



A REPORT
TO THE
ARIZONA LEGISLATURE

Financial Audit Division

Management Letter

**Department of
Economic Security**

Division of Developmental
Disabilities ALTCS Contract
Year Ended June 30, 2004



Debra K. Davenport
Auditor General

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

DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

WILLIAM THOMSON
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October 25, 2004

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, Arizona Long-Term Care System (ALTCS) Contract for the year ended June 30, 2004, 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 an internal control weakness and an instance of noncompliance with laws and regulations. Management should correct this deficiency to ensure that it fulfills its responsibility to establish and maintain adequate internal controls and comply with laws and regulations. Our recommendation is described below.

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 Arizona Health Care Cost Containment System (AHCCCS) and the *Reporting Guide for Arizona Long-Term Care System (ALTCS) Program Contractors with the Arizona Health Care Cost Containment System*. In addition, 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 its accounting estimates reported in the financial statements and supplementary schedules are reasonable, based on current information, and consistently follow the methods established by AHCCCS. However, the Division did not always accurately record and classify amounts presented in the financial statements and supplementary schedules. For example, management's accounting estimates for incurred but not reported (IBNR) claims payable were overstated by approximately \$2.6 million because ventilator dependent services were improperly included in the home- and community-based services' (HCBS) IBNR claims payable as well as in other medical payables. This was caused because management used appropriation codes to determine IBNR claims payable instead of placement settings as required by AHCCCS. The overstatement of IBNR was corrected on the financial statements and supplementary schedules.

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

- Develop institutional care and HCBS payment lag schedules that report claim payments by placement setting as required by 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 Professional Billing Service interface as a possible method.
- Assign a second employee to review supplementary schedules to detect and correct any compilation errors that may have occurred.

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



ARIZONA DEPARTMENT OF ECONOMIC SECURITY

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Janet Napolitano
Governor

David A. Berns
Director

Ms. Debbie Davenport
Auditor General
State of Arizona
Office of the Auditor General
2910 North 44th 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, 2004, 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 response to each of the bullet points listed:

- The Division is in the process of changing selection criteria for the lag reports to categorize by placement settings.
- The Division has been separating Vent Incurred But Not Reported obligations and expenditures after totals had been derived. The Division will now pull the expenses out prior to that calculation. The change in process will have no material effect on the resulting Incurred But Not Reported amounts.
- A more detailed ventilator lag schedule is in the developmental stage. Assuming resources, it should be completed by next year's audit.
- As has been noted in prior audits and AHCCCS reviews, the Arizona Social Services Information Tracking System does not have the ability to generate Received But Unpaid Claims information. The Division will continue to look for ways that it may be able to identify and report Home and Community Based Services and institutional Received but Unpaid Claim 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.

If you have any questions, please call Ric Zaharia at (602) 542-6857 or me at (602) 542-5678.

Sincerely,

David A. Berns
Director