DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Memorandum

Date MAY 20 1992

From Richard P. Kusserow
Inspector General

Subject Third Party Liability Collections Under the Medicaid Program - Indiana Department of Public Welfare (A-05-91-00052)

To William Toby
Acting Administrator
Health Care Financing Administration

This memorandum alerts you to the issuance on May 20, 1992 of our final audit report. A copy is attached.

In Indiana, Medicaid claims are processed by a contractor under an agreement with the State agency. The contractor assumed an underwriting risk to pay for medical services provided to Medicaid recipients in exchange for a premium (per beneficiary) paid by the State. The agreement provided for an annual calculation, called a quota-share calculation, that compared the amount of the premium income paid to the amount of the actual Medicaid claims paid less the amount of third party liability (TPL) collections. The net profit or loss amounts were to be shared by the contractor and the State agency according to a formula prescribed in the agreement.

Federal regulations require States to pay the Federal Government a portion of TPL collections. The appropriate amount is determined by applying the Federal Medicaid matching percentage to total TPL collections. The State agency attempted to credit the applicable portion of TPL collections to the Federal Government on quarterly expenditure reports but, through clerical errors, the effect of the credits was negated by offsetting entries on the same reports. We are recommending that the State agency refund $15 million, the aggregate Federal share of TPL credits due, and improve internal controls over TPL collections.

The State agency did not provide a formal response to our findings and recommendations although we allowed, at the request of the State Medicaid Director, a 60-day extension of time to prepare the response.

The Health Care Financing Administration's (HCFA) regional office concurred with our recommendations regarding State agency internal controls, but did not fully concur with our other recommendations. Regional officials did not concur with our recommendations regarding the financial adjustment and the reporting of TPL collections stating that it is not appropriate to separate reporting of TPL from quota-share settlements.

Because the State's agreement with the contractor expired June 30, 1991, we believe that prompt action to recover the Federal Government's share of TPL collections is necessary. We do not agree with HCFA's regional office because Federal regulations require States to pay the Federal Government its share of TPL collections irrespective of contractual agreements between the State and a contractor. Also, TPL collections currently held by the contractor are excessive because quota-share settlements were not made annually as required under the contract and TPL collections and premium income exceeding expenditures have grown to a large reserve fund.

Since HCFA officials did not concur with our recommendations regarding the refund and the reporting of TPL collections, we are immediately placing this report in the Department's formal audit resolution process.

For further information contact:

Martin D. Stanton
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Attachment

Department of Health and Human Services

OFFICE OF INSPECTOR GENERAL

THIRD PARTY LIABILITY COLLECTIONS UNDER THE MEDICAID PROGRAM

INDIANA DEPARTMENT OF PUBLIC WELFARE

DEPARTMENT OF HEALTH & HUMAN SERVICES • USA

Richard P. Kusserow
INSPECTOR GENERAL

A-05-91-00052

DEPARTMENT OF HEALTH AND HUMAN SERVICES
REGION V
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OFFICE OF
INSPECTOR GENERAL

Common Identification No. A-05-91-00052

Ms. Marilyn Scales
Commissioner
Indiana Department of Public Welfare
402 West Washington Street, Third Floor
Indianapolis, Indiana 46204

Dear Ms. Scales:

Enclosed for your information and use are two copies of an Office of Inspector General report entitled "Third Party Liability Collections Under the Medicaid Program." The audit covered amounts claimed during the period March 1, 1986 through March 31, 1991. Your attention is invited to the audit findings and recommendations contained in the report. The Health Care Financing Administration will be communicating with you in the near future regarding implementation of these items.

In accordance with the principles of the Freedom of Information Act (Public Law 90-23), Office of Inspector General reports issued to the Department's grantees and contractors are made public, to the extent information contained therein is not subject to exemptions in the Act, which the Department chooses to exercise (see 45 CFR Part 5.)

To facilitate identification, please cite the above common identification number in all correspondence relating to this audit.

Sincerely,

Martin D. Stanton

Martin D. Stanton
Regional Inspector General
for Audit Services

Enclosures

SUMMARY

The Medicaid program did not receive credit due for funds obtained from third party liability (TPL) collections totaling $23,857,038. This amount is applicable during the period March 1, 1986 through March 31, 1991. The amount of interest earned on these funds was not readily determinable.

The State agency believed that TPL collections were offset against expenditures on quarterly expenditure reports submitted to the Health Care Financing Administration. However, we found that internal control weaknesses caused intended offsets to be cancelled by other errors on the expenditure reports.

We are recommending a financial adjustment for the $23,857,038 (Federal share $15,155,230) plus interest. Also, future TPL collections should be adjusted quarterly and several improvements need to be made in internal control procedures.

We are issuing this report without a written response from the State agency. Although we granted a 60-day extension of time at the State agency's request, we received no response to our findings and recommendations.

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INTRODUCTION

BACKGROUND

The Medicaid program, established by Title XIX of the Social Security Act, authorizes Federal financial participation (FFP) in costs incurred by the States in providing medical services to eligible low income and medically needy persons. The medical services are furnished by health care providers such as physicians, medical laboratories, pharmacies, hospitals, nursing homes, and other organizations. The program is jointly administered by the Federal Government through the Health Care Financing Administration (HCFA) and by the States through State designated agencies. The designated agency in Indiana is the Indiana Department of Public Welfare (State agency).

Included in Federal regulation 42 CFR 433, subpart D, are provisions that each State must take reasonable measures to determine the legal liability of third parties to pay for services furnished under the Medicaid program. A third party is defined as any individual, entity, or program that is or may be liable to pay all or part of the Medicaid expenditures. The regulations further provide that FFP is not available for Medicaid payments if the State agency receives reimbursement from a liable third party.

Also, 42 CFR 456, subpart A, provides that each State must implement a statewide surveillance and utilization review (SUR) control program that:

- safeguards against unnecessary or inappropriate use of Medicaid services and against excess payments,
- assesses the quality of those services,
- provides for the control of the utilization of all services provided under the program, and

Funds recovered as a result of these SUR activities are to be credited to the Medicaid program.

State agencies must submit an accounting of their Medicaid expenditures to HCFA on a form HCFA-64 (Quarterly Medicaid Statement of Expenditures for the Medical Assistance Program). In addition, the State Medicaid Manual provides that the HCFA-64 is to be used by the States to report to the Federal

Government its pro rata share of applicable recoveries and collections, including amounts collected from TPL payers, if FFP had been claimed for the original expenditures.

Indiana was one of only two States that paid Medicaid expenses through a Health Insuring Organization (HIO). An HIO is an entity which assumes an underwriting risk to pay for medical services provided to Medicaid recipients in exchange for a premium paid by the State. In Indiana, the premiums were a negotiated fixed amount per beneficiary per month to cover the cost of providing all Medicaid services, except long term care services. The agreement provided that yearly quota-share calculations would be made to compare the premium income paid to the HIO to the actual paid Medicaid claims less TPL and SUR collections. The net profit or loss amounts were to be shared by the HIO and the State agency according to a formula prescribed in the agreement.

The State agency contracted with Blue Cross/Blue Shield of Indiana, now known as Associated State Government Contracts Inc. (ASGCI), to serve as the HIO for the risk costs and to process and pay Medicaid claims as the fiscal agent for the nonrisk costs (i.e., the long term care costs). In addition to the monthly premium payments the State agency made to ASGCI for the at risk costs, ASGCI was also reimbursed on a weekly basis for the long term care costs. The period of the contract was from March 1, 1986 to June 30, 1991. As part of the contract, ASGCI was responsible for TPL and SUR activities. In addition, ASGCI operated the Medicaid Management Information System (MMIS) which generated the reports used by the State agency to account for its Medicaid expenditures.

Effective July 1, 1991, National Heritage Insurance Company (NHIC), an affiliate of E.D.S. Federal Corporation, replaced ASGCI as the HIO and fiscal agent contractor for Indiana. The contract with NHIC is from July 1, 1991 to June 30, 1993 with an option for a 2-year extension through June 30, 1995.

SCOPE OF AUDIT

Our audit was conducted in accordance with Government Auditing Standards except we were not able to obtain auditee comments. The State agency requested and received a 60-day extension to respond. At the end of the extension, the State agency wrote that ...we cannot commit to an estimated date by which our response will be completed.... The purpose of our audit was to determine if the Federal Government received its pro rata share of TPL and SUR collections in a timely manner.

We conducted our audit at both the State agency and ASGCI in Indianapolis, Indiana. We reviewed the quarterly HCFA-64s, reports generated by the MMIS system, TPL Saving Summary Reports, SUR Saving Summary Reports, and other reports generated by ASGCI. Our audit covered the period from March 1, 1986 to March 31, 1991.

We reviewed the State agency's internal controls over reporting of TPL collections on the HCFA-64 reports. In addition, we did a limited review of ASGCI controls over reporting TPL and SUR amounts to the State agency.

During our audit, the State agency's internal auditors also started a review of the TPL activities. We were advised that after a brief review of overall TPL activities, the internal auditors were to review the appropriateness of ASGCI's Fiscal Year 1989 quota-share calculation. We collaborated our efforts with these auditors to the extent that was feasible.

Our field work was performed from January 1991 to May 1991.

FINDINGS AND RECOMMENDATIONS

FEDERAL SHARE OF TPL COLLECTIONS

The ASGCI recorded a total of $23,857,038 in TPL collections during the period March 1, 1986 through March 31, 1991. The ASGCI was liable to the State agency for interest on these funds. As of March 31, 1991, the Federal Government had received neither its share of the $23,857,038 nor the interest that was earned by ASGCI on these collections. Although the State agency believed that the Federal Government received its share of TPL collections through offsets to expenditures shown on the quarterly HCFA-64 reports, errors on the reports negated the effect of the offsets.

BACKGROUND

The Federal Government is entitled to a share of TPL collections applicable to Medicaid patients if the State agency received reimbursement from a liable third party. According to 42 CFR 433.140(c),

> "...If the State receives FFP in Medicaid payments for which it receives third party reimbursement, the State must pay the Federal Government a portion of the reimbursement determined in accordance with the FMAP for the State...."

For the period from March 1, 1986 to March 31, 1991, the rate of FFP for Medicaid expenditures in Indiana varied from a low of 62.82 percent to a high of 63.76 percent.

According to section 2500.1 of the State Medicaid Manual, TPL collections received each quarter are to be reported on line 9.A of the HCFA-64. These TPL collections and other collections on line 9, along with other decreasing adjustments on line 10, are to be subtracted from expenditures identified on lines 6, 7, and 8 to arrive at net expenditures for the quarter. Such a procedure, if followed, would result in the Federal Government receiving its proper share of TPL collections.

The TPL collections received by ASGCI were reported monthly to the State agency on a TPL Saving Summary Report. These TPL collections totaled $23,857,038 for the period March 1, 1986 through March 31, 1991, as follows:

Source of TPL Collections	Total
Medical provider*	$ 5,013,661
Insurance company**	18,843,377
Total	$23,857,038

*Also called "specific" collections
**Also called "nonspecific" collections

Based upon the rate of FFP in effect for the period, the Federal share of these collections would be $15,155,230.

The contract between the State agency and ASGCI did not specify into whose bank account the TPL and SUR collections were to be deposited upon receipt. In practice, these collections were deposited into ASGCI's Medicaid account. This was the same account that the monthly premium payments for the underwriting risk and weekly payments for long term care costs were deposited. Also, Medicaid payments to providers were made from this account. Funds placed in the account exceeded expenditures and a cash reserve developed. As of May 31, 1991, the cash reserve was about $233 million. According to the terms of the contract, ASGCI was permitted to invest the reserve cash as long as the State was paid interest on the use of the amount in the reserve. The interest rate payable was tied to Treasury Bill rates.

FINDING

Our review disclosed that TPL collections were reported each quarter on the HCFA-64 reports. However, the amounts reported for TPL collections made by ASGCI did not result in a reduction of Medicaid expenditures. As a result, the Federal Government did not receive its share of the $23,857,038 in TPL collections and the interest applicable to those collections. Details follow.

Reporting TPL Collections - Although the $23,857,038 in TPL collections received by ASGCI through March 31, 1991 were included on line 9.A of the quarterly HCFA-64s, the State agency also added that same amount to expenditures reported on line 6. The effect was to "zero-out" the TPL amounts because they were reported as an addition on line 6 and a subtraction on line 9.A to reported expenditures. State agency officials could not explain the reason for adding the amount of TPL collections received by ASGCI to line 6.

If reported expenditures on line 6 were net of TPL collections, then it would be necessary to add in the TPL collections to line 6 to preclude giving credit twice. However, the expenditures reported on line 6 were essentially the premium payments made to ASGCI for risk underwriting and the cost of long term care (nonrisk) expenditures. The premium payments reported on line 6 were not offset by TPL collections received by ASGCI. Also, our analysis of TPL collections received by ASGCI disclosed that they were not for long term care expenditures. Therefore, TPL collections were already included in the expenditures on line 6 and should not have been added to line 6.

<u>Quota-Share Calculations</u> - For each year after July 1, 1986, a quota-share calculation was to be made by the State agency and ASGCI. As a part of this calculation, the premium payments made to ASGCI were to be compared to actual claims paid to providers less TPL and SUR collections. According to the contract, if for any year, costs (payments to providers less TPL and SUR collections) were less than premiums received by ASGCI, ASGCI was entitled to 15 percent of the difference.

As of March 31, 1991, the only quota-share calculations that were finalized covered two periods: from March 1, 1986 to June 30, 1986 and July 1, 1986 to June 30, 1987. Those calculations, finalized September 22, 1989, indicated that the monthly premium payments received by ASGCI exceeded expenditures to medical providers less TPL and SUR collections by $20,647,463. According to the quota-share agreements, ASGCI received $3,460,392 of the $20,647,463. The balance of $17,187,071 ($20,647,463 less $3,460,392) remained in the Medicaid account.

The contract provided for ASGCI to receive its quota-share settlement annually. Also, based on the quota-share calculations, the State agency was supposed to receive its share of the quota-share settlement annually. No such return of funds was made to the State agency as of March 31, 1991. Within 12 months of termination of the contract, any funds, including interest, still in the account are to be turned over to the State agency. According to the contract with NHIC, if the State agency so elects, any funds remaining in the ASGCI account can be transferred to NHIC to pay for any claims processed after June 30, 1991 with service dates before July 1, 1991.

Conclusion - It is unrealistic to expect the Federal Government to wait 6 years to receive its share of TPL collections made by ASGCI. There was uncertainty among State agency officials about how these TPL collections were reported on the HCFA-64s. We concluded that clerical errors caused offsets to intended TPL credits. The Federal Government might have received the $23,857,038 (Federal share $15,155,230) in TPL collections plus interest at some future date; however, we saw or were told of no plan in which the Federal Government was to receive its share. As previously mentioned, some State agency officials were under the misconception that the Federal Government already had received its share through the HCFA-64 reporting.

We reviewed the terms of the new contract awarded to NHIC effective July 1, 1991. The contract provision for risk and nonrisk type costs, premium payment arrangements, provisions for holding monies in a separate bank account, accumulating a cash reserve, paying interest on this reserve, having an annual quota-share settlement, and delaying any return of excess funds in the account to the State agency until 1 year after the end of the contract are essentially the same provisions contained in the ASGCI contract. The NHIC contract, like the prior ASGCI contract, is silent on where the TPL and SUR collections made by NHIC will be deposited.

The practice of permitting the contractor to accumulate large amounts of reserve funds, which includes TPL collections, the Federal and State share of quota-share calculations, and interest, is contrary to Federal regulations. Generally, a grantee and subgrantees are authorized to draw down only sufficient funds to meet their immediate needs. The $233 million that ASGCI had in its Medicaid account as of May 31, 1991 was sufficient to fund the risk portion of the contract for over 3 months. The average monthly reserve balance in the account for the contract period, through May 31, 1991, was about $103 million. To preclude such large amounts of funds to accumulate under the contract with NHIC, we believe the NHIC contract should be amended, if necessary, to permit only enough build-up in reserve cash to meet immediate needs.

RECOMMENDATIONS

We recommend that the State agency:

1. Make a financial adjustment on the next quarterly HCFA-64 report in the amount of $23,857,038 (Federal share $15,155,230) plus interest.

2. Make any necessary adjustments to the amount recommended in 1. above, after the quota-share calculations are completed for the period of the contract.

3. Make future adjustments for TPL collections on a quarterly basis on the HCFA-64 reports.

4. Have the contractor return TPL and SUR collections to the State agency on a quarterly basis.

5. Establish controls to ensure that cash reserves accumulated by NHIC do not exceed its immediate needs. If necessary, the State should amend its contract with NHIC.

INTERNAL CONTROLS OVER TPL AND SUR COLLECTIONS

Improvements are needed in internal controls over TPL and SUR collections. Our review disclosed that existing internal controls did not ensure that all TPL and SUR collections were deposited and properly classified. In addition, our review of collections was often delayed and adversely affected by the lack of hard-copy documentation on the details of collections and a lack of a good understanding by either ASGCI or the State agency of the TPL and SUR collection process. These weaknesses reduce the reliability that can be placed on the accounting records and could increase the costs of the Medicaid program through incorrect quota-share calculations. Details follow.

Deposits - The TPL and SUR collections were deposited into the same Medicaid account as the risk premium payments, nonrisk payments, other collections, and refunds received by ASGCI. The finance unit within ASGCI deposited the TPL and SUR collections into the Medicaid account. However, there was no overall control to ensure that all TPL and SUR collections were in fact deposited.

Classification - For TPL collections, the designation on the TPL Saving Summary Report as to whether the collection was "specific" or "nonspecific" was often incorrect. The specific collections refer to collections sent in by the providers. The ASGCI enters these collections into the MMIS claims processing system as credits so that health providers' Forms 1099 filed with the Internal Revenue Service reflect only the "net" payments made to them. The nonspecific collections refer to collections sent in by TPL payers directly to ASGCI. These collections are not entered into the MMIS claims processing system as credits.

We tested the TPL Saving Summary Reports for August 1989, August 1990, and December 1990. All three reports included some TPL collections received from providers as "nonspecific" collections when they should have been identified as "specific." We traced a few of these TPL collections from providers and found that the collections were credited against the providers' claim records on the MMIS system. A summary of our review of the 3 months disclosed the following:

	Month Received			
	August 1989	August 1990	December 1990	Total
Per our review - Correct Amount of Specific Collections	$76,400	$73,372	$38,610	$188,382
Per TPL Saving Summary Report - Amount of Specific Collections	68,406	56,709	14,205	139,320
Amount by which Specific Collections were Understated and NonSpecific Collections were Overstated	$ 7,994	$16,663	$24,405	$49,062

For the 3 tested months, TPL collections from providers were understated by about 35 percent ($49,062 ÷ $139,320) on the TPL Saving Summary Report.

In the quota-share calculations, the specific collections are ignored since they already resulted in a reduction to the MMIS claim payment records used in the calculation. However, since the nonspecific collections are not credited against the MMIS claim payment records, these collections are identified and credited against the claim payments at the time of the quota-share calculations. If the nonspecific collections should incorrectly include some specific collections, the quota-share calculation would overstate ASGCI's gain or understate its loss.

We found similar misclassifications of SUR collections. Total SUR collections reported to the State agency by ASGCI on the SUR Savings Summary Reports for the period March 1, 1986 through March 31, 1991 were as follows:

Cash collections	$1,001,141
Provider offsets	98,283
Total	$1,099,424

The totals were incorrect because ASGCI, in some instances, combined cash collections and provider offsets into one figure reported under the cash collection line. We tested the August 1990 SUR Saving Summary Report which listed $50,558 in SUR cash collections for the month. We found that the amount included five transactions totaling $11,712 in provider offsets, and four transactions totaling $38,846 in cash collections.

This misclassification increases program costs through the quota-share calculations. The provider offsets reduce the paid claim records that the quota-share calculations are based on, and thus increase the profits, or lessen the losses reported by the quota-share calculations. When the provider offsets are misclassified as cash collections, the effect is to count them again as a credit to paid claim records when the SUR cash collections are netted against the paid claim amounts at the time of the quota-share calculation.

<u>Documentation and Understanding of the TPL Collection Process</u> - Our audit was hampered by a general lack of written documentation in readily reviewable form and a general lack of understanding by both the State agency and ASGCI personnel of the overall TPL collection process. When we began our audit at ASGCI in January 1991, we were not able to obtain supporting data for TPL collections received in December 1990 and for earlier months. Basic data such as the monthly TPL logs were not available. At our request, ASGCI re-ran some of this data from its computer system. Readily verifiable audit trails were not built into ASGCI's system of documentation. As a result, it was generally a lengthy process for ASGCI personnel to identify supporting details behind the monthly TPL logs.

We also were not able to identify personnel, within ASGCI or the State agency, who had a good understanding of the entire sequence of events involved in the TPL collection, recording, reporting, and quota-share calculation process. For example, the format, nomenclature, and program logic behind the TPL Saving Summary Report did not appear to be well understood by either the State agency or ASGCI personnel. Also, key personnel seemed to have different understandings as to whether a procedure existed whereby the Federal Government would receive its share of the TPL collections.

RECOMMENDATIONS

We recommend that the State agency establish internal controls over the TPL and SUR collections to ensure that:

1. Funds received are deposited.
2. Collections which reduce provider claims on the MMIS system are properly identified and reported.
3. Designated employees are fully aware of and monitor the collection process.
4. An audit trail including written documentation is maintained.
5. The various types of collections and their effect on the quota-share calculations are properly considered.