

REPORT HIGHLIGHTS
 FINANCIAL STATEMENT AUDIT

About the ALTCS Contract

Subject

The Department of Economic Security issues financial statements annually for the Division of Developmental Disabilities Arizona Long-Term Care System (ALTCS) Contract. The Division is responsible for preparing the financial statements, maintaining strong internal controls, and demonstrating compliance with its contractual arrangements with the Arizona Health Care Cost Containment System (AHCCCS). As auditors, our job is to determine whether the Division has met its responsibilities.

Our Conclusion

The information in the financial statements was fairly stated in all material respects, and the financial statements can be relied upon. Our audit also determined that the internal control system was adequate, and the Division substantially complied with AHCCCS contract requirements. However, we made a recommendation in our management letter for improving the Division's internal controls over financial reporting and compliance with AHCCCS' accounting and reporting requirements.

The Department of Economic Security, Division of Developmental Disabilities (DDD) contracts with AHCCCS to provide long-term medical and healthcare services to the developmentally disabled under the ALTCS program. Such services include the following:

- Home- and community-based services, including state- and vendor-operated group homes and home-based services provided where enrollees live.
- Acute care inpatient and outpatient services.
- Institutional care, such as skilled nursing, and intermediate care in institutional settings.
- Other care, including mental health and ventilator dependent services.

During the year, the ALTCS Contract spent \$442.4 million to provide medical and healthcare services to its enrollees. These costs were reported as aid to individuals expenditures in the financial statements and represented over 88 percent of total ALTCS Contract expenditures of \$502.3 million.

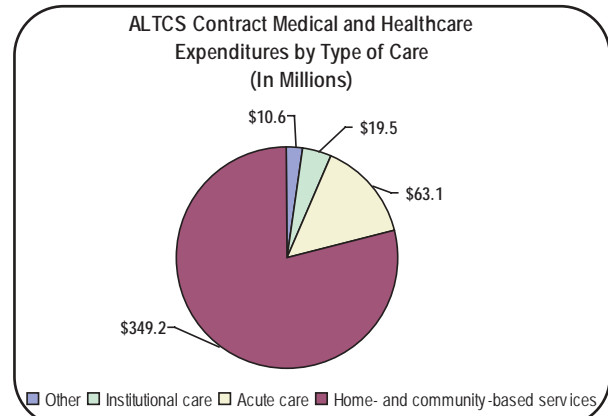
The tables and figure to the right summarize the Contract's Balance Sheet and Statement of Revenues, Expenditures, and Changes in Fund Balance, and a breakdown of the ALTCS Contract's medical and healthcare expenditures by type of medical and healthcare services provided.

Balance Sheet
June 30, 2004
(In Millions)

Assets:	
Cash and investments held by State Treasurer	\$57.2
Due from other state funds	5.1
Total assets	\$62.3
Liabilities and Fund Balance:	
Accrued administrative and payroll costs	\$ 2.0
Accrued medical and healthcare claims	47.2
Due to other state funds	7
Total liabilities	49.9
Unreserved fund balance	12.4
Total liabilities and fund balance	\$62.3

Statement of Revenues, Expenditures, and Changes in Fund Balance
Year Ended June 30, 2004
(In Millions)

Revenues:	
Capitation	\$497.4
Other	10.9
Total revenues	508.3
Expenditures:	
Health and welfare:	
Aid to individuals	442.4
Allocated administrative expenditures	23.5
Case management	22.4
Professional and outside services	6.1
Premium tax	7.9
Total expenditures	502.3
Excess of revenues over expenditures	6.0
Other financing uses:	
Transfers to other state funds	(.6)
Net change in fund balance	5.4
Fund balance—beginning	7.0
Fund balance—ending	\$ 12.4



2004

Year Ended June 30, 2004

Fund Balance Increases for the ALTCS Contract

During the year, the ALTCS Contract's fund balance increased by \$5.4 million. The increase was primarily attributable to the following:

- Average monthly membership of the Contract's enrollees increased approximately 8.5 percent from the prior year. This increase in membership was responsible for most of the increase in revenues and expenditures of 15 percent and 12 percent, respectively. In addition, revenues also increase because the capitation rate per member per month increased 5.6 percent.

- Transfers of interest earnings to the State-Fund Long-Term Care Program decreased from \$1.1 million in fiscal year 2003 to approximately \$625,000 in fiscal year 2004.

Change in Fund Balance (In Millions)

Fund balance, July 1, 2003	\$ 7.0
Excess of revenues over expenditures	6.0
Transfers to other state funds	(.6)
Fund balance, June 30, 2004	<u>\$12.4</u>

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Division Needs to Accurately Record and Report Financial Information

The Division's management is responsible for preparing accurate financial statements, demonstrating compliance with AHCCCS' accounting and reporting requirements, and reporting accurate information to AHCCCS and the public. However, these objectives were not fully achieved, as the financial statements and supplementary schedules contained numerous errors. For example, management's accounting estimates for incurred but not reported claims payable were overstated by approximately \$2.6 million. Ultimately, the Division adjusted its financial statements and supplementary schedules for all significant errors that the auditors noted.

To help ensure that the Division's management achieves these objectives, it should establish procedures to ensure the following:

- All financial transactions are accurately recorded and classified in the Division's accounting records.
- All accounting estimates reported in the financial statements are prepared in accordance with AHCCCS' requirements.

REPORT HIGHLIGHTS FINANCIAL STATEMENT AUDIT

Year Ended June 30, 2004