



A REPORT  
TO THE  
ARIZONA LEGISLATURE

Financial Audit Division

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Management Letter

**Department of Economic  
Security**

Division of Developmental  
Disabilities ALTCS Contract  
Year Ended June 30, 2003

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**Debra K. Davenport**  
Auditor General

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**STATE OF ARIZONA  
OFFICE OF THE  
AUDITOR GENERAL**

**DEBRA K. DAVENPORT, CPA**  
AUDITOR GENERAL

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December 11, 2003

David A. Berns, Director  
Department of Economic Security  
1717 West Jefferson Street  
Phoenix, AZ 85007

In planning and conducting our audit of the Department of Economic Security, Division of Developmental Disabilities, ALTCS Contract for the year ended June 30, 2003, we performed the following as required by U.S. generally accepted auditing standards and the *Arizona Administrative Code*, Title 9, Chapter 28, as detailed in the *Reporting Guide for Arizona Long-Term Care System (ALTCS) Program Contractors with the Arizona Health Care Cost Containment System*:

- Considered the Division's internal controls over financial reporting and
- Tested its compliance with laws and regulations that could have a direct and material effect on the ALTCS Contract's financial statements.

Our audit disclosed internal control weaknesses and instances of noncompliance with laws and regulations. Management should correct these deficiencies to ensure that it fulfills its responsibility to establish and maintain adequate internal controls and comply with laws and regulations. Our recommendations are described in the accompanying summary.

This letter is intended solely for the information of the members of the Arizona State Legislature, the Arizona Health Care Cost Containment System, and the Director of the Department of Economic Security and is not intended to be and should not be used by anyone other than the specified parties. However, this letter is a matter of public record, and its distribution is not limited.

Should you have any questions concerning its contents, please let us know.

Sincerely,

Debbie Davenport  
Auditor General

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# BACKGROUND

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The Department of Economic Security, Division of Developmental Disabilities (Division) contracts with the Arizona Health Care Cost Containment System (AHCCCS) to provide medical and healthcare services to eligible enrollees of the Arizona Long-Term Care System (ALTCS) program for the developmentally disabled. The ALTCS program provides inpatient and outpatient medical and nursing services, as well as managed institutional and home- and community-based long-term care services. The ALTCS program is administered by the AHCCCS under the State of Arizona's Medicaid Program, which is subject to federal guidelines and participation under Title XIX of the *Social Security Act* (Title XIX).

## The Division should establish procedures to accurately record and report financial information

The Division's management is responsible for preparing accurate financial statements and demonstrating compliance with the accounting and reporting requirements of contractual arrangements with the AHCCCS and the *Reporting Guide for Arizona Long-Term Care System (ALTCS) Program Contractors with the Arizona Health Care Cost Containment System*. In addition, the AHCCCS depends on accurate financial information so it can fulfill its contract oversight responsibilities. The Division also has a responsibility to report accurate information to the public. To achieve these objectives, management should ensure that transactions are recorded correctly in the appropriate accounts and in the proper fiscal year. Management should also ensure that its accounting estimates reported in the financial statements are reasonable, based on current information, and consistently follow the methods established by the AHCCCS. However, the Division did not always accurately record and classify amounts presented in the financial statements and supplemental schedules. In addition, some balances reported were not supported by or reconciled to the Division's accounting records. For example, the Division was unable to readily reconcile the ALTCS portion of cash and investments held by the State Treasurer to its accounting records. Additionally, management's accounting estimates, although not materially misstated, were not always prepared in accordance with the AHCCCS' requirements. The Division adjusted its financial statements and supplemental schedules for all significant errors noted.

The Division should ensure that the financial information reported to the AHCCCS and the public is accurate and complete. Therefore, division management should establish procedures to ensure that all transactions are correctly recorded in the proper accounts and fiscal year, and are accurately accumulated and reported in the financial statements. Specifically, the Division should implement the following procedures:

## Accounting Records

- Use the AHCCCS estimation methods for estimating the institutional care incurred but reported (IBNR) claims payable for the last 2 months of the fiscal year.
- Develop institutional care and home- and community-based services (HCBS) payment lag schedules that report claim payments by placement setting as required by the AHCCCS.
- Exclude ventilator dependent claim payments from the institutional care and HCBS payment lag schedules when developing estimates of IBNR claims payable.
- Develop a ventilator dependent payment lag schedule based on actual payment information to estimate the Ventilator Dependent IBNR claims payable.
- Develop a method to identify and report institutional care and HCBS reported but unpaid claims payable. The Division should consider using the Arizona Social Services Information Tracking System (ASSISTS) Professional Billing Service interface as a possible method.
- Improve the quality control review process to minimize compilation errors when preparing lag schedules.

## Financial Statements

- Separately account for all account balances and transactions, including accruals and reclassifications, in a single fund or set of funds to use when preparing financial statements.
- Properly classify and report all prior and current year expenditures and revenues in the financial statements.
- Ensure that all account balances and transactions are properly supported by or reconciled to its accounting records.

# The Division should complete the processing and reporting of rehabilitation medical and healthcare claims payments

In fiscal year 2002, the AHCCCS approved the Division's request to cover certain Title XIX members under the ALTCS Contract for whom the Department of Economic Security was providing other rehabilitation services within its Rehabilitation Services Administration (RSA). As a result, the Division's management is responsible for ensuring that medical and healthcare claims paid for these members are for eligible services and are accurately reported in the ALTCS Contract financial statements and to the AHCCCS.

During fiscal years 2002 and 2003, RSA medical and healthcare claims paid from the ALTCS Contract were processed and recorded on a different accounting system than was used by the Division to process, record, and prepare its ALTCS Contract financial statements, and to report claims payment information for its other ALTCS Contract plan members to the AHCCCS. In order for the Division to report medical and healthcare claims payments for these Title XIX members on the ALTCS Contract financial statements and to the AHCCCS, the Division had to convert the medical and healthcare claims payment information for these members onto its ASSISTS. The conversion required substantial data modification and manual intervention and was very time consuming. Consequently, the Division used unsupported estimates to pay members' medical and healthcare claims and report expenditures on the June 30, 2003, ALTCS Contract financial statements. Further, as of November 18, 2003, the Division still had not completed the conversion of fiscal year 2003 RSA Title XIX members' medical and healthcare claims payments onto its ASSISTS. During the year ended June 30, 2003, the Division paid \$12.7 million of RSA medical and healthcare claims from the ALTCS Contract, \$4.6 million of which was recognized as expenditures in the prior year. Since the Division had not completed the processing of these payments during our audit, we were unable to determine whether the RSA claims paid from the ALTCS Contract and reported in the financial statements were for eligible Title XIX expenditures.

Effective July 1, 2003, the responsibility for monitoring, contracting with, and paying rehabilitation organizations to provide Title XIX eligible rehabilitation services to ALTCS Contract members, as well as accounting for these activities, was transferred to the Division.

The Division needs to ensure that all contract-related RSA Title XIX members' medical and healthcare claims payments made prior to July 1, 2003, are accurately identified, accounted for, and reported to the AHCCCS. Therefore, the Division should complete the conversion of all RSA Title XIX members and related medical

and healthcare claims payment information onto ASSISTS. Once the conversion is completed, the Division should reconcile the eligible expenditures for these members with the related RSA expenditures paid from the Contract and recorded on the June 30, 2003, financial statements and make all necessary adjustments.

## The Division should account for contract revenues and expenditures by rate code classification

Contractual arrangements with the AHCCCS and the *Reporting Guide for Arizona Long-Term Care System (ALTCS) Program Contractors with the Arizona Health Care Cost Containment System* require that the Division report to the AHCCCS an analysis of revenues and expenditures by major rate code classification annually. However, the Division's claims processing systems were unable to account for contract revenues and expenditures by rate code classifications as required by the AHCCCS. As a result, the *Analysis of Profitability by Major Rate Code Classification* was excluded from the supplemental schedules accompanying the financial statements.

The Division should make the appropriate program modifications to its claims processing systems to account for revenues and expenditures in the level of detail required to prepare the *Analysis of Profitability by Major Rate Code Classification*. Doing so will help the Division comply with the provisions in the ALTCS Contract and the *Reporting Guide for Arizona Long-Term Care System (ALTCS) Program Contractors with the Arizona Health Care Cost Containment System*.





ARIZONA DEPARTMENT OF ECONOMIC SECURITY

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Janet Napolitano  
Governor

David A. Berns  
Director

DEC 10 2003

Ms. Debbie Davenport  
Auditor General  
State of Arizona  
Office of the Auditor General  
2910 North 44<sup>th</sup> Street, Suite 410  
Phoenix, Arizona 85018

Dear Ms. Davenport:

In response to the Management Letter for the State of Arizona, Department of Economic Security, Division of Developmental Disabilities (DDD), Arizona Long Term Care system (ALTCS) Contract audit for the fiscal year ended June 30, 2003, the Department submits the following responses:

**Recommendation 1:**

**The Division should establish procedures to accurately record and report financial information.**

Following are the Department's responses to each of the bullet points listed under "Accounting Records":

- Changes to the estimation of the institutional IBNR have already been made.
- The Division is in the process of changing selection criteria for the lag reports to categorize by placement settings.
- DDD has been separating Vent IBNRs and expenditures after totals had been derived. DDD will now pull the expenses out prior to that calculation. The change in process will have no material effect on the resulting IBNR amounts.
- A more detailed ventilator lag schedule is in the developmental stage. Assuming resources, it should be completed by the time of next year's audit.
- As has been noted in prior audits and AHCCCS reviews, ASSISTS does not have the ability to generate RBUC information. The Division will continue to look for ways that it may be able to identify and report HCBS and institutional RBUC information.
- The compilation errors did not result in any material misstatement, and the Division has made the corrections. The Division will continue to look for ways to improve the quality control process.

Following are the Department's responses to each of the bullet points listed under "Financial Statements":

- The Department does not concur with this portion of the finding. DES uses funds and funding streams that provide the accounting information necessary to prepare complete and accurate financial statements. The funds used are a necessary part of the DES accounting system and the DHHS-approved cost allocation process utilized throughout the entire Department.
- The Department concurs with these portions of the finding. These errors were not material and have been corrected. In the future, the Department will exercise more care to properly classify and report all prior and current year revenues and expenditures and to ensure that all account balances and transactions are properly supported by or reconciled to its accounting records.

#### **Recommendation 2**

**The Division should complete the processing and reporting of rehabilitation medical and healthcare claims payments.**

At the time of the audit, not all of the RSA information was available for audit purposes. The Division has now received the data. There will continue to be claim information received for these services for this period as there is a normal claims lag involved. All claims received are reconciled with the information provided by RSA and for SFY 2003, \$6.1 out of \$6.4 million has been already encountered to AHCCCS. In addition, the expenditure and estimated amounts on the financials related to these services are now supported completely by the services the Division paid for and the eligibility of the client as dictated by AHCCCS.

As noted above, this program was transitioned to DDD on July 1, 2003, so any problems in the transition of service codes and expenditure amounts from RSA to DDD are no longer an issue.

#### **Recommendation 3**

**The Division should accurately record and report contract profitability by classification.**

The ASSISTS system is not capable of collecting information by classifications at this time. AHCCCS is aware of this. The Division will continue to look for ways it can record and report accurately on this data, or will ask for the AHCCCS requirement for submittal to be removed.

Sincerely,

David A. Berns