

# MANAGEMENT DIRECTIVE

Commonwealth of Pennsylvania  
Governor's Office

**Subject:**

Audit Inquiry Relative to Agency  
Litigation, Claims, and Assessments

**Number:**

325.2 Amended

**Date:**

December 17, 2014

**By Direction of:**

  
Charles B. Zogby, Secretary of the Budget

**Contact Agency:**

Office of the Budget, Office of Comptroller Operations, Bureau of Accounting and  
Financial Management, Telephone 717.787.6496

**This directive establishes policy, responsibilities, and procedures for initiating responses to Letters of Audit Inquiry (LAI) relative to agency litigation, claims, and assessments prepared and issued by independent auditors during the normal audit process. This amendment reassigns responsibilities from the Bureau of Audits to the Bureau of Accounting and Financial Management and updates references to the comprehensive annual financial report, state-level single audit, and Governmental Accounting Standards Board. Previously enclosed guidance on responses to letters of audit inquiry is now available online. Marginal dots are excluded due to major changes.**

- 1. PURPOSE.** To establish uniform policy, responsibilities, and procedures for processing responses to letters of audit inquiry.
- 2. SCOPE.**
  - a.** This directive applies to all departments, boards, commissions, and councils (hereinafter referred to as "agencies") under the Governor's jurisdiction. Policy and procedures contained herein have been coordinated with and approved by independent auditors and the Office of Attorney General. Agencies not under the Governor's jurisdiction should adopt the policy and procedures contained herein.

- b. This directive applies to LAI relative to agency litigation, claims, and assessments prepared by independent auditors during audits of the commonwealth's basic financial statements and federal awards programs, also known as the comprehensive annual financial report (CAFR) and state-level single audits. Similar policy and procedures should be adopted, as applicable, for other audits of commonwealth agencies and programs.
3. **OBJECTIVE.** To ensure that agencies and agency counsel understand the nature and importance of LAI to agency litigation, claims, and assessments and that responses are prepared within the framework required by generally accepted auditing standards and American Bar Association standards during the conduct of the commonwealth's CAFR and state-level single audits.

#### 4. DEFINITIONS.

- a. **Chief Accounting Officer.** The Office of the Budget, Office of Comptroller Operations, Deputy Secretary for Comptroller Operations.
- b. **Commonwealth Legal Counsel.** With respect to LAIs, commonwealth legal counsel refers to agency counsel, the Office of General Counsel (OGC), the Office of Attorney General, and outside counsel providing litigation services to the commonwealth.
- c. **Commonwealth Financial Reporting Entity.** Includes all funds, agencies, and other entities for which elected commonwealth officials are responsible (primary government) and legally separate organizations (established as independent agencies) for which the commonwealth itself is financially accountable or for which exclusion would result in misleading financial statements.
- d. **Letter of Audit Inquiry (LAI).** An inquiry of an agency's counsel concerning litigation, claims, and assessments, both asserted and unasserted, against that agency. The LAI is the independent auditors' primary means of obtaining information relative to actual or potential litigation, claims, and assessments that may have a material impact on the financial statements and federal awards programs under examination.
- e. **State-Level Single Audit.** A financial audit, as defined in [Government Auditing Standards](#), of the commonwealth's organizations, programs, activities, functions and federal awards under the provisions of *2 CFR Part 200, Subpart F – Audit Requirements*.

#### 5. POLICY.

- a. Audits of commonwealth organizations, programs, activities, and functions are to be made, where applicable, in accordance with generally accepted government auditing standards and policy established in *Management Directive 325.3, Performance of Audit Responsibilities*.

- b. An independent auditor ordinarily does not possess comprehensive legal skills and, therefore, cannot and should not make legal judgments and determinations regarding commonwealth litigation, claims, and assessments disclosed during the normal audit process without first addressing such issues within the framework of the commonwealth's legal environment. Therefore, independent auditors normally direct an LAI to the commonwealth, which seeks responses from all agency counsel providing litigation services to it. For the commonwealth's CAFR and state-level single audits, the auditors request LAI information from the chief accounting officer acting as the audit liaison, who, in conjunction with the OGC, requests LAI information from each commonwealth agency included in the scope of the respective audit. For all other audits, the auditors will request LAI information directly from the agency being audited.

**Note:** Failure to respond properly to the LAI impairs the scope of the independent auditors' examination and may adversely affect the auditors' opinion rendered on the financial statements being audited.

- c. The OGC, acting as legal counsel for the commonwealth, coordinates preparation of requests for information from affected commonwealth legal counsel and submission of responses to the independent auditors.
- d. Responses to LAIs submitted by commonwealth legal counsel must be prepared in accordance with Guidance for the Preparation of Responses to Letters of Audit Inquiry.
- e. Responses to LAIs must be addressed on a priority basis and prepared timely. In order to meet time constraints specified by the independent auditors, agencies must prepare both a preliminary and final response in relation to the CAFR audit and an updated final response in relation to the state-level single audit, and submit them to OGC in accordance with established timeframes. Information contained within a response should encompass the period from the date of the prior response up to and including the actual date of the current response for a given audit.
- f. Materiality limits with regard to agency litigation, claims, and assessments are established by the independent auditors and communicated in the LAI request.
- g. The independent auditors will assess the impact of litigation, claims, and assessments on the commonwealth's basic financial statements and federal awards programs, in accordance with generally accepted government auditing standards.

## 6. RESPONSIBILITIES.

- a. **Agency Counsel** shall:

- (1) Ensure that the preliminary, final, and updated final agency responses to OGC concerning litigation, claims, and assessments are appropriately researched, accurately and completely prepared in conformance with the procedures herein, and submitted within established timeframes.

- (2) Request the Attorney General and outside counsel provide current information concerning matters being handled on their behalf for incorporation in preliminary, final, and updated final agency responses to OGC. This includes matters of litigation, claims, and assessments that are agency specific and where the agency is directly represented by the Attorney General or outside counsel on general commonwealth matters affecting the agency.
- b. Agency Counsel and Department of General Services (DGS)** shall determine tort actions against the commonwealth pursuant to *42 Pa. C.S. Chapter 85B*.
- c. Agency Head** shall review preliminary, final, and updated final agency responses to the LAI to ensure completeness.
- d. Attorney General** shall provide current information to agency counsel concerning matters being handled by the Attorney General on behalf of other commonwealth agencies for incorporation in preliminary, final, and updated final agency responses to OGC.
- e. Chief Accounting Officer** shall coordinate the preparation of commonwealth responses to the independent auditors' LAI requests.
- f. Independent Auditors** shall:
  - (1) Transmit LAI request for summary of litigation, claims, and assessments to the Chief Accounting Officer and Office of the Budget, Office of Comptroller Operations, Bureau of Accounting and Financial Management (BAFM).
  - (2) Review preliminary, final, and updated final agency responses to their LAI request and assess whether the commonwealth is properly reporting and disclosing the impact of litigation, claims, and assessments on the commonwealth's basic financial statements and federal awards programs as part of the normal audit process.
- g. Office of the Budget, Office of Comptroller Operations, Bureau of Accounting and Financial Management** shall:
  - (1) Provide technical assistance, when needed, relative to the LAI process.
  - (2) Prepare materials for the LAI package for review and distribution by OGC.
  - (3) Maintain a database of all litigation, claims, and assessments disclosed in agency responses and prepares appropriate summary reports.
- h. Office of General Counsel** shall:
  - (1) Coordinate the issuance of individual LAI packages to agencies and the receipt of preliminary, final, and updated final agency responses.

- (2) Review all preliminary, final, and updated final agency responses.
- (3) Provide to the auditors all preliminary, final, and updated final agency responses.
- (4) Provide to the auditors a CAFR audit final letter and a state-level single audit updated final letter on behalf of OGC and commonwealth management, specifying pertinent litigation, claims, and assessments in which OGC directly represents the agency or commonwealth as well as matters included in agency responses.

## 7. PROCEDURES.

- a. **Independent Auditors.** Transmits LAI request for summary of litigation, claims, and assessments to Chief Accounting Officer and BAFM.
- b. **Office of the Budget, Office of Comptroller Operations, Bureau of Accounting and Financial Management.**
  - (1) Prepares documentation to be included in the LAI package and forwards the LAI package to OGC.
  - (2) Coordinates preparation of the LAI package with OGC to ensure all deadlines are met.
- c. **Office of General Counsel.** Prepares and transmits LAI package to agency counsel for completion. Both CAFR and state-level single audit LAI packages are distributed to counsel for all agencies in the commonwealth financial reporting entity.
- d. **Department of General Services, Bureau of Risk and Insurance Management.** Distributes listings of pending tort claims (and reserve allocations) under *42 Pa. C.S. Chapter 85B* for review and analysis. Agency specific listings are transmitted to agency counsel and a summary listing of tort claims affecting all agencies is distributed to the Office of Attorney General.
- e. **Agency Counsel.**
  - (1) Prepares, on behalf of the agency head, requests to the Office of Attorney General and outside counsel providing litigation services for the agency for current information concerning litigation, claims, and assessments, other than tort claims under *42 Pa. C.S. Chapter 85B*. Requests Attorney General and outside counsel document such information in formal written preliminary, final, and updated final responses to the agency counsel.
  - (2) Reviews and approves or adjusts the listing of pending tort claims and reserve allocations.
  - (3) Responds to the Department of General Services with adjustments, as necessary.

**f. Office of Attorney General.**

- (1) Performs research and analyses to determine general litigation, claims, and assessments in which the Office of Attorney General is directly representing an agency.
- (2) Performs research and analyses to determine litigation, claims, and assessments that are not agency-specific but relate to the commonwealth in general.
- (3) Reviews and approves or adjusts the listing of pending tort claims and reserve allocations.
- (4) Prepares and issues preliminary, final, and updated final responses to agency counsel requests disclosing results of research and analyses performed in accordance with section 7.f.(1) of this directive.

**NOTE:** The Attorney General's preliminary, final, and updated final responses to the agency counsel of the Department of General Services shall include applicable tort information reviewed in accordance with section 7.f.(3) of this directive (in addition to agency-specific information determined in accordance with section 7.f.(1) of this directive).

- (5) Prepares and issues preliminary, final, and updated final responses to OGC's request regarding litigation, claims, and assessments that are not agency-specific and not included in accordance with section 7.f.(4) of this directive.

**g. Agency Counsel.** Performs research and analyses to determine status of agency litigation, claims, and assessments, including those cases being administered by outside counsel and the Office of Attorney General on behalf of the agency. Tort actions against the commonwealth, pursuant to *42 Pa. C.S. Chapter 85B*, are to be addressed only by the agency counsel of the Department of General Services and the Office of Attorney General; however, other civil actions, such as those related to the Employee Liability Self Insurance Program (ELSIP), shall be addressed by all agency counsel as agency-specific cases.

**h. Department of General Services.**

- (1) Adjusts listing of tort actions against the commonwealth based on comments received from agency counsel and the Office of Attorney General.
- (2) Incorporates summary listings of tort actions affecting all agencies in preliminary, final, and updated final agency responses to OGC.

**i. Agency Counsel.**

- (1) Completes preliminary, final, and updated final agency responses to OGC's LAI based on research and analyses performed in accordance with sections 7.d. and 7.g. of this directive.

- (2) Summarizes information provided by outside counsel and the Office of Attorney General in preliminary, final, and updated final agency responses.
  - (3) Transmits preliminary, final, and updated final agency responses to LAI to OGC, with copies to agency heads.
- j. Agency Head.** Reviews preliminary, final, and updated final agency responses to OGC's LAI to ensure completeness.
- k. Office of General Counsel.**
- (1) Reviews preliminary, final, and updated final agency responses to LAI to ensure accuracy, completeness, and timeliness.
  - (2) Performs research and analyses to determine litigation, claims, and assessments where OGC directly represents the agency or the commonwealth.
  - (3) Maintains copies and forwards originals of preliminary, final, and updated final agency responses to the auditors, with copies to BAFM.
- l. Office of General Counsel and Office of the Budget, Office of Comptroller Operations, Bureau of Accounting and Financial Management.** Reviews and summarizes preliminary, final, and updated final agency responses.
- m. Office of General Counsel.**
- (1) Adds any additional information concerning litigation, claims, and assessments not disclosed in agency responses to final summary of responses.
  - (2) Prepares final and updated final letters specifying pertinent litigation, claims, and assessments in which OGC directly represents the agency or the commonwealth and which are not included in preliminary, final, and updated final agency responses.
  - (3) Transmits final and updated final letters to the auditors and BAFM with final summaries of responses, confirming that information concerning all litigation, claims, and assessments for all agencies and programs within the scope of the audit have been included in the final summaries.

**This directive replaces, in its entirety, *Management Directive 325.2*, dated September 12, 2008.**