M E M O R A N D U M

TO: Joint Budget Committee

FROM: Caroline Smith, JBC Staff, 303-866-4963

SUBJECT: Recommended exemptions for H.B. 11-1307

DATE: June 20, 2011

Pursuant to Section 24-30-203.5 (4) (b), C.R.S., the State Controller is to submit a letter by March 1, 2011, to the State Auditor, Legislative Audit Committee, and Joint Budget Committee that details any of the State Controller's proposed exemptions from recovery audits. A copy of this letter is attached, as well as an update that the Controller provided on June 16, 2011.

The Legislative Audit Committee and the Joint Budget Committee may veto any exemptions proposed by the State Controller by a majority vote of the members of each committee, taken prior to June 30, 2011 (Section 24-30-203.5 (4) (b), C.R.S.).

The Joint Budget Committee may respond to State Controller's proposed exemptions in one of the following manners:

1) The Committee may, through a majority vote, veto any exemption from recovery audits.

2) If the Committee wishes to make clear that they agree with the exemptions proposed by the State Controller, they may vote to reflect their position that they concur with the suggested exemptions requested by the Controller.

3) The Committee may choose to not take action prior to June 30, 2011, in which case the State Controller's proposed exemptions from recovery audits will take effect.

State of Colorado

John W. Hickenlooper
Governor

Kathy Nesbitt
Executive Director

Jennifer Okes
Deputy Executive Director

David J. McDermott
State Controller

DPA

Department of Personnel & Administration

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June 16, 2011

Senator Mary Hodge, Chair Joint Budget Committee
200 East 14th Avenue
Denver, Colorado 80203

Dear Senator Hodge:

The following information was prepared as a handout to accompany the State Controller's presentation to the Committee in regards to the recommendation for partial exemption of the Department of Health Care Policy & Financing (DHCPF), required by HB 10-1176, as amended by HB 11-1307.

RECOVERY AUDITS BY THE STATE CONTROLLER

- The recovery audit process is governed by House Bills 10-1176 and 11-1307.

SPENDING AUTHORITY

- The Department of Personnel & Administration is unable to enter into a contract with a recovery audit vendor without an appropriation. For that reason, the Department has requested $1,600,000 in cash funds spending authority for FY 2011-12 from the Recovery Audit Cash Fund through the 1331 Emergency Supplemental process. The requested amount serves as a reasonable proxy for the amount of money that will be identified, collected, and reimbursed through the recovery audit process. Without an appropriation, by statute the Office of the State Controller (OSC) will not be able to enter into a contract with the recovery auditor, and no recovery audit will be performed until an appropriation is made.

EXEMPTION RECOMMENDATION

- The State Controller previously recommended the entire DHCPF agency be exempted from recovery audits based upon statutory requirements to make recommendations at the agency level. The Legislative Audit Committee expressed concerns that this would leave some expenditures uncovered by a recovery audit. Subsequently, the statutory requirements were changed to allow for exemption of a portion of a state agency.

- The OSC is recommending the portion of the DHCPF that is subject to recovery audits be exempted from State of Colorado recovery audits managed by the OSC. Upon a recent review by DHCPF, the portion of DHCPF spending that is not subject to recovery audits is currently estimated to be $1,014,575,315. This amount would be subject to recovery audits managed by the OSC under C.R.S. 24-30-203.5.

- CRS 25.5-4-301(2)(f) and (3)(a)(III) prohibit Medicaid expenditures in DHCPF from being subject to multiple audit processes. The recommendation avoids duplicative audit processes, which are prohibited by state law and are logistically unworkable, and it avoids a gap in coverage by any recovery audit process.

- Options for the Joint Budget Committee pursuant to CRS 24-30-203.5(4)(b):
    - Vote to Support the Recommendation: In this case, the OSC will proceed with the current recovery audit RFP process (assuming the LAC votes to approve or declines to vote). It is estimated that a contract will be executed and recovery audit work would begin by August 15, 2011.
    - Decline to Vote: In this case, the OSC's recommendation will stand and the OSC will proceed with the recovery audit contract (assuming the LAC also declines to vote or votes to approve). It is estimated that a contract will be executed and recovery audit work would begin by August 15, 2011.
    - Vote to Veto the Recommendation: In this case, the OSC would cancel the current recovery audit RFP process. A new recovery audit RFP would be issued including all expenditures from DHCPF. It is estimated that a contract will be executed and recovery audit work would begin by October 1, 2011. This option will likely result in duplication of recovery audit review, which is contrary to statute and risks potential loss of recoveries. Such a loss may occur when the OSC recovery auditor identifies a potential improper payment but does not have the DHCPF integrity program oversight. This case will also apply if the LAC votes to veto the State Controller's recommendation.

Sincerely yours,

David J. McDermott

David J. McDermott, CPA
Colorado State Controller

Joint Budget Committee Members
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Senator Pat Steadman
Senator Kent Lambert
Representative Jon Becker
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May 18, 2011

Sally Symanski, State Auditor,
Sen. Lois Tochtrop, Chair Legislative Audit Committee,
Sen. Mary Hodge, Chair Joint Budget Committee
200 East 14th Avenue
Denver, Colorado 80203

Dear Auditor Symanski, Senator Tochtrop, and Senator Hodge:

Pursuant to C.R.S. 24-30-203.5(4)(b), the Office of the State Controller (OSC) is providing our recommendation on State agency exemptions to recovery audits. Based on our review, we recommend that the portion of the Department of Health Care Policy and Financing (HCPF) that is subject to recovery audits be exempt from State of Colorado recovery audits managed by the OSC. The portion of HCPF that is not subject to recovery audits, approximately $328 million or about 8% of FY 2009-10 expenditures would be subject to recovery audits managed by the OCS under C.R.S. 24-30-203.5,

The State Controller previously recommended the entire HCPF agency be exempt from recovery audits (letters to Legislative Audit Committee and Joint Budget Committee dated February 24, 2011 and March 21, 2011). At that time, HB 11-1176 required the State Controller's recommendation to be made at the agency level. The bill did not allow for partial exemption of an agency. Since then, SB 11-1307 (relevant portion codified in CRS 24-30-203.5(4)(a)), was introduced and passed, and provided for an exemption of a portion of a State agency.

Before explaining our reasoning for recommending a partial exemption for HCPF, I thought it would be helpful to further explain the process used in recovery audits. Based on our conversations with staff at the State of Texas and the Commonwealth of Virginia, both have implemented recovery audit programs, with two general types of recovery audits performed: 1) Medicaid and 2) Non-Medicaid, which are also referred to as an accounts payable recovery audits. Medicaid recovery audits are required by federal statute. Section 6411 of the Affordable Care Act of 2010 required States and territories to establish Medicaid Recovery Audit Contractor (RAC) programs. Medicaid RACs are tasked with identifying and recovering Medicaid overpayments and identifying underpayments. RACs are paid on a contingency fee basis, receiving a percentage of the improper overpayments and underpayments they collect from providers. RACs are also required for Medicare under *The Tax Relief and Health Care Act of 2006.* The Centers for Medicare & Medicaid Services (CMS) manages these Medicare recovery audits of providers.

Federal statute does not require states to perform accounts payable audits. Texas has a state statute that requires recovery audits; Virginia does not. Recovery audits generally include three parts:

1. Data Mining – RACs apply data mining techniques using their proprietary software to identify potential improper payments. State agencies then need to review the potential improper payments to determine their validity. For identified improper payments that the State agencies determine to be improper, the RAC collects the improper payment from the vendors. The RAC is paid a on contingency fee basis, receiving a percentage of the collected improper payments.

2. Statement Analysis – RACs requests statements from the state's large vendors. If the statements show credits, the RAC identifies these credits with other improper payments, and collects these credits from the vendors. The RAC is paid a contingency fee for the collection of these credits.

3. Purchasing/Contract Review – Based on the findings in the data mining process, the RAC will identify areas for further investigation because of the high rate of improper payments. These areas could be for certain agencies or certain types of contracts. For Texas and Virginia, the RACs focused on information technology and transportation contracts. The RAC reviews the contracts and the billings to determine whether there are improper payments. This is the most labor-intensive part of the recovery audit, and is similar to a program audit, although the recovery audit is solely focused on improper payments and not any other compliance issues. The RAC is paid a contingency fee on the collected improper payments identified in the purchasing/contract review.

Texas and Virginia collected much lower amounts than anticipated for accounts payable recovery audits. Virginia collected $1.1 million on a base of $46.1 billion, or 0.00239%. Virginia has not conducted a recovery audit since 2007 and does not plan to conduct further recovery audits due to this low return. Texas recovered $1.08 million on a base of $57.6 billion, or 0.00188%. The primary sources of the recoveries in Texas included 40% from improperly paid hotel tax related to employee travel (higher education was included in the Texas recovery audit, which accounts for the majority of state travel), 34% due to duplicate payments, and 13% for credits collected due to statement reviews. The employees who are responsible for recovery audits in the Comptroller of Public Accounts Texas indicated their office planned to request statutory changes to make recovery audits permissive at the discretion of the comptroller, rather than required by statute.

For the State of Colorado, HCPF is the only State agency that conducts recovery audits, and it conducts recovery audits for Medicaid expenditures, as required by federal statute. Recovery audits covered approximately 92% of HCPF expenditures in FY 2006-10. The remaining 8% of expenditures or about $328 million are not subject to recover audits, and include administrative costs for HCPF and the Colorado Department of Human Services and certain department grant programs, such as the Indigent Care Program.

Because these payments are not included in recovery audits, it is possible that a RAC could identify improper payments using data mining or other techniques that are not identified in other audits. Therefore, the OSC recommends that the portion of HCPF expenditures not covered by HCPF recovery audits be subject to recovery audits managed by the OSC.

The OSC does not recommend that all of HCPF be subject to recovery audits managed by the OSC. HCPF has released an RFP to fulfill the requirement for Medicaid recovery audits and a new RAC contract is scheduled to be in place early next fiscal year. As a result, we would duplicate efforts if we included HCPF in the recovery audit process managed by the OSC. Such duplication would be problematic if both RACs identified the same improper payment and both attempted to collect that amount from the State agencies vendor.

No other State agency is subject to recovery audits, and so the OSC recommends that all other State agencies be subject to recovery audits managed by the OSC. The only exemption to recovery audits managed by the OSC would be for the portion of HCPF representing Medicaid expenditures that is already subject to recovery audits.

Sincerely yours,

David J. McDermott

David J. McDermott, CPA
Colorado State Controller

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