Sent: July 19, 2006
To: Ms. Jill M. Peterson, Assistant Secretary
From: Jeff Barber
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Re: File S7-11-06

A common gap in internal controls is causing approximately 1,600 corporations to pay excessive healthcare charges. This accounting deficiency applies to publicly traded firms that operate self-funded health plans for their employees. As executives look for a "top-down, risk-based approach," they can generate significant results by focusing on internal controls used in the payment of healthcare expenses.

I addressed the healthcare accounting issue in written comments to the SEC, prior to the Roundtable of May 10, 2006. My comments (as well as other submissions that pertained to internal control gaps in healthcare) were posted on the SEC Website. The issue was not mentioned, however, by any of the 20+ panelists who participated in the Roundtable.

Studies (by Equifax and others) have determined that over 90% of hospital bills contain errors—most of which are overcharges.

According to the Centers for Medicare and Medicaid Services, the average Medicare hospital bill contains overcharges amounting to 9.3%. The overcharge rate is higher in some states; e.g., 23.1% per bill in Florida and 20.5% per bill in California.

I represent a hospital bill auditing practice. We have found the percentage of overcharges to be higher in bills submitted to corporate health plans than in those submitted to the Medicare program.

Since the May 10 Roundtable, the U.S. Attorney's office has settled two cases involving allegations of healthcare providers overcharging the Federal Government. The settlements have amounted to $900 million and $265 million.

In spite of the fact that hospital bills have a notoriously high error rate, healthcare invoices are being paid, without review, by corporations with self-funded health plans. CFOs and CEOs are routinely certifying the adequacy of internal controls in SEC filings, even though no one is verifying the accuracy of a single hospital bill.

Self-insured firms establish a trust for the direct payment of employee healthcare expenses. Most self-insured health plans hire a Third Party Administrator (TPA) to verify eligibility and pay claims. In essence, the TPA runs a healthcare Accounts Payable Department, with little or no oversight by the corporation's internal auditors or outside CPA.

There is a common misconception that TPAs verify the accuracy and validity of employee healthcare bills, prior to paying claims. In actuality, most TPAs are not contractually obligated to confirm the accuracy of specific line-item charges.

Most TPAs pay employees' hospital expenses from "UB-92s," billing summaries that list charges by department only (e.g., "Pharmacy: $8,400.50"). Given that such bills do not provide an itemized breakdown of charges, it is impossible to verify the accuracy of the billing.

Another accounting gap is that many corporate officers are kept in the dark in matters of healthcare pricing. In fact, most TPAs and networks refuse to disclose the hospitals' prices, because they deem such information "confidential."

If a corporation received an invoice that included a $12,000 charge described only as "Office Supplies," the Accounts Payable Department would probably request additional information, before issuing payment. If the company's TPA received a non-itemized invoice for $12,000 worth of "Operating Room Services," the TPA would probably issue payment, without question.

Such practices represent a duality of standards, inconsistent with the intent of SOX 404. Clearly, one cannot evaluate a firm's internal control deficiencies, if one does not know what the firm has agreed to pay for healthcare. Internal audit staff cannot confirm the accuracy of a single invoice if they don't know what the prices *should* be.

In many corporations, the task of verifying the accuracy of healthcare invoices is delegated to Human Resources or Employee Benefits personnel. Many HR executives feel comfortable in knowing that they have secured a 20% discount. If the base pricing is not disclosed, however, the "discount" is meaningless.

As an example, a hospital charged $53.60 per pill for a medication that retailed for 45 cents per pill. The hospital charged a corporate health plan a "discounted" rate of $42.88 per pill, or 95 times more than the retail price.

Inflated prices create significant risk exposure for corporate executives. If a corporation overpays for healthcare, the employees are forced to pay co-payment expenses that they do not owe.

Under the current system, corporations and their employees routinely pay for:

a) Healthcare that was not provided (e.g., canceled medical tests and procedures);
b) Healthcare provided to an individual who was not associated with the corporation;
c) Healthcare provided to a plan member, but charged at an inflated rate.

Executives of corporations with self-funded health plans need clear guidance as to how they can confirm the accuracy of hospital billing, without violating patient confidentiality.

If financial controls were tightened and healthcare fraud eliminated, corporations and their employees would reduce expenses dramatically. SOX compliance would be a means to increase profitability and shareholder value, rather than an administrative nightmare with negligible rewards.

Concept Release:

1. Regarding evaluation of the effectiveness of a company's internal control over financial reporting; I suggest that the Commission provide guidance to management of the following subset: The 1,600 publicly traded corporations that operate self-funded employee benefit or Workers' Compensation health plans. Corporations with self-funded plans bear the risk of failing to identify healthcare fraud.

   Guidance would not be required for corporations that purchased HMO or indemnity insurance for their employees. By purchasing insurance, such corporations transfer the risk.

3. I believe guidance should be specific and detailed. In many cases, insurance "consultants" and brokers have a vested interest in preventing the identification of fraud. I see cases in which the insurance broker is also the SOX advisor for healthcare accounting.

   One common deficiency is that most corporations with self-funded health plans do not know what they have agreed to pay for healthcare. They may know the discount rate (e.g., 20%) that has been negotiated with the hospital, but they do not have a specific price list or an established "benchmark" (e.g., the "Usual Customary and Routine" rate).

4. I suggest adding the topic of "Healthcare Accounting." Of the various items that appear on an income statement, Healthcare Accounting represents the greatest risk exposure.

5. Commission rules should be established to clarify standards for internal controls. For example, the Commission might require internal auditors to reconcile claims runs quarterly, to assure that all claims were paid on behalf of employees, dependents, spouses, or retirees of the corporation.

7. The drawback of providing additional guidance is that the interests of the healthcare lobby will conflict with Sarbanes-Oxley's stated mission to provide investors with accurate and correct financial reports. Many healthcare providers benefit from the submission of confusing and/or misleading billing. Shareholders will benefit (in terms of increased earnings per share and shareholder value) if specific guidance is provided and implemented.

Risk Control and Identification

12. The existing guidance is inadequate as it pertains to healthcare benefit accounting. The risk of material misstatement is extremely high in healthcare benefit accounting. Overcharges often amount to more than $500 per employee per year, an amount that would be deemed "material" for hundreds of publicly traded firms. Additional guidance regarding healthcare benefit costs and eligibility would help executives identify fraud.

16. Guidance should be given about the risk exposure related to the "Healthcare" expense line item. Many senior level executives fail to realize that at least 90% of their employees' hospital bills contain errors (most of which are overcharges). Additionally, most do not realize that hospital invoices are paid from billing summaries, which provide no itemization of individual charges.

17. The Commission should provide guidance about fraud controls. In addition to monitoring hospital bills for overcharges, health plans should monitor billing for pharmacy items, doctors' visits, rehabilitation services, and other health-related items and services. In a rehab invoice, for example, I found that a firm was being charged $1,000 per hour for the services of a Physical Therapy assistant.

Management's Evaluation

In healthcare accounting, the top-down risk-based approach presents a challenge. In most self-funded plans, the corporation outsources the payment of bills to a Third Party Administrator, who is uses a lower accounting standard than the corporation uses in its Accounts Payable Department.

If a corporation reviews the accuracy of its employees' hospital billing for a one-year period; management will develop data as to the significance and complexity of overcharges by vendors. If internal auditors find overcharges in 100% of the invoices submitted by a particular hospital, then special evaluation rules need to be established for that vendor. If certain types of overcharges prove to be minor; e.g., 50-cent errors in pharmacy administration fees, then the cost of evaluating such overcharges may exceed the savings achieved.

19. If adequate entity level controls are implemented, fraudulent healthcare billing will be identified in most invoices. In fact, one could expect to find billing errors in 90% of the hospital invoices submitted for payment. If entity level controls are already examining 100% of high-risk invoices, there is no need for subsequent testing at the individual account or transaction level.

20. Guidance on how management's assessment can be based on evidence other than that derived from separate evaluation-type testing of controls would be helpful. In healthcare, ongoing monitoring is critical. A hospital may charge the correct price for 4-5 items in one invoice, then charge 100% *more* for these items in another invoice. Some vendors have patterns of overbilling for particular items and/or services.

    Whistleblower actions illustrate the need for ongoing monitoring. If a healthcare provider settles allegations of overcharging the Federal government by paying $100 million; there is a possibility that the provider is overcharging publicly traded firms as well.

22. Guidance should be specific. It would be helpful to have guidance on how risk, materiality, attributes of the controls, and other factors (e.g., the vendors' invoices being reviewed) will impact on the decision to use separate evaluations versus ongoing monitoring activities.

24. Employee benefit healthcare is the only line item of an income statement in which employee benefit contributions are reflected. Any internal control deficiencies will cause employees to overpay (or possibly underpay) for healthcare. I suggest that the Commission give corporate executives and Audit Committee members an amnesty period, during which time corporations may disclose any internal control deficiencies and make arrangements to reimburse employees who have overpaid for healthcare as a result of inadequate internal controls. SOX Sec 904 calls for up to ten years' imprisonment for ERISA violations (including fiduciary breach). Given that most major TPAs do not disclose their prices to their publicly traded clients, there are a variety of internal control deficiencies that need to be disclosed.

25. I suggest that the Commission provide definitions of "material weakness" and "significant deficiency."

28. Our team has used information technology to compare fraudulent hospital charges against the data developed by the Centers for Medicare and Medicaid (CMS). CMS evaluated the accuracy of 160,000 hospital bills, gleaned from every U.S. county that had a Medicare licensed hospital. CMS found that the average Medicare hospital bill contained overcharges amounting to 9.3%. The overcharge rate varied by state; e.g., 6.2% per bill in Iowa and 26.1% per bill in Arkansas. I have found a significant correlation between overcharges of the Medicare program and overcharges of publicly traded corporations.

Documentation to Support the Assessment

32. Guidance should be provided concerning the form, nature, and extent of documentation required. Given that most healthcare data will be protected by HIPAA privacy rules, executives need guidance as to how to record and store information. For example, a health plan may have evidence to document eligibility; i.e., the fact that invoices are being paid only for employees, spouses, dependents, and retirees. Obviously, personal identifiers are necessary to ensure that expenses are being paid for current health plan participants *only*.

33. Guidance should be provided as to the extent of documentation that management must maintain about its evaluation procedures that support its annual assessment of internal controls. Guidance should also be provided concerning documentation of results achieved (i.e., billing errors identified).

General Recommendations:

1. Require corporate officers to have baseline healthcare pricing data on file. All corporate executives should know what they have agreed to pay for their employees' healthcare. (It should be a violation of SOX Sec. 404 for a corporate officer to certify the adequacy of a firm's internal controls, without having this information.) Simply knowing the hospital's negotiated discount rate should not constitute SOX compliance.

2. Require corporations to have their Third Party Administrators (TPAs) secure billing detail (itemized billing) for all health benefit invoices that meet a given threshold; e.g., $1,000.

3. Require corporations to have their health benefit and/or hospital bill auditing consultants disclose, in writing, any relationships with and/or compensation received from a TPA, Stop Loss Carrier, Preferred Provider Network, hospital, or any other health-related entity that would represent a conflict of interest.

4. Provide specific guidelines for the verification of employee hospital billing (including detailed, itemized billing).

5. Prohibit corporate officers from certifying the adequacy of internal controls, if the corporation has entered into an outsourced payer's contract that includes a "no audit" provision. (It should be a violation of Sec 404 to sign such a contract.)

6. Require corporate Internal Audit personnel to include Health Benefits in their annual Audit Plan and report their findings to the Audit Committee. Report should include certification that all health benefit payments have been made on behalf of eligible plan participants (employees, retirees, or dependents).

7. Require corporate Internal Audit personnel to conduct an annual Eligibility Audit and report their findings (including any health benefit overcharges and fraud) to the Audit Committee.

8. The Commission should address the fact that corporations are relying on the SAS70 Type 2 audit of external accounting firms. By relying on such audits, a corporation is <u>not</u> meeting its requirements under ERISA (e.g., the "Prudent Man Standard") or any requirements under SOX 404.

9. The Commission should develop an amnesty plan for executives who have certified the adequacy of internal controls, even though their corporations have <u>not</u> had adequate internal controls for employee benefit healthcare

10. Smaller public companies should be given additional time to comply with regulations pertaining to internal controls for employee healthcare.

<u>Background</u>: For 15 years, I have served as an auditor, assisting clients with cost containment. For the last five years, I have served as Vice President of a hospital bill auditing practice. My team has not seen a single correct employee benefit hospital bill in two years and nine months.