedures to ensure adequate control over receipt, issuance, valuation, and disposition of inventory items. Prenumbered forms should be used when inventory items are issued. A monthly reconciliation should be performed to

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ensure that perpetual records agree with amounts recorded in GFS, and journal entries should be reviewed before input into GFS. In a letter dated February 18, 1997, Mr. Otey M. Dear, Hospital Administrator, concurred with the finding and stated that, effective February 1, 1997, the rehabilitation center implemented the procedures recommended.

Controls Over Professional Service Contracts

The NOHRC does not have a system in place to monitor and evaluate professional service contracts and does not ensure that professional service contractors comply with the contract provisions. Louisiana Revised Statute (LSA-R.S.) 39:1497(4) requires that state agencies certify to the Office of Contractual Review that they have developed and intend to implement a written plan for professional service contract monitoring. In addition, LSA-R.S. 39:1500 requires an agency to evaluate contract performance and to deliver the evaluation to the Office of Contractual Review within 120 days after completion of performance. As of November 30, 1996, NOHRC did not perform or remit evaluations on the contracts totaling \$70,750.

Our review of 17 payments, totaling \$25,140, for 11 different professional service contracts, disclosed that the NOHRC paid 6 contractors a total of \$8,242 for services that were not supported by documentation. Although documentation was specifically required by the contract, none existed. Furthermore, interviews conducted with the personnel authorized to approve the payments to the contractors indicated that the specific requirements of the professional service contracts were not reviewed before approving these payments. Without reviewing contract requirements, the NOHRC cannot determine that services were rendered in accordance with the contract. Since the contracts were not monitored or evaluated, the performance of the contractors may not have been satisfactory.

Management of the NOHRC should implement a contract monitoring and evaluation system and should remit the evaluations to the Office of Contractual Review, as required by statute. Before payment, management should also ensure that services from professional service contractors are rendered in accordance with the contracts. In a letter dated February 18, 1997, Mr. Otey M. Dear, Hospital Administrator, concurred with the finding and recommendation and stated that procedures have been updated relating to monitoring and evaluating of professional service contracts, sign-in sheets, invoice processing and approval.

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Weaknesses in Electronic Data Processing Controls

The NOHRC has not established an adequate internal control structure over electronic data processing (EDP) controls. An adequate system of internal control is necessary to safeguard assets, to ensure accounting data is accurate and reliable, and to ensure errors and irregularities are detected within a timely manner. Individuals should be permitted access only to the data files and programs necessary to perform their duties. Duties should be segregated so that no one employee is in a position to both initiate and conceal errors or irregularities, and periodic validations should be performed to ensure the integrity of the data within the system.

During our review of the rehabilitation center's EDP controls, the following weaknesses were observed:

1. The contract payment document number, which is assigned by the accounting system, is not being referenced on the supporting documentation. Therefore, the payment recorded in the accounting system cannot be traced to the corresponding contract vendor invoice.
2. There are no written procedures pertaining to the issuance of user identification (ID) codes or the deletion of user ID codes once an employee terminates or no longer has a legitimate need for access. Our review of the accounting system security report revealed that two employees who terminated employment with the rehabilitation center had not been deleted from the system.
3. Two employees in the accounting department had both data entry and approval user ID codes, which allowed them to add new vendors and approve payments. These are incompatible functions and should be segregated.
4. There was no indication that validation procedures had been performed for time entry or wage adjustment reports. The Louisiana Department of Civil Service performed an audit of the August 30, 1996, payroll and determined that two employees were underpaid by approximately \$165 and \$315 each. Our follow-up of the rehabilitation center's correction entries recorded on the September 27, 1996, payroll indicated that the employees were still underpaid by approximately \$58 and \$184 each. The rehabilitation center finally corrected the underpayments on the January 3, 1997, payroll.

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The lack of adequate controls in an on-line data entry environment could result in the loss of data, inconsistent use of on-line data entry procedures, and failure to prevent or detect errors or irregularities in processing nonpayroll and payroll transactions.

To improve controls over electronic data processing, the NOHRC should:

- Record the contract payment document numbers on the contract vendor invoices
- Establish written procedures for the issuance and deletion of user ID codes
- Delete terminated employees' user ID codes immediately
- Separate the incompatible functions relating to the establishment of new vendors and payment approval authorization
- Ensure that periodic validations are conducted on data entry and output and are documented to show the date and signature of the person performing the validation

In a letter dated February 18, 1997, Mr. Otey M. Dear, Hospital Administrator, concurred with the finding and recommendation and stated that procedures would be implemented regarding user ID controls. In addition, a request to remove incompatible access has been made, and periodic validations will be performed.

Financial Reporting

The NOHRC did not prepare its 1995 and 1996 annual fiscal reports in accordance with the instructions provided by the Office of Statewide Reporting and Accounting Policy (OSRAP) and did not adequately review these reports before submission. Necessary characteristics of useful financial reports include reliability, consistency, and comparability. Financial reports must contain information that is both verifiable and compiled on a basis common to similar entities, and a review of the financial report should be performed so that any preparation errors can be detected and corrected in a timely manner.

Corrections by OSRAP to the NOHRC's 1995 fiscal report indicated that total assets had been overstated by \$155,814; total liabilities and fund equity had been overstated by \$56,353; and revenues were understated by \$538,459. Our review of 39 account

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balances on the NOHRC's fiscal report for the fiscal year ended June 30, 1996, disclosed 5 (13 percent) account balances which could not be traced to the accounting records as follows:

1. The balance sheet reported total assets of \$1,256,624, of which one account balance totaling \$55,238 (4 percent) could not be traced to the accounting records.
2. The balance sheet reported total liabilities and fund equity of \$1,256,624, of which 3 account balances totaling \$910,160 (72 percent) could not be traced to the accounting records.
3. The statement of revenue and expenditures, included an adjustment to beginning fund balance of \$663,885, which could not be traced to the accounting records.

Failure to follow prescribed instructions in the preparation of financial statements and inadequate supervisory review increases the risk that the rehabilitation center's fiscal report could be misleading to those individuals and organizations that rely on the statements.

The NOHRC should prepare its annual fiscal report in accordance with instructions provided by OSRAP and should implement a review procedure to ensure that financial statements are prepared correctly. In a letter dated February 18, 1997, Mr. Otey M. Dear, Hospital Administrator, stated that the rehabilitation center concurred with the finding and recommendation and indicated that he or his designee will assist in the preparation of all fiscal reports and will review the report and supporting documentation.

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

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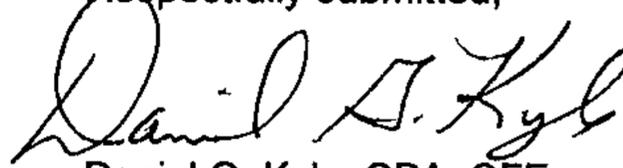
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This report is intended for the information and use of the rehabilitation center and its management. By provisions of state law, this report is a public document, and it has been distributed to appropriate public officials.

Respectfully submitted,

A handwritten signature in cursive script that reads "Daniel G. Kyle".

Daniel G. Kyle, CPA, CFE
Legislative Auditor

JMS:THC:dl

[NOHRC]