

LEGISLATIVE AUDITOR
STATE OF LOUISIANA



————— OFFICE OF RISK MANAGEMENT —————
EXECUTIVE DEPARTMENT
STATE OF LOUISIANA

MANAGEMENT LETTER
ISSUED JANUARY 12, 2005

**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.

This document is produced by the Legislative Auditor, State of Louisiana, Post Office Box 94397, Baton Rouge, Louisiana 70804-9397 in accordance with Louisiana Revised Statute 24:513. Three copies of this public document were produced at an approximate cost of \$6.18. This material was produced in accordance with the standards for state agencies established pursuant to R.S. 43:31. This report is available on the Legislative Auditor's Web site at www.la.state.la.us. When contacting the office, you may refer to Agency ID No. 8402 or Report ID No. 04301980 for additional information.

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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December 16, 2004

OFFICE OF RISK MANAGEMENT
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, 2004, 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 department'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 an opinion.

In our prior management letter on the Office of Risk Management for the year ended June 30, 2003, we reported findings relating to the deficit in the road hazard line of insurance, inaccurate data recorded in the claims management system and untimely reimbursement requests, and misstated reserves and untimely reimbursement requests for second injury claims. The finding related to the inaccurate data recorded in the claims management system and untimely reimbursement requests has been resolved by management. The finding related to misstated reserves and untimely reimbursement requests for second injury claims is addressed again in this letter. While elements of the prior year finding related to the deficit in road hazard line of insurance were resolved through the courts, the deficit still exceeds \$628 million at June 30, 2004, and a finding is included in this report.

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* have also been included in the State of Louisiana's Single Audit Report for the year ended June 30, 2004.

LEGISLATIVE AUDITOR

**OFFICE OF RISK MANAGEMENT
EXECUTIVE DEPARTMENT
STATE OF LOUISIANA**

Management Letter, Dated December 16, 2004

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**Unfunded Claims Costs for the
Road Hazard Line of Insurance**

The Office of Risk Management (ORM) is allocating costs associated with processing road hazard claims (including legal fees) to the road hazard line of insurance and making payments for small claims losses (that are not the result of settlements or judgments), without collecting premiums or direct appropriations to cover the costs. The deficit in the road hazard line of insurance increases each year by the costs incurred in the road hazard line of insurance because ORM does not receive any funds to cover these costs. At June 30, 2004, ORM has accumulated a deficit of over \$628 million in the road hazard line of insurance. For the year ended June 30, 2004, costs associated with processing road hazard claims and payments made on small claims of the road hazard line of insurance totaled \$11.1 million, but no insurance premiums or sufficient state appropriations were collected for this line of insurance. Sound business practices dictate that premiums or appropriations should be collected to fund required claim payments, settlements and associated costs, including legal fees, 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, salaries for the adjusters handling the claims, and small claims losses that are not the result of settlements or judgments.

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, 2004. 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 and small claims losses of the road hazard line of insurance, as well as a funding methodology to eliminate the accumulated deficit over time. Management concurred with the finding and recommendations and outlined a plan of corrective action (see Appendix A, page 1).

LEGISLATIVE AUDITOR

OFFICE OF RISK MANAGEMENT EXECUTIVE DEPARTMENT STATE OF LOUISIANA

Management Letter, Dated December 16, 2004

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Misstated Reserves and Untimely Reimbursement Requests

For the eighth consecutive year, ORM has misstated reserves for second injury claims and has not requested timely reimbursements from the Second Injury Fund. Louisiana Revised Statute (R.S.) 39:1527 *et al.* created ORM as the state's self insurance agency. The Second Injury Fund exists to encourage employment of physically handicapped employees who have a permanent, partial disability by protecting employers and their insurers from excess liability when a subsequent injury to such an employee merges with his/her preexisting disability. R.S. 23:1378 divides the financial responsibility for paying second injury claims between the state's insurer (ORM) and the Second Injury Fund. In addition, ORM policy states that a notice of claim must be filed against the Second Injury Board within one year from the date of the issuance of the first payment, and the adjuster must request reimbursement once every three to six months until the claim is closed. ORM policy also outlines reserve requirements for medical and indemnity claims.

In 38 (58%) of 65 second injury claims tested, errors were noted resulting in \$871,151 not collected by ORM from the Second Injury Fund and a \$662,956 understatement of liabilities in the financial statements.

Management has developed policies and procedures for requesting reimbursements from the Second Injury Fund and adjusting and setting reserves on claims. However, the policies and procedures for setting reserves have not been enforced. In addition, the policies and procedures are not adequate to ensure that all reimbursement requests have been submitted to the fund in a timely manner. Errors in the reserves may cause misstatements of liabilities in the state's financial statements. Failure to request reimbursement in a timely manner may affect ORM's ability to recover costs.

Management should ensure that the reserves for claims are adjusted to reflect the actual and estimated expenditures or the required reserve limit per ORM policies and procedures. Second Injury Fund reimbursements for medical and weekly benefit expenditures should be requested in a timely manner. ORM should develop policies and procedures that would allow ORM to more closely monitor claim reimbursement requests handled by the contracted vendor. ORM should include reconciliation procedures to ensure that all claim payments due in the claim management system are requested for reimbursement from the Second Injury Fund. Management concurred with the finding and recommendations and outlined a plan of corrective action (see Appendix A, page 2).

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**OFFICE OF RISK MANAGEMENT
EXECUTIVE DEPARTMENT
STATE OF LOUISIANA**

Management Letter, Dated December 16, 2004

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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 the office's 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", written over a horizontal line.

Steve J. Theriot, CPA
Legislative Auditor

DG:ES:PEP:dl

ORM04

Appendix A

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

November 19, 2004

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 \$628 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.

We will continue to actuarially calculate premiums for the road hazard insurance line and submit them in the Office of Risk Management annual budget request.

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

Sincerely,

A handwritten signature in cursive script, appearing to read "Bud Thompson, Jr.", written over a horizontal line.

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

JST/THA/tha



State of Louisiana
DIVISION OF ADMINISTRATION
OFFICE OF RISK MANAGEMENT

KATHLEEN BABINEAUX BLANCO
GOVERNOR

JERRY LUKE LEBLANC
COMMISSIONER OF ADMINISTRATION

November 19, 2004

Mr. Steve Theriot
Legislative Auditor
Office of the Legislative Auditor
State of Louisiana
P. O. Box 97397
Baton Rouge, LA 70804-9397

RE: Office of Risk Management Audit Findings

Dear Mr. Theriot

Finding: Misstated Reserves and Untimely Reimbursement Requests

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

The claims in the finding are dated prior to the date (July 1, 1983) that medical expenses became eligible for reimbursement by the Second Injury Fund (SIF) and established the maximum medical reserve at \$7,500. The Office of Risk Management implemented a new Risk Management Information System on July 1, 2004 that contains validations that limit the reserve amount that can be set on SIF claims dated prior to July 1, 2004 to the insurer's retention amount (a maximum of \$7,500). It is anticipated that an enhancement to the system will be implemented by January 1, 2005 that will allow ORM adjusters to be able to correct the understated reserves.

The Office of Risk Management utilizes a contract vendor to help secure Second Injury Fund approval and also to request reimbursements on regular intervals. The contract vendor reviews ORM claims once every four months to identify potential SIF claims and to gather documentation to request reimbursements on approved claims. ORM will have a diary tickler placed on each SIF claim so that the Risk Management Information System will provide a reminder to the adjuster when action is necessary to secure reimbursement. The adjuster will follow up to get the claim to the vendor for processing.

ORM supervisors will process and review reports quarterly to ensure SIF claims procedures are being followed.

Karen Jackson is the contact person for this finding.

Sincerely,


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

JST/THA/tha