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United States General Accounting Office
Washington, DC 20548

October 31, 2000

The Honorable Bill Archer
Chairman
Committee on Ways and Means
House of Representatives

Subject: Medicare Financial Management: Clerical Errors in the Medicare Hospital Insurance and Supplementary Medical Insurance Trust Funds

Dear Mr. Chairman:

The Department of Health and Human Services (HHS) reported to Congress in its Accountability Report for fiscal year 1999 that the Health Care Financing Administration (HCFA) had made several clerical errors in accounting for the Medicare trust funds that caused the Hospital Insurance (HI) Trust Fund to be overinvested by approximately $14 billion and the Supplementary Medical Insurance (SMI) Trust Fund to be underinvested by approximately $18 billion. You asked us to determine (1) what errors were made and how they occurred, (2) what effect the errors had on the financial status of the General Fund, the HI Trust Fund, and the SMI Trust Fund, (3) whether similar errors have occurred in other trust funds, and (4) whether the Departments of HHS and Treasury have acted to ensure that similar errors will not occur in the future. This letter summarizes the results of our review to address your questions and provides recommendations to HCFA and Treasury to further ensure that similar errors do not occur in the future.

Results in Brief

During fiscal year 1999, an inexperienced HCFA staff person inadvertently submitted incorrect documentation to the Bureau of the Public Debt (BPD) for adjusting the HI and SMI Trust Funds and the noninterest-bearing accounts related to the HI and SMI Trust Funds. The clerical errors in the HI and SMI Trust Funds resulted in the HI Trust Fund being overinvested by approximately $14 billion and the SMI Trust Fund being underinvested by approximately $18 billion. The HCFA Office of the Actuary estimated that, as a result, the HI Trust Fund realized excess interest earnings of about $112 million and the SMI Trust Fund suffered a loss of about $232 million in interest earnings. The net interest lost by the Medicare trust funds was about $120 million. During the fiscal year, the general fund of the Treasury benefited from the error by not paying the $120 million of net lost interest earnings to the trust funds.

Therefore, the aggregate net effect on the trust funds and the general fund after full implementation of the corrective actions was zero.

These errors went undetected throughout the year due to weaknesses in the internal control structure at HCFA. Specifically, inadequate training and supervision compounded by inconsistent and ineffective reconciliations were the key factors that allowed these clerical errors to occur without being detected in a timely manner. However, once the errors were identified, HCFA took immediate action to correct the errors and address the internal control weaknesses that contributed to the errors. The corrective actions included restoring the Medicare trust funds to the financial positions that would have existed had the errors not occurred, in accordance with recent legislation, and developing and implementing actions to correct HCFA's internal control weaknesses. Our review of selected financial reporting documentation related to nine other major trust funds administered by other government agencies did not identify similar errors.

Although HCFA has taken steps to help prevent similar errors from occurring in the future, we are recommending that HCFA further enhance monthly benefit adjustment procedures, formally include these procedures in HCFA policy guidance, and develop training for the adjustment process. In addition, Treasury has begun informally performing procedures to review and analyze HCFA's requests adjusting trust fund balances. We are recommending that Treasury formalize its procedures for reviewing and analyzing HCFA requests to adjust trust fund account balances. In written comments on a draft of this letter, BPD and HCFA agreed with our findings and recommendations and stated that they have begun taking steps to implement our recommendations.

Background

HCFA, an HHS agency, is responsible for administering Medicare, Medicaid, and other programs that address the nation's health care needs. In this role, HCFA is responsible for ensuring that Medicare program benefits are provided to eligible beneficiaries,[1] and safeguarding the fiscal integrity of the Medicare programs, which reported over $200 billion in payments in fiscal year 1999. Funds for the two largest Medicare programs administered by HCFA, the HI and SMI programs, are held in the federal HI Trust Fund and SMI Trust Fund. The HI program is financed primarily by payroll taxes paid by employees and employers. The SMI program is financed primarily by transfers from the general fund and by monthly premiums paid by beneficiaries. Payroll tax revenues held in the HI Trust Fund that are not currently needed to pay HI benefits and expenses are invested in interest-bearing Treasury securities. Similarly, premiums and matching contributions not needed to pay current SMI benefits, held in the SMI Trust Fund are invested in interest-bearing special Treasury securities.

HCFA, like other program agencies that direct BPD's actions, is responsible for the ultimate disposition of the trust fund assets. To transfer funds to and from the trust

[1]At the end of fiscal year 1999, there were 39.5 million beneficiaries enrolled in Medicare.

funds, BPD, acting upon directions from HCFA, submits to the Treasury's Financial Management Service (FMS) a nonexpenditure transfer authorization form requesting the transfer of the funds. BPD, as trust funds manager, is responsible for processing certain receipt, investment, redemption, and transfer transactions for 15 trust funds, including the Medicare HI and SMI Trust Funds, and for reporting the results of these transactions as processed to FMS and the program agencies.

Each month, HCFA and BPD execute the necessary transactions to (1) transfer assets to and from the trust funds, maintaining minimum balances in the accounts, (2) administer current HI and SMI benefits and expenses, and (3) record these transactions in their respective financial systems. Each day, BPD redeems securities from the trust funds based on the total amount of funds drawn by Medicare contractors the day before to pay Medicare benefit payments. BPD then determines how to allocate this amount between HI and SMI using allocation percentages provided monthly from HCFA.[2] BPD then transfers these amounts into noninterest-bearing accounts administered by HCFA, referred to as the HI and SMI transfer accounts, from which payments are made to health care providers and suppliers. BPD then reports the transfer amounts to Treasury's FMS and to HCFA.

As illustrated in figure 1, throughout each month, as Medicare contractors make payments to providers for beneficiary services and supplies, the outlays reduce the amounts in the transfer accounts. In managing the transfer accounts, HCFA attempts to maintain a daily balance close to but not less than zero in these accounts, as they do not earn interest. At the beginning of every month, HCFA staff determine whether an adjustment is needed in the transfer accounts. This process is known as the monthly benefit adjustment. HCFA staff compare the actual Medicare benefit outlays for the prior month to the amounts that BPD transferred into the noninterest-bearing transfer accounts in the prior month[3] and calculates the differences for each transfer account. HCFA then prepares the necessary documentation directing BPD to either return excess amounts to the trust funds or transfer additional amounts into the transfer accounts. When amounts deposited in a transfer account exceed the actual Medicare benefit outlays in a month, HCFA instructs BPD to return the surplus amounts to the trust funds to be reinvested in interest-bearing Treasury securities. Conversely, when amounts in a transfer account are insufficient to cover actual outlays, HCFA requests that BPD transfer additional amounts to the trust fund transfer account. In this case, BPD redeems interest-bearing securities from the Medicare trust funds, transfers the amounts, and reports the amount transferred to HCFA and FMS.

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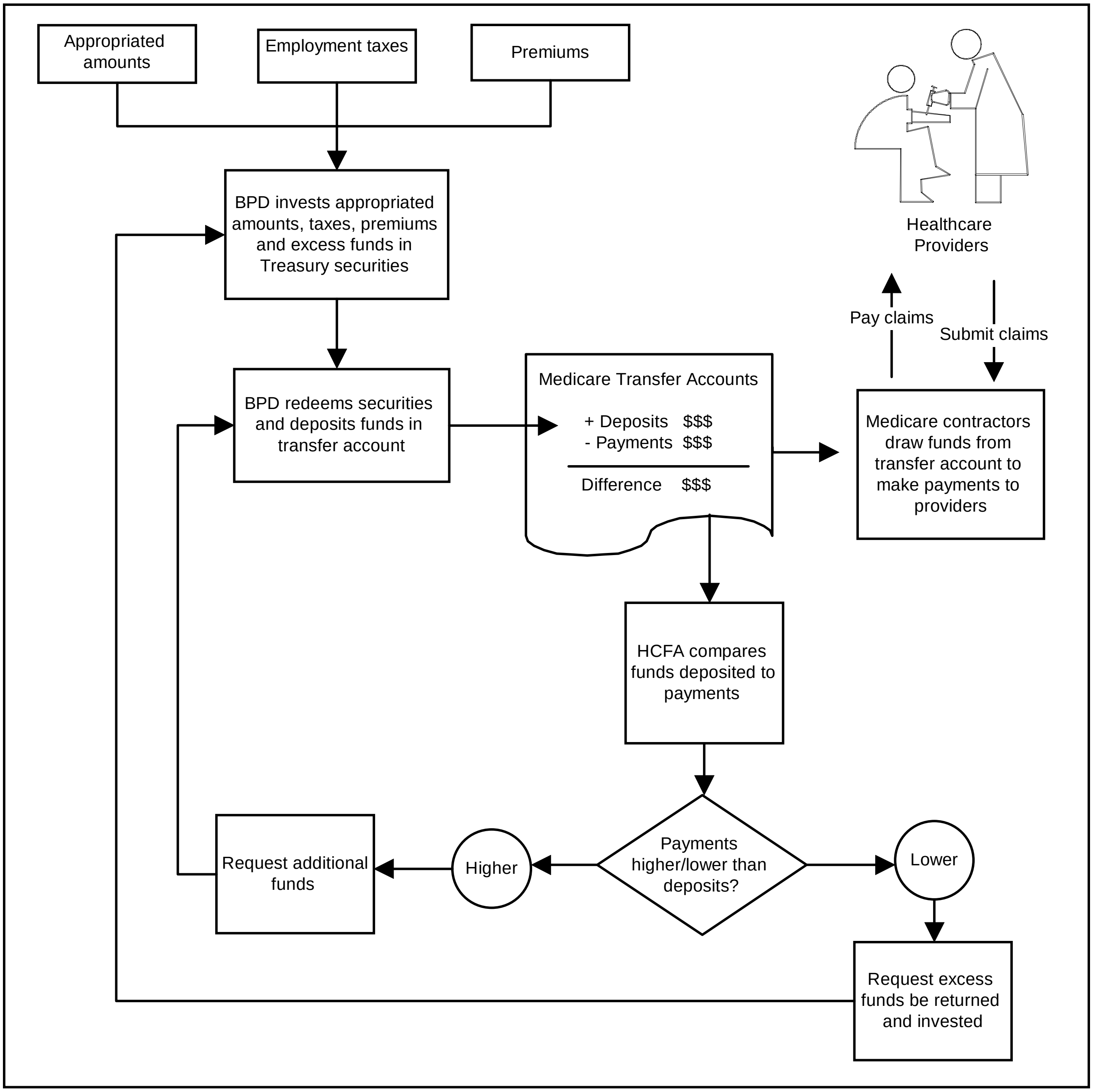
[2]HCFA's allocation percentages fluctuate from month to month and are based on HCFA's budget estimates of monthly Medicare outlays. For example, the July 1999 outlay percentages were 53.3 percent for HI outlays and 46.7 percent for SMI. In the previous month, the percentages were 58.4 percent and 41.6 percent for HI and SMI, respectively.

[3]These amounts will normally differ each month because the amounts deposited by BPD are estimated payments, not actual payments. Medicare contractors report actual payment amounts each month for the previous month.

Figure 1: Overview of HCFA's Monthly Benefit Adjustment Process



HCFA is responsible for ensuring that its staff properly execute the monthly benefit adjustment procedure and that the balances in the Medicare transfer accounts are reconciled each month. HCFA is expected to use the Undisbursed Appropriation Account Ledger (FMS-6653) that FMS supplies each month for both the HI and SMI transfer accounts in its reconciliation process. The FMS 6653 provides the opening fund balance for the month, amounts transferred into and out of the transfer accounts during the month by BPD, the actual amount of Medicare benefit outlays that were reported, and the closing balance at the end of the month. HCFA is responsible for reconciling the ending fund balances on the FMS-6653s with its official records.

Scope and Methodology

To identify the errors that were made and how they occurred, their effects on the HI and SMI Trust Funds and the General Fund, and the corrective actions taken by HHS and Treasury, we interviewed BPD and HCFA officials and staff and reviewed Treasury and HCFA documents. In addition, we reviewed the legislation for correcting the clerical errors. We also included the final estimates of the interest effects on the HI and SMI Trust Funds as determined by HCFA's Office of the Actuary, but we did not test, or recalculate the interest estimates.

To identify whether similar significant errors have been made in other trust funds, we interviewed BPD officials and GAO staff responsible for reviewing financial data for those agencies. We also reviewed the fiscal year 1999 financial reports and/or fiscal year 1999 accountability reports for those agencies responsible for administering nine of the largest federal trust funds to determine whether similar errors had been reported for those trust funds. The trust funds reviewed were the Federal Old Age and Survivors Insurance (OASI) and Disability Insurance (DI) Trust Funds, the Unemployment Trust Fund, the Hazardous Substance Superfund, the Highway Trust Fund, the Airport and Airway Trust Fund, the Civil Service Retirement and Disability Fund, the Military Retirement Fund, and the Railroad Retirement Trust Fund.[4] We conducted our review from May 2000 through August 2000 in accordance with generally accepted government auditing standards. We requested comments on a draft of this report from the HCFA Administrator and the Commissioner of the Public Debt. Their comments along with technical suggestions have been incorporated as appropriate and reprinted in enclosures I and II.

HCFA Made Errors in the HI and SMI Trust Fund Adjustment Process

During fiscal year 1999, HCFA made systematic errors in its monthly benefit adjustment process. The monthly benefit adjustment amounts were calculated correctly. However, the memorandums prepared by HCFA staff detailing the adjustments to be made between the trust funds and the transfer accounts were prepared incorrectly. The transfers called for in the memorandums were the reverse of what was actually required. For example, during July 1999, SMI benefit payments equaled $7,078,151,311. The total funds deposited in the SMI transfer account equaled $7,739,943,000. As a result, a surplus of $661,791,688 remained in the SMI transfer account at month-end and should have been returned to the SMI Trust Fund. However, the memorandum prepared and submitted by HCFA staff requested that an

[4]The Federal Old-Age and Survivors Insurance and Disability Insurance trust funds are administered by the Social Security Administration; the Unemployment Trust Fund, by the Department of Labor; the Hazardous Substance Superfund, by the Environmental Protection Agency; the Highway Trust Fund and Airport and Airway Trust Fund, by Department of Transportation; the Civil Service Retirement and Disability Fund, by the Office of Personnel Management; the Military Retirement Fund, by the Department of Defense; and the Railroad Retirement Trust Fund, by the Railroad Retirement Board.

additional $661,791,688 be transferred from the SMI Trust Fund to the SMI transfer account.

Beginning with the April 1999 adjustments and continuing through the September 1999 adjustments, HCFA incorrectly requested that Treasury transfer funds into the SMI transfer account that actually should have been returned to the SMI Trust Fund for investment. These transfers resulted in a large surplus in the SMI transfer account at year-end. During the same period, HCFA incorrectly requested that Treasury transfer funds from the HI transfer account to the HI Trust Fund that actually should have remained in the transfer account. These transfers resulted in a large deficit in the HI transfer account at year-end. An additional result of HCFA's errors was that the amounts available for investment in interest-bearing securities were less for SMI (underinvested) and more for HI (overinvested) than should have been had the errors not occurred.

The errors were detected by HCFA's Office of the Actuary, which is responsible for monitoring the trends and activities of the Medicare trust funds through a periodic analysis of the HI and SMI Trust Fund transactions, and brought to the attention of HCFA officials. Upon discovery of the errors, as discussed in detail later in this letter, the trust fund balances were corrected.

Internal Control Weaknesses Contributed to the Errors

The Comptroller General's *Standards for Internal Control in the Federal Government* states that an agency's control environment is significantly affected by the competence of its personnel and the agency's ability to (1) identify appropriate knowledge and skills needed for various jobs and (2) provide needed training to maintain skill levels for particular jobs. In addition, the standards state that all transactions and other significant events need to be clearly documented and that the documentation should be properly managed and maintained.

Several internal control weaknesses in HCFA's Medicare trust fund adjustment process contributed to the errors that affected the trust funds. After an employee who previously prepared the adjustments left the agency, HCFA assigned an inexperienced employee responsibility for calculating adjustments to the trust funds and the related transfer accounts. HCFA officials did not sufficiently train the new employee, and there were no documented procedures of the adjustment process to assist the new employee in performing the monthly adjustment. As a result, there was a lack of understanding of how to properly adjust the transfer account balances. In addition, the employee did not understand that the growing month-end balances for the transfer accounts (positive and negative) were indicative of problems in the adjustment process.

Further, HCFA staff did not reconcile account balances affected by the adjustment process as required by Treasury regulations. This resulted in the error going unnoticed for several months. Lastly, HCFA officials did not provide adequate supervisory review and approval of the monthly adjustment procedures, although such procedures are a critical internal control.

The Comptroller General's *Standards for Internal Control in the Federal Government* states that ongoing monitoring activities should include comparisons and reconciliations to identify inaccuracies or exceptions that alert management to any internal control problems. In addition, other important control activities included in the standards are (1) assigning authority and responsibility in a manner that ensures each individual knows how his or her actions interrelate and contribute to meeting the agency objectives and (2) requiring supervisors to continually review and approve the assigned work of their staff.

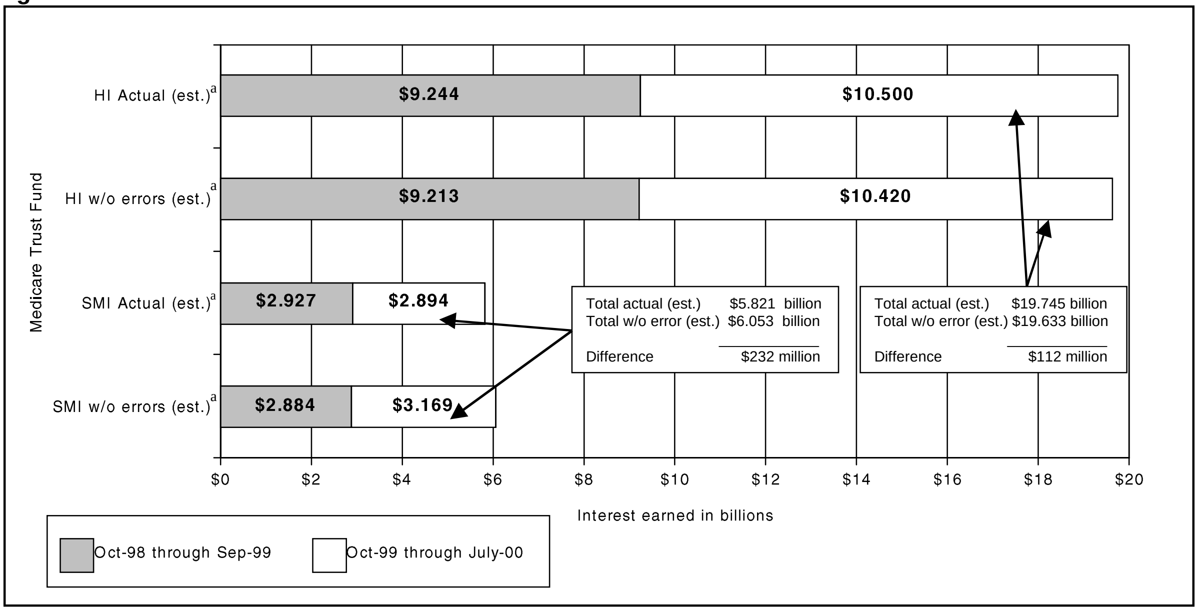
Errors Affected the Medicare Trust Funds and the General Fund

As a result of HCFA's internal control weaknesses and resulting adjustment errors, the holdings and interest income for both Medicare trust funds were affected. Approximately $18 billion of the SMI Trust Fund's interest-bearing securities was unnecessarily redeemed and the amounts transferred to HCFA's noninterest-bearing SMI transfer account. Consequently, the SMI Trust Fund lost interest earnings on the securities redeemed of approximately $232 million as of August 1, 2000.[5] Approximately $14 billion in additional interest-bearing securities were purchased for the HI Trust Fund due to the error. The HI Trust Fund earned approximately $112 million in excess interest on these additional securities as of August 1, 2000. The difference between the amount of interest lost by the SMI Trust Fund and the excess interest earned by the HI Trust Fund is approximately $120 million. This difference is primarily due to the difference between the interest rates of the securities incorrectly redeemed and those purchased to initially correct the error.

After the error was discovered, HCFA's first corrective action was to instruct BPD to redeem the $14 billion in excess HI securities purchased and to acquire $18 billion in SMI securities to replace the securities redeemed in error. HCFA acquired and sold the respective securities in October 1999. The interest rate on the newly acquired SMI securities was 6.50 percent, while the securities that they replaced had been earning interest at rates ranging from 5.875 percent to 8.75 percent. This meant that the SMI Trust Fund was in effect earning up to 2.25 percent less interest on a portion of the $18 billion of newly acquired securities than if the error had not occurred. As illustrated in figure 2, the HCFA actuary determined that the total loss of interest to the SMI Trust Fund from October 1998 through July 2000 was $232 million, and the total excess interest earned by the HI Trust Fund was approximately $112 million.

[5] HCFA's Office of the Actuary calculated the interest effects of the clerical errors through July 31, 2000. In August of this year, BPD made the appropriate adjustments to the HI and SMI Trust Funds, effective August 1, 2000.

Figure 2: Interest Earned on HI and SMI Investments



[a]The estimated interest amounts in figure 2 were calculated by HCFA's Office of the Actuary using a model based on Treasury's investment and redemption policies, and actual HI and SMI Trust Fund data for the period from October 1, 1998, through July 31, 2000.

Source: HCFA's summary chart and statistics for final HI/SMI interest and asset adjustments

The clerical errors had a direct effect on the HI and SMI Trust Funds as discussed above. During the period October 1998 through July 2000, the General Fund benefited by not paying the net amount of approximately $120 million in interest on the trust fund securities. After the full implementation of the corrective actions, the aggregate net effect on the trust funds and the general fund and thus for the federal government as a whole was zero.

HHS and Treasury Have Taken Corrective Actions

HCFA, in coordination with Treasury, determined that specific corrective actions were needed both to restore the assets of the HI and SMI Trust Funds and to correct the internal control weaknesses at HCFA. As described in tables 1 and 2, HCFA developed and executed a corrective action plan approach to correct the monetary effect of the errors on the trust funds and address the underlying internal control weaknesses that prompted the errors. HCFA's corrective actions for the Medicare trust fund investment adjustment process are documented in HCFA's fiscal year 1999 Medicare Trust Fund Investment Adjustment Process Corrective Action Plan.

Table 1: HCFA Corrective Action Plan to Correct the Trust Fund Errors

Weakness	Corrective action[a]
The HI Trust Fund has earned excess interest and the SMI Trust Fund has not earned interest due in fiscal year 1999 as a result of clerical errors.	Analyze the condition of the trust funds as of October 1999 and determine the corrective action necessary to eliminate the cause and internal control weaknesses of the inappropriate account balances.
	Determine the impact on the interest earnings of the trust funds account.
	Adjust the trust funds to correct the miscalculations and make the trust funds whole.

[a]Detailed steps for implementing the corrective actions were included in the Corrective Action Plan.

Source: HCFA's fiscal year 1999 - Medicare Trust Fund Investment Adjustment Process Corrective Action Plan

In consultation with Treasury, HCFA developed more precise corrective action plan steps that addressed making the trust funds whole. Specifically, to correct the most significant effect of the errors on the HI and SMI Trust Funds holdings, BPD was instructed to purchase Treasury securities for the SMI Trust Fund using the underinvested amount ($18 billion) and redeem Treasury securities held by the HI Trust Fund in the amount of the deficit in the HI transfer account ($14 billion). Further, to completely restore the trust funds to where they would have been in the absence of the errors required transferring the amount of excess interest income earned by the HI Trust Fund to the SMI Trust Fund and reestablishing for both trust funds the security holdings that would have been held by the trust funds if the clerical errors had never happened. Lastly, the difference in interest lost to the SMI Trust Fund and the excess interest earned by the HI Trust Fund needed to be transferred from the General Fund of the Treasury.

In October 1999, BPD purchased approximately $18 billion in securities for the SMI Trust Fund and redeemed approximately $14 billion of HI securities to correct the most significant effect of the errors. The remaining corrective actions required congressional approval.

Legislation to correct the interest earnings and restore the status of the trust fund holdings was signed into law by the President on July 13, 2000. Specifically, section 2703 of Public Law 106-246 required that within 120 days after the effective date of the act, the following actions would be taken:

(1) Correct the holdings of the trust funds by replicating, to the extent practicable, the holdings of the trust funds that would have been held by the trust funds if the clerical errors had not occurred.
(2) Correct the trust fund interest income, by transferring the amount of excess interest income from the HI Trust Fund to the SMI Trust Fund that would not have been earned if the errors had not occurred.
(3) Appropriate to the SMI Trust Fund the difference between the interest income lost by the SMI Trust Fund and the amount transferred from the HI Trust Fund.

The actions required by the legislation were completed by BPD in August 2000, with an effective date of August 1, 2000. Specifically, BPD adjusted the HI and SMI Trust

Fund holdings as of July 31, 2000, through redemptions and acquisitions resulting in a net reduction in the holdings of the HI Trust Fund of approximately $112 million and an increase in the holdings of the SMI Trust Fund of approximately $232 million on August 1, 2000. Further, effective August 1, the trust funds' portfolios of securities were restored, as to principal and interest rate, to the state that they would have been had the clerical errors never occurred.

HCFA's corrective action plan also included actions to strengthen the internal controls to prevent further errors. HCFA's approach to correcting the internal control weaknesses, as shown in table 2, included identifying the key weaknesses contributing to the clerical errors at HCFA and the corresponding corrective action step.

Table 2: HCFA Corrective Action Plan to Address Internal Control Weaknesses

Internal control weaknesses	Corrective action[a]
The Medicare trust fund adjustment process had the following internal control weaknesses that caused the clerical errors:	
(1) Inadequate verification and reconciliation of transactions to ensure accuracy.	Implement the monthly use of the benefit adjustment spreadsheet for use in the calculation and verification of the monthly adjustment.
(2) Inadequate analysis of monthly financial account balances.	The Treasury income statement is received monthly in the Accounting Systems Management Branch (ASMB) and is distributed to the Financial Reporting & Oversight Branch (FROB). An accountant in FROB will analyze for reasonableness the Treasury income statement amounts for fund balance and investments, including comparing the current month with the prior month and years. ASMB will also distribute the Treasury income statement to the Office of the Actuary (OACT). OACT will also review the amounts for reasonableness.
(3) Inadequately trained staff.	Staff responsible for the preparation of certain Treasury forms used to transfer funds and report fund transactions will receive detailed training on the preparation of these forms and the use of the benefit adjustment spreadsheet.
(4) Lack of detailed written procedures for the monthly adjustment process.	Develop written detailed procedures on use of the Benefit Adjustment Spreadsheet and the preparation of certain Treasury forms used to transfer funds and report fund transactions.
(5) Inadequate supervision, review, and approval of work.	All supporting documentation will be reviewed and approved at least monthly by an accountant, the ASMB Chief, Division of Accounting Director, and the Deputy Director of the Financial Services group.
(6) The allocation percentages for HI and SMI were not updated on a regular basis.	The Division of Budget will supply the Division of Accounting with the updated Budget Outlay Plan each quarter.

[a]Detailed steps for implementing the corrective actions were included in the Corrective Action Plan.

Source: HCFA's Fiscal Year 1999 - Medicare Trust Fund Investment Adjustment Process Corrective Action Plan.

Although progress has been made, HCFA has not implemented all corrective actions outlined above. HCFA has developed and implemented a benefit adjustment spreadsheet to use in performing analyses, calculations, and verification of the monthly trust fund account adjustment. Further, HCFA has provided detailed training to staff on preparing the accounting adjustment and documentation and using the benefit adjustment spreadsheet. In addition, HCFA developed procedures specifying the supervisory review steps for all supporting documentation related to the monthly adjustment to the trust funds transfer accounts. However, HCFA has only developed a draft of written detailed procedures for completing the benefit adjustment spreadsheet and preparing the required Treasury accounting documentation.

Treasury officials at BPD, who act as managers of the Medicare trust funds, stated that they were not aware of the errors because they are not responsible for reviewing the balances of the Medicare noninterest-bearing transfer accounts. HCFA has responsibility for monitoring the transfer accounts. Although not required to do so under Treasury regulations, Treasury officials at BPD have begun reviewing certain reports and related documentation for the Medicare transfer accounts to ensure that requests from HCFA to adjust the balances of the transfer accounts and trust funds are reasonable.

Similar Errors Were Not Reported by Other Trust Funds

Our review of fiscal year 1999 financial reporting documentation for nine other major trust funds did not identify any reported errors similar in nature to the errors reported for the HI and SMI Trust Funds. The errors affecting the HI and SMI Trust Funds and related transfer accounts were the result of internal operational mistakes made by HCFA and appear to be unique to HCFA. In our review of other major trust funds, such as the OASI and the DI Trust Funds, we did not look at the extent to which errors may have resulted from activities such as the allocation of gross tax receipts[6] since it was outside of the scope of this review.

During our review, we did not identify evidence that the other trust funds use transfer accounts similar to HCFA to pay program expenditures or require monthly trust fund adjustments similar to HCFA's. For example, monthly program expenditures are paid from the OASI and DI Trust Funds administered by the Social Security Administration. However, SSA does not perform a month-end adjustment process similar to the one performed by HCFA. This is due to the fact that expenditure amounts for the programs funded by the OASI and DI Trust Funds are normally fixed and known amounts, and therefore the amount transferred to cover the expenditures is the same as the expenditure level. Conversely, Medicare benefit payments fluctuate from month to month, and the deposits made for these payments are, of necessity estimates.

Conclusions

As more and more beneficiaries rely on Medicare to provide health coverage and health care security, it is imperative that the finances of the program are properly accounted for. HCFA, responsible for the fiscal integrity of the Medicare programs,

[6] *Excise Taxes: Internal Control Weaknesses Affect Accuracy of Distributions to the Trust Funds* (GAO/AIMD-99-17, November 1998).

and Treasury, trust fund manager, must ensure that adequate controls are in place to safeguard Medicare assets. The errors that occurred in accounting for the trust funds during fiscal year 1999 demonstrate how weak internal controls and limited oversight can affect Medicare program assets. It will be important that HCFA and Treasury develop and implement formal procedures to ensure that the activities related to accounting for the Medicare trust funds are properly managed.

Recommendations for Executive Action

To ensure that adequate controls are in place to safeguard Medicare assets, we recommend that the HCFA Chief Financial Officer take the following actions:

- Further enhance the monthly Medicare benefit adjustments procedures to include monthly analysis of the transfer account ending balances to detect anomalies.
- Formalize the written procedures for preparing the monthly Medicare benefit adjustment spreadsheet and incorporate them in official HCFA policy guidance.
- Conduct training for those staff responsible for preparing, processing, and reviewing the monthly benefit adjustment and any staff whose job performance is directly related to the daily transfer account transactions.

In addition, to further strengthen the controls in place to safeguard Medicare assets, we recommend that the Commissioner of the Public Debt formalize BPD's informal procedures for reviewing certain reports and related documents for the Medicare transfer accounts to ensure that HCFA's requests to adjust the balances of the transfer accounts and trust funds are reasonable.

Agency Comments and Our Evaluation

BPD and HCFA agreed with our findings, conclusions, and recommendations. BPD stated that it has already implemented a reasonableness review of HCFA requests and that it will formally document this procedure by December 31, 2000. In its comments, HCFA discussed the steps it has taken to improve the benefit adjustment process and strengthen internal controls. The Acting Administrator described some of these steps, such as developing and implementing procedures for preparation of the monthly benefit adjustments and providing training to staff on these procedures. In addition, HCFA stated that one of its key initiatives will be the development and implementation of a HCFA accounting manual that will detail the procedures for significant activities, including the benefit adjustment process. The steps that HCFA and BPD have outlined in their comments appear reasonable. Formalizing and institutionalizing these procedures should improve financial accountability over the Medicare trust funds.

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We are sending copies of this report to Representative Charles Rangel, Ranking Minority Member, Committee on Ways and Means, and appropriate congressional committees. We are also sending copies to Michael M. Hash, Acting Administrator of the Health Care Financing Administration, and the Honorable Van Zeck, Commissioner of the Bureau of the Public Debt. Copies will be available to others on request. This report was prepared under the direction of Gloria Jarmon, Director, who may be reached at (202) 512-4476 or by email at *jarmon.aimd@gao.gov* if you or your staff have any questions. Kim Brooks, Ed Brown, Kay Daly and Meg Mills were key contributors to this letter.

Sincerely yours,

Jeffrey C. Steinhoff
Managing Director
Financial Management and Assurance

Enclosures

Comments From the Health Care Financing Administration

Note: GAO comment supplementing those in the report text appears at the end of this enclosure.

DEPARTMENT OF HEALTH & HUMAN SERVICES Health Care Financing Administration

Washington, D.C. 20201

DATE: OCT 25 2000

TO: Gloria L. Jarmon, Director
Health, Education, and Human Services
Accounting and Financial Management Issues

FROM: Michael M. Hash Michael M Hash
Acting Administrator

SUBJECT: General Accounting Office (GAO) Report, Medicare Financial Management: Clerical Errors in the Medicare Hospital Insurance and Supplementary Medical Insurance Trust Funds (GAO-01-39R)

Thank you for your letter to Nancy-Ann Min DeParle concerning the draft report entitled, "Medicare Financial Management: Clerical Errors in the Medicare Hospital Insurance and Supplementary Medical Insurance Trust Funds" (GAO-01-39R).

The report outlines the issues that contributed to the clerical errors made during fiscal year 1999 and the procedures that we have implemented to prevent further errors. As the General Accounting Office (GAO) states, there was no loss to either of the Medicare trust funds or to the General Treasury fund as a result of these errors. However, we take full responsibility for the clerical errors made by the Health Care Financing Administration (HCFA) and regret the incidents that contributed to these errors. We fully agree with GAO that stringent controls are necessary to ensure that errors of this kind never occur in the future.

When HCFA identified the problem in July 1999, we immediately began a root cause analysis and notified the Office of the Department of Health and Human Services (DHHS) Office of Inspector General (OIG). We took immediate actions to address the issues and establish procedures to prevent further errors. In addition, we immediately self reported the errors in accordance with requirements of the Federal Managers' Financial Integrity Act (FMFIA).

After identifying the internal control weaknesses that allowed these errors to occur, we took aggressive actions to implement new procedures that have improved the benefit adjustment process and strengthened internal controls. Specifically, HCFA identified the cause of the error and made appropriate adjustments to correct the errors. We notified the Bureau of Public Debt (BPD), Office of Management and Budget (OMB) and DHHS OIG of the problem. We developed and implemented detailed written procedures and trained all staff on the new procedures. We believe our aggressive actions to correct the situation have produced more accurate amounts being drawn down from the Medicare

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trust funds, which have reduced the amount of the monthly benefit adjustments and the closing balances in the transfer accounts.

These efforts are in keeping with other aggressive actions we have taken to safeguard the fiscal integrity of the trust fund and protect both the beneficiaries who depend on Medicare and the American taxpayers. One indication of these aggressive actions is the unqualified audit opinion we received on our fiscal year 1999 financial statements. In the spring of this year, we also hired a new Deputy Chief Financial Officer, who is assisting the agency in developing a comprehensive business plan to define financial management objectives and goals for HCFA. Within the last six months we have:

- Produced interim financial statements that entailed analyzing and reconciling account balances. All unusual variances were investigated. The interim financial statement gave HCFA a mid-year, concise picture of its financial status and is in keeping with private-sector financial practices.

- Reconciled Medicare cash outlays against claim data in the national claims history file. This reconciliation effort allowed HCFA to ensure that Medicare outlays are in line with claim activity.

- Improved our oversight of contractors' financial data, including the analysis of contractors' reports of accounts receivable and expenditures.

- Enhanced HCFA's automated accounting system to facilitate the electronic submission of data to the Department of the Treasury (DOT) for inclusion in government-wide financial reports. These improvements also facilitated the reconciliation of this data to HCFA's financial statements.

- Improved management of the transfer accounts by performing reconciliations earlier in the month. Transfer accounts do not earn interest, whereas both the Part A and Part B trust funds do. Therefore, ensuring that there is not too much money in the transfer accounts and that as much money as possible stays in one of the trust funds, saves American taxpayers money and is good financial policy.

- Improved audit follow-up procedures to ensure that all CFO audit findings are corrected timely and effectively.

We believe that the above actions have improved the financial accountability of the agency itself, as well as the private contractors that process Medicare claims. We will continue to identify areas where further financial controls are needed.

See comment 1.

We would also note that while GAO reviewed nine other agencies and similar errors were not detected in FY 99, our discussions with DOT staff indicated that similar kinds of errors have occurred in past years in other trust funds.

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Thank you for the opportunity to review the draft report. We look forward to working closely with GAO on these and other issues. Attached are our comments on the specific recommendations in the report.

Comments of the Health Care Financing Administration on the General Accounting Office (GAO) Draft Report, "Medicare Financial Management: Clerical Errors in the Medicare Hospital Insurance and Supplementary Medical Insurance Trust Funds"

GAO Recommendation 1

Further enhance the monthly Medicare benefit adjustments procedures to include monthly analysis of the transfer account ending balances to detect anomalies.

HCFA Comment

We agree and have taken steps to address this issue. In December 1999, we developed and implemented procedures for preparing the monthly Medicare benefit adjustments. Although not documented in the procedures, we routinely review the ending balances in the transfer accounts for dollar reasonableness. If there are abnormally large ending balances in the transfer accounts, additional analysis and inquiry are performed.

In addition, staff members within the Health Care Financing Administration's (HCFA) Division of Accounting have prepared detailed reconciliations of the monthly net benefit adjustment amounts in order to determine the various items that result in the net benefit adjustments. The results of the reconciliation were discussed with the Bureau of the Public Debt (BPD), and it was determined that the BPD's process of drawing amounts from the Hospital Insurance and Supplementary Medical Insurance Trust Funds for daily Medicare payments should be revised. HCFA and BPD have implemented a revised process resulting in more accurate amounts being drawn from the Trust Funds and therefore reducing the amount of the monthly benefit adjustments and the closing balances in the transfer accounts. HCFA and BPD are working together to revise the Memorandum of Understanding pertaining to this process. In addition, there are senior accountant and management reviews performed monthly to ensure that we identify anomalies and that procedures are being followed.

GAO Recommendation 2

Formalize the written procedures for preparing the monthly Medicare benefit adjustment spreadsheet into official HCFA policy guidance.

HCFA Comment

We agree, and have formalized our procedures. As mentioned, we drafted detailed written procedures in December 1999 and formalized them in May 2000. Staff received training on these procedures and understand that they are expected to follow the procedures. Recognizing the importance of documented procedures, we have established a goal in the Chief Financial Officer Comprehensive Plan for Financial Management for improving internal accounting operations. A key element in improving internal accounting operations and ensuring that the financial statements and other external reports properly reflect the Agency's activities is having comprehensive written accounting policies and procedures that can be used by staff in carrying out their day-to-day responsibilities. Therefore, one of the key initiatives will be the development and implementation of a HCFA Accounting Manual detailing the procedures for significant activities, including the benefit adjustment process and related reconciliations. Until we have an accounting manual, we will continue to formalize procedures in a written format similar to the way we issued the benefit adjustment procedures. A consulting firm has been hired to assist us in developing these comprehensive written accounting procedures in accordance with Federal accounting standards and HHS policies and procedures. Our monthly Medicare benefit adjustment procedures will be among the first incorporated within this manual.

<u>GAO Recommendation 3</u>

Conduct training for those staff responsible for preparing, processing, and reviewing the monthly benefit adjustment and any staff whose job performance is directly related to the daily transfer account transactions.

<u>HCFA Comment</u>

We agree and have already taken steps to address this issue. All staff involved in the preparation, processing, and review of the monthly benefit adjustment received adequate training on the new and improved procedures by March 2000. As new staff are assigned to perform these functions or related responsibilities, they will also be adequately trained before assuming these important functions.

The following is GAO's comment on HCFA's letter dated October 25, 2000.

<u>GAO's Comment</u>

1. Our review focused on fiscal year 1999 activity in other trust funds. Although errors in other trust funds may have occurred, as discussed in the report, errors similar to those reported for the HI and SMI Trust Funds were not reported in the agencies' financial reports.

Comments From the Bureau of the Public Debt

DEPARTMENT OF THE TREASURY
BUREAU OF THE PUBLIC DEBT
WASHINGTON, DC 20239-0001

October 20, 2000

Mr. Jeffrey C. Steinhoff
Managing Director
Financial Management and Assurance
United States General Accounting Office

Dear Mr. Steinhoff:

Thank you for the opportunity to provide comments on the draft report, *Medicare Financial Management: Clerical Errors in the Medicare Hospital Insurance and Supplementary Medical Insurance Trust Funds.*

We are pleased you noted that Public Debt performed properly and effectively with regard to our functions related to the administration of the Hospital Insurance and Supplementary Medical Insurance Trust Funds and in promptly restoring the Trust Funds to their correct balances. We are committed to doing what we can to help ensure that similar errors do not occur in the future.

As you noted, we have already implemented a reasonableness review of Health Care Financing Administration (HCFA) requests to adjust Trust Fund account balances. This procedure was implemented early in Fiscal Year 2000 after discussions with HCFA. We concur with the recommendation that Treasury formalize this procedure. We will formally document this procedure by December 31, 2000.

I hope these comments are helpful to you in finalizing your report. If we can be of further assistance to your staff, or should you have any questions about this matter, please don't hesitate to call me at (202) 691-3500.

Sincerely,

Van Zeck
Commissioner

www.publicdebt.treas.gov

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