Review of Charges for Unemployment Compensation Insurance

New Orleans Public Schools

FINAL AUDIT REPORT

Audit Control Number 06-60010

January 98

U.S. DEPARTMENT OF EDUCATION
OFFICE OF INSPECTOR GENERAL
Dallas, TX

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January 28, 1998 Audit Control No.06-60010

Cecil J. Picard
Superintendent of Education
Louisiana Department of Education
P.O. Box 94064
Baton Rouge, LA 70804-9064

Dear Mr. Picard:

This is our audit report, *Review of Charges for Unemployment Compensation Insurance, New Orleans Public Schools.* The report incorporates the comments you provided in response to a draft report which was provided to you. If you have any additional comments or information that you believe may have a bearing on the resolution of this audit, you should send then directly to the following U.S. Department of Education official, who will consider them before taking final Departmental action on the audit:

Gerald N. Tirozzi, Assistant Secretary
Office of Elementary and Secondary Education
U.S. Department of Education
Portals Building, Room 4000
1250 Maryland Avenue, SW
Washington, DC 20202-6100

Office of Management and Budget Circular A-50 directs Federal agencies to expedite the resolution of audits by initiating timely action on the findings and recommendations contained therein. Therefore, please send your comments within 30 days.

In accordance with the Freedom of Information Act (Public Law 90-23), reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemption in the Act. Please refer to the above audit control number in all correspondence relating to this report.

Sincerely,

Daniel J. Thaens
Western Area Manager
Dallas, Texas

copy: Marlyn Langley, Deputy Superintendent, Louisiana Department of Education
Dr. Morris L. Holmes, Superintendent, New Orleans Public Schools

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Review of Charges for Unemployment Compensation Insurance

Executive Summary

The New Orleans Public Schools (NOPS) charged $2,265,212 in unreasonable unemployment compensation insurance costs to U.S. Department of Education (ED) programs for State Fiscal Years (FY) 1992 through 1996[1]. NOPS did not use a reasonable methodology for charging ED programs. Although personnel associated with ED programs accounted for only 8.4 percent of NOPS payroll costs, the ED programs were charged 48 percent of the total unemployment compensation insurance costs. Federal Regulations allow grantees to charge Federal programs only to the extent that the costs are reasonable and are allocated in accordance with the benefits received as a result of the costs. In the absence of extenuating circumstances, a reasonable basis for allocating unemployment compensation insurance costs to ED programs would have been to allocate based on the percentage of premium costs that represented the percentage of payroll for ED programs as related to the total NOPS payroll.

The Louisiana Department of Education provided ED funds to NOPS. NOPS charged an unreasonable proportion of unemployment insurance costs to various ED programs. We recommend that the Secretary require the Louisiana Department of Education to: (1) refund $2,265,212 to ED; (2) ensure that only a reasonable proportion of unemployment insurance costs are charged for periods after Fiscal Year 1996.

NOPS officials provided a management representation letter which did not contain all of the requested representations. The following representation was totally omitted:

> *"We are responsible for the fair representation of documents, records, and other information provided for your review."*

Because of the significance of the deficiencies discussed in this report, and because of the inadequacy of the management representation letter submitted by NOPS officials, we cannot provide assurance that there is not further noncompliance with laws and regulations. (See Qualification of Audit Results on page 11.)

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[1]The fiscal year discussed in this report pertains to an annual period beginning on July 1 and ending on June 30 of the following year. For example, FY 1992 began on July 1, 1991.

AUDIT RESULTS

The total cost of unemployment compensation insurance for NOPS was $5,707,526 based on paid invoices for Fiscal Years 1992 to 1996. NOPS charged ED programs $2,747,043 or 48 percent of the total using a method which did not result in a reasonable allocation of ED's share of the costs. A total of $481,831 or 8.4 percent of the total would have been a reasonable charge to ED programs based on the ratio of total salaries for NOPS personnel working on Federal programs to total NOPS salaries.

NOPS used the services of Unemployment Compensation Control Systems, Inc. (UCCS) for unemployment compensation insurance. UCCS bills NOPS for unemployment compensation insurance services based on payroll data provided by NOPS. UCCS calculates its charges by multiplying various rates times payroll dollar amounts for the three categories of fund accounts used by NOPS. As shown in the following table, the Special Revenue Fund, which contains Federal funds, is assessed a rate that is about *22 times higher* than that of the General Fund.

Billing Rates for 07/01/84-12/31/94		**Billing Rates for 01/01/95-06/30/96**	
Fund	**Rate**	**Fund**	**Rate**
Special Revenue	3.30%	Special Revenue	2.10%
Food Service	2.00%	Food Service	1.30%
General	0.15%	General	0.10%

The UCCS contract which took effect on July 1, 1984 did not provide for a single unemployment premium rate; rather, it provided for the three different rates shown above. Those rates were applied to total payroll dollars for the respective funds.

The 1995 contract provided for a single rate of 0.335 percent of payroll dollars. The use of the 0.335 percent applied to all salary dollars was expected to total the amount of the total premium charged by UCCS. For the first year of the contract, UCCS billed NOPS on the single-rate basis, using the 0.335 percentage rate. However, NOPS then requested that UCCS provide *revised invoices* for the quarters in which UCCS had billed the school district with the single rate. UCCS complied with that request, and sent four revised invoices. Those invoices broke the premium cost down into three distinct rate groups, with the cost to the Special Revenue Fund increasing and the cost to the General Fund decreasing, although the overall premium changed very little. In fact, the revised invoices contained the words "NO PAYMENT DUE". The revised rates which took effect in 1995 were in about the same ratio as the rates which were used during the period July 1, 1984 through December 31, 1994.

We visited UCCS to determine what documentation was available to support the high rate for the Special Revenue Fund (which includes primarily ED grant funds). UCCS officials stated that a 3.3 rate used for the Special Revenue Fund was established in 1984 but documentation was not currently available to support the rate. Further, UCCS officials stated that their current data base did not show the funds from which employees were being paid when they were terminated. Officials did point out that the contract negotiated for 1995 included a reduction in the rate used for the Special Revenue fund. Again, officials did not have information showing that the reduction was based on actual claims by individuals assigned to the Special Revenue Fund prior to unemployment. In fact, all of the rates decreased because the total costs of the unemployment insurance decreased.

NOPS maintains that Federal programs deserve to bear a higher cost than others for the following two related reasons:

1. Federal funds are not dependable since grants often last for only one year, with no guarantee of renewal.

2. General Fund employee layoffs are caused by Federally-funded employees who generally have more tenure and bump when layoffs are necessary.

Our review disclosed that the total Federal funds awarded to NOPS increased by 9 percent from FY 1992 to 1996. As a result, although funds for some programs may have fluctuated, Federal funds available to NOPS were stable. In addition, NOPS did not have documentation to show that employee bumping rights provided a basis for charging higher rates to Federal programs.

Federal *Cost Principles for State, Local and Indian Tribal Governments*, OMB Circular A-87 (May 17, 1995), provides regulatory guidance for costs charged to Federal grant awards. Attachment A, Section C.1 of the Circular states that allowable costs must be necessary and reasonable. Attachment B, Section 11.d specifically states that the costs of fringe benefits, including unemployment benefit plans, are allowable to the extent that the benefits are reasonable. It also states that the costs shall be allocated to Federal awards and all other activities in a manner consistent with the pattern of benefits attributable to the employees whose salaries and wages are chargeable to such Federal awards and other activities. Attachment A, Section C.3 states that a cost is allocable to a particular cost objective in accordance with the relative benefits received. Circular A-87 (January 15, 1981) included similar language.

We considered two possible methods that could be used to allocate a reasonable share of unemployment compensation costs to ED programs. One method would be to allocate the costs based on the ratio of actual dollars for claims paid to ED- funded employees[2] to the total dollars for claims paid for all employees. Data for this type of allocation was not readily available at the time of our review. In addition, this type of allocation would depend on an employee's status as of the date of termination and would not consider status during the year. The second method that we considered was to allocate the ED share based on the ratio of salary of ED-funded employees to total salary for all NOPS employees. This method does consider an employee's status over a period of time. We concluded that this was the best method available to assign the unemployment compensation insurance costs to ED.

During our audit period, ED funds were used to pay 8.4 percent of the total salaries paid by NOPS. The remaining 91.6 percent of salary cost was funded from other sources. Using 8.4 percent of total salaries as the basis of allocation, ED's share of unemployment compensation insurance costs was $481,831 for the audit period. ED was actually charged $2,747,043 which represents 48 percent of the total costs for unemployment insurance. In our opinion, the method used by NOPS for billing unemployment insurance premiums resulted in overcharges to ED totaling $2,265,212.

For the 12-month period ending June 1995, the NOPS Internal Audit Department analyzed actual claim payments associated with employees of the three different funds. The analysis showed that 91 percent of the total payments pertained to employees paid from the General Fund, whereas only 6 percent pertained to employees paid from the Special Revenue Fund, which includes ED programs. The remaining 3 percent applied to employees paid from the Food Service Fund. Although this data was not verified by an independent source, it does indicate that use of actual claim data to allocate unemployment insurance costs would not be materially different than the use of salary ratios.

[2]The funding status (ED or non-ED) of an employee would need to be determined as of the date of termination.

We calculated the excess charges to ED by subtracting the reasonable amount that *should* have been charged from the amount *actually* charged. The calculations are presented on an annual basis in the following table. Appendix I (pages 1 through 5) details the excess charges to the various Education programs for each of the five fiscal years covered by this audit.

Charges to ED for Unemployment Insurance			
Fiscal Year	**Amount That Was Actually Charged**	**Reasonable Charges**	**Excess Amount Charged to ED**
1992	$ 579,285	$ 99,234	$ 480,051
1993	$ 656,590	$111,446	$545,144
1994	$ 646,293	$120,118	$526,175
1995	$ 495,606	$ 83,720	$411,886
1996	$ 369,269	$ 67,313	$301,956
Total	$2,747,043	$481,831	**$2,265,212**

As shown, our calculations disclosed that excess unemployment compensation costs of $2,265,212 were charged to ED. Further, when we completed our review in March 1997, NOPS was continuing to use the method described in this report to charge costs for unemployment compensation insurance.

RECOMMENDATION

We recommend that the Secretary require the Louisiana Department of Education to: (1) refund $2,265,212 to ED; and (2) ensure that only a reasonable proportion of unemployment insurance costs are charged for periods after Fiscal Year 1996.

AUDITEE COMMENTS

We received comments from the Louisiana State Department of Education (LSDE) and New Orleans Public Schools (NOPS). Both of these entities disagreed with our finding and recommended actions.

Comments from the Louisiana State Department of Education

LSDE commented that if historical data indicated a higher incidence of unemployment for individuals funded under Federal programs, then it would be reasonable that those Federally-funded programs have higher premium cost. LSDE also stated that UCCS provided documents to KPMG Peat Marwick (Peat Marwick) indicating that the premiums charged to Federal programs were based on historical experience. LSDE questioned whether the OIG had considered UCCS records and the work performed by Peat Marwick. LSDE's complete comments are included as Attachment I to this report.

Comments from New Orleans Public Schools

NOPS pointed out that the OIG position concerning the recommended refund was based on reasonableness. Reasonableness involved the use of a salary ratio to allocate unemployment insurance cost as opposed to the variable rate methodology used by UCCS. NOPS stated that OMB circular A-87 neither defined "reasonableness" nor restricted cost allocation methods to only one reasonable method. The majority of the response was geared toward documenting the reasonableness of the varying interest rates used for billing unemployment insurance premiums. Risk, uncertain future Federal funding sources, and General Fund stability were three reasons given to justify the tiered rates used by NOPS.

NOPS commented that two studies have been performed which related claims paid to the funding sources of individuals at the time of termination. One study included four quarters of data ending June 30, 1995. The other included six quarters of data ending June 30, 1997. The first study was within our audit period whereas the second study included only two quarters of data that was within our audit period.

In the first study, which covered four quarters of data in our audit period, NOPS concluded that based on "Pure Premiums", the Special Revenue Fund (which includes Federal funds) had a ratio of claims paid to payroll which was seven times greater than that of the General Fund. Based on the theory of "Benefit Relativity", the ratio was also seven times greater for the Special Revenue Fund. Considering the theory of "Claims Relativity", the ratio was eleven times greater for the Special Revenue Fund. Results were similar for the six-quarter study. (Note: NOPS data excluded claims for day-by-day employees which accounted for about 45 percent of the claims paid. These claims are all paid with General funds.)

Bumping was also mentioned as a reason for some General Fund employee layoffs which resulted in unemployment claims. Bumping was explained as the process of one employee replacing another employee based on seniority. In some instances, a senior employee is funded through a Federal program. If the Federally-funded position is terminated, it results in the bumping of a General Fund employee with less seniority.

Regarding Federal fund stability, NOPS pointed out that while Federal funds may have increased, the draft report failed to mention that some Federal programs had significant fluctuations which prompted terminations and subsequent unemployment claims.

NOPS also pointed out that the 3.30 rate used to allocate unemployment costs to the Special Revenue fund was less than the overall percentage charged by the state of Louisiana.

NOPS also engaged the consulting firm of Milliman and Robertson, Inc. (M & R) to address concerns regarding the reasonableness of charging tiered rates for unemployment insurance costs. The M&R report, which concluded that tiered rates were appropriate, is included as part of the NOPS response. Page three of the consultant report included a comparison of payroll, actual benefits paid, and pure premiums for Federally-funded and non-Federally funded programs. That comparison showed that the pure premium was nearly seven times greater for Federal programs than for non-Federal programs.

Although NOPS officials did not concur with our finding or recommendation, their response expressed a willingness to discuss areas of disagreement with ED.

OIG RESPONSE TO COMMENTS

Louisiana State Department of Education

We agree with LSDE's comment that Federal programs should bear a higher premium cost if historical data indicates a higher incidence of unemployment for individuals funded under Federal programs. However, historical data does not support that premise.

LSDE also commented that UCCS provided documents to Peat Marwick indicating that premiums charged to Federal programs were based on historical experience. We visited UCCS on two occasions and were told that the rates used until January 1995 were established in 1982 and were based on historical data. However, neither UCCS nor NOPS could provide that historical data. Further, we were told that UCCS could not analyze any claim data by type of program because UCCS did not have information showing the funding source of a claimant prior to claim submission. According to UCCS, only NOPS could determine the funding source of an individual prior to that individual making an unemployment claim.

New Orleans Public Schools

The NOPS response attempted to show why a tiered rate structure was an acceptable method of charging unemployment insurance cost. The response also indicated that, based on different scenarios, Federal programs should be charged more than programs paid with General funds. The response, however, never identified amounts that should have been charged to ED. Also, the NOPS analysis of claim payments excluded temporary day-by-day workers (paid from the General Fund) which account for about 45 percent of claim payments.

Regardless of the type of rate used, a tiered rate or an across-the-board rate, the rate used to allocate costs to ED and other Federal programs should reasonably reflect the actual costs and benefits received by the various Federal programs. We found that NOPS had used the same tiered rate structure since 1982 to allocate unemployment insurance premiums. Although the rate applied to Federal programs was about 22 times greater than the rate applied to General Fund programs, NOPS had no documentation to support the rates used.

We revisited NOPS and UCCS during December 1997 and reviewed actual claim data pertaining to information included in the NOPS response to the draft report. UCCS had isolated all claim payments, and NOPS had determined the funding sources of individuals receiving unemployment insurance claim payments.

For the 18-month period ending June 30, 1996, claim payments totaled $216,962. Of those payments, we verified that only $33,970 or 15.7 percent was related to individuals employed under Federal programs prior to making unemployment claims. Based on our audit work, we concluded that about 9.7 percent of the claims identified by UCCS pertained to ED programs. This rate is similar to the salary rate of 8.4 percent which we used in our audit calculations. Since data was provided and verified for only 18 months instead of the 60 months of the audit period, and since data for the other months could cause the 9.7 percent figure to change, we still maintain that the 8.4 percent salary ratio rate is a reasonable rate to use in this audit.

After analyzing the NOPS response and reviewing claim data, our finding and recommendation remain essentially the same. At the time of our review, NOPS was not analyzing historical claim data to determine if actual claims were in line with charges for premiums. If NOPS plans to accumulate and analyze claim data in the future, then premiums for unemployment insurance could be charged to ED on the basis of the actual claim rate. Until such time that historical data is available, we believe that allocating unemployment insurance premiums to ED should be based on the percentage-of-salaries method. A complete text of each response is included with this report as Attachments I and II.

OTHER MATTERS

Our review disclosed that NOPS did not bill its General Fund in FY 1994 for its share of the Worker's Compensation Self-Insurance Fund. This problem was also documented by Peat Marwick and Bruno & Tervalon in a special report issued on November 7, 1995. Peat Marwick concluded that the appropriate costs should be charged to the General Fund, and stated that the charge could be amortized over a period of up to five years. Additionally, former internal auditors provided information indicating that some of the charges to the Worker's Compensation Fund were inappropriate.

Except for NOPS not contributing to the fund in FY 1994, which was addressed in Peat Marwick's report, we did not pursue this area any further. While there may be problems with this fund, the percentage of charges to Education programs is minimal and any recovery would not be commensurate with effort. For our five-year audit period, $16.4 million was allocated to various funds for worker's compensation coverage. Only 2.6 percent (or $430,000) was allocated to ED programs.

In our opinion, NOPS, in coordination with the Louisiana Department of Education, should follow Peat Marwick's recommendation. NOPS should also implement controls to ensure that all future charges are allocated properly. Regarding inappropriate charges to the fund, the Louisiana Department of Education may want to examine this area, as the majority of funds affected are State and Local funds.

AUDIT SCOPE AND METHODOLOGY

The primary objective of our audit was (1) to determine whether NOPS appropriately allocated unemployment compensation insurance premium costs to ED programs and (2) to quantify any overcharges applicable to inappropriate allocations. A secondary objective was to determine if there were other significant costs that were being inappropriately allocated to ED programs.

In order to accomplish our objective, we reviewed prior audit reports prepared by Peat Marwick, interviewed appropriate officials of NOPS and UCCS, and obtained relevant documents. We also gained an understanding of how NOPS accounts for its insurance costs, including the allocation of those costs to different accounting funds and grant programs. Focusing on the ED funds that flowed through the Louisiana Department of Education to NOPS, we determined the amount of unemployment costs that could reasonably be charged to ED programs, and then compared our calculation with the allocated charges. We also determined the percentage of worker's compensation costs that were charged to ED programs.

The audit period was July 1, 1991 through June 30, 1996 (Fiscal Years 1992 through 1996). Field work was performed periodically from July 1996 to March 1997. The audit was conducted in accordance with generally accepted government auditing standards appropriate to the scope of the audit described above *except* that NOPS officials provided a management representation letter which we considered to be inadequate. We considered the letter to be inadequate because management did not state its responsibility for the fair representation of documents, records, and other information provided for our review. (See Qualification of Audit Results section.)

BACKGROUND

NOPS is located in New Orleans, Louisiana, and is the largest school district in the state of Louisiana. The student enrollment is about 85,000. The District has over 9,000 employees, and operates with an annual budget of about $400 million. About 16 percent of the total budget comes from Federal funds, with about 10 percent of the budget coming from the United States Department of Education.

On September 1, 1995, the NOPS Internal Audit Department issued a report of Risk Management activities. The report maintained that NOPS was overcharging Federal programs for unemployment and worker's compensation insurances. On September 26, 1995, the NOPS management issued a response to the Risk Management report, disagreeing with all findings contained in the report. On October 10, 1995, the Internal Audit Department issued additional comments, stating that the audit report was accurate.

Since there was a disagreement between NOPS management and the Internal Audit Department, the NOPS attorney retained the accounting firms Peat Marwick and Bruno & Tervalon to do some special work. The work of the two firms was a joint effort, and one report was produced. The report, dated November 7, 1995, stated that charges to the Federal programs for unemployment compensation insurance and worker's compensation insurance were in compliance with OMB Circular A-87. The OIG disagreed that costs charged for unemployment compensation insurance were in compliance with OMB Circular A-87.

STATEMENT ON INTERNAL CONTROLS

As part of our review, we assessed the system of internal controls, policies, procedures, and practices applicable to accounting for and charging unemployment compensation insurance and worker's compensation insurance costs. Our assessment was performed to determine the level of control risk for determining the nature, extent, and timing of our substantive tests to accomplish the audit objectives. For the purpose of this report, we limited our review to gaining an understanding of the significant management controls over accounting for and charging the insurance costs to different funding sources. We identified the following management controls:

-- accounts established to accumulate insurance costs

-- methods used for billing costs to various funding sources

Because of inherent limitations, a study and evaluation made for the limited purpose described above would not necessarily disclose all material weaknesses in internal controls. However, our assessment identified weaknesses in the methods used to allocate costs to various funding sources. The weaknesses are discussed in detail in the Audit Results section of this report.

QUALIFICATION OF AUDIT RESULTS

As discussed in the Executive Summary and Audit Scope and Methodology sections, NOPS representatives provided a management representation letter which we considered to be inadequate. Generally accepted auditing standards require us to request a management representation letter from the officials of an entity we audit. The letter acknowledges management's responsibility for the fair presentation of records and reports, and asserts that the auditors have been provided all requested records. It also states that, to the best of management's knowledge, there have been no irregularities or violations of laws or regulations in connection with the scope of the audit.

A management representation letter was discussed with NOPS officials in July 1997 and on several other occasions, but NOPS did not provide a representation letter until January 23, 1998. However, the letter was dated December 4, 1997 *because* we had made a return visit to NOPS at that time to verify information that was submitted in the NOPS response to our draft report. NOPS viewed that date as our last day of field work. The NOPS letter provided three of our four requested written representations. However, management did not state its responsibility for the fair representation of documents, records, and other information provided for our review. We consider the omission of the statement to be serious. Therefore, because of the significance of the deficiencies discussed in the Audit Results section of this report and the failure of NOPS to provide an adequate management representation letter, we cannot provide assurance that there is not further noncompliance with laws and regulations.

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Schedule of Excess Unemployment Insurance Charges to ED Flow-Through Grant Programs

Fiscal Year 1992 (7/1/91-6/30/92)

Name of U.S. Department of Education Program	Program Charge Code	Special Revenue Ledger Page	Amounts Charged to Specific Programs	Reasonable Charges per OIG	Excess Amount Charged per OIG
Vocational Education (Title II-A Disadvantaged)	428	93	$2,682	$460	$2,223
ECIA Chapter 1 (IASA Title I)	431	204	$404,119	$69,227	$334,891
ECIA Chapter 1 (IASA Title I) - Carryover	432	208	$81,427	$13,949	$67,478
ECIA Chapter 1 (IASA Title I), Migrant Education	433	212	$7,236	$1,240	$5,997
Chapter 2 Parent Pilot Program	435	215	$1,371	$235	$1,136
EHA-Education for All Handicapped (P.L. 94-142)	436	225	$19,174	$3,285	$15,889
ECIA Chapter II	438	246	$13,197	$2,261	$10,937
Adult Basic Education	439	249	$5,371	$920	$4,451
Adult Basic Education - Supplemental Allocation	440	250	$125	$21	$104
Special Education Preschool Program	454	264	$847	$145	$702
Special Education Preschool Program	454	493	$55	$9	$45
EESA Title II	460	287	$8,383	$1,436	$6,947
EESA Title II - Carryover	461	293	$2,674	$458	$2,216
Drug Free Schools	472	320	$20,578	$3,525	$17,053
Drug Free Schools - Carryover	473	325	$798	$137	$662
Drug Free Schools - Advisor Grant	475	331	$162	$28	$134
Chapter 2 - Carryover	481	346	$271	$46	$225
Chapter 2 - Carryover	481	528	$245	$42	$203
Special Education (P.L. 99-457) - Carryover	482	349	$190	$33	$157
Even Start	494	363	$4,149	$711	$3,438
EHA-Education for All Handicapped (P.L. 94-142)	436	459	$5,229	$896	$4,333
Even Start	494	542	$1,002	$172	$830
Total			**$579,285**	**$99,234**	**$480,051**

Schedule of Excess Unemployment Insurance Charges to ED Flow-Through Grant Programs

Fiscal Year 1993 (7/1/92-6/30/93)

Name of U.S. Department of Education Program	Program Charge Code	Special Revenue Ledger Page	Amounts Charged to Specific Programs	Reasonable Charges per OIG	Excess Amount Charged per OIG
Vocational Education (Title II-A Disadvantaged)	428	98	$13,403	$2,275	$11,128
ECIA Chapter 1 (IASA Title I)	431	215	$441,880	$75,002	$366,878
ECIA Chapter 1 (IASA Title I) - Carryover	432	217	$102,661	$17,425	$85,236
ECIA Chapter 1 (IASA Title I), Migrant Education	433	222	$7,223	$1,226	$5,997
Homeless Assistance Program	434	226	$1,221	$207	$1,014
Chapter 2 Parent Pilot Program	435	228	$0	$0	$0
EHA-Education for All Handicapped (P.L. 94-142)	436	243	$20,214	$3,431	$16,783
ECIA Chapter II	438	268	$4,455	$756	$3,698
Adult Basic Education	439	272	$8,494	$1,442	$7,052
Adult Basic Education - Supplemental Allocation	440	274	$0	$0	$0
Section 353 Adult Training	441	276	$1,248	$212	$1,037
Special Education Preschool Program	454	292	$1,262	$214	$1,048
EESA Title II	460	314	$11,169	$1,896	$9,273
EESA Title II - Carryover	461	320	$230	$39	$191
Emergency Immigrant Act	464	326	$783	$133	$650
Drug Free Schools	472	347	$19,501	$3,310	$16,191
Drug Free Schools - Carryover	473	350	$3,578	$607	$2,971
Drug Free Schools - Advisor Grant	475	358	$1,336	$227	$1,109
Chapter 2 - Carryover	481	369	$1,464	$248	$1,215
Special Education (P.L. 99-457) - Carryover	482	371	$0	$0	$0
Even Start	494	386	$4,185	$710	$3,475
ECIA Chapter 1, Compensatory Education	431	461	$4,762	$808	$3,954
EHA-Education for All Handicapped (P.L. 94-142)	436	470	$6,123	$1,039	$5,084
Special Education Preschool Program (Grant Closeout	454	483	$172	$29	$143
Emergency Immigrant Act	464	495	$266	$45	$221
Even Start	494	531	$960	$163	$797
Total			**$656,590**	**$111,446**	**$545,145**

Allocation of Unemployment Insurance Charges to ED Flow-Through Grant Programs

Fiscal Year 1994 (7/1/93-6/30/94)

Name of U.S. Department of Education Program	Program Charge Code	Special Revenue Ledger Page	Amounts Charged to Specific Programs	Reasonable Charges per OIG	Excess Amount Charged per OIG
Vocational Education (Title II-A Disadvantaged)	428	112	$9,381	$1,744	$7,638
ECIA Chapter 1 (IASA Title I)	431	219	$441,141	$81,989	$359,152
ECIA Chapter 1 (IASA Title I) - Carryover	432	221	$113,452	$21,086	$92,366
ECIA Chapter 1 (IASA Title I), Migrant Education	433	225	$5,187	$964	$4,223
ECIA Chapter 1 (IASA Title I), Migrant Education	433	427	$237	$44	$193
Homeless Assistance Program	434	229	$1,212	$225	$986
Homeless Assistance Program	434	429	$174	$32	$142
Chapter 2 Parent Pilot Program	435	233	$0	$0	$0
EHA-Education for All Handicapped (P.L. 94-142)	436	250	$21,236	$3,947	$17,289
EHA-Education for All Handicapped (P.L. 94-142)	436	435	$5,680	$1,056	$4,624
ECIA Chapter II	438	268	$6,118	$1,137	$4,981
Adult Basic Education	439	273	$5,875	$1,092	$4,783
Section 353 Adult Training	441	278	$0	$0	$0
Migrant Education, Even Start	442	280	$1,105	$205	$899
Migrant Education, Tangipohoa	444	282	$89	$17	$72
Vocational Education Section 120, Set Aside	445	447	$594	$110	$484
Special Education Preschool Program	454	291	$1,378	$256	$1,122
Special Education Preschool Program	454	450	$287	$53	$234
EESA Title II	460	317	$8,941	$1,662	$7,279
EESA Title II - Carryover	461	321	$305	$57	$248
Emergency Immigrant Act	464	329	$894	$166	$728
Drug Free Schools	472	350	$14,956	$2,780	$12,177
Drug Free Schools - Carryover	473	351	$593	$110	$483
Chapter 2 - Carryover	481	363	$4,184	$778	$3,406
Even Start	494	376	$3,273	$608	$2,665
Total			**$646,293**	**$120,118**	**$526,176**

Allocation of Unemployment Insurance Charges to ED Flow-Through Grant Programs

Fiscal Year 1995 (7/1/94-6/30/95)

Name of U.S. Department of Education Program	Program Charge Code	Special Revenue Ledger Page	Amounts Charged to Specific Programs	Reasonable Charges per OIG	Excess Amount Charged per OIG
Vocational Education (Title II-A Disadvantaged)	428	121	$7,040	$1,189	$5,851
Vocational Education - Consumer Homemaking	430	122	($46)	($8)	($38)
ECIA Chapter 1 (IASA Title I)	431	241	$336,568	$56,855	$279,713
ECIA Chapter 1 (IASA Title I) - Carryover	432	243	$102,862	$17,376	$85,486
ECIA Chapter 1 (IASA Title I), Migrant Education	433	247	$4,494	$759	$3,735
Homeless Assistance Program	434	252	$1,179	$199	$980
Homeless Assistance Program	434	414	$444	$75	$369
Education for Exceptional Children	436	268	$15,828	$2,674	$13,154
Education for Exceptional Children	436	420	$6,028	$1,018	$5,010
ECIA Chapter 2	438	285	$2,201	$372	$1,829
Adult Basic Education	439	289	$5,745	$970	$4,775
Section 353 Adult Education Teacher Training	441	293	$851	$144	$708
Migrant Education, Even Start	442	295	$846	$143	$703
Migrant Education, Even Start	442	426	$278	$47	$231
Special Education Preschool Program	454	300	$978	$165	$813
Special Education Preschool Program	454	428	$153	$26	$127
EESA Title II	460	323	$2,310	$390	$1,920
EESA Title II - Carryover	461	324	$4,643	$784	$3,859
Emergency Immigrant Act	464	330	$337	$57	$280
Emergency Immigrant Act	464	441	$223	$38	$185
Drug Free Schools	472	353	($503)	($85)	($418)
Drug Free Schools - Carryover	473	355	$3,681	$622	$3,059
Chapter 2 - Carryover	481	359	($703)	($119)	($584)
Even Start	494	369	$0	$0	$0
Even Start	494	459	$170	$29	$141
Total			**$495,606**	**$83,720**	**$411,886**

Allocation of Unemployment Insurance Charges to ED Flow-Through Grant Programs

Fiscal Year 1996 (7/1/95-6/30/96)

Name of Program	Program Charge Code	Special Revenue Ledger Page	Amounts Charged to Specific Programs	Reasonable Charges per OIG	Excess Amount Charged per OIG
Vocational Education (Title II-A Disadvantaged)	428	118	$6,057	$1,104	$4,953
Vocational Education - Consumer Homemaking	430	120	($2)	($0)	($2)
ECIA Chapter 1 (IASA Title I)	431	279	$316,464	$57,687	$258,777
ECIA Chapter 1 (IASA Title I) - Carryover	432	283	$10,857	$1,979	$8,878
ECIA Chapter 1 (IASA Title I), Migrant Education	433	288	$2,766	$504	$2,262
Homeless Assistance Program	434	293	$815	$149	$667
Homeless Assistance Program	434	470	$323	$59	$264
Education for Exceptional Children	436	307	$11,531	$2,102	$9,429
Education for Exceptional Children	436	475	$5,008	$913	$4,095
IASA Title VI	438	320	$1,120	$204	$916
Adult Basic Education	439	325	$5,831	$1,063	$4,768
Section 353 Adult Education Teacher Training	441	327	$4	$1	$3
Migrant Education, Even Start	442	331	$768	$140	$628
Migrant Education, Even Start	442	481	$208	$38	$170
Special Education Preschool Program	454	335	$902	$164	$737
Special Education Preschool Program	454	484	$105	$19	$86
EESA Title II	460	356	$730	$133	$597
Emergency Immigrant Act	464	365	$473	$86	$387
Drug Free Schools	472	400	$5,852	$1,067	$4,785
Drug Free Schools - Carryover	473	401	$0	$0	$0
IASA Title VI Carryover	481	405	($545)	($99)	($446)
Total			**$369,269**	**$67,313**	**$301,956**

Grand Total for Fiscal Years 1992-1996			**$2,747,043**	**$481,831**	**$2,265,212**

NEW ORLEANS PUBLIC SCHOOLS
3510 GENERAL DEGAULLE DRIVE • NEW ORLEANS, LOUISIANA 70114

MORRIS L. HOLMES, Ed.D.
Superintendent

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October 10, 1997

Mr. Daniel J. Thaens
Western Area Manager, Dallas
United States Department of Education
Office of the Inspector General
1200 Main Tower Building
Room 2130
Dallas, TX 75202-5040

Subject: Draft Audit Report -- Audit Control No. 06-60010
Review of Charges for Unemployment Compensation Insurance and Worker's Compensation Insurance, New Orleans Public Schools.

Dear Mr. Thaens:

The New Orleans Public Schools (NOPS) appreciates the opportunity to respond to the Department of Education's (DOE) draft audit report reviewing charges for unemployment compensation insurance and workers' compensation insurance. This response is an appendix to the Louisiana Department of Education's response dated August 25, 1997. NOPS has carefully considered this matter and hopes this response will resolve the issues raised in the audit to the satisfaction of all concerned.

Along with the Louisiana Department of Education, NOPS does not concur with the findings or recommendations presented in the draft audit report of the New Orleans Pubic Schools (NOPS) dated July 24, 1997, and consequently believes that no refund to the Department of Education is due. Per your request, NOPS will take this opportunity to provide written comments and additional data NOPS feels will affect the findings and recommendations included in your draft audit report.

Background

The Board contracted Unemployment Compensation Control Systems, Inc. (UCCS) in 1982 as its servicer for unemployment insurance. NOPS receives unemployment compensation services from UCCS in lieu of utilizing self-insurance or state-taxed insurance for unemployment programs. The Board based its decision to use UCCS on four factors:

1. UCCS offered a substantial savings over the state tax to the Board, as well as all programs NOPS administers.

2. Contracting with UCCS offered a reduction in risk in comparison to a self-insurance fund.

3. UCCS provides the day-to-day management of the NOPS unemployment compensation cost control program, including: attending claims hearings, filing any necessary appeals and providing all required legal representation up to appearances before the Supreme Court. These are services that *are not available* through the State Tax Rate method.

4. UCCS's fixed fee for the Bonded Service Contract includes assumption of the Board's exposure. This contract represents a classic program of risk transfer of insurance.

The NOPS' Response

The audit report highlights reasons why the audit team believes a refund is due DOE. These reasons are based primarily on the premise that, "a reasonable allocation method" for allocating unemployment insurance costs is a salary ratio, not the variable rate methodology employed by UCCS. NOPS hopes to resolve the issues of reasonableness of variable rates within this letter.

DOE audit report states:

> *"Our use of the salary ratio to allocate... ...total unemployment insurance cost to ED is a reasonable allocation method and reflects relative benefits received."*

The audit cites "a" reasonable method for allocating unemployment insurance costs, but does not suggest it is the only reasonable method. Moreover, the Office of Management and Budget's Circular A-87 (amended January 15, 1981) neither defines "reasonableness," nor restricts cost allocation methods to only one reasonable method. This response will show NOPS' methodology is a reasonable methodology for allocating unemployment insurance costs. Further, its methods does reflect the relative benefit received.

Reasonableness of Varying Rates

The audit team wrote in its report that it neither concurs with nor understands NOPS' rationale for charging varying rates to the different funds. NOPS now provides additional data to show the rationale behind the use of the varying rates for unemployment compensation insurance.

UCCS explained that their research, based on historical experience, indicates that funds with higher incidence rates of unemployment should expect to pay higher premiums. It is reasonable, therefore, to expect federally-funded activities to have higher premiums if those activities have historically higher rates of unemployment incidence. NOPS has now looked beyond the bills and UCCS's explanation to the derivation of the rates for the purpose of responding to the audit. NOPS' research unveiled three reasons for tiered rates:

- *risk,*
- *uncertain future Federal funding sources, and*
- *general fund stability.*

1. Risk

Risk equals the anticipation or probability of future exposure. Risk must be considered by any vendor assuming all future payments of unemployment benefits.

An example of risk can be seen in the area of Worker's Compensation. Worker's Compensation Insurance rates are higher for employees whose risk of injury is greater -- such as a fireman, policeman, or a roofer -- than for a office employee. May we assume that different risks exist between federally funded employees and non-federally funded employees for unemployment insurance? **Yes**.

UCCS research indicates that risk can be and is dependent upon the extent to which control over the funds can be exercised. Not only is there a risk, the grantor may reduce the grant awarded, but the program or even the grantor agency could be eliminated through Federal government budget reduction. This is all "real risk" that cannot be measured, but must be considered when setting rates.

Risk can be measured against that which can be historically proven. UCCS is in the risk and risk assumption business. Data gathered prove experience and exposure exist between the various funds, General and Special Revenue Funds.

Two sample studies were done:

- a four-quarter study beginning third quarter 1994 and ending second quarter 1995; and

- a six-quarter study beginning first quarter 1996 and ending second quarter 1997.

The two sample studies show that the historical data supports the use of varying rates and that the methodology employed is rational.

The relativity of risk when comparing the benefits paid to special revenue funded positions (SRFP) vs benefits which were paid to general funded positions (GFP) is different. The 94-95 table shows an average relativity factor for SRFP of 4.10 and an average relativity factor for the GFP of 0.65. The six quarter 96-97 table shows a relativity factor of 4.03 or SRFP and a 0.67 relativity factor for GFP.

In actuarial terms the difference between the variation in rates is called relativity. Relativity of risk is the relationship of benefits paid to payroll costs by classification. Calculating the relativity for each fund:

Pure Premium Rates

Pure Premium rates are calculated by dividing the actual benefits paid by the actual payroll of the funded position:

1) *Special revenue benefits paid for the quarter / Special revenue payroll for the quarter*

2) *General fund benefits paid for the quarter / General fund payroll for the quarter*

Table 1

	Pure Premiums		
	SRFP	GFP	Ratio
94-3	0.00229	0.00055	4
94-4	0.00136	0.00011	12
95-1	0.00088	0.00011	8
95-2	0.00033	0.00010	3
	0.00121	0.00022	7

Table 2

	Pure Premiums		
	SRFP	GFP	Ratio
96-1	0.00138	0.00036	4
96-2	0.00105	0.00028	4
96-3	0.00421	0.00033	13
96-4	0.00286	0.00013	23
97-1	0.00057	0.00010	6
97-2	0.00019	0.00019	1
	0.00171	0.00023	8

Pure premium rates ***including only benefits paid, excluding any administration, processing, or risk of UCCS,*** (and any profit) for SRFP equals ***seven and eight*** times that of GFP. As illustrated in Table 4, it is not unlikely for the ratio of SRFP to GFP to be ***twenty-three times greater*** for SRFP, without any administration costs.

Benefits Relativity

1) *Pure premium rate of SRFP / Total pure premium rate*

2) *Pure premium rate of GFP / Total pure premium rate*

Table 3

	Relativity		
	SRFP	GRP	Ratio
94-3	3.09	0.74	4
94-4	5.88	0.47	12
95-1	4.80	0.61	8
95-2	2.64	0.80	3
	4.10	0.65	7

Table 4

	Relativity		
	SRFP	GFP	Ratio
96-1	3.09	0.80	4
96-2	2.92	0.78	4
96-3	4.99	0.39	13
96-4	8.03	0.35	23
97-1	4.17	0.71	6
97-2	1.00	1.00	1
	4.03	0.67	8

The relativity factor for SRFP is ***seven and eight times*** that of GFP for benefits paid. This relativity factor takes into consideration only that of benefits paid. This is a post-risk factor which does not include the administration of the benefits paid, including the day-to-day management of the UCCS unemployment compensation cost control program. Day-to-day management responsibilities include: attending claims hearings, filing appeals that are necessary and providing all required legal representation to the Supreme court as well as many other indirect costs such as banking charges, secretarial, space, equipment, and other costs. Further, both sample studies show there were ***more SRFP claims*** made in the pure sense than in the GFP, therefore increasing the SRFP share of the indirect costs, a factor not included in the relativity ratios.

Claims Relativity

Table 5

	Relativity		
	SRFP	GFP	Ratio
94-3	4.69	0.54	9
94-4	6.21	0.44	14
95-1	5.86	0.49	12
95-2	5.03	0.50	10
	5.45	0.49	11

Table 6

	Relativity		
	SRFP	GFP	Ratio
96-1	3.62	0.75	5
96-2	4.61	0.58	8
96-3	4.57	0.45	10
96-4	7.26	0.42	17
97-1	6.12	0.52	12
97-2	4.64	0.60	8
	7.71	0.83	15

The relativity factor for SRFP is ***eleven and fifteen times*** that of GFP for claims processed, without adjusting upward for the exposure relativity factor. This also proves that exposure and/or risk for each factor is ***eleven and fifteen times*** greater for the SRFP than the GFP.

Bumping

One other *real* factor left out of the Risk, Relativity Factor, and Pure Premium equations is the process called bumping. Bumping as explained in a memo dated January 16, 1997, by the Interim Personnel Director of NOPS to DOE is as follows:

> "Bumping is the process of one employee's replacing another employee based upon seniority. ...in some instances the most seniored employee is funded through a federal program, resulting in the bumping of a Board (general) funded employee. ...result is either a lay off or a surplus... (to the general fund)

The unemployment claim and benefits paid would be classified as a GFP unemployment claim and not an SRFP unemployment claim. The cause in the actual case sample provided by NOPS is a cut back in a special revenue funded program, resulting in a general funded lay-off and unemployment claim.

> *..a most recent lay-off of sixty paraprofessionals from the summer 1995... At the time of this lay-off, the Title I program reduced paraprofessionals by 52 and special education reduced paraprofessionals by 30.*

The list of the employees laid off was included in the memo submitted to DOE in January. The list illustrates that bumping is a real problem with several GFP bumped because of a reduction in special revenue funding.

Neither UCCS nor NOPS has tracked bumping instances in the past. Because the instances of the bumping process have been doubted in the audit report by DOE, UCCS's computer system is now tracking this information for future rate studies.

2. Uncertain future Federal funding sources

The audit team's report states:

> *"Our review disclosed that the total federal funds awarded to NOPS increased by 9 percent from 1992 to 1996, demonstrating the amount of Federal money available for NOPS increased during that period and is stable"*

The audit team's review may have disclosed an increase in NOPS's total Federal funds over the audit period; however, the team failed to report that in examining all the program's over the period there was, is, and always will be a fluctuation in each programs funding dollars. The audit team should have considered this factor given that new programs have been granted to NOPS and some programs have been discontinued; an increase in overall funding is not an indication of employment stability.

For example, assume a new $10,000 program began in 1993 while a $9,500 program was discontinued. The audit would view this as an increase of $500, or 5%. According to the audit, the increase in funding precludes any changes to unemployment insurance charges. In fact, the new program dollars may be dedicated to funding capital improvements, while the old program's discontinuance has just displaced a teacher, therefore prompting an unemployment claim or a general fund absorption of $9,500.

Even if the new program were intended to fund a teacher's salary and benefits, stable charges to unemployment insurance would imply that the program benefits the same student population and therefore the same displaced teacher could be used. However, more often than not, the new program will be used to fund a teacher requiring very different qualifications than those possessed by the displaced teacher. The result is an unemployment claim despite stability in the total amount of program dollars. In both the aforementioned examples, the funding has increased and a claim has still been filed.

Attachment A illustrates the true fluctuation in federal funding, both pass-through from the State Department of Education and from the DOE. The audit team *"disclosed that the total federal funds awarded to NOPS increased by 9 percent from 1992 to 1996."* Its disclosure fails to document the ***over 1.4 million dollar decrease*** in 1993-94 ***and the over 1.6 million dollar decrease*** in 1994-95 federal awards. Despite the audit's implication that the overall 9 percent increase indicates funding and employment stability and therefore has no effect on the unemployment risk, fluctuations of this size within the audit period prove that federal funding and, therefore, stable employment has not been fully predictable. The attachment will further detail the fluctuation in funding of programs including: ECIA (IASA) Chapter I and Chapter 2; Impact Aid; Drug Free Schools; and Dropout Prevention funding. These programs are the major source of federal funding for NOPS.

Therefore, NOPS does not believe that an overall increase in Federal funds throughout the audit period equates to stable employment for federally funded employees and cannot be incorporated into a sound rationale for using a single rate. This illustration is, in part, a solid rationale for using varying rates rather than one flat rate for unemployment insurance premiums.

Other signs of growing instability of federal funding from DOE is the reduction of staff at the Department of Education over the last several years, as well as Presidential campaign platforms which include the elimination of DOE. These issues and many others present serious risks to educational programs all across the country whose funding is generally granted only one year at a time.

3. *General fund stability*

Historically, state and local funding for general education in NOPS has been very stable. The public education system in New Orleans and the State of Louisiana, as well as many other places across the country, are protected by state constitutions and laws. Further, Louisiana law even prohibits the laying off of tenured teachers (but not federally funded teachers). Education funds would be the last to be cut if there were economic hard times in the State of Louisiana. Not only do the laws protect generally funded teachers and teacher to student ratios, but collective bargaining agreements also must be abided by. This is not true for federally funded programs where DOE sets the conditions upon which the money will be spent each year.

Reasonableness of the Rates

Gayle F. Truly, Secretary of Labor for the State of Louisiana, cites in a letter to UCCS dated August 10, 1994, an available overall state tax rate of:

- 3.89% for the 1992 unemployment tax; and
- 3.96% for the 1993 unemployment tax.

During the same period, NOPS's special revenue fund paid only 3.30% for unemployment coverage to UCCS. NOPS believes this *"...is reasonable for the services rendered..."* as defined in the federal regulations. NOPS also relies on the following:

Attachment B. Section 10. ***<u>Compensation for personal services:</u>***

> *"Compensation for employees engaged in federally-assisted activities will be considered reasonable to the extent that it is consistent with that paid for similar work in other of the State, local, or Indian tribal government."*

A comparison of UCCS' rates to the State Tax Rate proves that other local governments are paying more for less service. UCCS offered NOPS a discounted rate from state coverage for more services. Good business dictates that NOPS work with UCCS to realize the savings. In addition, effective January 1, 1995, UCCS further discounted its rate to 2.10% for the special revenue fund in comparison to the State's charge of 2.21%.

Had the Board elected to use the State Unemployment Tax Rate from July 1982 through June 1997 in lieu of UCCS' Bonded Service Contract, the cost would have been approximately $51 million in taxes to the state program. The Board expended only approximately $15 million. Approximately $35.6 million dollars have been saved by using UCCS over the 15-year period and approximately $9.4 million over the five year audit period, FY 92 - FY 96.

The audit team has indicated in its report that NOPS over charged the Special Revenue fund and the DOE a total of $2,265,212 for unemployment compensation costs. The Board believes that the services UCCS rendered to the Special Revenue fund and DOE ***saved a significant amount of money*** through the discounted rates. NOPS does, in fact, use a reasonable methodology for charging unemployment coverage. The charges are ***less than*** *"...that paid for similar work in other of the State, local, or Indian tribal government(s),"* and, therefore, are reasonable.

In addition, OMB's Circular A-87 does not require governmental units to review its vendor's billing practices. UCCS quoted a price to insure unemployment compensation for NOPS. The Board determined the price to be both reasonable and more cost beneficial than the State Unemployment Tax program. The price was lower than alternative solutions; therefore, the Board believed the price to be reasonable according to the regulations and was not obligated to research the basis for the pricing structure.

The audit cites Office of Management and Budget Circular A-87, "Cost Principles for State, Local, and Indian Tribal Governments" (May 17,1997) for a definition of reasonableness. This revised version of A-87 applies to all awards issued after August 31, 1995. This version was not effective for 45 months of the 60 month audit period. OMB Circular A-87 (amended January 15, 1981) **Attachment B. Section 10. <u>Compensation for personal services</u>** and **Attachment B. Section 13. <u>Employee fringe benefits</u>** is the proper guidelines for state and local governmental entities for the treatment of federal funds.

Risk Factors in Developing Rates

To address the audit team's concerns and questions regarding the reasonableness of charging tiered rates to cover varying risks to different funders, NOPS engaged the nationally known third party independent actuarial and consulting firm of Milliman & Robertson, Inc. (M&R). M&R has issued a letter report which finds that, "it is appropriate and reasonable to use a tier-rating structure to price NOPS's unemployment insurance." This letter is attached.

Conclusion

In closing, the Orleans Parish School Board and New Orleans Parish Schools do not concur with the findings and/or recommendations presented in the draft audit report dated July 24, 1997, by the DOE. There was no overcharge to the Special Revenue Fund and, therefore, no refund is due.

If after considering this response, DOE does not agree with NOPS' position, NOPS will be prepared to discuss with DOE what can be done to solve those areas of disagreement as well what mutually agreeable steps may be taken in the future.

If you have any question regarding this response to your audit or would like to review any additional data, please contact my office (504) 365-8730.

Sincerely,

Anthony J. Stoltz

Anthony J. Stoltz
Comptroller
New Orleans Public Schools

Approved:

Morris L. Holmes, Jr.
Superintendent
New Orleans Public Schools

fx: Mr. Daniel J. Thaens (214) 767-2024

cc: Cecil J. Picard, Superintendent, Louisiana Department of Education

Attachment A

New Orleans Public Schools
Schedule of Federal Financial Assistance
U.S. Department of Education
Fiscal Analysis of Expenditures

Federal Grantor/Pass Through Grantor/Program Title	Federal CFDA Number	FY 1988-89	FY 1989-90	FY 1990-91	FY 1991-92	FY 1992-93	FY 1993-94	FY 1994-95	FY 1995-96
US Department of Education									
Direct Programs									
Bilingual Education CY	84.003C	147,104	166,667	32,556	21,250	-	-	-	-
Bilingual Education PY Liquidation	84.003C	145,632	18,989	-	-	4,315	-	-	-
Dropout Prevention CY	84.201B	338,909	479,169	302,419	608,491	625,517	624,273	534,919	291,868
Dropout Prevention PY Liquidation	84.201B	-	-	24,132	90,943	153,137	71,462	111,053	70,511
Follow Through CY	84.014B	65,823	66,872	56,609	314	3,677	291	3,162	-
Follow Through PY Liquidation	84.014B	-	-	7,349	5,299	-	-	-	-
Impact Aid		1,303,352	2,531,915	1,525,912	2,285,726	2,285,726	2,319,717	1,971,759	1,798,228
Magnet Schools	84.164A	-	1,835,659	2,146,079	764,661	-	-	-	-
Even Start Program CY	84.213	-	-	250,048	199,525	-	-	-	-
Even Start Program PY Liquidation	84.213	-	-	64,339	104,483	-	-	-	-
Project Newbee		-	-	-	-	-	-	784	-
Project Best CY	84.233A	-	-	-	154,326	249,077	215,564	71	-
Project Best PY	84.233A	-	-	-	-	275,580	-	-	-
Subtotal Direct from U.S.D.E.		2,000,820	5,099,271	4,409,443	4,235,018	3,597,029	3,231,307	2,621,748	2,160,607
Pass-Through State Department of Education									
ECIA Chapter I CY	84.010	17,867,572	16,816,454	18,480,533	20,690,133	23,477,731	22,395,229	23,756,677	26,592,558
ECIA Chapter I C/O from PY	84.010	-	-	2,061,278	3,273,512	4,019,179	4,421,460	4,142,652	600,850
ECIA Chapter I PY Liquidation	84.010	1,986,280	398,362	11,913	1,071,940	1,963,345	1,515,794	1,015,494	1,506,954
ECIA Chapter I PY C/O Liquidation	84.010	801,816	-	-	28,000	-	-	-	-
ECIA Chapter I Capital Expense	84.010	-	365,780	445,082	321,061	125,308	261,977	201,250	478,780
ECIA Chapter I Capital Expense PY Liquidation	84.010	-	-	101,718	-	100,047	374,254	182,380	208,952
Migrant Education	84.011	561,545	346,600	255,698	307,000	316,903	242,502	245,186	185,510
Migrant Education/Even Start	84.011	-	-	-	-	-	42,742	64,300	61,359
ECIA Chapter 2 CY	84.151	856,404	793,739	703,173	785,849	624,670	711,944	536,956	538,640
ECIA Chapter 2 C/O from PY	84.151	38,197	11,107	57,326	118,829	85,391	215,611	8,067	8,027
ECIA Chapter 2 PY Liquidation	84.151	62,120	37,689	90,062	(5,835)	13,465	19,638	151,576	106,524
ECIA Chapter 2 PY C/O Liquidation	84.151	28,957	19,966	38,167	29,074	23,193	(316)	246	57,651
ECIA Chapter 2 Parent Pilot	84.151	-	-	-	57,961	45,425	9,638	-	-
EESA Title II Math/Science CY	84.161	113,294	19,216	141,756	375,860	485,029	374,465	359,399	322,636
EESA Title II Math/Science C/O from PY	84.161	12,438	49,371	197,591	2,855	75,374	47,137	171,595	113,775
EESA Title II Math/Science PY Liquidation	84.161	19,929	(1,909)	723	132,946	5,346	1,005	10,670	5,820
EESA Title II Math/Science PY C/O Liquidation	84.161	7,886	574	491	31,902	5,162	2,492	8,984	-
Drug Free Schools Eisenhower	84.184	11,158	-	3,201	4,958	-	-	-	-
Drug Free Schools CY	84.184	248,257	234,047	773,387	1,008,160	1,146,058	928,788	281,035	766,084
Drug Free Schools C/O from PY	84.184	-	32,700	91,645	(12,898)	140,076	23,108	223,820	282,125
Drug Free Schools PY Liquidation	84.184	38,112	33,533	26,318	149,153	42,361	51,843	17,680	19,207
Drug Free Schools PY C/O Liquidation	84.184	-	87,599	7,027	36,208	25,236	-	-	-
Drug Free Schools Governors Program	84.184	-	-	-	106,235	55,686	-	-	-
Drug Free Schools Drug Advisor	84.184	-	-	4,518	14,358	39,582	-	-	-
Idea PL 101-476 CY (formerly P.L. 94-142)	84.027	1,294,535	1,326,653	1,000,865	1,142,224	1,498,091	1,569,820	1,796,474	1,608,949
Idea PL 101-476 PY	84.027	271,574	60,296	170,239	246,777	463,298	457,394	375,194	323,597
Idea PL 101-476 C/O from PY	84.027	1,889	-	110,380	218,217	96,598	108,593	87,916	87,366
Idea PL 101-476 Discretionary	84.027	1,000	703	2,494	9,815	20,035	9,265	-	-

Source: Single Audit Reports

Attachment A

New Orleans Public Schools
Schedule of Federal Financial Assistance
U.S. Department of Education
Fiscal Analysis of Expenditures

Idea PL 101-476 Discretionary PY Liquidation	84.027	-	-	-	24,671	-	-	-	-
EHA Special Arts	84.027	2,744	(499)	1,088	603	2,808	-	2,786	-
PL 89-313 CY	84.009	9,148	9,986	19,971	18,124	14,474	3,927	-	-
PL 89-313 PY Liquidation	84.009	-	19,126	10,667	102	2,775	2,766	-	-
PL 89-313 C/O from PY	84.009	-	-	20,505	(6,724)	5,526	(2)	-	-
IDEA PL 101-476 Preschool CY (formerly PL 99-457)	84.024	154,959	128,403	133,366	169,894	198,480	253,677	236,330	302,459
IDEA PL 101-476 Preschool PY	84.024	46,132	56,089	96,948	7,603	32,169	63,696	14,400	44,413
IDEA PL 101-476 Preschool C/O from PY	84.024	-	-	56,165	121,549	111,561	42,473	15,100	25,137
IDEA PL 101-476 Preschool PY C/O Liquidation	84.024	-	-	20,274	(361)	-	6,418	2,376	-
IDEA PL 101-476 Preschool Discretionary	84.024	-	-	1,698	28,785	-	-	-	-
EHA Parent Training	84.024	-	5,439	6,643	3,989	-	-	-	-
Adult Basic Education CY	84.002	120,617	242,402	224,378	241,717	368,301	241,861	277,961	344,615
Adult Basic Education PY Liquidation	84.002	-	-	-	16,547	10,471	84,605	(1)	-
Adult Basic Education C/O from PY	84.002	-	-	-	11,553	-	25,250	910	-
Adult Basic Education 353 CY	84.002	-	-	-	-	46,871	43,817	48,614	-
Adult Basic Education 353 PY	84.002	-	-	-	-	35,603	1,040	-	-
Project Independence CY	84.002	-	-	413,564	1,228,314	831,932	527,736	426,299	566,218
Project Independence PY Liquidation	84.002	-	-	-	91,518	12,345	162,290	119,180	10,258
Vocational Educ-Basic Grants CY	84.048	636,481	166,086	201,701	333,930	728,657	751,117	773,722	913,628
Vocational Educ-Basic Grants PY Liquidation	84.048	-	293,177	144,280	121,220	792,463	664,330	398,722	314,857
Vocational Educ-Homemaking Educ CY	84.048	-	-	-	7,212	43,713	31,299	6,109	64,595
Vocational Educ-Homemaking Educ PY Liquidation	84.048	-	-	-	8,363	74,787	88,144	14,223	-
Vocational Educ-CBO CY	84.048	-	-	-	54,515	28,513	36,867	56,597	46,642
Vocational Educ-CBO PY Liquidation	84.048	-	-	-	25,149	42,789	89,962	84,896	-
Transition Refugee Program	84.146	123,749	144,915	-	-	-	-	-	-
Homeless Assistance Program PL 100-77		-	146,817	(6,999)	-	97,640	66,231	77,698	71,137
Homeless Assistance Program PL 100-77		-	-	-	-	-	-	26,609	-
Starting Point Preschool	93.576	-	-	-	-	-	318,537	288,866	396,625
Effective Schools Consortium		-	-	-	-	-	10,000	-	-
Event Start/TANG/PAHOA	84.213	-	-	-	-	-	5,000	-	-
Event Start Program	84.213	-	-	-	-	237,583	147,160	(6,391)	-
Event Start Program	84.213	-	-	-	-	-	69,185	-	-
Subtotal Pass Through State Dept. of Education		25,316,793	21,844,421	26,119,834	32,652,567	38,632,050	37,521,769	36,502,557	36,975,948
Total Department of Education Expenditures		27,317,613	26,943,692	30,529,277	36,887,585	42,229,079	40,753,076	39,124,305	39,136,555

Legend:
CY = Current Year
PY = Prior Year
CO = Carryover
CBO = Community Based Organization
Source: Single Audit Reports

MILLIMAN & ROBERTSON, INC.
Actuaries & Consultants
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1947 - 1997
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October 9, 1997

Mr. Frank Endom
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Re: **An Actuarial Analysis of Pricing Structures for Unemployment Insurance**

Dear Frank:

Milliman & Robertson, Inc. (M&R) has been retained by the New Orleans Public Schools (NOPS) to provide an analysis of their unemployment program. More specifically, we have been asked to discuss the appropriateness of applying a *tier rating* structure to this program. This letter presents the results of our analysis.

Summary. Based on a review of actuarial principles, statutory considerations and rating structures in use for other types of insurance, we believe it is appropriate and reasonable to use a tier rating structure to price NOPS's unemployment insurance. As opposed to the same single rate applying for everyone, tier rating means different rates apply for employment programs funded by different sources.

Based on a review of past claims experience there is clearly a difference in cost levels between the federally funded and non-federally funded programs. In particular, the claim costs (per unit of payroll) are significantly greater for the federally funded programs.

Actuarial Principles. Actuaries are trained to estimate costs of uncertain future events. The most common application of actuarial science is in the pricing of insurance products. The Casualty Actuarial Society (CAS) has developed standards of conduct and competence for its members. In quarters beginning with the first quarter of 1996 and ending with the second quarter of 1997. Table 1 highlights the overall results.

Table 1: Comparison of Unemployment Costs		
Description	Federally Funded	Non-Federally Funded
A. Payroll (in $1,000)	$62,989	$585,027
B. Actual Benefits Paid	81,535	113,665
C. Pure Premium (per $1,000 of payroll)	$1.29	$0.19

Items A and B in Table 1 are data that was provided by UCCS. The *pure premium* shows the indicated cost per $1,000 of payroll. These costs are shown in relation to payroll because unemployment insurance is rated on this basis. Table 1 shows that the pure premium for the federally funded program is nearly **7 times greater** than for the non-federally funded program.

The calculations shown in Table 1 use data compiled by UCCS. This data included claims identified as "Day by Day." These represent temporary employees whose tier assignment (i.e., federal or non-federal) depends on whom they are replacing. Because the database did not contain enough information to assign these claims to one of the two groups, we ignored them for this analysis. However, even assuming that all of these claims should be classified as non-federally funded, a very conservative assumption, the federally funded pure premiums would still be 2.5 times greater than for non-federally funded.

The past claims were assigned to employment group based upon the budget code of the individual making the claim. However, NOPS has a seniority program that can distort the data. For example, a federally funded program can be terminated and some of the senior employees in that program can be reassigned to non-federally funded programs. As a result, employees in that non-federally funded program may be "bumped" out of their jobs. Thus, a claim that was caused by a federally funded employee will show up in the data as a non-federal claim. In theory, this could also work in the reverse direction. However, since the average seniority is greater for workers in federally funded programs, the expectation is that the federal rate should be higher and the non-federal rate.

The pure premiums shown in Table 1 can be used to compare the relative difference in costs between the two programs. However, many additional factors (e.g., trend, expenses, etc.) must be considered before these amounts can be used to determine future insurance rates.

Sources of Data. The loss, LAE, claim count, premium, and reinsurance data underlying our actuarial analysis were provided by UCCS. If the underlying data is inaccurate or incomplete, the results of our analysis may likewise be inaccurate or incomplete. This does not necessarily imply that the data is faulty, only that an audit of the data was beyond the scope of our assignment.

The Statement of Principles Regarding Property and Casualty Insurance Ratemaking the CAS offers the following guideline to practicing actuaries:

> A rate is reasonable and not excessive, inadequate, or unfairly discriminatory if it is an actuarially sound estimate of the expected value of all future costs associated with an individual risk transfer.

In developing rates and rating structures, actuarial equity is achieved when all risks pay for their own expected costs. Stated differently, no risk should have to subsidize another. A subsidy occurs if two risks with different expected costs are charged the same rate.

Statutory Considerations. Section 22:1404 of the Louisiana Insurance Code (LIC) requires "Rates shall not be excessive, inadequate or *unfairly discriminatory*" (emphasis added). This section also states "Risks may be grouped by classifications for the establishment of rates ... Such standards may measure any *differences among risks that can be demonstrated to have probable effect upon losses or expenses*" (emphasis added).

Examples From Other Types of Insurance. Tier rating systems are widely used in Louisiana and throughout the country for many types of insurance. For example, the most recent workers' compensation filing approved by the Louisiana Insurance Rating Commission contained separate loss costs for over 500 different classifications of employees. These loss costs (per $100 of payroll) range from less than $1 for clerical workers to over $50 for certain construction and logging classes. The large disparity in insurance costs exists despite the fact that all injured employees receive the same benefits regardless of their employment classification. The reason for the price differences is that the expected *frequency* (number of claims) and/or *severity* (cost per claim) are not the same for all employment classifications.

Tier rating exists in many other types of insurance. For automobile insurance, young unmarried males living in urban areas pay much higher premiums than married females in rural areas. For homeowners coverage, rates differ based on construction type, protection class and territory, among other variables. Even federal programs, like crop and flood insurance, use multiple tier pricing structures. In all these cases, the rates differ for individual risks because the expected costs differ.

Nature of the NOPS Employment Programs. The NOPS employment programs can be broadly classified into two categories: federally funded and non-federally funded. Using historical claims data provided by Unemployment Compensation Control Systems, Inc. (UCCS) we have reviewed the costs for these two groups separately. Exhibit 1 shows the raw data and summary statistics for two sample periods. The first sample includes four quarters beginning with the third quarter of 1994 and ending with the second quarter of 1995. The second sample is of the previous six

Closing. Milliman & Robertson, Inc. has appreciated this opportunity to work with the New Orleans Public Schools. We would be happy to answer any questions you may have on this analysis.

Best regards,

Guy A. Avagliano

Guy A. Avagliano
FCAS, MAAA
GAA:crg

Exhibit 1

New Orleans Public Schools

Unemployment Benefits

HISTORICAL FREQUENCY & PURE PREMIUM

	(A) {Data}	(B) {Data}	(C) {Data}	(D) {Data}	(E) {Data}	(F) {Data}	(G) = {E / C}	(H) = {F / D}	(I) = {A / C}	(J) = {B / D}
	Benefits Paid		Payroll (in $000)		Number of Claims		Claim Frequency		Pure Premiums	
Quarter	Special Revenue	General Fund	Special Revenue	General Fund	Special Revenue	General Fund	Special Revenue	General Fund	Special Revenue	General Fund
94-3	$7,799	$14,917	$3,412	$27,330	25	23	7.3	0.8	$2.29	$0.55
94-4	10,170	7,551	7,484	69,146	20	13	2.7	0.2	1.36	0.11
95-1	5,913	7,173	6,747	64,969	16	13	2.4	0.2	0.88	0.11
95-2	2,429	5,945	7,394	59,987	16	13	2.2	0.2	0.33	0.10
95-3										
95-4										
96-1	9,493	25,976	6,870	72,481	16	35	2.3	0.5	1.38	0.36
96-2	6,862	15,632	6,526	55,850	28	30	4.3	0.5	1.05	0.28
96-3	16,497	8,275	3,914	25,427	36	23	9.2	0.9	4.21	0.33
96-4	16,865	7,988	5,898	63,889	27	17	4.6	0.3	2.86	0.13
97-1	4,097	7,462	7,220	77,766	13	12	1.8	0.2	0.57	0.10
97-2	1,410	12,746	7,524	68,182	12	14	1.6	0.2	0.19	0.19
Old 4	$26,311	$35,586	$25,037	$221,432	77	62	3.1	0.3	$1.05	$0.16
New 6	55,224	78,079	37,952	363,595	132	131	3.5	0.4	1.46	0.21
Total	$81,535	$113,665	$62,989	$585,027	209	193	3.3	0.3	$1.29	$0.19

Notes:

1. The data in columns (A) through (F) was provided by UCCS; it excludes all "Day by Day" claims.
2. Claim Frequency equals the number of claims per million dollars of payroll.
3. Pure Premium equals the amount of benefits paid per thousand dollars of payroll.
4. Data for the second half of 1995 was not available.