



STATE OF NORTH CAROLINA

RESULTS OF STATEWIDE FINANCIAL AUDIT PROCEDURES AT THE NORTH CAROLINA TEACHERS' AND STATE EMPLOYEES' COMPREHENSIVE MAJOR MEDICAL PLAN

FOR THE YEAR ENDED JUNE 30, 2006

OFFICE OF THE STATE AUDITOR

LESLIE W. MERRITT, JR., CPA, CFP

STATE AUDITOR



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March 21, 2007

The Honorable Michael F. Easley, Governor
Members of the North Carolina General Assembly
Mr. George C. Stokes, 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 of North Carolina reporting entity as presented in the *Comprehensive Annual Financial Report (CAFR)* and *Single Audit Report* for the year ended June 30, 2006. Our audit was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

In the *CAFR*, the State Auditor expresses an opinion on the State's financial statements. In the *Single Audit Report*, the State Auditor presents the results of tests of internal control and 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 the Single Audit Act as applicable. Our audit scope at the North Carolina Teachers' and State Employees' Comprehensive Major Medical Plan included the following:

State of North Carolina's Financial Statements

Pension and Other Employee Benefit Trust Fund: State Health Plan

State of North Carolina's Administration of Federal Financial Assistance Programs

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 its administration of federal programs. Therefore, we do not express such conclusions.

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

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.

Leslie W. Merritt, Jr.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

AUDIT FINDINGS AND RECOMMENDATIONS

Matters Related to Financial Reporting or Federal Compliance Objectives

The following findings and recommendations were identified during the current audit and discuss conditions that represent deficiencies in internal control and/or noncompliance with laws, regulations, contracts, or grant agreements. The first finding was identified by the Plan's independent auditor, Thomas and Gibbs, CPA, PLLC, and has been adapted for inclusion in the State's *Single Audit Report*. Similar findings were also reported in the prior year.

1. CLAIM PAYMENTS MADE IN ERROR

During the 2006 State fiscal year, five HealthChoice medical claims were processed incorrectly by the Claims Processing Contractor (CPC). One claim that should have been denied resulted in a duplicate overpayment of \$126, while the other four erroneous claims resulted in underpayments totaling \$1,645. The CPC's five errors resulted in a claim payment error rate of .05% for the 2006 contract year for HealthChoice claims. The projected underpayment of HealthChoice medical claims was \$85,507. This amount is considered to be immaterial to the Plan's Statement of Medical Claims Paid for the year ended June 30, 2006.

The \$126 HealthChoice claim that resulted in a duplicate overpayment projects to a questioned costs amount that would likely exceed \$10,000; therefore, the actual known error amount of \$126 is identified as questioned costs. The projected underpayment of \$85,507 is deemed to be immaterial noncompliance with the allowable costs/cost principles compliance type for 2006.

All medical claims should be processed accurately in accordance with the *North Carolina General Statutes*. Office of Management and Budget (OMB) Circular A-87 requires allowable costs to be adequately documented and program costs to be necessary and reasonable for proper and efficient administration of the grant program. In accordance with section 501(a)(3) of OMB Circular A-133, the auditor shall report in an audit finding known questioned costs that are greater than \$10,000 for the allowable costs/cost principles compliance type. The auditor must also report known questioned costs, regardless of amount, when likely questioned costs are greater than \$10,000 for the allowable costs/cost principles compliance type.

Recommendation: Plan management should continue its efforts to ensure that the CPC accurately processes all medical claims.

Plan Response: The Plan's CPC has identified the cause for the claim payments made in error and has implemented corrective actions with its claim processors.

AUDIT FINDINGS AND RECOMMENDATIONS (CONCLUDED)

2. CONTRACT MONITORING

In the prior year, we identified deficiencies associated with contract management and monitoring procedures at the Plan. Deficiencies included no formal written contract to support actuarial services, undocumented approvals of amendments to the contract with the Claims Processing Contractor (CPC), and inadequate documentation to support contract monitoring.

This finding is partially resolved. The results of our testwork did not disclose deficiencies related to contract management practices, which included the execution of contracts and filing of contract amendments. However, we continued to note that contract monitoring policies and procedures were not fully developed and implemented. As a result, documentation to support comprehensive monitoring procedures of the CPC contract was not available.

The Plan is responsible for ensuring compliance with contract requirements and specifications. Contract monitoring is an essential element of contract administration, involving technical, business, and administrative oversight by the Plan. Failure to adequately monitor the activities under contract could lead to an increased risk that the funds are not being spent for their intended purpose.

Recommendation: Plan management should continue to develop and implement policies and procedures that support monitoring efforts for all contracts.

Plan Response: Currently, the Plan meets monthly with the CPC to discuss and review operational issues affecting claim processing and customer service. We have implemented quarterly meetings and financial reporting requirements for our major contractual vendors (i.e. BCBS, Medco). We are also evaluating a contract management system to enhance our contract monitoring process. In addition to establishing standard contract processing procedures and contract approval levels, we have identified business owners for outstanding contracts and plan to include them in the monitoring process.

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