

STATE OF LOUISIANA LEGISLATIVE AUDITOR

Executive Department
State of Louisiana
Baton Rouge, Louisiana

February 28, 1997



Financial and Compliance Audit Division

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

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**EXECUTIVE DEPARTMENT
STATE OF LOUISIANA
Baton Rouge, Louisiana**

**Management Letter
Dated February 3, 1997**

Under the provisions of state law, this report is a public document. A copy of this report has been submitted to the Governor, to the Attorney General, and to other public officials as required by state law. A copy of this report has been made available for public inspection at the Baton Rouge office of the Legislative Auditor.

February 26, 1997



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February 3, 1997

HONORABLE BL. J. "MIKE" FOSTER, JR., GOVERNOR
EXECUTIVE DEPARTMENT
STATE OF LOUISIANA
Baton Rouge, Louisiana

As part of our audit of the State of Louisiana's financial statements for the year ended June 30, 1996, we conducted certain procedures at the Executive Department. Our procedures included: (1) a review of the department's internal control structures; (2) tests of financial transactions; (3) tests of adherence to applicable laws, regulations, policies, and procedures governing financial activities; and (4) a review of compliance with prior year report recommendations.

The June 30, 1996, Annual Fiscal Report of the Executive Department was not audited or reviewed by us, and, accordingly, we do not express an opinion or any other form of assurance on that report. The department's accounts are an integral part of the financial statements of the State of Louisiana, upon which the Louisiana Legislative Auditor expresses an opinion.

Our procedures included interviews with management personnel and selected department personnel. We also evaluated documents, files, reports, systems, procedures, and policies as we considered necessary. After analyzing the data and based upon the application of the procedures referred to previously, we developed recommendations for improvements. We then discussed our findings and recommendations with appropriate management personnel before submitting this written report.

In our prior management letter dated December 14, 1995, we reported several findings relating to the department's internal control structure and compliance with laws and regulations. The findings relating to internal audit function, fund balance requirements - Patient's Compensation Fund, and subsequent monitoring and audit resolution - Louisiana Federal Property Assistance Agency have not been resolved and are addressed again in this report. The remaining findings addressed in our prior year management letter were resolved by management. Based upon the application of the procedures referred to previously, all significant findings are included in this report for management's consideration.

Internal Audit Function

For the fifth consecutive year, the Executive Department does not have an effective internal audit function to examine, evaluate, and report on its internal control structure, including data processing, and to evaluate its compliance with the policies and procedures of the control system.

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Considering the department's reported assets (approximately \$79 million) and its operating revenues (approximately \$201 million), we believe that an effective internal audit function is needed to ensure that the state's assets are safeguarded and that state policies and procedures are uniformly applied. Furthermore, the Appropriation Act (Act 95, Section 6C) of the 1995 Regular Session of the Louisiana Legislature states that the budget request of any agency with an appropriation level of \$30 million or more must include within its existing table of organization the position of internal auditor. Although the Executive Department established this position, it was not filled during the year.

The Executive Department should take the necessary steps to establish an effective internal audit function. In a letter dated August 23, 1995, Mr. Mark C. Dreesen, Commissioner of Administration, stated that the department concurred with the finding and recommendation. However, the Commissioner stated that several issues must be addressed before implementation within the department, including pay grade allocations provided by Civil Service and how the internal audit function is to be managed.

**Inadequate Fund Balance -
Patients' Compensation Fund**

For the fifth consecutive year, the Executive Department, Patients' Compensation Fund Oversight Board, did not maintain an adequate surplus in the Patients' Compensation Fund as required by Louisiana law. Louisiana Revised Statute (LSA-R.S.) 40:1299.44(A)(3)(a) requires that a surplus of 50 percent of the annual surcharge premiums, reserves established for individual claims, reserves established for incurred but not reported claims, and expenses be maintained in the fund.

For the fiscal year ended June 30, 1995, the accumulated balance of surcharges, reserves, and expenses is estimated to be approximately \$264 million, which under Louisiana law would require a fund balance of approximately \$392 million. As of June 30, 1995, the actual fund balance was approximately \$68 million, resulting in a shortfall of \$324 million. This shortfall resulted from practices in effect before the Patients' Compensation Fund Oversight Board was created, whereby rates for medical retraction premiums were not set based on experience ratings, including historical losses, interest payments, and future medical amounts.

The board should maintain an adequate rate level to achieve the 50 percent surplus requirement over a reasonable period of time. In a letter dated September 18, 1995, the executive director of the board concurred with the finding and recommendation and stated that the Insurance Rating Commission refused to approve a 15 percent rate increase for 1995, but that the board intends to request a rate increase effective January 1, 1997, which should increase the surplus to \$75 million next year.

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**Lack of Subrecipient Monitoring and
Audit Resolution System**

For the fourth consecutive year, the Louisiana Federal Property Assistance Agency (LFPAA) does not have a system to ensure that subrecipients who receive \$25,000 or more of federal surplus property annually from the Division of Federal Surplus Personal Property Program (DFPPA, 39.000) are audited, and that audit reports are received for resolution as required by Office of Management and Budget (OMB) Circular A-128. For the fiscal year ended June 30, 1995, we noted that six state agencies received property valued at over \$25,000 (23.3 percent of original acquisition cost), two of which received over \$100,000. We also noted that 12 local government or nonprofit subrecipients received over \$25,000 (23.3 percent of original acquisition cost), two of which received over \$100,000. The LFPAA has not obtained audit reports on the local government or nonprofit subrecipients.

A monitoring system should ensure that independent audits are performed; audit reports are reviewed; desk reviews of the independent audit reports are performed to determine compliance with OMB Circular A-128 for state and local governments and A-133 for nonprofit organizations and colleges and universities, and corrective action is taken in instances of noncompliance within six months after receipt of audit reports.

The LFPAA should develop a system to ensure that subrecipients who receive \$25,000 or more of federal surplus property annually from the program are audited, and reports are received for resolution in a timely manner. In a letter dated September 11, 1995, Mr. Jack Luzzo, Acting Director, stated that the agency concurred with the finding and recommendation. However, the agency has not been able to comply due to a lack of personnel and because software to provide information enabling LFPAA to monitor subrecipients was not developed by the Office of Information Services as promised.

Noncompliance With the Cash Management Act

The Executive Department, Division of Administration did not comply with the Cash Management Improvement Act (CMIA) when the division requested federal funds under the Community Development Block Grants Program (CDBG 14.238) in excess of its immediate needs. The CMIA agreement between the State of Louisiana and the U.S. Department of the Treasury requires the state to schedule the receipt of federal funds such that the funds received and credited to a state account are in accordance with check clearance patterns. We determined that there were instances where the division drew federal funds in advance rather than using the check clearance patterns as a basis for the draws. They include the following:

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1. On October 3, 1995, \$1,600,000 of federal funds were drawn in advance with the actual disbursement of funds occurring on varying dates during the period October 8, 1995, through October 30, 1995.
2. On November 16, 1995, \$3,900,000 of federal funds were drawn in advance with the actual disbursement of funds occurring on varying dates during the period November 22, 1995, through December 16, 1995.
3. On December 29, 1995, \$1,111,580 of federal funds were drawn but were not disbursed until December 29, 1995.

The excess funds were drawn in anticipation of a furlough of federal employees, which occurred during the periods November 14 to November 17, 1995, and December 16, 1995, to January 5, 1996, and were used to fund grantees during the furlough periods. The division's failure to comply with the CMAA agreement has subjected the state to a potential interest liability of \$20,404.

The Division of Administration should ensure that federal funds are drawn in compliance with the CMAA agreement. In a letter dated October 26, 1995, Mr. Mark C. Dreesen, Commissioner of Administration, concurred with the finding and stated that the division drew these funds early because of the impending and resulting actual shutdown of the federal government to ensure that funds were on hand to meet grantees' needs. The Executive Department has had and continues to have established procedures to ensure compliance with the CMAA agreement.

Office of Urban Affairs and Development :
Lack of Controls for Grant Administration

The Executive Department, Office of Urban Affairs and Development did not establish and maintain adequate internal controls for administration of Urban Development grants. Good internal controls require written policies and procedures for awarding and monitoring grants, including detail eligibility requirements to be used in the evaluation process. In our consideration of internal controls, the following weaknesses were noted in the administration of the Urban Development grants:

- The office does not have formal policies and procedures for awarding and monitoring grants.
- No criteria exist for selecting grant recipients.
- The office does not use a formula or any other formal criteria for determining the level of funding or the areas of the state to be funded.

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- The cooperative endeavor agreement form does not require a detailed description of services to be provided.
- Grant funds are disbursed at one time in the beginning of the year or grant term.

These same conditions were included in the Legislative Auditor's Office, Performance Audit Division's Staff Study, dated December 13, 1995. Because these conditions continue to exist, program objectives may not be met, improper grant awards may be made, grant expenditures may not be cost beneficial, and remaining grant funds may not be returned to the Urban Program. In the fiscal year ended June 30, 1996, Urban Development disbursed \$9,879,771 to 110 nonprofit organizations.

The Executive Department, Office of Urban Affairs and Development should establish formal policies and procedures for awarding and monitoring grants, including eligibility requirements for receiving grants. The cooperative agreement form should contain a detailed description of services to be provided, and grant funds should be disbursed periodically as needed. In a letter dated November 25, 1996, Mr. Kevin E. Cunningham, Assistant Chief of Staff, stated that the Office of Urban Affairs and Development agreed with the finding and that steps have been taken to address these weaknesses. A new application package has been developed along with a monthly monitoring report. These initiatives along with the reforms already in place should address these deficiencies.

Carry-Over of Funds in Excess of Bond Sale Obligations

The Division of Administration carried over funds in excess of bond sale obligations existing as of June 30, 1996. LSA-R.S. 38:8230 authorizes the Commissioner of Administration, with the approval of the Joint Legislative Committee on the Budget, to incorporate into the new fiscal year's appropriation any appropriations from the subsequent fiscal year against which bond sale obligations existed on the last day of the fiscal year. The Division of Administration obtained approval on a budget amendment form (BA-7) dated July 10, 1996, to carry over \$1,422,875 of General Fund means of financing to the 1996-97 fiscal year appropriation for professional service contracts. The contracts had a remaining balance of only \$1,244,140; therefore, funds carried over into the 1996-97 fiscal year exceeded bond sale obligations by \$178,732 at June 30, 1996.

The Division of Administration, Office of Finance and Support Services prepared the BA-7 before paying some additional invoices in the 45-day period after the end of the fiscal year and did not consider these payments in computing the carry-over amount. As a result, the Division of Administration is not in compliance with Louisiana law relating to carry-over of funds.

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The Division of Administration should submit a BA-7 to adjust the funds carried over to the amount of bona fide obligations as of the end of the fiscal year June 30, 1996, to avoid overspending in the current fiscal year. In a letter dated November 27, 1996, Mr. Whitman J. King, Jr., Deputy Undersecretary, Division of Administration, did not concur with the finding that the Division of Administration was in noncompliance with Louisiana law relating to carry-over of funds. He stated that the BA-7 dated July 10, 1996, in the amount of \$1,422,576 represented the balance remaining on professional services contracts as of that date. Therefore, the Division of Administration did have bona fide obligations totaling \$1,422,576, and did consider invoices received and/or paid through July 10, 1996, in the determination of the balances to be requested for the carry-over. However, based on the audit finding, the Division of Administration will submit a BA-7 to reduce the funds carried over to fiscal year 1996-97 by \$175,532. This represents the amount paid between July 10, 1996, and August 13, 1996, for services provided on or before June 30, 1996, and, therefore, charged to fiscal year 1995-96.

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

This report is intended for the information and use of the department 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,



Daniel G. Kyle, CPA, CFE
Legislative Auditor