



STATE OF NORTH CAROLINA

AUDIT RESULTS FROM

CAFR AND SINGLE AUDIT PROCEDURES

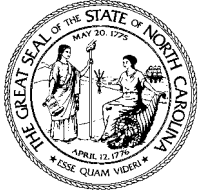
**NORTH CAROLINA TEACHERS' AND STATE EMPLOYEES'
COMPREHENSIVE MAJOR MEDICAL PLAN**

FOR THE YEAR ENDED JUNE 30, 2003

OFFICE OF THE STATE AUDITOR

RALPH CAMPBELL, JR.

STATE AUDITOR



Ralph Campbell, Jr.
State Auditor

STATE OF NORTH CAROLINA
Office of the State Auditor

2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699-0601
Telephone: (919) 807-7500
Fax: (919) 807-7647
Internet <http://www.osa.state.nc.us>

April 27, 2004

The Honorable Michael F. Easley, Governor
Members of the North Carolina General Assembly
Dr. Jack Walker, Executive Administrator,
North Carolina Teachers' and State Employees' Comprehensive Major Medical Plan

We have completed certain audit procedures at the North Carolina Teachers' and State Employees' Comprehensive Major Medical Plan related to the State's *Comprehensive Annual Financial Report (CAFR)* and the State's *Single Audit Report* for the year ended June 30, 2003. Our audit was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

The results of these procedures, as described below, yielded audit findings and recommendations for the Plan related to the State's financial statements or federal financial assistance programs that required disclosure in the aforementioned reports. These findings are included in the findings and recommendations section contained herein. Our recommendation for improvement and management's response follow each finding.

The accounts and operations of the Plan are an integral part of the State's reporting entity represented in the *CAFR* and the *Single Audit Report*. In the *CAFR*, the State Auditor expresses an opinion on the State's financial statements. In the *Single Audit Report*, the State Auditor also presents the results of tests on the State's internal control and on the State's compliance with laws, regulations, contracts, and grants applicable to the State's financial statements and to its federal financial assistance programs. Our audit procedures were conducted in accordance with auditing standards generally accepted in the United States of America, *Government Auditing Standards* issued by the Comptroller General of the United States, and Office of Management and Budget Circular A-133 as applicable. Our audit scope at the North Carolina Teachers' and State Employees' Comprehensive Major Medical Plan included the following:

Audit Scope for the *Comprehensive Annual Financial Report*

Other Employee Benefit Trust Fund: State Health Plan

Audit Scope for the *Single Audit Report*

State Children's Insurance Program

Our audit procedures at the North Carolina Teachers' and State Employees' Comprehensive Major Medical Plan were less in scope than would be necessary to report on the financial statements that relate solely to the Plan or the administration of federal programs by the Plan. Therefore, we do not express such conclusions.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

A handwritten signature in black ink that reads "Ralph Campbell, Jr." in a cursive script.

Ralph Campbell, Jr.
State Auditor

AUDIT FINDINGS AND RECOMMENDATIONS

Matters Related to Financial Reporting or Federal Compliance Objectives

Finding numbered 1 was identified during the current and prior audit and discusses conditions that represent significant deficiencies in internal control and/or noncompliance with laws, regulations, contracts, or grants. Finding numbered 2 summarizes follow-up actions taken by the Plan on prior year audit findings.

1. INADEQUATE CONTROLS OVER THE PROCESSING OF FINANCIAL TRANSACTIONS

The Plan's accounting procedures and internal control system are inadequate to effectively process the Plan's financial activity. The Plan processes in excess of \$1.3 billion in transactions annually. The failure to establish and implement an effective internal control system and follow reliable accounting practices increases the risk of loss of critical accounting data and the risk of misappropriation of funds. The results of our tests uncovered many errors and omissions as follows:

- The Plan failed to reconcile material accounts to the year-end financial statement balances and reconcile general ledger balances to the monthly summary spreadsheets provided by the Plan's Claims Processing Contractor. The Plan was unable to explain significant variances in the balances for eight year-end financial statement accounts.
- The Plan's financial statements contained two reporting errors and the Health Choice financial statements contained a material reporting error caused by the failure to reverse a prior year audit adjustment.
- Many expenditure vouchers tested were not adequately supported, reviewed or approved by an authorized official, or cancelled or defaced to prevent duplicate payment.
- Many of the deposit journal vouchers tested were not reviewed or approved by an authorized official, were not adequately supported and missing basic information such as date reported in the general ledger, debit and credit totals and proper transaction descriptions.
- Sixteen of the 28 deposit journal vouchers tested were not recorded in the general ledger in a timely manner, some as late as 20 days.

Recommendation: Management should review and revise its internal control policies and procedures for the processing of financial transactions. Accounts should be reconciled to year-end financial statement balances and supporting subsidiary worksheets. Invoices

AUDIT FINDINGS AND RECOMMENDATIONS (CONTINUED)

should be paid in a timely manner, properly supported, and reviewed and approved by authorized officials. Documentation should be cancelled or defaced to prevent duplicate payment. The Plan should ensure that deposit voucher transactions are promptly recorded in the general ledger, properly supported, and reviewed and approved by authorized officials.

Agency's Response: The Plan is currently working to revise the Policy and Procedures Manual for the Accounting Section of this office. In the manual we have addressed the findings of the State Auditor's Office.

The Plan will reconcile all material accounts to the year-end financial statement balances and reconcile general ledger balances to the monthly summary spreadsheets provided by BCBS. This will be available to the State Auditor's office when they are working on the audit of the Plan.

The reporting errors are due to the fact that the entries were entered into the system the prior year so that they would automatically reverse themselves. Evidently the system did not reverse them as it should have. It is the Plan's belief after speaking with the Controller's Office that DHHS should have made any entries for the CHIP Program.

It is now the policy of the Plan to provide copies of all contracts with any invoice paid. There is a procedure in place whereby each invoice is reviewed and approved by an authorized official. It is also our policy to ensure that all invoices are stamped paid so as to prevent duplicate payment. There is also another mechanism in place to ensure that no invoice is paid twice. The NCAS system will let us know if an invoice number has already been paid. If the Plan receives this message when entering an invoice it is our policy to investigate when it was paid and the amount. The vendor will then be notified that they invoiced us previously and that we will not pay this second invoice.

Currently all Journal Vouchers are reviewed prior to the Accounting Technician entering them into the system. The form is currently being filled out completely. In the past it was left blank on prior entry forms since these were two sided entries which must equal and the total was the same for both debit and credit. Descriptions are now being entered into NCAS with all Journal Entries.

It was the practice of the Plan to enter the Journal Entries after all reports were received from BCBS. The entries were made towards the end of the month since reports were not available on line until the last week of the month. This allowed the Plan to reconcile what was entered into the Cash Management System with what BCBS reported on their Daily Cash Report. Since there were only two to three entries a day it was felt that it was more cost effective to only enter Journal Entries on a weekly or monthly basis. Our policy has changed to meet the requirements of the State Auditor to enter the Journal Entries within two to three days after entering them into the Cash Management System.

AUDIT FINDINGS AND RECOMMENDATIONS (CONTINUED)

In summary, with the revision of the Policy and Procedure Manual we have incorporated the recommendation of the State Auditor's Office.

2. FOLLOW-UP ACTIONS TAKEN BY THE PLAN ON PRIOR YEAR AUDIT FINDINGS HAVE CORRECTED MANY DEFICIENCIES

The Plan took corrective action on nearly all prior year audit findings. With the exception of prior year findings numbered 3 and 5, the Plan corrected or substantially corrected the findings presented in last year's audit report. The conditions presented in finding 5 from last year's report were not corrected as explained in finding 1 above. Summarized below are the conditions and subsequent action taken by the Plan for each finding as first noted in the prior year audit report.

- A. The Plan did not include some options in its healthcare plan research. The Plan did not have an active program in place to evaluate whether established healthcare plan options, as well as less traditional ones, could be beneficial to the Plan and/or its members.

The Plan explored lower cost options and certain healthcare insurers made presentation proposals to the Plan.

- B. The Plan did not have effective contract monitoring procedures in place. The Plan did not adequately monitor nor administratively organized itself to monitor its contractors effectively.

Although still refining its monitoring program for the various contracts, the Plan has documented and established strict monitoring procedures. The Plan has added four new employees, allowing the Plan's contract monitors to more actively focus on monitoring and, in one case, to uncover contract violations resulting in refunds to the Plan.

- C. Fees were not adjusted for reduced services. The Plan did not seek nor receive a reduction in the fee structure paid the Claims Processing Contractor when the Plan removed the drug claims processing function from the Claims Processing Contractor and contracted it to a pharmacy benefit manager.

The Plan did not agree with the auditor's conclusions and did not take the recommended action. The Plan does not intend to pursue this matter further.

- D. The promotion of mail order prescriptions was limited. The Plan did not realize certain available savings because it had not actively promoted and achieved the increased use of its mail order prescription service.

AUDIT FINDINGS AND RECOMMENDATIONS (CONCLUDED)

Management has stated that use of mail order prescriptions has picked up since the audit was released and certain promotion efforts were employed. The Plan included information pamphlets in two mailings; however, membership response was insignificant.

- E. The Plan lacks clearly written, specific policies and procedures.

The Plan is in process of upgrading its policies and procedures and internal control procedures using both internal resources and contract help.

- F. The administrator's performance in managing the health plan is not formally evaluated and does not require concurrence from any person or group.

The Plan has stated that the Committee on Employee Hospital and Medical Benefits was in charge of evaluating the administrator's performance.

- G. The Plan does not have a formal written long-range plan.

The Plan presented a draft copy of its long-range plan in June 2003. The centerpiece of the plan revolves around forming a combined healthcare related entity by the year 2007. The Plan is also moving forward in the areas of disease management, wellness programs and evaluation of the utilization management programs. The Plan has added a staff member dedicated to working on these endeavors full time.

- H. The Plan is not in compliance with State personnel regulations on employee evaluations and criteria related to the selection of new employees.

The Plan hired an employee who now oversees the State Personnel compliance requirements in the areas of hiring, evaluations, employee management, and compliance with all provisions of the State Personnel Act. Employee evaluations are complete and up to date. Managers have been made aware of their duties as outlined in the State Personnel Act. We noted during our audit that files were not maintained on the selection of employment applicants. The written policies outlining the criteria for determining applicant ratings had not been completed. Interview questions and evaluations are shredded upon completion of the selection process. This finding has been partially implemented.

- I. The Plan did not obtain a certification regarding debarment and suspension from its contractors receiving awards greater than \$100,000.

The required missing debarment certification has been obtained.

DISTRIBUTION OF AUDIT RESULTS

In accordance with General Statutes 147-64.5 and 147-64.6(c)(14), copies of this report have been distributed to the public officials listed below. Additional copies are provided to other legislators, state officials, the press, and the general public upon request.

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| The Honorable Richard H. Moore | State Treasurer |
| The Honorable Roy A. Cooper, III | Attorney General |
| Mr. David T. McCoy | State Budget Officer |
| Mr. Robert L. Powell | State Controller |
| Dr. Jack Walker | Executive Administrator, North Carolina Teachers' and State Employees' Comprehensive Major Medical Plan |

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| Mr. James D. Johnson | Director, Fiscal Research Division |
|----------------------|------------------------------------|

May 11, 2004

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Office of the State Auditor
State of North Carolina
2 South Salisbury Street
20601 Mail Service Center
Raleigh, North Carolina 27699-0601

Internet: <http://www.ncauditor.net>

Telephone: 919/807-7500

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