

OFFICE OF RISK MANAGEMENT  
DIVISION OF ADMINISTRATION  
STATE OF LOUISIANA



MANAGEMENT LETTER  
ISSUED JANUARY 18, 2012

**LOUISIANA 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. One copy of this public document was produced at an approximate cost of \$3.91. 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.la.gov](http://www.la.la.gov). When contacting the office, you may refer to Agency ID No. 8402 or Report ID No. 80110071 for additional information.

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LOUISIANA LEGISLATIVE AUDITOR  
DARYL G. PURPERA, CPA, CFE

January 4, 2012

**OFFICE OF RISK MANAGEMENT  
DIVISION OF ADMINISTRATION  
STATE OF LOUISIANA**  
Baton Rouge, Louisiana

As required by Louisiana Revised Statute 24:513 and as a part of our audit of the State of Louisiana's financial statements for the fiscal year ended June 30, 2011, we conducted certain procedures at the Office of Risk Management (ORM) for the period from July 1, 2010, through June 30, 2011.

- Our auditors obtained and documented an understanding of the ORM operations and system of internal controls through inquiry, observation, and review of its policies and procedures, including a review of the related laws and regulations applicable to ORM.
- Our auditors performed analytical procedures consisting of a comparison of the most current and prior year financial activity using ORM's annual fiscal reports and/or system-generated reports and obtained explanations from ORM management of any significant variances.
- Our auditors reviewed the status of a finding identified in our prior year report on ORM, dated December 10, 2010, relating to an ineffective internal audit function. That finding has been resolved by management.
- Our auditors considered internal control over financial reporting; examined evidence supporting ORM's current and long-term claims liability, claims and litigation handled by ORM, annuities, and claims liability for state risk programs; and tested ORM's compliance with laws and regulations that could have a direct and material effect on the State of Louisiana's financial statements, as part of our audit of the state's Comprehensive Annual Financial Report for the fiscal year ended June 30, 2011, in accordance with *Government Auditing Standards*.

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

Based on the application of the procedures referred to previously, the following significant finding is included in this letter for management's consideration.

### **Weaknesses in Controls Over Claim Reserves**

ORM has not ensured that established controls for monitoring, adjusting, and approving claim reserves are followed by its staff.

In a test of 24 claim reserves, we noted:

- Six (25%) were overstated by \$388,381 because the reserves were not reduced once final settlement was known, when excess insurance carriers paid the claim, or when the claim was determined to be abandoned. Two of the six overstatements are part of a group of 40 claims related to the same incident. Audit procedures performed on the remaining 38 claims identified that reserves for 28 of the claims were overstated by \$8,482,257.
- One (4%) increase of \$45,000 was not approved by a supervisor as required.

In a test of 19 claim reserves managed by the third-party administrator (TPA) that exceed \$100,000, nine (47%) were not approved by ORM as required.

ORM's written procedures require (1) supervisors to ensure that claim adjusters establish adequate claim reserves that reflect the state's liability and exposure and periodically review reserve amounts to maintain an adequate balance; (2) adjusters to obtain supervisory approval for reserve increases that exceed their authority; and (3) its approval of claim reserves managed by the TPA that exceed \$100,000.

Management has not sufficiently emphasized the importance of following established procedures for ensuring that reserves are monitored and adjusted to accurately reflect the state's estimated claim liability and exposure and has not identified all reserves managed by the TPA that exceed \$100,000 for approval. Failure to adequately monitor and adjust claim reserves increases the risk of misstatement of the state's estimated claim liability.

ORM's management should identify all reserves managed by the TPA that exceed \$100,000 and ensure that the adjusters and supervisors follow established procedures for monitoring, adjusting, and approving claim reserves. Management concurred with the finding and outlined a plan of corrective action (see Appendix A).

The recommendation in this letter represents, in our judgment, that most likely to bring about beneficial improvements to the operations of ORM. The nature of the recommendation, its implementation cost, and its potential impact on the operations of ORM should be considered in reaching decisions on courses of action.

This letter is intended for the information and use of ORM and its management, others within the entity, and the Louisiana Legislature 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 blue ink that reads "Daryl G. Purpera". The signature is fluid and cursive, with the first name being the most prominent.

Daryl G. Purpera, CPA, CFE  
Legislative Auditor

MMG:CRV:BQD:THC:dl

ORM 2011

## Appendix A

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### Management's Corrective Action Plan and Response to the Finding and Recommendation

**BOBBY JINDAL**  
GOVERNOR



**PAUL W. RAINWATER**  
COMMISSIONER OF ADMINISTRATION

**State of Louisiana**  
Division of Administration  
**Office of Risk Management**

December 9, 2011

Mr. Daryl G. Purpera, CPA  
Legislative Auditor  
Office of the Legislative Auditor  
State of Louisiana  
P. O. Box 94397  
Baton Rouge, LA 70804-9397

Dear Mr. Purpera:

**Finding: Weaknesses in Controls Over Claim Reserves**

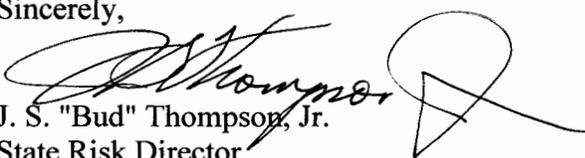
The Office of Risk Management (ORM) concurs with the finding.

ORM has a policy and procedures in place for reserve changes. The State Risk Administrator – Claims has met with all claims managers and supervisors to emphasize the importance of complying with ORM policies and procedures on reserving practices. In addition, an email was issued to all claims staff stressing the importance of establishing adequate reserves based on liability and exposure and properly documenting the claims management record as to the reason for the reserve change. ORM Senior Management will require supervisors/managers to develop and run monthly reports of reserve changes that they will review to ensure that reserves for claims are adjusted to reflect the actual and estimated expenditures and that the reserve limits established per ORM's policies and procedures are followed.

In cases handled by the TPA, procedures require that all reserve changes totaling \$100,000 must be approved by ORM. The TPA adjuster must submit justification for the reserve increase. ORM advised the TPA that all requests for reserve changes totaling \$500,000 must additionally be reviewed and approved by the TPA unit manager prior to sending the reserve request to ORM. Upon approval of the reserve change by the appropriate ORM personnel, the confirmation email noting ORM approval will be sent to the TPA and attached to the claim file record. ORM managers on lines of coverage handled by the TPA will be required to run a claim reserve change report from ICE for reserve changes over \$100,000 which will be reviewed to ensure that approval was granted by ORM for the reserve change.

The contact person for this finding is Ann Wax, State Risk Administrator – Claims.

Sincerely,

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