

## REPORT HIGHLIGHTS PERFORMANCE AUDIT

### Subject

The Human Resources Division administers the State's self-funded health benefits program, maintains a job classification and compensation system, provides human resources services, and maintains the State's new online hiring and recruiting software.

### Our Conclusions

The Department needs to review its use of consultants in managing the new self-funded health benefits program and require vendors to meet quality-of-care performance measures. The Department should require audits of its vendors' claims payment processing controls and review the accuracy of claims payments. Agencies report initial satisfaction with the new recruiting software, Hiring Gateway.



2005

## Strengthening the Self-Funded Health Benefits Program

The Human Resources Division (Division) of the Department of Administration (Department) manages the largest government human resources system in Arizona.

The Division serves over 62,000 active employees from 100 state agencies, boards, and commissions; 3 state universities; and approximately 9,000 retirees.

A significant benefit the Division provides is a self-funded health benefits program. This program, referred to as Arizona Benefit Options, was implemented in October 2004. It was developed with the intent to limit the State's growth in healthcare costs and to increase employees' choice of providers.

**Benefit Options**  
Choice. Value. Health.

Source: <http://www.hr.state.az.us>

Under the program, the State contracts directly with vendors to provide health services. The Department pays for the services using premiums it receives from employees, retirees, and state agencies.

**Consultant's role needs clarification**—The Department planned all along to use a consultant's services to help oversee the program. However, it also planned to hire and train additional staff. Because the Department had only 4 months to complete what it estimated to be a 12-



Source: <http://www.hr.state.az.us>

month implementation process, it gave up its staffing plan and relied more heavily on the consultant's expertise.

As of June 30, 2005, the Department paid the consultant approximately \$1.67 million, more than three times the original budget for this consultant and about 35 percent of its total administrative budget for fiscal year 2005.

Because of the limited time to implement the program, the Department did not clearly define the consultant's role and responsibilities. As a result, the consultant performs functions that the Department had intended to perform, and due to the lack of clearly defined roles and responsibilities for the consultant, some of these shared duties could potentially overlap or duplicate each other.

Now that the program is operating, the Department should review and develop a written policy regarding the consultant's role and responsibilities. In addition, the consultant should file regular, written reports with the required information.

#### Selected performance measures:

- Issue member identification cards within 10 business days.
- Not more than 2-5 percent of member telephone calls abandoned.
- Process eligibility information within 5 business days.
- 98-99 percent of medical claims processed accurately.

#### More oversight of healthcare vendors is needed

—The Department's vendors, which are those companies that provide program services such as healthcare, prescription drug services, and medical claims processing, are required to report on their performance either monthly, quarterly, semi-annually, or annually, and they may forfeit fees if performance is below standards.

As of May 2005, vendors have met several of the performance measure standards. However, two vendors have not met some of their required performance standards, and the Department has begun corrective action.

The Department can further ensure the adequacy of vendor performance by:

- **Establishing quality-of-care performance measures**—The Department does not have measures regarding adequacy of services and/or healthcare outcomes, such as the percentage of women receiving breast cancer screenings or the percentage of adults receiving wellness checkups.
- **Validating self-reported information**—The Department does not verify vendor reports or

ensure that it has the information to verify reports. For example, one vendor provides graphs showing telephone wait times, but does not provide documentation to support the graphs.

To help ensure compliance with contract requirements, the Department should develop a plan to conduct operational and financial reviews (OFR). An OFR is a comprehensive annual evaluation of vendor contract compliance and the quality and availability of healthcare.

Three of eight states we contacted and our own Arizona Health Care Cost Containment System regularly conduct OFRs to assess their vendors' performance. The Department should identify the staff and expertise needed to conduct OFRs and whether they will be conducted by in-house staff or an outside consultant.

The Department also needs to determine its staffing needs. The Department has begun to develop a staffing plan, but should ensure this plan addresses all the issues previously mentioned. It should consider what types of expertise are needed and the types of management and oversight functions it intends to perform.

#### Recommendations

The Department should:

- Identify and define the consultant's role and responsibilities.
- Ensure that its consultant provides regular, written reports with the required information.
- Establish quality-of-care performance measures, and validate vendors' reported compliance with performance measures.
- Develop a plan for conducting operational and financial reviews of vendors.
- Continue efforts to develop a staffing plan.

## Additional Steps Needed To Ensure Program's Financial Soundness

When an employer self-funds health benefits, it assumes the financial responsibility of ensuring that monies are available to pay for the benefits. Thus, if

the expenses from the State's self-funded health benefits program exceed revenues, the State is responsible for the deficit.

**Actions to limit risk**—To ensure that the program is viable and solvent, the Department:

- Contracted with an actuary to develop a 5-year cost projection as the basis for the premiums paid by the State, employees, and retirees.
- Established reserves to cover claims that exceed projections. The amount of the reserves represents nearly 2 months of healthcare claims payments.
- Purchased insurance to cover very large (over \$500,000 per insured individual) medical and prescription drug claims.

**Ensuring appropriate, accurate claims**—Because claims used approximately 79 percent of the program's revenues, improvements to the claims payment processes would help protect the program's long-term stability.

Two of the Department's vendors process and pay medical claims, and a third vendor processes and pays the prescription drug claims. These three vendors process over 99 percent of the program's claims. Although the Department requires these vendors to meet standards for timeliness and accuracy, the vendors self-report their success.

The Department has contracted for reviews of its vendors' claims payment processes, but these reviews did not or will not assess the adequacy and effectiveness of these vendors' processing controls.

The Department should require its vendors to obtain independent audits of their internal controls over claims payment processes and their claims payment data. Audits can help ensure the appropriate and accurate processing of claims and the accuracy of claims data. For example, the State's previous health plan vendor asserted that 99.3 percent of its claims were processed accurately, but an audit of the claims data concluded that the actual number was only 86.8 percent.

Equally important, the Department should conduct its own reviews. It should:

- Verify claims data from all vendors against member eligibility data. Currently, it does so for only two vendors.
- Review the accuracy of payments to ensure claims were paid in accordance with the benefit plan provisions.
- Based on its consultant's findings, establish procedures to address recommendations made regarding its processes for transferring eligibility data to and paying its vendors.

**Need to ensure actuary is independent**—The Department's consultant provided the actuarial services to implement the program. However, because the consultant has also helped manage and oversee the program, the State now needs an independent actuary to ensure the cost projections are objective and unbiased.

#### State Health Benefits Program Fiscal Year 2005

- \$333.3 million in revenues.
- \$282.6 million in claims and administration.
- \$49.6 million reserve.

## Recommendations

The Department should:

- Require its vendors to obtain independent annual audits of their claims payment processes and data.
- Verify the accuracy and appropriateness of claims payments, and establish procedures to address recommendations made regarding its processes for transferring eligibility data and paying vendors.
- Contract with an independent actuary.

## State's Online Hiring Software



Source: <http://hr.state.az.us>

The Department is in the process of completing the implementation of Yahoo!® Hiring Gateway, a Web-based recruiting and hiring software. The Department expects to complete implementation in November 2005.

Agency users report that the software saves time and assists in recruiting more qualified candidates.

The new software has several advantages over the previous software the Department was using. Hiring Gateway permits agency users to:

- Create job specifications at their desktop computer and transmit the information by e-mail to the Department.

- Generate hiring lists and rank the applicants on the list, eliminating the least qualified.
- Receive applications from only those interested in the job.
- Create specific screening questions to develop a better applicant pool.

Information received from Hiring Gateway is also automatically transferred to the State's integrated payroll and benefits system when an agency hires a person. Twenty-two of the State's larger agencies have direct access to the software. While most smaller agencies do not have access to Hiring Gateway, DOA provides the services and benefits available on this software to these agencies.

### TO OBTAIN MORE INFORMATION

A copy of the full report can be obtained by calling  
**(602) 553-0333**



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our Web site at:  
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## Accounting for Post-retirement Benefits

The Governmental Accounting Standards Board (GASB) is a national organization that prescribes the financial accounting and reporting standards that state and local government entities follow in reporting their financial condition. Beginning in fiscal year 2008, GASB's new reporting standard, Statement No. 45, requires government entities to recognize on their financial statements the long-term cost of nonpension, post-employment benefits, such as healthcare, that employees earn and will receive upon retirement.

Currently, the State and its employees subsidize the participation of retirees in the State's health plan. Such coverage would cost retirees more if they did not participate in the plan because their average monthly medical claims costs are often greater than active members' claims costs. The difference between retirees' medical costs and the premiums they pay

represents the subsidy, or benefit, the State provides and must begin to recognize on its fiscal year 2008 financial statements. The subsidy, or benefit amount, must be actuarially determined.

The State has several options. It can:

- Continue providing the benefits at the same level and recognize the unfunded health benefits. It is unclear how this unfunded liability would affect the State's financial position and stability.
- Change the retiree benefits by requiring retirees to make contributions to pay for the benefits, or reduce or eliminate the benefit, thereby either limiting or eliminating the liability.

The Legislature currently has a retiree health insurance committee that is studying options for providing post-employment health insurance.