

STATE OF NORTH CAROLINA

**DEPARTMENT OF PUBLIC SAFETY
DIVISION OF ADULT CORRECTION
FINANCIAL RELATED AUDIT**

MAY 2012

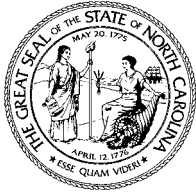
OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

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AUDITOR'S TRANSMITTAL

May 24, 2012

The Honorable Beverly Eaves Perdue, Governor
Members of the North Carolina General Assembly
Reuben F. Young, Secretary, Department of Public Safety

This report presents the results of our financial related audit at the Department of Public Safety, Division of Adult Correction (Division). Our work was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes* and was conducted in accordance with the performance audit standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

The objectives of our audit were to (1) determine if the Division took appropriate corrective action to adequately address recommendations made to management in the *Inmate Medicaid Eligibility* performance audit issued in August 2010, and (2) identify other areas of potential medical cost containment.

The results of our audit determined that the Division took appropriate corrective action to address the recommendations made in the August 2010 audit report. Our audit also identified other opportunities to contain medical costs. These items are described in the Audit Findings and Responses section of this report.

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 cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor

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FINANCIAL RELATED AUDIT

BACKGROUND

As authorized by Article 5A of Chapter 147 of the *North Carolina General Statutes*, we have conducted a financial related audit at the Department of Public Safety, Division of Adult Correction.

This audit is a follow-up to the *Inmate Medicaid Eligibility* performance audit issued in August 2010. In that audit, auditors recommended that the Division of Adult Correction develop procedures in order to charge Medicaid for eligible inmate inpatient health care costs in order to save an estimated \$11.5 million a year.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of this financial related audit included (1) determining if the Division of Adult Correction took appropriate corrective action to adequately address recommendations made to management in the *Inmate Medicaid Eligibility* performance audit issued in August 2010, and (2) identifying other areas of potential medical cost containment.

Management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that relevant objectives are achieved. Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate. Our audit does not provide a basis for rendering an opinion on internal control, and consequently, we have not issued such an opinion.

Our audit scope included a review of procedures and results for the period February 1, 2011, to January 31, 2012.

To accomplish our audit objectives, we gained an understanding of internal control over matters described below and evaluated the design of the internal control. We then performed further audit procedures consisting of tests of control effectiveness and/or substantive procedures that provide evidence about our audit objectives. Specifically, we performed procedures such as interviewing personnel, observing operations, reviewing policies, analyzing accounting records, and examining documentation supporting recorded transactions and balances. Whenever sampling was used, we applied a nonstatistical approach but chose sample sizes comparable to those that would have been determined statistically. As a result, we were able to project our results to the population but not quantify the sampling risk.

As a basis for evaluating internal control, we applied the internal control guidance contained in professional auditing standards. As discussed in the standards, internal control consists of five interrelated components, which are (1) control environment, (2) risk assessment, (3) control activities, (4) information and communication, and (5) monitoring.

FINANCIAL RELATED AUDIT

We conducted this audit in accordance with generally accepted government auditing standards applicable to performance audits. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

RESULTS

We determined that the Division of Adult Correction took appropriate corrective action to address the recommendations made in the August 2010 audit report. Our audit also identified other opportunities to contain medical costs. These items are described in the Audit Findings and Responses section of this report.

AUDIT FINDINGS AND RESPONSES

1. NEW PROCEDURES WILL SAVE STATE MILLIONS

In response to a previous audit by the State Auditor¹ and legislation enacted pursuant to that audit,² new Division of Adult Correction (Division) procedures have saved the State approximately \$10 million, according to Division estimates. The savings came from shifting certain inmate medical costs to the State's Medicaid Program.

The Division now identifies inmates in need of inpatient medical care that were or are likely Medicaid eligible and submits Medicaid applications to the county Department of Social Services on their behalf. Hospital and doctor bills for Medicaid eligible inmates are sent to the State's Medicaid Program for payment.

Because bills are paid (1) at the lower Medicaid reimbursement rate and (2) the State is only responsible for approximately one third of the Medicaid cost, there is a significant cost savings for the State.

\$10 Million in Estimated Annual Savings Expected

Based on management reports, the Division estimates \$10 million in savings to the State for the period from February 1, 2011 through January 31, 2012.

The savings amount is estimated because many applicable bills are sent directly to the State's Medicaid program for payment; therefore, the Division can not compute the actual cost savings related to the new procedures. However, auditors reviewed the Division's way of estimating the savings and determined that the method was reasonable.

While the savings are less than the \$11.5 million estimated in our previous audit report, the savings are reasonable in light of other legislation enacted to contain inmate medical costs.³

Procedures Established

As recommended by the State Auditor and required by legislation, the Division developed procedures to charge the State's Medicaid program for the cost of inpatient care Medicaid eligible inmates.

The Division established procedures to identify potential Medicaid eligible inmates. The Division worked with the Department of Health and Human Services' Division of Medical Assistance to identify previously Medicaid eligible inmates currently in the prison system. The Division also implemented procedures to compare inmate medical history records to Medicaid eligibility criteria. This is done to identify inmates that are likely Medicaid eligible before the inmate is sent to a local hospital for advanced medical care.

¹ *Inmate Medicaid Eligibility*, August 2010

² *Session Law 2010-31 section 19.6 (c)*.

³ *Session Law 2011-145 section 18.10 (a) & (b)* limits reimbursement to medical providers for inmate medical services to the lesser of 70% of the amount charged or two times the Medicaid rate for any service and encourages DOC to contain inmate medical costs by using DOC medical facilities to the extent possible.

AUDIT FINDINGS AND RESPONSES

Inpatient medical care for Medicaid eligible inmates is now billed to Medicaid.

The Division submits a Medicaid application to the local Department of Social Services for inmates determined to likely be Medicaid eligible when those inmates are admitted to a local hospital.

Hospitals and doctors bill the State's Medicaid program for eligible inmates. The State's Medicaid program bills the Division for the State's portion of inmate care.

Recommendation:

The Division is commended for effectively addressing the recommendation made in our audit and the intent of legislation to use the Medicaid program to reduce the cost of inmate medical care.

Agency Response:

It is the intent of the Department of Public Safety, Division of Adult Correction to continue to manage and operate the Medicaid Program for Offenders in a manner complying with the intent of the legislation and in the spirit of the State Auditor's reports.

2. INMATES WITH ACTIVE MEDICAID CARDS DETECTED

While developing its new procedures in 2010, the Division and the Department of Health and Human Services' Division of Medical Assistance (DMA) unexpectedly identified 947 inmates with active Medicaid cards. These cards could have been used by persons outside the prison to obtain fraudulent Medicaid services. To the State's loss, DMA did not review their records to determine if the 947 cards were fraudulently used and did not keep a record of the cards in question for any later investigation or audit.

Identification of Cards

The Division worked with DMA to match the prison population against the Medicaid recipient database in an effort to identify former (terminated and suspended) Medicaid eligible inmates.

While this match identified over 11,000 inmates as once being Medicaid eligible, surprisingly, the match also identified 947 inmates with current and active Medicaid cards.

Medicaid eligibility for incarcerated inmates should have been suspended when the inmate was first detained. Through self reporting, the county Department of Social Services (DSS) offices were supposed to receive reports from DMA that identify living arrangement changes for incarcerated individuals. The county DSS was then supposed to suspend Medicaid eligibility for the inmate.

AUDIT FINDINGS AND RESPONSES

Potential Fraud Not Pursued

The potential for fraud involves 947 active Medicaid cards, which do not have a participant photo on them, circulated in public and used by others to obtain fraudulent medical services. DMA did not review its records to determine if the 947 cards were fraudulently used after the date of the cardholder's incarceration and did not keep a record of the cards in question for any later investigation or audit.

Procedures Changed to Reduce Risk

Beginning September 1, 2010, the Division and DMA changed their procedures to automatically update the living arrangements designation for all newly admitted inmates on a daily basis, thus reducing the risk of inmates with active Medicaid cards. The living arrangement designation controls the active or inactive status of a prisoner's eligibility for Medicaid.

Recommendation:

The Division should continue to work with DMA to refine processes and procedures that ensure accurate Medicaid living arrangement status for all North Carolina inmates.

The Division should work with the DMA to identify and recover any fraudulent payments resulting from misuse of prisoner Medicaid eligibility.

Agency Response:

It is the intent of the Department of Public Safety, Division of Adult Correction and the Department of Health and Human Services, Division of Medical Assistance to maintain the automated matching system initiated to identify inmates who are receiving Medicaid or who have received Medicaid in the past. These matches serve to notify DMA of inmate Medicaid eligible situations which require assessment and evaluation for potential fraud or abuse and will notify DAC of inmate Medicaid history for potential Medicaid eligibility in the present and future.

NCDPS/DAC and NCDHHS/DMA will continue to collaborate in efforts to identify and recoup fraudulent payments resulting from misuse of inmate Medicaid eligibility.

It is the intent of the Department of Public Safety, Division of Adult Correction to continue quarterly Medicaid Program meetings, as well as open, direct lines of communication interdepartmentally to discuss, assess, and resolve these and other issues as they arise in the Medicaid Program for Offenders.

3. RECOVERY AUDIT EFFORT NEEDS IMPROVEMENT

The cost of non-Medicaid eligible inmate medical care could be reduced further if the Division of Adult Correction (Division) strengthened its recovery audit efforts. While the Division's recovery audit efforts are successful, they are limited in their scope. Based on the Division's recovery scope, the Division could be failing to recover approximately \$1.56 million of overpayments a year.

AUDIT FINDINGS AND RESPONSES

Current Recovery Efforts are Limited

Recovery auditing is a cost containment practice used to identify and recover improper payments made to errors such as:

- Administrative non-compliance (non-covered items, duplicate payments, ineligible recipients, etc.);
- Intentional (fraudulent) and unintentional billing errors; and
- Inappropriate or unnecessary services.

The Division reports gross recoveries of approximately \$195,256 during the six months ending December 2011 (the only time span in which data was available). Annualized, this represents approximately \$390,000 a year.

According to the Division, the most common errors identified in its current sampling efforts are keying errors and selection of the wrong payment amount by Division medical claim staff (e.g. not paying the lesser of 70% of billed charges or two times the Medicaid rate).

However, there is only one full-time recovery auditor charged with reviewing pre-payment or post-payment claims processed by the medical claims processors for accuracy. Due to the limited staff, only a 20% random sample of medical claims is performed each day, meaning that 80% of all medical claims go unchecked.

If accuracy reviews were performed on the entire population, current recoveries rates suggest that approximately \$1.56 million in recoveries could be realized.¹

Focused Recovery Audits are Not Performed

The Division does not perform focused recovery audits that look for specific items or characteristics across all claims.

The Division could expand its recovery audit efforts by performing focused audits. Focused audits would involve the Division's auditor scanning the entire claims population to identify claims with characteristics similar to the characteristics of claims already identified as overpayments and identify the root causes of the errors. This effort could also include looking for billing errors made by the medical providers.

The Division could contract with a professional recovery audit firm to provide focused recovery audits. With a professional firm, the Division would get:

- Expertise in medial claim recovery audits
- Review of entire fiscal year (no samples used)
- More detailed level of review per transaction
- Complete and thorough audit

¹ By randomly reviewing 20% (1/5) of the claims, the Division is on pace to recover \$390,000 a year. Assuming similar results, the Division would recover \$1.56 by looking at the other 80% (4/5) of claims ($\$390,000 \times 4 = \1.56 million).

AUDIT FINDINGS AND RESPONSES

In addition, it is industry standard that recovery audit firms are “paid-for-performance”. The firms are paid from a percentage of the recoveries that are identified which leads the auditors to be motivated to conduct thorough and precise audits.

Recommendation:

The Division should expand its recovery audit efforts.

The Division should consider using software or other automated methods to perform focused audits to identify additional overpaid claims, collect the additional amounts, and identify root causes of errors.

The Division should consider contracting with a professional recovery audit firm on a contingency fee basis to enhance its recovery audit effort.

Agency Response:

The Department will review its procedures and consider its options in relation to the recommendations by the auditor.

ORDERING INFORMATION

Audit reports issued by the Office of the State Auditor can be obtained from the web site at www.ncauditor.net. Also, parties may register on the web site to receive automatic email notification whenever reports of interest are issued. Otherwise, copies of audit reports may be obtained by contacting the:

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