

DEPARTMENT OF ECONOMIC DEVELOPMENT



COMPLIANCE AUDIT

ISSUED JANUARY 18, 2006

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January 18, 2006

MICHAEL J. OLIVIER, SECRETARY
DEPARTMENT OF ECONOMIC DEVELOPMENT
Baton Rouge, Louisiana

We have audited certain transactions of the Louisiana Department of Economic Development in accordance with Title 24 of the Louisiana Revised Statutes. Our audit was performed to substantiate or refute allegations of improprieties within the Department.

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 Department's financial statements or system of internal control nor assurances as to compliance with laws and regulations.

The accompanying report presents our findings and recommendations as well as management's response. Copies of this report have been delivered to the United States Attorney for the Middle District of Louisiana, the District Attorney for the Nineteenth Judicial District of Louisiana, and others as required by state law.

Respectfully submitted,

Steve J. Theriot, CPA
Legislative Auditor

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DED05

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The Louisiana Department of Economic Development (DED) reimbursed Transcaribbean Airways, N.V. (TCA), a contractor in the Department's Workforce Development and Training Program, \$519,308 for training expenses that were not adequately documented and may not have been provided. The contract, as drafted and executed by DED, did not require any documentation of expenses other than cost reports to support the reimbursements to TCA. In addition, the contract did not link disbursement of funds to progress toward performance objectives.

DED administers the Workforce Development and Training Program, a program designed to assist employers in training a labor force for new or expanding businesses in Louisiana. Businesses that want to participate in the program submit an application detailing the amount of funds requested, the number of people to be trained, and the number of jobs to be created. The application is then sent to the Louisiana Economic Development Corporation (LEDC) for review and approval.

TCA is a start-up airline domiciled in Curacao, Netherlands Antilles that was incorporated on February 19, 2002. The business plan for TCA envisioned the establishment of cargo and passenger flights from Baton Rouge and New Orleans to the Caribbean and on to Europe.

TCA submitted an application to DED requesting assistance in training its Louisiana workforce. The application by TCA was approved by the LDEC on October 14, 2002. On November 14, 2002, DED entered into a two-year (November 2002 - November 2004) contract with TCA for \$500,000. On March 14, 2003, the contract was amended to increase the funding from \$500,000 to \$639,345.

According to the contract, DED was to reimburse TCA for courses/instruction expenses, travel expenses for instructors and familiarization trips to St. Martin and Curacao, and materials/supplies expenses necessary to train up to 162 people. The training was to include ticketing/reservations, accounting, handling agents, sales, computer, customer service, tour desk, and security. The contract also requires TCA to hire 162 new employees and retain those positions until November 13, 2004, the termination date of the contract.

Reimbursement to TCA

According to the contract, TCA's training and travel expenses were to be paid on the basis of cost reports. The contract specified that expenses were to be reimbursed at 90% with the remaining 10% to be retained by DED until all performance objectives were met. A TCA designee was required to certify that the expenses listed on the cost reports were in accordance with the contract terms, the law, and the rules of the Workforce Development and Training Program. In addition, the contract required TCA to submit semiannual progress reports, the first being due in April 2003, and Louisiana Department of Labor ES-4 Forms (Quarterly Report of Wages Paid), due with each cost report.

Between November 26, 2002, and April 11, 2003, DED made five disbursements totaling \$519,308 to TCA. The expenses were divided among courses/instruction expenses (\$316,538), travel expenses (\$175,270), and materials/supplies expenses (\$27,500). Each disbursement was

supported by a signed cost report as required by the contract. In addition to the cost reports, DED requested a listing of the courses and the students who attended each course (training schedules). TCA provided training schedules to support the \$316,538 in courses/instruction expenses. TCA did not provide any support for the \$175,270 in travel expenses and the \$27,500 in materials/supplies expenses other than the cost reports.

Even though \$120,037 (\$639,345 contract amount - \$519,308 of reimbursed training expenses) of the contact funds were still available, TCA did not request any disbursements subsequent to April 11, 2003. TCA also failed to submit the required semiannual progress reports and ES-4 forms.

Training Reimbursement Discrepancies

Our review of the limited documentation that was provided to DED revealed several discrepancies. These discrepancies include:

- (1) excessive training cost per trainee;
- (2) excessive training hours;
- (3) over billed training costs;
- (4) instructors listed as trainees; and
- (5) training not provided.

Excessive Training Costs Per Student

Although the contract covered a two-year period (November 2002 - November 2004), TCA spent \$519,308, over 80%, of the contract funds in the initial five months of the contract. TCA provided documentation indicating 60 of the projected 162 trainees received instruction during this period leaving \$120,037 to train the remaining 102 people. Based on contract amounts, the projected training cost for each trainee was \$3,947 ($\$639,345 \text{ projected training costs} / 162 \text{ projected trainees}$). Based on the cost reports submitted by TCA, the actual cost per trainee was \$8,655 ($\$519,308 \text{ reimbursed training costs} / 60 \text{ trainees}$). TCA has not provided any information indicating that any individual other than the initial 60 trainees has received training or been hired.

Excessive Training Hours

The contract between DED and TCA includes a fee schedule that details the number of hours for each course. The training schedules supplied by TCA identify the specific courses taken by each trainee and the number of sessions of each course that was taken. We calculated the total number of hours of course instruction per month for each trainee using these documents.

Our review of TCA records indicated that on 46 occasions, trainees received more than 336 hours of training in a one-month period. To complete 336 course hours in a month, a trainee had to work 12 hours every day for the entire month. In 26 of the 46 occasions, records indicate that trainees received 730 or more hours of training in a one-month period. A trainee working 24 hours a day 7 days a week could only complete approximately 730 hours of training in a month's time. Therefore, a trainee receiving more than 730 hours of training time in a month is impossible. Five trainees received 1,000 or more hours of training in a given month.

For example, G. Matherne is listed on the March 2003 training schedule as having received 1,010 hours of training. His training included 280 hours of ticketing training, 280 hours of reservation training, and 450 hours of customer service training. Records indicate that Mr. Matherne attended four 70-hour sessions of ticketing training, four 70-hour sessions of reservation training, and five 90-hour sessions of customer service training.

Over Billed Training Costs

The fee schedule also lists the per hour cost for each of the nine different training courses. During the period November 2002 through March 2003, TCA requested and received reimbursements totaling \$316,538 for training courses. Based on the fee schedule, TCA should only have been reimbursed \$268,620 for the training courses. Therefore, TCA charged substantially more for the training courses than allowed by the fee schedule.

For example, the December 2002 training courses should have cost \$39,180 according to the fee schedule. However, TCA requested reimbursement from DED totaling \$68,471 for these courses. In total, TCA received \$47,918 more in reimbursements from DED than it should have.

Instructors Enrolled as Students

A separate addendum to the contract indicates that TCA was to hire seven instructors to teach the training courses. This addendum provides the names, qualifications, and courses to be taught by the seven instructors. However, five of the instructors' names appear on the training schedules as trainees. The training schedules indicate that four of these instructors attended courses they taught. The following are examples:

Mr. R. Duboureq is listed as the instructor for customer service. Mr. Duboureq's qualifications indicate he has 32 years of experience in the leisure travel business. Mr. Duboureq is listed as having received 270 hours of customer service training and 240 hours of security training.

Mr. R. Gorsline is listed as an instructor for the handling course and the security course. Mr. Gorsline is listed as having received 90 hours of handling training and 240 hours of security training.

Training Not Provided

Louisiana Department of Labor records for TCA indicate that between January 2003 and March 2005, TCA employed three people in Louisiana. The training schedules TCA provided to DED indicate that two of these individuals received extensive training. According to the training schedules, each of these two individuals attended courses in customer service, tour desk, ticketing, reservations, sales, and computer. The training schedules also indicate that these courses were held in Baton Rouge, St. Martin, and Curacao. However, both individuals stated that they did not receive any formal training from TCA nor did they visit the Caribbean for any type of TCA-sponsored training.

In addition, TCA claims that its courses were provided by Avon Associates Ltd. and Carnema N.V. To date we have been unable to identify either corporation. Therefore, we cannot verify that any training services were provided.

Contract Weaknesses

The contract as drafted by DED allows TCA to be reimbursed for its training expenses on the basis of cost reports and ES-4 forms alone. The contract does not require the submission of receipts or invoices to substantiate expense reimbursements. However, TCA is required to maintain records of all reimbursable expenses and make those records available for audit at the end of the contractual period.

Because of the lack of documentation, DED cannot verify that reimbursed expenses were in accordance with contract provisions. For example, the contract requires that all travel expenses be in compliance with state travel regulations as outlined in Policy and Procedure Memorandum (PPM) 49. Because of the lack of documentation, DED cannot verify that the travel expenses were in compliance with PPM 49 or even whether they were incurred at all.

Although the purpose of the contract with TCA was to train and employ Louisiana workers, no provision in the contract requires TCA to provide DED with contact information for each trainee or even the name of the people who receive training. The contract compliance officer, on her own initiative, requested documentation from TCA for the individuals trained and the courses they attended. The training schedules that TCA supplied did not even indicate the first name of most of the trainees. DED, consequently, has no way to determine whether the services were provided or even whether the trainees were Louisiana residents.

According to Daryl Manning, legal counsel, DED use to require detailed support for all reimbursable expenses. This practice was discontinued because of the heavy review burden placed on DED employees and the delays in making timely disbursements to contract vendors.

In addition, the contract did not require disbursements to be tied to measurable progress toward performance objectives. Although the contract requires TCA to submit semiannual reports describing progress toward performance objectives, TCA was able to circumvent this control by requesting reimbursement from DED for over 80% of the contract funds in the initial five months of the contract. DED made all of these payments prior to the first performance report becoming due.

Although the contract was for two years, there was no provision requiring distribution of the disbursements over the two-year contractual period so that adequate performance information could be acquired and evaluated. In addition, the contract did not contain a provision that unsatisfactory performance, as reflected in the performance reports, could result in denial of future payments.

To date, TCA has not established any scheduled or charter flights between Louisiana, the Caribbean, and Europe nor does it currently employ any Louisiana workers. Furthermore, TCA has denied repeated requests from DED and this office to inspect records pertaining to this contract even though the contract specifically requires TCA to maintain these records and allow inspection of these records at any time.

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The Department of Economic Development should adopt the following recommendations with regard to the Workforce Development and Training Program:

1. The practice of reimbursing contract vendors on the basis of cost reports alone should be discontinued. Contract language should be revised to require detailed support, such as invoices and receipts, for all reimbursable expenses. Disbursements should be contingent upon receipt and review of this documentation.
2. Contract language should be modified to require the vendor to provide contact information for all trainees so that DED can verify whether training services are actually provided.
3. Disbursements of contract funds should be tied to demonstrable progress toward performance objectives. Performance progress reports should be scheduled at regular intervals during the disbursement of the contract funds. DED should reserve the right to deny reimbursements based on unsatisfactory performance.
4. DED should develop a process to assess the viability of proposed projects. The viability assessment should be included in the application review process and should be approved by senior management. This practice would increase accountability and lead to more objective decision-making.
5. Applications should require detailed financial information from prospective vendors, including recent financial statements, tax returns, and documentation of additional sources of funding for proposed projects. Such information is essential in assessing the ability of companies to successfully complete proposed projects.

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The Louisiana Department of Economic Development was created in accordance with Title 36, Chapter 3 of the Louisiana Revised Statutes, as a part of the executive branch of government. DED is responsible for fostering the growth of industry and other commercial enterprises that will contribute to the overall improvement of the economy of the state.

As part of its economic development efforts, DED established the Workforce and Development Training Program in January 1997. The program offers financial assistance in the form of grants to companies for workforce training and development. In November 2002, DED entered into a Workforce and Development Training contract with Transcaribbean Airways N.V. In October 2004, DED filed suit against Transcaribbean Airways N.V. citing noncompliance with certain contract provisions.

The procedures performed during this compliance audit consisted of:

- (1) interviewing employees and officials of the department;
- (2) examining selected records of the department;
- (3) performing analytical tests; and
- (4) reviewing applicable state and federal laws and regulations.

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Management's Response



State of Louisiana

LOUISIANA ECONOMIC DEVELOPMENT

Kathleen Babineaux Blanco
Governor

Michael J. Olivier
Secretary

August 10, 2005

Mr. Steve J. Theriot, CPA
Legislative Auditor
Post Office Box 94397
Baton Rouge, Louisiana 70804-9397

Dear Mr. Theriot:

We concur with most of your recommendations as outlined on page 7 of your compliance report on the Department of Economic Development.

1. Recommendation The practice of reimbursing contract vendors on the basis of cost reports alone should be discontinued. Contract language should be revised to require detailed support, such as invoices and receipts, for all reimbursable expenses. Disbursements should be contingent upon receipt and review of this documentation.

Response Since February 2004, we are now requiring invoices and receipts to support the cost report before disbursements are approved for payment.

2. Recommendation Contract language should be modified to require the vendor to provide contact information for all trainees so that DED can verify whether training services are actually provided.

Response We don't concur with the recommendation that we obtain contact information for all trainees to determine that training was actually provided. Each company that submits a training project that is approved maintains the records for each employee trained, which courses they take, and the completion of the course. We can review those files at the company's office at any time for verification of their expenses.

3. Recommendation Disbursements of contract funds should be tied to demonstrable progress toward performance objectives. Performance progress reports should be scheduled at regular intervals during the disbursement of the contract funds. DED should reserve the right to deny reimbursements based on unsatisfactory performance.

Response We concur. Our fiscal department has designed a reimbursement worksheet which measures and calculates the percentage of performance objectives achieved based on the information supplied by the company for employees hired and payroll paid. This calculation provides us with the dollar amount of reimbursement that the company will be paid. Therefore, if the company doesn't achieve its total objectives, they will not be reimbursed for the total contract amount that had been approved.

Progress reports are required whenever a cost report is submitted for reimbursement. Specific time frames, number of hired employees, and total payroll amounts are included in our contracts.

Our contracts do provide for remedies of default by the company for the return of monies disbursed or denial of additional funds.

We did take legal action against Transcaribbean Airways on October 12, 2004. We are in the process of preparing a motion for summary judgment.

4. Recommendation DED should develop a process to assess the viability of proposed projects. The viability assessment should be included in the application review process and should be approved by senior management. This practice would increase accountability and lead to more objective decision making.
5. Recommendation Applications should require detailed financial information from prospective vendors, including recent financial statements, tax returns, and documentation of additional sources of funding for proposed projects. Such information is essential in assessing the ability of companies to successfully complete proposed projects.

Response Our response to recommendation four and five follows. We do have a process that reviews the viability of the requested training program by a company. The eligibility rules are provided to the company and then they submit the training proposal to us. If they don't meet the eligibility requirements, our staff notifies the company that their proposal for training will not be funded. If eligibility is met, financial statements and business plans are reviewed in house, cost benefit analyses are performed, and then the projects for training that are less than \$1,000,000 are reviewed by an executive loan committee from the Louisiana Economic Development Corporation for approval. Projects over \$1,000,000 are reviewed by the full board of the Louisiana Economic Development Corporation.

Mr. Steve J. Theriot, CPA
Legislative Auditor
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Our contracts also require a contractor to have a contract compliance audit be performed by a Certified Public Accountant at the end of its fiscal or accounting year. This audit must be performed in accordance with generally accepted auditing standards and the results must be made available to DED within 12 months after the fiscal or accounting year end.

We are taking steps to ensure that the contractors comply with the terms of the contract. We have also instituted a contract management function in the department for the benefit of the contract monitors.

Thanks for the opportunity to respond to your report.

Sincerely,

A handwritten signature in black ink, appearing to read "Michael Olivier". The signature is written in a cursive style with a large initial "M" and "O".

Michael Olivier, Secretary
Department of Economic Development

I:burch/letters/LA -TCA