



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Region IX  
Office of Audit Services  
50 United Nations Plaza, Room 171  
San Francisco, CA 94102

CIN: A-09-01-00094  
February 8, 2002

Debra Logan, Corporate Director  
PacifiCare Health Systems, Inc.  
3120 Lake Center Drive  
Santa Ana, CA 92799-5186

Dear Ms. Logan:

Enclosed are two copies of the U.S. Department of Health and Human Services (HHS), Office of Inspector General, Office of Audit Services' final report titled "Audit of Medicare Payments to PacifiCare for Beneficiaries Classified as Institutionalized in States Other Than California in January 1998."

Final determinations as to actions taken on all matters reported will be made by the HHS action official named below. We request that you respond to the action official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

In accordance with the principles of the Freedom of Information Act, 5 U.S.C. 552, as amended by Public Law 104-231, Office of Inspector General, Office of Audit Services' reports are made available to members of the public to the extent information contained therein is not subject to exemptions in the Act. (See 45 CFR Part 5) As such, within 10 business days after the final report is issued, it will be posted on the world wide web at <http://oig.hhs.gov/>.

To facilitate identification, please refer to Common Identification Number (CIN) A-09-01-00094 in all correspondence relating to this report.

Sincerely,

A handwritten signature in black ink, appearing to read "Lori A. Ahlstrand".

Lori A. Ahlstrand  
Regional Inspector General  
for Audit Services

Enclosures

Direct Reply to Action Official:

Director, Office of Managed Care  
Centers for Medicare & Medicaid Services  
Department of Health and Human Services  
7500 Security Boulevard, Room 33-02-01  
Baltimore, Maryland

**Department of Health and Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**AUDIT OF MEDICARE PAYMENTS TO  
PACIFICARE FOR BENEFICIARIES  
CLASSIFIED AS INSTITUTIONALIZED  
IN STATES OTHER THAN CALIFORNIA  
IN JANUARY 1998**



**JANET REHNQUIST  
Inspector General**

**February 2002  
A-09-01-00094**

# *Office of Inspector General*

<http://oig.hhs.gov/>

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**Department of Health and Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**REGION IX**

**AUDIT OF MEDICARE PAYMENTS TO  
PACIFICARE FOR BENEFICIARIES  
CLASSIFIED AS INSTITUTIONALIZED  
IN STATES OTHER THAN CALIFORNIA  
IN JANUARY 1998**



**JANET REHNQUIST  
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**THIS REPORT IS AVAILABLE TO THE PUBLIC**  
at <http://oig.hhs.gov/>.

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**OAS FINDINGS AND OPINIONS**

*The designation of financial or management practices as questionable or a recommendation for the disallowance of costs incurred or claimed as well as other conclusions and recommendations in this report represent the findings and opinions of the HHS/OIG/OAS. Final determination on these matters will be made by authorized officials of the HHS divisions.*



Region IX  
Office of Audit Services  
50 United Nations Plaza, Room 171  
San Francisco, CA 94102

CIN: A-09-01-00094  
February 8, 2002

Debra Logan, Corporate Director  
PacifiCare Health Systems, Inc.  
3120 Lake Center Drive  
Santa Ana, California 92799-5186

Dear Ms. Logan:

This report provides you with the results of our audit of Medicare payments to PacifiCare for beneficiaries classified as institutionalized in January 1998. The report covers PacifiCare plans in: Arizona, Colorado, Nevada, Ohio, Oklahoma (2), Oregon (2), Texas, Utah, and Washington. These plans are collectively referred to as PacifiCare in the body of this report. The scope of this review excludes all PacifiCare plans within California. We issued a separate report on those plans titled "Audit of Medicare Payments to PacifiCare of California for Beneficiaries Classified as Institutionalized in January 1998" (CIN: A-09-01-00056), dated September 21, 2001.

During our previous audit, we determined that PacifiCare of California had not implemented a policy letter issued by the Centers for Medicare & Medicaid Services (CMS)<sup>1</sup> in a timely manner. This policy letter revised the definition of an institution for all institutional payments made for those months after December 1997. In most cases, this change reduced the monthly payment that a health maintenance organization (HMO) would receive for its enrolled beneficiaries who no longer met the criteria for institutional status. We found that PacifiCare interpreted this change in policy to apply to the beneficiary's residential status after January 1, 1998. This interpretation made the change effective for the February 1998 payment rather than the January 1998 payment.

In our current audit, we selected two statistical samples of 100 monthly payments each from a universe of 3,673 monthly Medicare payments to PacifiCare. These payments were for beneficiaries classified by PacifiCare as institutionalized in January 1998. We determined that 96 of these 200 payments were for beneficiaries inappropriately classified as institutionalized. Based on our audit results, we estimate that PacifiCare received Medicare overpayments of at least \$712,802 for beneficiaries incorrectly classified as institutionalized in January 1998. Details of our sample appraisals are shown in APPENDIX A.

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<sup>1</sup> In June 2001, the name of the Health Care Financing Administration was changed to CMS.

The first sample was taken from beneficiaries who were reported as institutionalized in January 1998 but were not reported as institutionalized in February 1998. From this sample, we identified 87 payments for beneficiaries who were inappropriately classified as institutionalized. We also identified additional Medicare overpayments for one beneficiary for months subsequent to our audit period.

The second sample was taken from beneficiaries who were classified as institutionalized in both January and February 1998. From this sample, we identified nine payments for beneficiaries who were inappropriately classified as institutionalized. Additionally, we identified one payment that had been inappropriately adjusted, resulting in a Medicare underpayment. We also identified additional Medicare overpayments for seven of these beneficiaries for months subsequent to our audit period.

We recommend that PacifiCare submit the appropriate adjustments in order to refund the Medicare overpayments identified. PacifiCare should also review the balance of the institutionalized beneficiary universe to identify and refund additional overpayments, which we estimate to be at least \$712,802. In the response to our draft report, PacifiCare stated that it was verbally informed by a Director at CMS that its interpretation of the policy change was reasonable. Based upon this conversation, PacifiCare does not agree with our report. PacifiCare's response is included in its entirety in APPENDIX B.

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## INTRODUCTION

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### BACKGROUND

PacifiCare is an HMO which is part of PacifiCare Health Systems, Inc.; a health care services company that provides managed care for employer groups and Medicare beneficiaries in nine states and Guam serving more than 3.5 million members (972,800 Medicare members).

An HMO is a legal entity that provides or arranges health services for its enrollees. Under the Medicare program, HMOs contract with CMS to provide health care services to beneficiaries. CMS makes monthly advance payments to HMOs at the per capita rate set for each beneficiary. Enhanced payments are made each month on behalf of certain high-cost categories of beneficiaries, such as those residing in a nursing home or other qualifying institution. The HMOs identify and report to CMS, on a monthly basis, beneficiaries who meet the definition of institutionalized status.

In order to be eligible for this enhanced institutional payment, the beneficiary must have been a resident of a qualifying facility for a minimum of 30 consecutive days. This period includes, as the 30th day, the last day of the month prior to the month for which the higher institutional rate is paid. For example, for January, the 30 days would be December 2 through December 31. This qualifying period of residency must be satisfied each month in order for the HMO to be paid the higher institutional rate.

Operational Policy Letter #54 (OPL #54), issued by CMS on July 24, 1997, revised the definition of institutionalized status to be effective for the months beginning after December 1997. With this revision, CMS limited institutionalized status to enrolled beneficiaries who were residents of specific types of Medicare or Medicaid certified institutions including skilled nursing facilities; intermediate care facilities for the mentally retarded; and psychiatric, rehabilitation, long-term care, or swing bed hospitals<sup>2</sup>. Both the independent and assisted living portions of facilities do not qualify for institutional status under this revised definition. The requirement for 30 consecutive days remained the same, only the types of qualifying facilities were changed.

### **OBJECTIVE, SCOPE, AND METHODOLOGY**

Our audit was performed in accordance with generally accepted government auditing standards. The objective was to determine if enhanced Medicare payments received by PacifiCare were appropriate for beneficiaries reported as institutionalized in January 1998. The scope of this review excludes all PacifiCare plans within California. Those plans were reviewed under our "Audit of Medicare Payments to PacifiCare of California for Beneficiaries Classified as Institutionalized in January 1998" (CIN: A-09-01-00056), dated September 21, 2001.

We did not review the internal controls at each PacifiCare plan. These controls vary by plan and reviewing them was not necessary to complete our audit objective.

We selected two statistical samples of 100 monthly payments each from a universe of 3,673 monthly Medicare payments to PacifiCare. These payments were for beneficiaries classified by PacifiCare as institutionalized in January 1998. The first sample of 100 payments was taken from 2,116 beneficiaries who were reported as institutionalized in January 1998 but were not reported as institutionalized in February 1998. The second sample of 100 payments was taken from 1,557 beneficiaries who were reported as institutionalized in both January and February 1998. We selected two separate samples to confirm that PacifiCare had not implemented OPL #54 in January 1998, but instead, waited until February 1998 to apply the new requirements.

PacifiCare provided us with the names, addresses, and phone numbers of the institutions where each of the selected beneficiaries resided during the 30-day period prior to January 1998. The institutional status for each beneficiary was determined by verifying residency and level of care information by telephone, fax, or letter. We were unable to verify institutional status for four beneficiaries. These four items were considered non-errors. All findings were discussed with PacifiCare officials to determine if additional information was available.

In determining the overpayments, we calculated the difference between (1) the actual amount paid to PacifiCare by Medicare for the month selected, and (2) the amount Medicare should have paid PacifiCare based on the results of our audit. Our audit was conducted from April through September 2001.

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<sup>2</sup> Section 1883 of the Social Security Act permits certain small rural hospitals and critical access hospitals to enter into a swing-bed agreement, under which the hospital can use its beds to provide either acute or skilled nursing facility care, as needed.

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## FINDINGS AND RECOMMENDATIONS

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We found that 96 of the 200 sample items were for beneficiaries inappropriately classified as institutionalized. Based on the results of our audit, we estimate PacifiCare received Medicare overpayments of at least \$712,802 for the month of January 1998.

We selected two statistical samples of 100 monthly payments each from a universe of 3,673 monthly Medicare payments to PacifiCare. These payments were for beneficiaries classified by PacifiCare as institutionalized in January 1998. The first sample of 100 payments was taken from 2,116 beneficiaries who were reported as institutionalized in January 1998 but were not reported as institutionalized in February 1998. Based on our review, we identified 87 payments for beneficiaries who were inappropriately classified as institutionalized. These payments included Medicare overpayments totaling \$36,293. We also identified additional Medicare overpayments for one beneficiary totaling \$1,116 for months other than January 1998. PacifiCare provided documentation indicating it had submitted adjustments to CMS for these additional overpayments prior to our audit. However, as of July 2001, CMS had not processed these adjustments.

The second sample of 100 payments was taken from 1,557 beneficiaries who were classified as institutionalized in both January and February 1998. Based on our review, we identified nine payments for beneficiaries who were inappropriately classified as institutionalized. These payments included Medicare overpayments totaling \$2,840. Additionally, we identified one payment that had been inappropriately adjusted, resulting in a Medicare underpayment of \$535. We also identified additional Medicare overpayments for seven beneficiaries totaling \$33,487 for months other than January 1998. PacifiCare had not submitted adjustments to CMS for these additional overpayments as of the conclusion of our fieldwork.

Based on our audit, PacifiCare received net Medicare overpayments of \$73,201 as follows:

	<u>ERROR</u>	<u>ADDITIONAL</u>	<u>TOTAL</u>
<b>First Sample</b>	\$36,293	\$1,116	\$37,409
<b>Second Sample</b>	2,840		
	<u>&lt;535&gt;</u>	<u>33,487</u>	<u>35,792</u>
<b>TOTAL</b>	<b><u>\$38,598<sup>3</sup></u></b>	<b><u>\$34,603</u></b>	<b><u>\$73,201</u></b>

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Only \$38,598 was used to project the overpayment amount. Additional details of our sample appraisals are shown in APPENDIX A.

## **QUALIFYING FACILITIES**

The CMS revised the definition of a qualifying facility with the issuance of OPL #54. To be considered institutionalized, an enrolled member must have been a resident of one of the following title XVIII (Medicare), or title XIX (Medicaid) certified institutions for at least 30 consecutive days immediately prior to the month for which a monthly Medicare payment is being made:

- C skilled nursing facility,
- C nursing facility,
- C intermediate care facility for the mentally retarded,
- C psychiatric hospital or unit,
- C rehabilitation hospital or unit,
- C long-term care hospital, or
- C swing-bed hospital.

Of the 200 payments reviewed, we found that 96 were for beneficiaries residing in an institution not meeting the requirements for institutional status. These beneficiaries were found to have resided in assisted living, independent living, board and care, or a non-certified portion of the facility. These facilities do not qualify for the enhanced institutional payment. Medicare overpayments related to these 96 beneficiaries total \$39,133.

PacifiCare provided documentation indicating that it had submitted adjustments for 3 of the 96 overpayments prior to our audit. These adjustments have not been processed by CMS and they were considered errors when calculating the total Medicare overpayment when projected to the universe of institutional payments.

## **PAYMENT INCORRECTLY ADJUSTED**

We identified one payment that had been previously adjusted in error. The beneficiary resided in a qualifying facility during the entire month of December 1997. The institutional payment for this beneficiary had been adjusted prior to our audit returning the enhanced payment to Medicare. PacifiCare should have received the enhanced institutional payment for January 1998 resulting in a Medicare underpayment of \$535.

## **PAYMENTS UNABLE TO VERIFY**

We identified four payments for beneficiaries whose institutional status could not be verified due to disconnected phone numbers, no response from letters sent, or lost records. These four items were considered non-errors.

## **RECOMMENDATIONS**

We recommend that PacifiCare:

1. Refund the \$73,201 Medicare overpayments identified.
2. Review the balance of the institutionalized beneficiary universe to identify and refund additional overpayments, which we estimate to be at least \$712,802.

## **PACIFICARE COMMENTS AND OIG RESPONSE**

In response to the draft report, PacifiCare disagreed with our recommendations. A summary of PacifiCare's comments and the OIG response to those comments are shown below. PacifiCare's written response has been included in its entirety in APPENDIX B.

### **PACIFICARE COMMENTS**

Based on discussions with CMS, PacifiCare did not agree with the finding in our report. According to PacifiCare, in April and October 2001, a Director of Accountability of Payment at CMS verbally acknowledged that OPL #54 was ambiguous.

### **OIG RESPONSE**

In August 2000, a CMS official in the Medicare Managed Care Group, Division of Program Policy confirmed that the OIG correctly determined that PacifiCare should have implemented the revised definition of qualifying facilities in OPL #54 beginning with January 1998 payments. The policy letter specifically stated that the change was effective for all institutional payment rate adjustments made for the months after December 1997.

Of the \$73,201 in Medicare overpayments identified, \$38,598 related to January 1998 payments received for beneficiaries who did not reside in qualifying facilities. The remaining \$34,603 was for payments made for months other than January 1998, which PacifiCare did not address in its response. The timing of the implementation has no impact on these additional overpayments. PacifiCare was provided with the specific member information for these payments and should make the necessary adjustments.

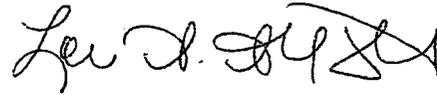
\* \* \* \* \*

Final determination as to actions taken on all matters reported will be made by the HHS office named below. We request that you respond to that office within 30 days from the date of this

Page 7 - Debra Logan

letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

Sincerely,

A handwritten signature in black ink, appearing to read "Lori A. Ahlstrand". The signature is fluid and cursive, with a large, sweeping flourish at the end.

Lori A. Ahlstrand  
Regional Inspector General  
for Audit Services

**Direct Reply to Action Official:**

Director, Office of Managed Care  
Centers for Medicare & Medicaid Services  
Department of Health and Human Services  
7500 Security Boulevard, Room 33-02-01  
Baltimore, Maryland 21244-1850

# **APPENDICES**

## APPENDIX A

### AUDIT OF MEDICARE PAYMENTS TO PACIFICARE FOR BENEFICIARIES CLASSIFIED AS INSTITUTIONALIZED IN JANUARY 1998

#### STATISTICAL SAMPLE INFORMATION Single Stage Variable Samples

	FIRST SAMPLE (Beneficiaries reported as institutionalized in January but not in February 1998)	SECOND SAMPLE (Beneficiaries reported as institutionalized in both January and February 1998)
POPULATION	2,116	1,557
SAMPLE SIZE	100	100
ERRORS	87	10 <sup>1</sup>

#### PROJECTION OF SAMPLE RESULTS Precision at the 90 percent Confidence Level

	FIRST SAMPLE (Beneficiaries reported as institutionalized in January but not in February 1998)	SECOND SAMPLE (Beneficiaries reported as institutionalized in both January and February 1998)
UPPER LIMIT	\$830,786	\$64,121
POINT ESTIMATE	\$767,963	\$35,892
LOWER LIMIT*	\$705,140	\$7,662

\*COMBINED LOWER LIMIT AT  
THE 90% CONFIDENCE LEVEL: **\$7 12,802**

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These 10 errors include 9 overpayments and 1 underpayment.

RECEIVED  
JAN 18 2002  
3120 Lake Center Drive  
Santa Ana, California 92704-6917  
Tel (714) 825-5200

January 7, 2002

Lori A. Ahstrand  
DHHS Office of Inspector General, Region IX  
Office of Audit Services  
50 United Nations Plaza, Room 171  
San Francisco, CA 94102

RE: CIN A-09-01-00094 "Audit of Medicare Payments to PacifiCare for Beneficiaries Classified as Institutionalized in States Other Than California in January 1998"

Dear Ms. Ahstrand:

This is in response to your October 16, 2001 letter providing the results of the Office of Inspector General (the "OIG") draft report titled "Medicare Payments Made to PacifiCare Companies Outside of California for Beneficiaries Classified as Institutionalized in January 1998".

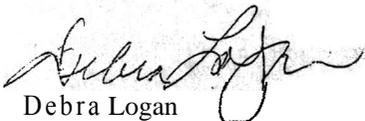
In previous communication with the OIG, PacifiCare stated that it had officially requested clarification from CMS in response to the OIG's interpretation of OPL#54. In approximately April of 2001 PacifiCare requested clarification from CMS of OPL54 in response to the OIG's audit report of Medicare payments made to PacifiCare of California (CIN A-09-03-00056). At that time Cynthia Moreno, director of Accountability of Payment at CMS Central Office, acknowledged that OPL54 was "clearly ambiguous" and that PacifiCare's interpretation was reasonable. Our response to that audit report indicated that Ms. Moreno was willing to discuss CMS's interpretation of OPL54 with the OIG.

On October 30, 2001, a conference call was held with CMS representatives for a second time. The purpose of this call was again to seek clarification from CMS regarding OPL54 in response to the OIG's draft audit report of Medicare payments made to PacifiCare Companies outside of California (CIN A-09-01-00094). This conference call was held with Cynthia Moreno, Scott Nelson and Mary McLean. Ms. Moreno acknowledged that OPL 54 is ambiguous and that PacifiCare's interpretation is reasonable. Moreover, Ms. Moreno suggested that this issue be escalated within CMS to get resolution between the OIG and CMS's interpretation of OPL 54.

Based on CMS's interpretation of OPL54, PacifiCare disputes the finding of the draft report "Medicare Payments Made to PacifiCare Companies Outside of California for Beneficiaries Classified as Institutionalized in January 1998".

If you should have any further questions regarding the above, please do not hesitate to contact me. I can be reached at (714) 825-5464 or at the address given below.

Sincerely,



Debra Logan  
Corporate Director  
Membership Accounting Services  
PacifiCare Health Services

arifi

Lori A. Ahstrand  
DHHS Office of Inspector General, Region IX  
Office of Audit Services  
1/7/02

Page 2 of 2

cc: Mary McLean, CMS Central Office  
Cynthia Moreno, CMS Central Office  
Scott Nelson, CMS Central Office  
Judy D'Ambrosio, PacifiCare Health Systems  
Steve Tucker, PacifiCare Health Systems  
Scott Neururer, PacifiCare Health Systems