OFFICIAL STATE CABINET AGENCY RESPONSE TO THE PERFORMANCE AUDIT ON THE HEALTH CARE AUTHORITY'S OVERSIGHT OF THE MEDICAID MANAGED CARE PROGRAM APRIL 2, 2014

This coordinated management response to the State Auditor's Office (SAO) performance audit report received March 12, 2014, is provided by the Washington State Health Care Authority (HCA) and the Office of Financial Management (OFM).

SAO Performance Audit Objectives:

Are managed care organizations overpaying for medical expenses? If so, why did they go undetected and how do the overpayments affect premium rates?

1. Are policies and procedures in place to ensure costs reported by managed care organizations to the third-party actuary:
   - Offset recoveries, rebates and refunds against medical costs;
   - Include only allowable administrative expenses and allocate costs on a reasonable basis; and
   - Report costs related to subcontractors properly?

SAO Issue 1: Inadequate oversight and data analysis led to overpayments.

SAO Issue 2: Undetected overpayments in 2010 resulted in potentially higher premium costs in 2013.

SAO Issue 3: Data used to set 2013 premium rates was not verified and retained.

SAO Issue 4: Inconsistent reporting of administrative costs, recoveries and rebates.

Please note that the state grouped some of the SAO's recommendations in a different order to allow for a more concise response.

SAO Recommendation 1: Create and implement a comprehensive revenue, cost reporting and monitoring system to enhance accountability and ensure the managed care organizations comply with contract provisions. This should include requiring the managed care organizations to report detailed claims and administrative cost data to the HCA in a prescribed format on a periodic basis, and reviewing the profitability of the organizations with respect to the Washington State Medicaid program. Best practices that could be followed to create a comprehensive monitoring program have been provided in Appendix D as guidance. Instructions for the regular reporting should include guidance on how to handle recoveries that apply to claims paid in a prior period.

STATE RESPONSE: HCA concurs with the recommendation to create and implement comprehensive revenue, cost-reporting and monitoring systems, as they will further strengthen HCA's ability to effectively manage and oversee the Medicaid Managed Care Plans. The development of these systems is a significant undertaking and will take considerable time to achieve. HCA must create a new infrastructure and develop staff expertise to accomplish this task.

As a part of these strategies, HCA implemented a process in the Managed Care Organizations (MCO) contract, effective January 2014, for reconciliation of submitted encounter data with MCO cost reports. This process will measure the completeness of encounter data submission. Associated withholding provisions reinforce the need for accurate, complete and timely encounter data. The data will be used to measure and monitor managed care plan quality, evaluate audit service utilization, monitor finance and rate setting, and ensure compliance with contract requirements.

Action Steps and Time Frame

HCA has established a Managed Care Executive Oversight Committee. The Committee will analyze other states' best practices and build upon an existing draft action plan and implementation strategy for the development of monitoring systems to address the areas noted in the recommendation. This action plan and implementation strategy will identify next steps, estimated timelines and resource needs.

- Develop Action Plan and Implementation Strategy. *By December 31, 2014.*

SAO Recommendation 2: Conduct regular audits according to a routine, ongoing schedule to ensure compliance with respect to appropriate medical costs, allowable administrative costs, cost recoveries and compliance with specific contract performance requirements.

STATE RESPONSE: HCA concurs that conducting regular audits of these areas is a critical component of appropriate MCO oversight.

Action Steps and Time Frame

The Managed Care Executive Oversight Committee will develop regular audit plans as a part of the action plan and implementation strategy noted above (response to SAO Recommendation 1).

- Complete Action Plan and Implementation Strategy. *By December 31, 2014.*

SAO Recommendation 3: Establish clear criteria, specific to Washington, to define cost principles in determining allowable expenses.

SAO Recommendation 12: Ensure that MCOs . . . strengthen their review process to determine if administrative expenses are allowable and properly allocated.

SAO Recommendation 14: Ensure that MCOs . . . structure contracts with delegated entities to ensure medical and administrative costs are clearly defined and distinguishable.

STATE RESPONSE: HCA partially agrees with the recommendations. HCA can establish cost principles with the MCO through the contract. MCOs can be required to ensure administrative expenses are allowable and allocation is appropriate. MCOs are responsible for contracting with providers and other entities to ensure accurate encounter data are reported and costs are maintained within the rate provided by the state. Appropriate designation of costs and the allowability of costs are determined through these processes.

The current rate-setting process does not rely on use of the plan's direct administrative costs but rather relies on industry standards.

Action Steps and Time Frame

- HCA will define cost principles for use by the MCOs in determining allowable expenses for inclusion in the 2015 contract. *By January 2015.*

SAO Recommendation 4: Provide specific guidance for the Medical Loss Ratio calculation, including the definition of medical and administrative costs. Using the National Association of Insurance Commissioners' recommendations would make the guidance consistent with commercial insurance industry practices and give the organizations clear instruction to perform the calculation on a consistent, comparable basis.

STATE RESPONSE: HCA agrees and has addressed this recommendation in the 2014 MCO contract.

Action Steps and Time Frame

- HCA has provided clearer guidance for the calculation of the Medical Loss Ratio in the 2014 contract. *Complete.*

SAO Recommendation 5: Create procedures and instructions for the organizations that addresses recording and reporting costs incurred and recoveries realized, including those following the date of submission of the Experience Reports to the HCA's third-party actuary.

STATE RESPONSE: HCA agrees with this recommendation.

Action Steps and Time Frame

- Procedures and instructions will be developed for inclusion in the MCO contract. *By January 2015.*

SAO Recommendation 6: Establish clear, specific, cost reporting guidance for the organizations that addresses the timing of reporting pharmacy rebates to ensure they all calculate and report pharmacy rebates consistently.

SAO Recommendation 13: Ensure that MCOs . . . create formal documented policies and procedures for the calculation and reporting of pharmacy rebates and reinsurance recoveries that comply with instructions provided by the HCA's third-party actuary.

STATE RESPONSE: HCA agrees with these recommendations.

Action Steps and Time Frame

- Procedures and instructions will be developed for inclusion in the MCO contract. *By January 2015.*

SAO Recommendation 7: Establish a specific schedule for the timing of rate re-determinations.

SAO Recommendation 8: Work with the actuary to require transparency and support in the rate setting process. We have included an example of actuarial review as a best practice for establishing a comprehensive monitoring program in Appendix D.

SAO Recommendation 9: Require the actuary to give the HCA information used to calculate the capitation rate, including how sub-capitation payments and related fee-for-service equivalents were taken into account in the rate setting process. By making this process more transparent, the state could monitor the development of premium rates and ensure these special pricing arrangements are properly considered in the rate setting process.

STATE RESPONSE: HCA agrees that the timing and transparency of managed care rate setting are important. As noted in the cover letter, HCA is working to implement the structure and staffing necessary to become a purchaser of quality health care, rather than a fee-for-service provider of health care. Part of this process involves developing internal expertise on managed care rate-setting processes to ensure appropriate time frames and development of structures for transparent rate-setting methodologies. These processes are significantly more complex than historical Washington state Medicaid fee-for-service rate-setting activities, and improvement requires development of staffing expertise not currently found at the state level.

Action Steps and Time Frame

HCA is implementing a process to continue to develop improved managed care rate-setting methodologies and standards. Time frames for implementation are as follows:

- Identify new expertise needed to implement the managed care rate-setting function. *Complete.*
- Recruit staff resources identified. *By December 2014.*
- Amend actuarial contract to require sharing of rate-setting information. *By January 2015.*
- Develop systems and processes to increase rate-setting transparency. *By July 2015.*
- Develop processes to appropriately review and communicate rate-setting information to the agency and the authorizing environment. *By July 2015.*

SAO Recommendation 10: Ensure that MCOs . . . review system edit checks and post-payment procedures to ensure claims are reviewed in sufficient detail to identify miscoding and other causes of overpayments. The contract should require that the managed care organizations use edits such as those of the National Correct Coding Initiative (NCCI).

STATE RESPONSE: HCA partially concurs with this recommendation. While system edit checks and post-payment procedures are critical to correcting claims payments, these activities exist on a continuum in an IT system. Claims adjudication systems cannot edit for every variable, and post-payment reviews must adapt to ever-changing provider behaviors. MCOs use different hardware and software to process claims, and the level of technical sophistication will affect the system edits and post-payment review functions as well as the MCOs' ability to implement the full complement of NCCI edits in their systems.

Action Steps and Time Frame

HCA will review best practices related to Medicaid review of MCO claims adjudication systems. This review may include a survey of other states and on-site visits to view systems in place. HCA will develop contract language and action plans to improve Washington's system to a level commensurate with other states.

- Research complete. *By December 2014.*
- HCA will add language to the MCO contracts to require the use of NCCI edits. *By January 2015.*
- Improvement plans adopted. *By April 2015.*
- MCO contract improvements implemented. *By January 2016.*

SAO Recommendation 11: Ensure that MCOs . . . retain a copy of the data file that is sent to the third-party actuary, with sufficiently detailed data fields to allow audit of the data.

STATE RESPONSE: HCA concurs that MCOs should retain a copy of the data file they send to the third-party actuary to facilitate the rate-setting process.

Action Steps and Time Frame

- HCA will add language to the MCO contracts to require retention of the data files sent to the actuary. *By January 2015.*

SAO Recommendation 15: Ensure that MCOs . . . are transparent in the treatment of claims and recoveries involving CHPW and the Network. These transactions should be recorded accurately and timely and appropriate documentation should be available for review by HCA when requested.

STATE RESPONSE: HCA agrees with the recommendation that Community Health Plan of Washington (CHPW) and its network must accurately record transactions between these entities on a timely basis.

Action Steps and Time Frame

- The 2015 CHPW contract will include a provision to require accurate and timely recording of transactions between CHPW and its network. *By January 2015.*

SAO Recommendation 16: Address these recommendations.

SAO Recommendation 17: HCA update its contract language with the managed care organizations to allow the state to recover overpayments identified in state and other audits.

STATE RESPONSE: HCA partially concurs with these recommendations. While we are in agreement about the need for clear contract language on the recovery of overpayments, recoveries identified as a result of state audits of MCOs or their providers is a complex issue that requires coordination among MCOs, the state Medicaid agency and federal funding authorities. HCA agrees

that policies and procedures related to the recovery of overpayments must be established, but the state may not be able to recover overpayments in every case.

Action Steps and Time Frame

HCA will review best practices of other states and develop a comprehensive strategy for the structure of an MCO audit plan, including provisions related to the recovery of identified overpayments. As stated in the response to SAO Recommendation 1, the action plan will include the development of internal audit guidelines, plans for processing state-identified provider overpayments, changes to state rule or law, if needed, and the addition of MCO contract language to specifically support the audits.

- Develop Action Plan and Implementation Strategy. *By December 31, 2014.*