UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

HUMAN RESOURCES
DIVISION

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MAY 29, 1981

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The Honorable Richard S. Schweiker
The Secretary of Health and Human Services

Dear Mr. Secretary:

Subject: Improving Medicaid Cash Management Will Reduce Federal Interest Costs (HRD-81-94)

In our June 10, 1980, report, 1/ we discussed our review of State systems for recovering Medicaid overpayments to providers and for returning the Federal share of these overpayments to HHS. We also communicated our findings to the Administrator of the Health Care Financing Administration (HCFA) in two other reports. 2/ These same findings, as well as others, were reported to HCFA headquarters and regional officials during several oral briefings.

Based on our reports and briefings, HCFA initiated reviews of State Medicaid cash-management systems. As of January 1980, HHS had recouped $41.9 million in Federal Medicaid funds from 14 States and was in the process of recouping $39.2 million from other States. However, in reviewing some States, HCFA regional office staffs examined the State's cash-management system without attempting to identify possible recoupable funds. While we believe identifying system deficiencies is important, it is also important to identify and recover the Federal share of Medicaid overpayments. Therefore, we made a follow-on review in seven States and the District of Columbia where HCFA reviews did not identify any recoupable funds. During the 12-month period (July 1979 through June 1980) covered by our review:

1/Report to the Secretary of Health and Human Services, "States Should Intensify Efforts to Promptly Identify and Recover Medicaid Overpayments and Return the Federal Share," HRD-80-77.

2/Our reports dated October 27, 1978, and May 4, 1979.

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--Over $11 million in Medicaid and other program funds were in non-interest-bearing checking accounts in three States. Because the banks had the use of this money, the Federal and State governments lost and/or incurred interest of over $1.3 million. One of the banks involved reported earning $512,000 on the Medicaid funds it held for an 11-month period.

--Some States drew Federal funds in excess of current disbursement needs and invested the balances and retained the interest earned.

--States had not returned the Federal share of $23 million in identified but uncollected overpayments.

--The long time that elapsed between when States made cash collections and when they returned the Federal share enabled States to earn substantial amounts of interest on Federal funds.

OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of our follow-on review was to determine if the States returned the Federal share of identified and/or recovered Medicaid overpayments. We also wanted to determine whether States hold Federal Medicaid funds for long periods and where these funds are held. We focused our review on the period from July 1979 through June 1980. We aged and analyzed overpayment account balances that we identified during our review. To determine or estimate the residual cash balances, we examined, when available, State records of bank data and, where necessary, obtained estimates from State officials. We conducted our review at HHS headquarters and in Delaware, Idaho, Maryland, Oregon, Virginia, Washington, West Virginia, and the District of Columbia.

BACKGROUND

Medicaid, or title XIX of the Social Security Act, established by the Social Security Amendments of 1965, is a Federal-State program in which the Federal Government pays 50 to 78 percent of State's cost for medical care provided to the poor. At the Federal level, HCFA is responsible for administering Medicaid.

Each State initiates and administers its own Medicaid program. The Federal Government commits its share of Medicaid program costs through quarterly grants to the States which cover estimated program expenditures. Cash is available to the States through the letter-of-credit method, whereby HHS specifies the amount and time frame so that States can withdraw funds as needed from a Federal

Reserve Bank. Cash withdrawals by States should be on the basis of meeting only immediate disbursement needs. Overpayments reported by the States are shown as adjustments to expenses which, in effect, reduces the amount of future grant awards. Through this mechanism, the Federal Government receives credit for its share of overpayments.

COMMERCIAL BANKS EARNED INCOME BY USING FEDERAL AND STATE FUNDS

In the 1-year period covered by our review, an average balance of over $11 million in Medicaid and other program funds was carried in non-interest-bearing checking accounts by Virginia, Delaware, and Washington. These funds provided interest income to the banks in which the funds were deposited, without the Federal and State governments receiving any of the income. This happened because the Federal and State agencies involved did not properly monitor the flow of program funds, and the States did not invest residual cash balances. The following discussion shows how this condition developed in each of the States.

Virginia

Virginia uses a fiscal agent to process Medicaid claims and to pay providers of Medicaid services. The fiscal agent maintains a checking account for this purpose. The State provides the fiscal agent with enough cash each week to cover Medicaid expenditures. After the cash is deposited in the bank, the Medicaid checks are mailed to the providers. Since it takes an average of 6 days for these checks to clear the banking system, there is usually a large balance in the fiscal agent's checking account. The "deposit balance" 1/ in this account, during the 11-month period from August 1979 through June 1980, averaged over $5.2 million.

Ordinarily, Virginia invests balances held in State bank accounts; however, the State did not invest the balance in this account because it was controlled by the fiscal agent. The fiscal agent did not execute a written agreement with the bank establishing procedures for the treatment of interest earned on the deposit balance and was not obligated to do so under its contract with the State. Therefore, the bank invested the funds for its own benefit.

1/The amount on deposit which could have been properly withdrawn by the depositor for investment but not so withdrawn. This amount arises because of cash-on-hand to cover checks that have not cleared the banking system.

Federal Reserve rules (12 CFR 204.5) allow banks to lend at least 83-3/4 percent of demand deposits on hand in checking accounts. The Virginia bank reported to the fiscal agent that its interest rates averaged 11.2 percent during the 11-month period and reported that it had earned more than $512,000 in interest during this period, before bank charges of about $31,000. The bank reported an average deposit balance of over $5.2 million on the fiscal agent's account during the 11 months.

If the bank had not held the Medicaid funds, the State could have earned about $266,000 on its share of the $5.2 million and the Federal Government could have avoided about $345,000 in interest expense at the average 3-month U.S. Treasury bill rate for the July 1979 through June 1980 period. This would be offset somewhat by bank charges for its services. This condition had existed in Virginia for several years, and could have been identified sooner if the State and HCFA had adequately monitored the flow of program funds.

Under the Medicare program, claims payment contractors (similar to Medicaid fiscal agents) are required by their contracts with HCFA to have written agreements with banks and to closely monitor the amounts held in checking accounts to ensure that the banks only earn enough interest on such funds to reimburse them for their services.

Delaware

Delaware uses the same fiscal agent as Virginia and has a similar Medicaid claims payment system. Our analysis of available bank data showed that deposit balance in the fiscal agent's account averaged about $540,000, based on an average time of 7 days for checks to clear the banking system. If the bank had not held these funds, the State could have earned (before bank charges) at the 11.63-percent Treasury bill rate about $31,000 on its share of the money and the Federal Government could have avoided about $31,000 in interest expense because of a decreased need to borrow.

Like Virginia, Delaware's policy is to invest cash balances held in State-administered bank accounts, but the Medicaid funds in the deposit balance were not invested because the fiscal agent's bank account is not administered by the State. This fiscal agent did not execute a written agreement with the bank and was not contractually obligated to do so. This situation has existed in Delaware since at least 1978 and could have been identified and corrected by good cash management surveillance by either the State or Federal Government.

Washington

Washington is required by State law to hold surplus funds in interest-bearing accounts, with an unspecified bare minimum allowed to be kept in non-interest-bearing demand deposits. The amount actually kept in these deposits was $6 million. The State maintained this $6 million balance each day by depositing whatever amount of funds was needed to raise the day's ending balance to $6 million.

Replenishing the funds as checks are paid to maintain a $6 million balance is questionable under the written agreement between the bank and the State. The agreement provides that there will be no predetermined balance requirement, except for the provision that the bank not end up with negative balances. Further, the agreement provides that the balance required to service the State's account will be adjusted on the first business day of each calendar quarter and based on a specific formula.

Although these funds are not exclusively from the Medicaid program, because the State commingles funds from various other Federal and State programs, such as Aid to Families with Dependent Children, the basic principle applies; that is, earnings on State and Federal program funds are providing profits to the private banking system. Furthermore, because other program funds were involved, it indicates that the problem goes beyond Medicaid. If the bank had not held these funds, a total of about $700,000 in State interest earnings and Federal interest avoidance could have been realized, before bank charges for services, at the 11.63-percent Treasury bill rate.

STATES BENEFITED FROM
FEDERAL CASH TRANSFERS

Two States we reviewed used the Federal Treasury's letter-of-credit financing procedures to earn interest on surplus Medicaid and other program funds. They did this by drawing and investing Federal funds in excess of current needs. The District of Columbia draw downs were not related to cash needs. Three other States invested funds on hand, generally in Federal securities, with the interest accruing to the State. However, State records did not permit us to readily identify excess Federal money. We estimate that the average elapsed time between transfers of Federal money to the States and presentation of provider checks to the bank for payment ranged from 6 to 20 days in the five States.

Although the Intergovernmental Cooperation Act (42 U.S.C. 4201 et seq.) allows the States to retain interest earned on Federal grant-in-aid funds pending disbursement, it does not appear that the Congress intended the law to result in large financial benefits to the States. Because of excessive amounts being withdrawn before the time needed, Treasury has to borrow, at high rates of interest, funds it would not otherwise need.

The Intergovernmental Cooperation Act holds heads of Federal agencies primarily responsible for monitoring the letter-of-credit system and for scheduling funds transfers to minimize the elapsed time between funds draw down and disbursement. However, States also have a responsibility not to draw funds in advance of program needs, and they were not meeting this responsibility.

Virginia maintained a Federal cash balance in its Medicaid program of $2.5 million greater than its disbursement experience dictated. (This is in addition to the funds in the fiscal agent bank account previously discussed.) Furthermore, the periodic Medicaid draw downs, which average about $3.9 million, are in the State treasury for a period of 5 days before any cash is disbursed. The State invests this Federal money. If the Federal funds held by the State and those held by the bank had not been drawn, the Federal Government could have avoided about $900,000 in interest expense based on the average 3-month U.S. Treasury bill rate of 11.63 percent for the July 1979 through June 1980 period.

Similarly, West Virginia maintains an average daily Medicaid cash balance of about $4.4 million, about $3 million of which is Federal money. These funds are in excess of the State's current program needs. This excess cash balance, at least in part, occurs because Federal money is drawn down an average of 8 days before checks are written and an average of 12 days elapses before these checks are presented for payment. Excess funds are invested each day. We estimate that the average daily balance of $3 million in Federal money cost the Federal Government about $350,000 in unnecessary borrowing costs.

The District of Columbia was drawing down Federal Medicaid funds by obtaining one-sixth of the quarterly award every 2 weeks. These draws were not related to an immediate need for funds. Records were not readily available to allow us to determine an average Medicaid balance because Medicaid funds were commingled with other program funds.

HHS has recognized that these kinds of situations arise and has taken steps to minimize their impact by employing cash-management techniques in some States. The Department is presently

implementing either a checks paid or delay of draw down letter-of-credit procedure in the 10 largest States, where feasible. Under these procedures, the letter-of-credit is not drawn on until recipient or provider checks are presented to the bank for payment (checks paid), or until program checks have been issued to recipients or providers (delay of draw down). How well these systems will work has not yet been determined.

Another problem we identified relates to uncashed Medicaid checks. In Maryland, if providers do not cash Medicaid checks, they are held for a period of 7 years and then written off and the funds deposited in the State's general fund. 1/ During the 7-year period, the State kept the Federal share of uncashed checks and the interest earned from investing such funds and it appeared that, when the checks were written off, the Government did not receive credit for its share. Records were not readily available to determine the amount of Medicaid funds tied up in uncashed checks, but a total of about $700,000 of such checks existed from all sources in the State. Similarly, West Virginia writes off checks each year but apparently does not credit the Federal Government with its share. In Washington, the HHS Office of Inspector General found that the State did not write off checks for at least 5 years. Again, records were not readily available in either State to determine the amount of Medicaid funds involved. The practice of not writing off checks for prolonged periods in all three States appeared to result from State laws governing uncashed checks.

STATES DO NOT RETURN THE FEDERAL SHARE OF IDENTIFIED OVERPAYMENTS UNTIL THEY ARE RECOVERED

All of the jurisdictions we reviewed return the Federal share of identified overpayments only after they are recovered. In the eight jurisdictions about $23 million in substantiated and potential overpayments had not been collected and the Federal share had not been returned. The following table summarizes the status of these overpayments.

1/We found similar situations in the Aid to Families with Dependent Children program (see HRD-79-63, Apr. 5, 1979).

Identified but Uncollected Overpayments (note a)

Jurisdiction	In the process of collection	Under appeal by provider	Written off by the State	Total
Delaware	$ 7,932	$ -	$ -	$ 7,932
District of Columbia	1,407,069	-	b/174,818	1,581,887
Idaho	195,577	143,425	-	339,002
Maryland	4,557,808	4,670,064	4,476,070	13,703,942
Oregon	1,419,283	187,446	-	1,606,729
Virginia	1,762,924	30,480	-	1,793,404
Washington	1,965,212	c/1,000,000	b/19,728	2,984,940
West Virginia	1,019,980	-	-	1,019,980
Total	$12,335,785	$6,031,415	$4,670,616	$23,037,816

a/Overpayments are defined as all payments made to providers which should not have been made whether such payments are due to provider or program error, fraud, abuse, or other.

b/Related to bankrupt health care institutions.

c/Estimated by the State since no records were available.

Of the $23 million, the Federal share is about $12 million. Based on the average 3-month U.S. Treasury bill interest rate of 11.63 percent, the interest cost to the Federal Government of these funds would be about $3,800 per day. The collection process can take months or years.

Most of the States we reviewed generally had overpayments outstanding for 1 year or less, and in some instances, partial payments were received. However, Maryland has had uncollected overpayments in the provider appeal process since 1968 with overpayments identified in each suceeding year. In some instances, providers go out of business or declare bankruptcy before appeals are resolved or collections are made.

In our June 10, 1980, report, we noted the three different views concerning when the Government should receive credit for its share of identified overpayments. These views involved States crediting the Federal share of overpayments

--immediately upon identification;

--after overpayment findings, contested by the provider, are sustained by State administrative hearings or appeal procedures; and

--after the overpayments are recovered.

Most guidance on the recovery of overpayments supports an immediate refund of the Federal share of overpayments. The Federal regulation (45 CFR 201.66) indicates that States should immediately repay the Government for unallowed expenses claimed under various assistance programs, including Medicaid. Repayment in installments is allowed when the amount due exceeds 2-1/2 percent of the estimated annual State share of allowable program expenses. Normally the amount due does not exceed the 2-1/2-percent limit.

Arguments have been made for each of these views, but the common practice is to withhold credit of the Federal share until after overpayments are recovered. HCFA continues to implicitly accept this view because it does not generally require States to refund the Federal share of uncollected overpayments.

THE TIME ALLOWED STATES TO RETURN THE FEDERAL SHARE OF CASH COLLECTIONS IS LIBERAL

When overpayments are collected, there is often a long delay in returning the Federal share of cash collections. This delay costs the Government money.

States can collect Medicaid overpayments (1) by offset to current provider billings and (2) by cash collections from providers. Overpayments collected by offset to provider bills often result in timely recovery of the Federal share because the need to draw down Federal funds, under the letter-of-credit payment system, is reduced immediately unless the overpayment is greater than the provider's current billings. However, State cash collections of overpayments do not immediately reduce the amount of Federal funds drawn down because these collections frequently are not returned for a long time. The States reviewed properly reported cash collections on the appropriate statement of quarterly expenditures. But, reporting cash collections under current Federal requirements does not reduce the grant award until the second quarter following the reporting of collections because that is the quarter in which the grant award is reduced due to the reported overpayment recovery. Therefore, a delay of up to 180 days (with an average of 135 days) can occur before the amount of Federal money

available for draw down is reduced and the Federal share of cash collections is returned.

This practice, although in accordance with Federal regulations, is costing the Federal Government the interest it pays on borrowed funds. Also, the Federal Government does not receive the interest earned by the States on collected funds. States generally invest moneys available, including cash collections of overpayments, and may invest this money in Federal securities. Therefore, the Government would pay interest to the States on Federal money. For example, in Washington, cash collections of overpayments during the period from July 1979 through June 1980 amounted to about $2.6 million. A State official accepted our estimate that funds remain with the State an average of 135 days until the Federal share is returned. Interest earned by the State on these funds would amount to about $113,000 at the 11.63-percent Treasury bill rate. We see no reason why States should be permitted to retain the interest earned on the Federal share of these cash collections. If the cash collections were returned by the State immediately, the amount of funds the Government had to borrow would have been reduced and the savings would have been about $56,000 at the Treasury bill rate of 11.63 percent.

CONCLUSIONS

In three of the States we visited, banks invested for their benefit the deposit balance on Medicaid and other State and Federal funds. We believe that a requirement, similar to Medicare's requirement for its paying agents, is needed to preclude banks' benefiting from the interest earned on State and Federal Medicaid funds.

States were also earning substantial interest income by investing Federal funds held by the States but not immediately needed. Under the Intergovernmental Cooperation Act, States are permitted to keep this interest, but it does not appear that the Congress meant for States to obtain such large earnings. There is a need for both the Federal and State governments to better monitor State draw downs to minimize the amount of Federal funds being held by States. HHS has acted to improve cash management in the 10 largest States, but we believe action is necessary for other States.

States were not writing off uncashed checks for extended periods, which resulted in the States holding and earning interest on Federal money for several years. Also, it appeared that the Government was not receiving its share of funds for uncashed checks when they were written off. HCFA needs to work with the

States to make sure that checks are written off sooner and the Federal share returned when they are written off.

In the States we visited, about $23 million in substantiated and potential Medicaid overpayments to providers had not been collected and the Federal share had not been returned. The collection process can take months or years at a substantial imputed cost to the Federal Government. Our June 10, 1980, report found the same conditions in other States and recommended that HHS prescribe standards for State Medicaid overpayment recovery systems. The findings in this report further substantiate the need for HHS to implement our prior recommendation.

States currently retain the Federal share of recovered overpayments, and all interest earned by investing such recoveries for an average of 135 days. We believe this is an unnecessarily long period and that it results in substantial imputed costs to the Federal Government. We believe HHS should modify its procedures to have the Federal share of Medicaid recoveries returned immediately.

RECOMMENDATIONS

We recommend that you direct the Administrator of HCFA to:

--Require States or their fiscal agents to have written agreements with the banks used for Medicaid checks, which ensure that Medicaid checking services are obtained at reasonable costs considering both bank charges and the ability of banks to invest deposit balances.

--Establish procedures for uniform crediting of the Federal share of uncashed Medicaid checks and ensure that such credits are timely and accurate.

--Review Medicaid cash management practices in all States (except the 10 largest where actions are currently underway) and take appropriate actions to minimize the amount of Federal money being held by the States.

--Modify the procedures through which the Federal share of recovered Medicaid overpayments are returned to eliminate the long elapsed time between recovery and return of the Federal share.

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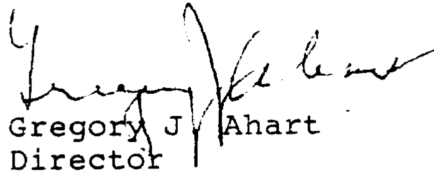
As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House Committee on Government Operations and the Senate Committee on Governmental Affairs not later than 60 days after the date of this report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

Copies of this report are being sent to the above-mentioned committees, the Director, Office of Management and Budget; the Inspector General of HHS; the Administrator of HCFA; and other interested parties.

Sincerely yours,



Gregory J. Ahart
Director