

**Department of Health and Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF MEDICARE PAYMENTS  
FOR BENEFICIARIES WITH  
INSTITUTIONAL STATUS**

**PACIFICARE OF ARIZONA  
PHOENIX, ARIZONA**



**JUNE GIBBS BROWN**  
Inspector General

**JUNE 1998**  
A-05-97-00017

# ***Office of Inspector General***

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**DEPARTMENT OF HEALTH AND HUMAN SERVICES**

**REGION V  
105 W. ADAMS ST.  
CHICAGO, ILLINOIS 60603-6201**

**OFFICE OF  
INSPECTOR GENERAL**

June 24, 1998

Common Identification Number: A-05-97-00017

Steve Lindstrom, President/CEO  
PacifiCare of Arizona  
410 North 44" Street  
Phoenix, Arizona 85072-2078

Dear Mr. Lindstrom:

This final report provides the results of our audit entitled, "Review of Medicare Payments for Beneficiaries with Institutional Status." Our objective was to determine if capitation payments to PacifiCare of Arizona (formerly FHP) under Medicare risk contract H0303 were appropriate for beneficiaries reported as institutionalized.

We determined PacifiCare received Medicare overpayments totaling \$8,941 for 13 beneficiaries incorrectly classified as institutionalized. The 13 beneficiaries were part of a statistical sample of 100 Medicare beneficiaries reported as institutionalized during the period October 1, 1994 through September 30, 1996. Based on our sample results, we estimate that PacifiCare received Medicare overpayments of at least \$100,173 for beneficiaries incorrectly classified as institutionalized during the audit period.

## **INTRODUCTION**

### **BACKGROUND**

In February 1997, PacifiCare Health Systems acquired FHP International. FHP had participated as a Medicare risk-based health maintenance organization (HMO) in Arizona under contract H0303 since 1986. An HMO is a legal entity that provides or arranges for basic health services for its enrolled members. An HMO can contract with the Health Care Financing Administration (HCFA) to provide medical services to Medicare beneficiaries. Medicare beneficiaries enrolled in risk based HMOs receive all services covered by Parts A and B of the program.

Under risk-based contracts, HCFA makes monthly advance payments to HMOs at the per capita rate set for each enrolled beneficiary. The rates are set at 95 percent of the expected fee-for-service costs that would have been incurred by Medicare had beneficiaries not enrolled in HMOs.

A higher capitation rate is paid for risk-based HMO enrollees who are institutionalized. Requirements for institutional status are met if a Medicare beneficiary has been a resident of a nursing home, sanatorium, rest home, convalescent home, long-term care hospital or domiciliary home for a minimum of 30 consecutive days immediately prior to the first day of

domiciliary home for a minimum of 30 consecutive days immediately prior to the first day of the current reporting month. Risk contract HMOs are required to submit to HCFA each month a list of enrollees meeting the institutional status requirements. The advance payments received by HMOs each month are subsequently adjusted to reflect the enhanced reimbursement for institutional status. For example, during 1996 HMOs received a monthly advance payment of \$513 for each non-Medicaid female beneficiary, 85 years of age or older, residing in a non-institutional setting in Maricopa County, Arizona. The Medicare payment to HMOs for a similar beneficiary living in an institutional setting was \$889. The monthly advance payment of \$513 would have been adjusted to \$889 after the beneficiary was reported to HCFA as having institutional status.

## **SCOPE OF AUDIT**

Our audit was performed in accordance with generally accepted government auditing standards. The objective was to determine if capitation payments to PacifiCare were appropriate for beneficiaries reported as institutionalized. We also conducted a review of PacifiCare's internal controls, focusing on procedures for verifying the institutional status of Medicare beneficiaries.

A simple random sample of 100 was selected from a universe of 2,427 Medicare beneficiaries claimed as institutionalized by PacifiCare during the period October 1, 1994 through September 30, 1996. From PacifiCare, we obtained the names and addresses of the institutions in which the beneficiaries in the sample resided. Confirmation letters were sent to institutional facilities to verify that the sample beneficiaries were institutionalized for the periods PacifiCare reported to HCFA. Based on responses received from institutional facilities, we identified Medicare beneficiaries who were incorrectly claimed as having institutional status. For each incorrectly reported beneficiary, we calculated the Medicare overpayment by subtracting the non-institutional payment that PacifiCare should have received from the institutional payment actually received.

Using the overpayments identified in our sample, we projected the probable value of Medicare overpayments to the universe of beneficiaries. Details of our statistical sample and projection are shown in Appendix A.

Our field work was performed from February through September 1997 at PacifiCare offices in Phoenix, Arizona; HCFA offices in San Francisco, California; and our field office in Columbus, Ohio.

## **RESULTS OF AUDIT**

PacifiCare received overpayments totaling \$8,941 for 13 Medicare beneficiaries incorrectly classified as institutionalized. The 13 were part of a statistical sample of 100 Medicare beneficiaries claimed as institutionalized during the period October 1, 1994 through September 30, 1996. Based on our sample results, we estimate that PacifiCare received

Medicare overpayments of at least \$100,173 for beneficiaries incorrectly classified as institutionalized during the audit period.

## **MEDICARE OVERPAYMENTS**

Our review of PacifiCare records indicated the Medicare overpayments occurred for the following reasons.

- Prior to May 1995, PacifiCare's internal control procedures for verifying the institutional status of Medicare beneficiaries were inadequate.
- Inaccurate discharge dates provided by the institutional facilities caused PacifiCare to incorrectly claim beneficiaries as institutionalized.
- Due to a clerical error, an adjustment was never submitted to HCFA for an overpayment that was identified by PacifiCare prior to our review.

## **INTERNAL CONTROLS**

Prior to May 1995, PacifiCare did not have a viable internal control system to verify the accuracy of claims submitted to HCFA for institutionalized beneficiaries. The internal control procedures established at PacifiCare after May 1995 are adequate to verify the institutional residency of Medicare beneficiaries and thus, the accuracy of claims. The institutional status of each beneficiary is confirmed prior to submitting the monthly list of institutionalized members to HCFA. PacifiCare mails a list of beneficiaries to each institutional facility by the 12<sup>th</sup> day of each month. The mailed list includes all members the HMO believes are residents of the facility. The facility is asked if any of the beneficiaries were discharged and is instructed to return the completed list to PacifiCare by the 25<sup>th</sup> of the month. Institutional facilities that do not return the list of beneficiaries are contacted by telephone and asked to verify the residency of PacifiCare members. A list of beneficiaries who meet institutional status requirements is then submitted to HCFA.

In addition, each month PacifiCare conducts a retroactive review of beneficiaries who were previously claimed as institutional. The beneficiary discharge data obtained in the current month from the institutional facilities is matched against the lists of institutional beneficiaries submitted to HCFA in the past. This process identifies beneficiaries who were discharged from the institutional facilities in the previous month after the listings of beneficiaries had been returned to PacifiCare. For all Medicare overpayments identified through the retroactive review, PacifiCare submits adjustments to HCFA to reverse the incorrect institutional payments.

## **RECOMMENDATIONS**

We recommend that PacifiCare:

- Refund the overpayments identified through our review totaling \$8,941.
- Review the balance of the institutionalized beneficiary universe to identify and refund additional overpayments. We estimate total overpayments to be at least \$100,173.

## **AUDITEE COMMENTS AND OIG RESPONSES**

In a letter dated April 20, 1998, Konowiecki & Rank, Attorneys at Law, responded to our draft report on behalf of PacifiCare. Below, we have summarized key aspects of the response and, where applicable, have provided our additional comments. The complete response is included with this report as Appendix B.

### **1. ERRORS PRIOR TO MAY 1995**

#### **AUDITEE COMMENTS**

PacifiCare's representatives commented that the majority of the overpayments discovered during the audit occurred prior to May 1995. They stated that because aged data becomes difficult to verify, HCFA established a three year limitation period for making retroactive payment adjustments. Because of this policy, PacifiCare believes that HCFA cannot recover overpayments received prior to May 1995. In addition, PacifiCare believes that if it is held liable for the overpayments that occurred prior to May 1995, the error rate applicable to the period prior to May 1995 should be considered separately from the error rate for the period after April 1995. Last, PacifiCare's representatives stated that they had discovered data that disputes our identification of an overbilling for one beneficiary.

#### **OIG RESPONSE**

We agree that the majority of the overpayments identified during the audit occurred prior to May 1995. However, we disagree with PacifiCare regarding HCFA's ability to recover overpayments that occurred prior to May 1995. Regulations governing risk-based HMOs do not specify a time limit for recovery of Medicare overpayments. In order to ensure consistency across the Medicare program, HCFA issued a policy for recovering overpayments to HMOs based on the rules in effect for fee-for-service claims. The fee-for-service rules provide that when recovering Medicare overpayments, HCFA may go back three years from the year the overpayments were discovered if the provider was not at fault. If the provider was at fault, HCFA can go back four years in recovering overpayments.

PacifiCare's ineffective procedures for verifying the institutional status of beneficiaries, and resulting Medicare overpayments, were first discovered by HCFA during a review completed in April 1995. Based on the fee-for-service rules, we believe HCFA can recover Medicare

overpayments resulting from PacifiCare's inadequate verification procedures for at least three years prior to the date of their review in 1995.

We also disagree with PacifiCare representatives regarding the need to split the error rate into two periods. They did not provide any data or evidence that would cause us to change either our sampling appraisal or our audit conclusions.

Regarding the beneficiary for whom PacifiCare representatives discovered data that seems to refute our contention of overbilling, the additional data did not alter our conclusion that the beneficiary was incorrectly reported to HCFA as institutionalized. PacifiCare's representatives provided information indicating that the beneficiary was admitted to an institutional facility on October 9, 1994 and discharged on December 14, 1994. Although these dates are correct, we received a confirmation letter from the institution showing that the beneficiary was first discharged on October 17, 1994; was readmitted on December 5, 1994; and then was discharged again on December 14, 1994. Therefore the beneficiary had been incorrectly claimed as institutionalized for the month of December 1994. During the course of our field work, PacifiCare officials agreed with our determination.

## **2. INCONSISTENT DATA PROVIDED BY THE INSTITUTIONS**

### **AUDITEE COMMENTS**

PacifiCare's representatives agreed that inaccurate admission and discharge data received from institutional facilities resulted in beneficiaries being incorrectly reported to HCFA as institutionalized. Regarding the beneficiaries who were incorrectly claimed, PacifiCare stated that the original designation as institutionalized was correct for one beneficiary, however, PacifiCare had claimed institutional status for March 1996 rather than February 1996.

PacifiCare believes the other four cases of incorrect reporting due to inaccurate admission and discharge dates are insignificant because the institutional facilities may have also provided inaccurate residency data that caused underpayments by Medicare. In addition, PacifiCare believes the data we sampled is biased and they do not believe it is reasonable to statistically extrapolate our results to the institutionalized population.

### **OIG RESPONSE**

For the beneficiary in question, we determined that the institutional payment PacifiCare received for April 1996 was unallowable, not for March 1996 as stated in PacifiCare's comments. Therefore, no adjustment to our finding was necessary.

We do not believe that the remaining cases of incorrect reporting are insignificant. Our review focused on claims submitted by PacifiCare to HCFA requesting reimbursement at the institutional rate. It is PacifiCare's responsibility to submit accurate claims. We identified beneficiaries from our sample who were not institutionalized, resulting in Medicare overpayments. If PacifiCare has identified Medicare beneficiaries that should have been

claimed at the institutional rate, but were not, PacifiCare should work with HCFA to determine if submitting retroactive claims is allowable.

In addition, we believe that the data sampled is unbiased and that it is reasonable to project our results to the institutional population as a means of estimating total overpayments contained in the universe of institutional claims. All of the beneficiaries in this universe were claimed as institutionalized and the enhanced reimbursement rate was claimed and recovered by PacifiCare. We are not recommending that the amount of our estimate be refunded, rather we are recommending that PacifiCare review the remaining beneficiaries included in the universe (those other than the 100 we reviewed) and refund the exact amount of overpayments that are identified. Because we used the lower limit of our projection, the actual amount of overpayments may be considerably higher (see Appendix A for more details).

### **3. RETROSPECTIVE OVERPAYMENT ADJUSTMENT**

#### **AUDITEE COMMENTS**

PacifiCare stated that HCFA has adjusted one of the unallowable institutional payments identified during our audit.

#### **OIG RESPONSE**

We verified that HCFA has processed an adjustment submitted by PacifiCare to reverse one of the unallowable institutional payments identified in our draft report. We have amended our audit results to reflect the adjustment.

### **4. CLERICAL ERRORS**

#### **AUDITEE COMMENTS**

PacifiCare's representatives stated that they had obtained documentation to confirm that one beneficiary questioned by us had been correctly reported as institutionalized in January and February 1996.

#### **OIG RESPONSE**

For the beneficiary in question, we determined that PacifiCare had incorrectly classified the beneficiary as having institutional status during February and March 1996, not January and February 1996 as stated in PacifiCare's comments. Our determination was based on a confirmation letter received from a provider that stated the beneficiary had been discharged on January 5, 1996. Based on this confirmation letter, we determined that the beneficiary should not have been classified as institutionalized during February and March 1996 and, therefore, PacifiCare had received overpayments from Medicare. Furthermore, PacifiCare employees



informed us that they had contacted the provider and received the same admit and discharge dates that we had received through our confirmation letter.

## **5. GENERAL COMMENTS**

### **AUDITEE COMMENTS**

PacifiCare asserts that it has an accuracy rate for reporting institutionalized beneficiaries that is greater than 99.9 percent. Based on this rate, PacifiCare believes extrapolation of our audit findings is unwarranted and further investigation is unnecessary.

### **OIG RESPONSE**

From our sample of 100, we identified 13 beneficiaries who were incorrectly reported to HCFA as having institutional status. Using PacifiCare's method, this data equates to a 13 percent error rate in PacifiCare's reporting of institutionalized beneficiaries during the audit period.

Based on our sample results, we estimated that PacifiCare received Medicare overpayments totaling between \$100,173 and \$333,802 during our two year audit period. We believe that a full review of the institutionalized beneficiary universe is necessary so that all specific overpayments can be identified and refunded.

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Final determination as to actions taken on all matters reported will be made by the U. S. Department of Health and Human Services (HHS) action official named below. We request that you respond to the HHS action official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

In accordance with the principles of the Freedom of Information Act (Public Law 90-23), Office of Inspector General, Office of Audit Services reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act that the Department chooses to exercise. (See 45 CFR Part 5.)

To facilitate identification, please refer to Common Identification Number A-05-97-00017 in all correspondence relating to this report.

Sincerely yours,

A handwritten signature in black ink that reads "Paul Swanson". The signature is written in a cursive, flowing style.

Paul Swanson  
Regional Inspector General  
for Audit Services

**Direct Reply to HHS Action Official:**

Director, Office of Managed Care  
33-02-01  
7500 Security Boulevard  
Baltimore, Maryland 21244-1850

PACIFICARE OF ARIZONA

VARIABLE APPRAISAL OF STATISTICAL SAMPLE

Universe:	2,427
Sample Size:	100
Nonzero Items:	13
Value of Nonzero Items:	\$8,941
Mean:	89.41
Standard Deviation:	296.04
Standard Error:	28.99
Skewness:	4.72
Kurtosis:	29.33
Point Estimate:	\$216,988

Projection at the 90 Percent Confidence Level:

Lower Limit:	\$100,173
Upper Limit:	\$333,802
Precision Amount:	\$116,815
Precision Percent:	53.83%

**KONOWIECKI & RANK**  
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RONAN COHEN

April 20, 1998

**VIA FACSIMILE (614) 469-2518  
AND FEDERAL EXPRESS**

Mr. John Hagg  
HHS/OIG Office of Audit Services  
Two Nationwide Plaza, Suite 710  
280 North High Street  
Columbus, Ohio 43215

Re: *Response to Draft Audit Review of Medicare  
Payments for Beneficiaries with Institutionalized  
Status (A-05-97-00017)*

Dear Mr. Hagg:

We represent PacifiCare with respect to the above-referenced matter. On January 20, 1998, your office submitted a draft audit report (the "Report") to PacifiCare of Arizona, Inc., ("PacifiCare") outlining your "Review of Medicare Payments for Beneficiaries with Institutionalized Status" (CIN A-05-97-00017). In the Report, the auditors requested that PacifiCare respond to their findings. As confirmed in our letter dated February 20, 1998, the auditors granted PacifiCare an extension until April 20, 1998, to respond to the Report.

The auditors randomly selected 100 Medicare beneficiaries who were identified as having been institutionalized at some time during the two-year period from October 1, 1994, through September 30, 1996. From those 100 members, the auditors identified 14 members (or 24 member-months), in which the auditors determined PacifiCare was paid as if the members were institutionalized when the members did not meet the qualifications for institutional status.

The Report identifies three types of errors. We outline each of the categories and following each description, we provide PacifiCare's response.

**1. Errors Prior to May 1995.**

HCFA is limited in its ability to recover for overpayments prior to May 1995. As noted in the Report, PacifiCare reviewed and changed its reporting system in 1995. We note that of the 24 member months identified by the auditors for the two year period as overbilled, 18 member months (75% of the cases) occurred in the seven months prior to May 1995. (While the auditors identified only 17 member-months, we note that the overbilling for member 340425842A in March 1995 also falls into this category). Further, HCFA was aware of PacifiCare's reporting problems, and understood that there could be both overbilling and underbilling errors relating to PacifiCare's prior procedures. HCFA specifically required that PacifiCare review its reporting back to May 1995. HCFA also understood that aged data becomes difficult to verify, and therefore, established a three year limitation period for making retroactive adjustments. Accordingly, PacifiCare does not believe that its over or underbilling errors prior to May 1995 should be in question. If, arguendo, PacifiCare remains liable to HCFA for overbilling prior to May 1995, PacifiCare believes, that the error rate applicable to the period prior to May 1995 must be considered separately from the error rate subsequent to this date since it is evident that most of the overbillings after April 1995 were corrected. In addition, PacifiCare has discovered data which disputes the auditors contention of overbilling for Member 351147878A.

**2. Inconsistent Data Provided by the Institutions.**

PacifiCare's internal controls for confirming institutionalized status with the institutions are rigorous. PacifiCare has a system in place to confirm the institutional status of a member in which employees spend hours each month contacting each institution prior to designating a member to HCFA as institutionalized. The institutions are expected to provide accurate information regarding the status of the member as well as accurate discharge dates. However, because non-contracting institutions have little or no incentive to accurately report this data, there is room for error. Based upon the records the auditors provided, there were five cases in which the institutions provided different discharge dates to the auditors than were originally provided to PacifiCare. Two cases were prior to April 1995, two cases subsequent to April 1995 and one case, which spans both periods. (We have added Member 402303092A in this category).

Of these five cases, PacifiCare has determined that the original designation as institutionalized was correct for Member 289207796A, however, PacifiCare billed for March 1996 rather than February 1996. We believe that the remaining four cases are insignificant for three reasons: First, institutions have no incentive to bias the data. Thus, the inaccuracies are as likely to decrease the length of stay in the institution as they are to increase the length of stay. Second, the auditors sampled members for whom the institutionalized rate cell had been paid. Thus, they could only identify

overpayments, even though there are likely to be an equal number of underpayments. Finally, PacifiCare has already identified and reported overbilling errors in its retroactive review (as explained below). However, when PacifiCare identifies an underbilling, HCFA guidelines do not permit PacifiCare to retrospectively report the underbilling. Thus, while the actual data reported by the institutions is unbiased, both the data sampled as well as the retrospective reporting process are biased in favor of underbilling. Accordingly, while PacifiCare will notify HCFA of the overpayment for the specific member-months identified in the Report, we do not believe it is reasonable to statistically extrapolate from this result to the entire institutionalized population.

**3a. Failure to Process Retrospective Adjustments to Overpayments.**

PacifiCare is required to report the institutionalized status of a member to the Health Care Financing Administration ("HCFA") immediately following the month in question. Accordingly, some members who are in institutions at the time of reporting are reported as eligible for institutionalized status, even though they may leave the institution near the end of the month and therefore lose their eligibility. In order to correct the overbilling, PacifiCare provides HCFA with retrospective corrections for members for whom PacifiCare has overbilled.

Of the fourteen members identified as overbilled, one falls into this category. PacifiCare review has determined that HCFA has already adjusted the overbilling for member 527420882A, in December 1997, subsequent to the audit.

**3b. Clerical Errors.**

PacifiCare has obtained documentation to confirm that Member 340425842A was correctly reported as institutionalized in January and February 1996. However, PacifiCare believes that Member 477034259A was reported as overbilled as a result of a clerical error. PacifiCare has reported this member as overbilled. Nonetheless, this is the only member since May 1, 1995, that was misreported due to an error by PacifiCare. That means that out of a universe of 1700 member-months of members who were known to have been reported as institutionalized (17 months multiplied by 100 members), PacifiCare's implementation of its own procedures incorrectly reported only one member for one month. This equates to an exceptional 99.94% compliance level.

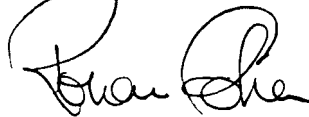
We welcome the opportunity to work with you to resolve any further questions that arise from your audit findings. We believe that the auditors conducted a very thorough audit and that as we have noted above, PacifiCare has a greater than 99.9%

Mr. John Hagg  
April 20, 1998  
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accuracy rate, and thus further investigation is unnecessary. In light of this, and notwithstanding that we believe that extrapolation from the audit findings as proposed by the auditors is unwarranted, we are willing to work toward a mutually satisfactory resolution of all the claims raised in the Report. Once you have reviewed our comments, please contact us at your earliest convenience. In the meantime, if you have any questions or require additional information, please do not hesitate to contact PacifiCare or me.

Sincerely,

KONOWEICKI & RANK

A handwritten signature in black ink, appearing to read "Ronan Cohen", written in a cursive style.

Ronan Cohen

cc JoAnn Spencer  
Debra Logan  
Patrick Ross  
Gretchen Smith