

OFFICE OF RISK MANAGEMENT
DIVISION OF ADMINISTRATION
STATE OF LOUISIANA



MANAGEMENT LETTER
ISSUED APRIL 18, 2007

**LEGISLATIVE AUDITOR
1600 NORTH THIRD STREET
POST OFFICE BOX 94397
BATON ROUGE, LOUISIANA 70804-9397**

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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.

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In compliance with the Americans With Disabilities Act, if you need special assistance relative to this document, or any documents of the Legislative Auditor, please contact Wayne "Skip" Irwin, Director of Administration, at 225-339-3800.



STEVE J. THERIOT, CPA
LEGISLATIVE AUDITOR

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STATE OF LOUISIANA
BATON ROUGE, LOUISIANA 70804-9397

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March 21, 2007

OFFICE OF RISK MANAGEMENT
DIVISION OF ADMINISTRATION
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, 2006, we considered the Office of Risk Management's internal control over financial reporting; we examined evidence supporting certain accounts and balances material to the State of Louisiana's financial statements; and we tested the office's compliance with laws and regulations that could have a direct and material effect on the State of Louisiana's financial statements as required by *Government Auditing Standards*.

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

In our prior management letter on the Office of Risk Management for the year ended June 30, 2005, we reported findings relating to the unfunded claims costs for the road hazard line of insurance, lack of internal audit function, and untimely reimbursement requests from the second injury fund. The finding related to untimely reimbursement requests for second injury claims has been resolved by management. The findings related to the unfunded claims costs for road hazards claims and lack of internal audit function are addressed again in this letter.

Based on the application of the procedures referred to previously, all significant findings are included in this letter for management's consideration. All findings included in this management letter that are required to be reported by *Government Auditing Standards* will also be included in the State of Louisiana's Single Audit Report for the year ended June 30, 2006.

Weakness in Controls Over Small Payments on Claims

The Office of Risk Management (ORM) did not develop and implement adequate internal control over small payments on claims after a fraud was uncovered and reported in 2001, allowing a similar fraud to occur again this year. ORM's internal policies allowed adjusters to authorize claims payments up to \$5,000 without supervisory approval. Although ORM had procedures in place that required claims supervisors to randomly review claim files, this review was not adequate to ensure that all claims payments were

properly processed. Moreover, management did not implement procedures to review exception reports to compensate for this limited review of claims payments less than \$5,000. A good system of internal control should include procedures to adequately review payments before processing to reduce the risk of fraud and error.

In recent years, ORM experienced two instances of reported fraud related to small payments on claims.

- In a report issued July 26, 2006, the Compliance Audit Division of the Office of Legislative Auditor reported that a claims adjuster improperly processed 50 checks totaling \$110,766 between December 11, 2002, and August 25, 2005. Forty of these checks, totaling \$79,613, were deposited into the adjuster's personal bank account. All of these checks were issued for amounts less than \$5,000.
- In a report issued April 2, 2001, the Office of Legislative Auditor reported that a claims adjuster improperly processed small claims resulting in a theft of at least \$1,036,972.

By not implementing adequate review and control over small payments on claims after the first reported fraud, ORM did not prevent a second occurrence of fraud and suffered additional loss. ORM said that it does not have the resources to review all small payments. Without the adequate assignment of resources and new internal controls, future fraud is likely to occur.

Management should implement adequate internal control procedures over small payments on claims to ensure that only valid claims payments are processed. Management concurred with the finding and outlined corrective action (see Appendix A, page 1).

Unfunded Claims Costs for the Road Hazard Line of Insurance

For the third consecutive year, ORM is allocating costs associated with processing road hazard claims, including legal fees, to the road hazard line of insurance without collecting premiums or receiving appropriations to cover these costs. The deficit in the road hazard line of insurance increases each year by new claims, as well as the costs associated with processing road hazard claims, because ORM does not receive any funds to cover these costs. At June 30, 2006, ORM has accumulated a deficit of over \$800 million in the road hazard line of insurance. For the year ended June 30, 2006, costs associated with processing road hazard claims totaled \$9.8 million, but no insurance premiums or state appropriations were collected to cover these costs. Sound business practice dictates that premiums or appropriations should be collected to fund required claim payments, settlements, and associated costs for each line of insurance.

The Division of Administration made a decision effective July 1, 2002, that ORM would no longer pay settlements and judgments for road hazard claims from premiums collected. Settlements and judgments are now paid through direct legislative appropriation. However, no provision has been made for the associated costs of processing road hazard claims, including legal fees, other professional services, and salaries for the adjusters handling the claims. ORM included an estimate of premiums for the road hazard line of insurance in its budget request submitted to the Office of Planning and Budget for the year ended June 30, 2006. However, the Office of Planning and Budget cut 100% of the road hazard premium from the budget request.

The Division of Administration and ORM should develop premiums and/or present suggestions to the legislature as to how the state might fund future costs associated with processing road hazard claims, as well as recommending a funding methodology to eliminate the accumulated deficit over time. Management concurred with the finding and outlined a corrective action plan (see Appendix A, page 2).

No Internal Audit Function

As reported in previous audits, ORM did not have an internal audit function to examine, evaluate, and report on its internal controls, including information systems, and to evaluate compliance with the policies and procedures that comprise internal controls. Act 46 of the 2005 Regular Session of the Louisiana Legislature requires ancillary agencies with budgets in excess of \$30 million to use existing program resources and the table of organization to establish an internal auditor position. Considering the size of ORM's reported assets (\$182,435,575) and revenues (\$389,234,417), an effective internal audit function is important to ensure that assets are safeguarded and that management's policies and procedures are uniformly applied.

Management should establish an internal audit function to provide assurance that assets are safeguarded and to ensure that management's policies and procedures are applied in accordance with management's intentions. Management concurred with the finding and outlined a corrective action plan (see Appendix A, page 3).

Checks Not Voided Timely or Reissued Properly

ORM does not have controls in place to ensure that claims-related checks are voided in a timely manner and that stale-dated checks are properly reissued when necessary. Good internal control requires that procedures be performed to ensure that checks are voided in a timely manner to reduce the risk that a payment will be made for services not rendered. In addition, good business practice dictates that a reasonable attempt should be made to contact the payee when a check becomes stale-dated to determine if a check should be reissued.

In a test of 54 stale-dated checks related to claims totaling \$77,980, we noted the following:

- Eleven checks (20%) totaling \$17,885 were not voided in a timely manner.
 - Five checks were duplicate payments. The adjuster issued a replacement check without first voiding the original check.
 - Four checks were issued for depositions that were subsequently canceled. These checks should have been voided when the adjuster became aware that a deposition was not going to occur.
 - One check was issued to a worker's compensation claimant who returned to work during the period covered by the check. This check should have been voided when the employee returned to work.
 - One check was issued to a state agency as a reimbursement for a deductible. The adjuster subsequently determined that the reimbursement was not owed by ORM. However, the adjuster did not void the check.
- Of 32 checks that should have been reissued, 28 checks (88%) totaling \$34,248 were not properly reissued. When these checks became stale-dated, the accounting department properly processed the void request forms submitted by the adjusters. However, the adjusters did not make a reasonable attempt to contact the vendors or claimants to determine whether ORM should reissue the checks.

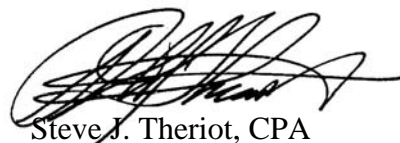
Because of the lack of adequate controls and processes, checks are voided untimely, which increases the risk that payment will be made for services not rendered. In addition, checks not properly reissued to a valid vendor subjects ORM to potential penalties for not making timely vendor payments.

Management should develop written procedures for processing void request forms and stale-dated checks to document the responsibilities of the accountants, claims adjusters, and claims supervisors, including timely processing and a reasonable attempt to contact the payee to determine if a check should be reissued. Management concurred with the finding and outlined corrective action (see Appendix A, page 4).

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

This letter is intended for the information and use of the office and its management and is not intended to be, and should not be, used by anyone other than these specified parties. Under Louisiana Revised Statute 24:513, this letter is a public document and it has been distributed to appropriate public officials.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Steve J. Theriot", is written over a faint, circular watermark or seal.

Steve J. Theriot, CPA
Legislative Auditor

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



State of Louisiana
DIVISION OF ADMINISTRATION
OFFICE OF RISK MANAGEMENT

KATHLEEN BABINEAUX BLANCO
GOVERNOR

JERRY LUKE LEBLANC
COMMISSIONER OF ADMINISTRATION

February 1, 2007

Mr. Steve J. Theriot
Legislative Auditor
Office of the Legislative Auditor
State of Louisiana
P. O. Box 94397
Baton Rouge, LA 70804-9397

RE: Office of Risk Management Audit Findings

Dear Mr. Theriot:

Finding: Weakness in Controls over Small Payments on Claims

The Office of Risk Management (ORM) concurs with the finding.

An internal report listing settlement and expense payments under \$5,000 processed through the Risk Management Information System (STARS) is being developed. This report will be distributed to claims supervisors for review prior to a check being issued for the payment. Supervisors will be instructed to select a sample number of payments from the report and verify the validity of those payments. Sample selection instructions will ensure that payments from each adjuster are included in the review process.

The contact person for this finding is Ann Wax.

Sincerely,

A handwritten signature in black ink, appearing to read "J. S. 'Bud' Thompson, Jr.", written over a white background.

J. S. "Bud" Thompson, Jr.
State Risk Director

JST/THA/tha



State of Louisiana
DIVISION OF ADMINISTRATION
OFFICE OF RISK MANAGEMENT

KATHLEEN BABINEAU BLANCO
GOVERNOR

JERRY LUKE LEBLANC
COMMISSIONER OF ADMINISTRATION

November 1, 2006

Mr. Steve J. Theriot
Legislative Auditor
Office of the Legislative Auditor
State of Louisiana
P. O. Box 94397
Baton Rouge, LA 70804-9397

RE: Office of Risk Management Audit Findings

Dear Mr. Theriot:

Finding: Unfunded Claims Costs for the Road Hazard Line of Insurance

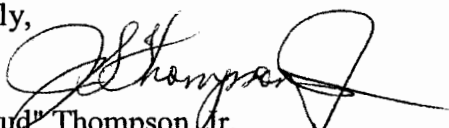
The Office of Risk Management (ORM) concurs with the finding.

ORM calculates and includes an amount for premiums in the road hazard line of insurance in its budget request each year to cover current year cash needs and reduce the \$816 million plus accumulated deficit. There is an Attorney General opinion that Transportation Trust Fund monies cannot be used to pay insurance premiums. Since Fees and Self Generated Revenue collected by the Department of Transportation and Development is not sufficient to pay the premium, the Legislature would have to appropriate monies from other funds to pay the premium. The Legislature has chosen to only appropriate funds to pay a limited number of settlements and judgments each year rather than fund the road hazard portion of the State self-insurance fund.

ORM will continue to actuarially calculate premiums for the road hazard insurance line and submit them in the Office of Risk Management annual budget request. In addition, ORM will emphasize the cost of processing road hazard claims within the budget request.

The contact person for this finding is J. S. "Bud" Thompson, Jr.

Sincerely,


J. S. "Bud" Thompson, Jr.
State Risk Director

JST/THA/tha



State of Louisiana
DIVISION OF ADMINISTRATION
OFFICE OF RISK MANAGEMENT

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November 1, 2006

Mr. Steve J. Theriot
Legislative Auditor
Office of the Legislative Auditor
State of Louisiana
P. O. Box 94397
Baton Rouge, LA 70804-9397

RE: Office of Risk Management Audit Findings

Dear Mr. Theriot:

Finding: No Internal Audit Function

The Office of Risk Management (ORM) concurs with the finding.

During the past three years, ORM has requested and received reviews from the State Inspector General's Office. Because of organizational changes and the two hurricanes, this was not accomplished in FY 06.

ORM management is exploring the avenues to establish and fill a resident Internal Auditor position in the next fiscal year or have the internal audit requirements satisfied by other means.

The contact person for this finding is J. S. "Bud" Thompson, Jr.

Sincerely,

A handwritten signature in black ink, appearing to read "J. S. Thompson, Jr.", written over a horizontal line.

J. S. "Bud" Thompson, Jr.
State Risk Director

JST/THA/tha



State of Louisiana
DIVISION OF ADMINISTRATION
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February 1, 2007

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Baton Rouge, LA 70804-9397

RE: Office of Risk Management Audit Findings

Dear Mr. Theriot:

Finding: Checks Not Voided Timely or Reissued Properly

The Office of Risk Management (ORM) concurs with the finding.

ORM has written procedures for processing daily void check requests which have been updated to include procedures for handling stale dated checks follow up. In addition, instructions to adjusters will include direction to secure possession of and subsequently void checks that have been issued in error or will not be negotiated by the payee on a timely basis. These instructions will emphasize the responsibility of the adjuster to be proactive in this process.

The contact person for this finding is Tom Averett.

Sincerely,

A handwritten signature in black ink, appearing to read "Bud Thompson, Jr.", written over a white background.

J. S. "Bud" Thompson, Jr.
State Risk Director

JST/THA/tha