

Audit Report

Maryland Health Care Provider Rate Stabilization Fund

January 1, 2008 to December 31, 2008



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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Karl S. Aro
Executive Director

DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Bruce A. Myers, CPA
Legislative Auditor

March 6, 2009

Delegate Steven J. DeBoy, Sr., Co-Chair, Joint Audit Committee
Senator Verna L. Jones, Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland

Ladies and Gentlemen:

As required by the Insurance Article, Section 19-808 of the Annotated Code of Maryland, we have audited the receipts and disbursements of the Maryland Health Care Provider Rate Stabilization Fund for the period beginning January 1, 2008 and ending December 31, 2008.

The Fund is administered by the Commissioner of the Maryland Insurance Administration (MIA), and consists primarily of revenues generated by an annual premium tax imposed on health maintenance organizations and managed care organizations. The Fund serves several purposes, including retention of certain health care providers in the State by subsidizing their malpractice insurance premiums for a specified number of years, and by increasing certain rates paid to providers by the Maryland Medical Assistance program and payments to managed care organizations that serve that program.

Our audit did not include procedures designed to verify the propriety of the subsidy payments made to medical professional liability insurers since State law requires MIA to conduct annual audits of each insurer for this purpose. However, our audit again disclosed that these audits were not being completed on a timely basis.

A schedule of the Fund's financial activity for the 2008 calendar year is included in this report. As disclosed in that schedule, the Fund's cash balance was approximately \$63.5 million as of December 31, 2008.

MIA's response to this audit is included as an appendix to this report. We wish to acknowledge the cooperation extended to us during the course of this audit by MIA.

Respectfully submitted,

Bruce A. Myers, CPA
Legislative Auditor

Background Information

Establishment and Purpose of the Fund

The Insurance Article, Section 19-802 of the Annotated Code of Maryland established the Maryland Health Care Provider Rate Stabilization Fund effective April 1, 2005. The law provides that the Fund will serve several purposes, including retention of certain health care providers in the State by subsidizing their malpractice insurance premiums for a specified number of years, and by increasing fee-for-service rates paid to providers by the Maryland Medical Assistance program (Medicaid) and payments to managed care organizations that serve that program. The Fund is administered by the Commissioner of the Maryland Insurance Administration (MIA).

The Fund consists primarily of revenues generated by an annual premium tax imposed on health maintenance organizations and managed care organizations. All revenues are to be initially deposited into the Fund, and then allocated, in accordance with a schedule established in the law, to two accounts: the Rate Stabilization Account and the Medical Assistance Program Account. Amounts allocated to the Rate Stabilization Account are to be paid, in accordance with established criteria, to medical professional liability insurers who apply to MIA for rate subsidies on behalf of insured health care providers. Amounts allocated to the Medical Assistance Program Account are to be paid by MIA to the State's Department of Health and Mental Hygiene to increase payments to Medicaid providers and managed care organizations. The law provides that revenue allocations to the two accounts will continue through fiscal year 2009. Beginning in fiscal year 2010, all Fund revenues are to be allocated to the Medical Assistance Program Account.

Allocation of Balance in Rate Stabilization Account

Chapter 589, Laws of Maryland 2008 provided that \$83,275,000 of the balance remaining in the Rate Stabilization Account at the end of fiscal year 2008 shall be transferred as follows:

- \$7,000,000 to the State's Medical Assistance Program Account to be used to increase fee-for-service provider rates to dentists in fiscal year 2009,
- \$3,000,000 to the State's Health Care Coverage Fund established under Title 15, Subtitle 7 of the Health – General Article to be used for allowable expenses in fiscal year 2009, and

- \$73,275,000 to the Health Care Coverage Fund to be used for allowable expenses in fiscal years 2010 and 2011.

These transfers were made by MIA in October 2008 and are included in the payments made to the Department of Health and Mental Hygiene as reflected in the Summary of Financial Information on page 5.

Status of Findings From Preceding Audit Report

Our audit included a review to determine the status of the two findings contained in our preceding audit report dated March 10, 2008. We determined that MIA satisfactorily addressed one of these findings. The remaining finding is repeated in this report.

Financial Information

On page 5 is a summary of the receipts and disbursements for the Maryland Health Care Provider Rate Stabilization Fund for the period beginning January 1, 2008 and ending December 31, 2008, based on the State's accounting records. This summary is not intended to and does not provide the financial position and results of operations in accordance with generally accepted accounting principles. Specifically, certain financial statements and disclosures (for example, balance sheet, summary of significant accounting policies) have not been provided as would be required had this summary been prepared in accordance with generally accepted accounting principles.

SUMMARY OF FINANCIAL ACTIVITY

**January 1, 2008 to
December 31, 2008**

RECEIPTS:

Premium taxes	\$ 85,956,072
Premium tax exemption value ⁽¹⁾	9,286,956
Interest income	7,885,600

Total receipts	<u>103,128,628</u>
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DISBURSEMENTS:

Payments to medical professional liability insurers	10,014,570
Payments to Department of Health and Mental Hygiene	161,860,826
Administration expenses	375,125

Total disbursements	<u>172,250,521</u>
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EXCESS OF DISBURSEMENTS OVER RECEIPTS	(69,121,893)
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FUND BALANCE (cash basis), December 31, 2007	<u>132,586,897</u>
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FUND BALANCE (cash basis), December 31, 2008	<u><u>\$ 63,465,004</u></u>
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⁽¹⁾ Premium tax exemption value represents amounts paid by non-profit health maintenance organizations in lieu of premium taxes.

Findings and Recommendations

Audits

Finding 1

Required audits of applications submitted by insurers for subsidy payments were not completed on a timely basis.

Analysis

Required audits of application information submitted by medical professional liability insurers that applied for and received subsidies from the Fund were not completed on a timely basis. Such audits provide assurance that insurers properly calculated subsidy amounts due the insurers. We were advised that, as of February 2009, the Maryland Insurance Administration (MIA) had completed audits and issued final reports for just two of the four insurers who had applied for and received subsidy payments for subsidy year 2005, although responses to one of those reports had not yet been received from the applicable insurer. Audits of the other two insurers were in process.

Regarding subsidy year 2006, none of the audits of the five insurers who had applied for and received subsidy payments were completed, although a draft report had been issued for two of the insurers. According to MIA, audits of the remaining three insurers had not yet been started. MIA also advised us that it was not practical to start these audits because the insurers anticipate requesting additional subsidy year 2006 reimbursements. This condition was commented upon in our preceding audit report. Subsidy payments to insurers totaled \$8.8 million and \$13.3 million for subsidy years 2005 and 2006, respectively (excluding payments initially made to then returned by the Medical Mutual Liability Insurance Society of Maryland).

The law requires the Commissioner (or designee) to conduct an annual audit to verify application information submitted by each medical professional liability insurer that applied for a subsidy payment from the Fund for an applicable subsidy year. Since all participating insurers do not implement rate changes on the same date and often renew policies on a staggered basis throughout the year, the subsidy year for each insurer will vary and may not end for months after the end of the related calendar year (for example, subsidy year activity may not be completed for more than a year after the related calendar year). MIA policy provides that audits will begin as soon as practicable after the end of the insurer's subsidy year. Furthermore, MIA has advised that, although a particular subsidy year for an insurer may have ended, the audit of the insurer for that year cannot be started until all related financial activity, such as any final subsidy requests, for

the year has been completed. However, we question why MIA must wait until all subsidy applications are processed for a particular insurer and subsidy year before beginning their audit. Under these conditions, the audit of an insurer may be delayed for an indefinite period subsequent to the end of the subsidy year since there is no specific deadline as to when all financial activity for a subsidy year must be completed. We believe that MIA should complete these audits on a timely basis.

Recommendation 1

We again recommend that MIA complete audits of subsidy application information submitted by insurers on a timely basis, and take any appropriate follow-up action deemed necessary.

Audit Scope, Objectives, and Methodology

As required by the Insurance Article, Section 19-808 of the Annotated Code of Maryland, we have audited the receipts and disbursements of the Maryland Health Care Provider Rate Stabilization Fund for the period beginning January 1, 2008 and ending December 31, 2008. The Fund is administered by the Commissioner of the Maryland Insurance Administration (MIA). The audit was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objectives of this audit were to examine the Fund's receipts and disbursements and related records and internal control, and to evaluate compliance with applicable State laws, rules, and regulations. We also determined the status of the findings contained in our preceding audit report.

Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of the Fund's operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives.

MIA is required by law to annually audit each medical professional liability insurer that applied for a subsidy payment from the Fund to verify application information submitted by the insurer; accordingly, our audit did not include procedures designed to verify the propriety of the amounts requested by medical professional liability insurers and the disposition of such payments. As previously mentioned, our audit disclosed that these audits were not being completed on a timely basis.

Our audit did not include certain support services provided to the Fund by MIA. These support services (such as maintenance of accounting records and related fiscal functions) are included within the scope of our audit of MIA.

MIA's management is responsible for establishing and maintaining effective internal control over the Fund. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes a finding that we consider to be a significant deficiency in the design and operation of internal control that could adversely affect MIA's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. We also considered that finding to be a significant instance of noncompliance with applicable laws, rules, or regulations.

MIA's response to our finding and recommendation is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise MIA regarding the results of our review of its response.

APPENDIX

MARTIN O'MALLEY
Governor

ANTHONY G. BROWN
Lt. Governor



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RALPH S. TYLER
Commissioner

BETH SAMMIS
Deputy Commissioner

March 4, 2009

Bruce A. Myers, CPA, Legislative Auditor
State of Maryland
Office of Legislative Audits
State Office Building, Room 1202
301 West Preston Street
Baltimore, Maryland 21201

Dear Mr. Myers:

Please find enclosed the Maryland Insurance Administration (MIA) response to the draft audit report on the Maryland Health Care Provider Rate Stabilization Fund January 1, 2008 to December 31, 2008.

In addition to the enclosed hard copy of the response, an electronic version was sent to response@ola.state.md.us.

If you have any questions or need additional information, please contact Lester C. Schott, Associate Commissioner. His direct telephone number is (410) 468-2119.

Sincerely,

Ralph S. Tyler
Commissioner

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Enclosure

MIA Response to Findings and Recommendations

Finding 1

Required audits of applications submitted by insurers for subsidy payments were not completed on a timely basis.

Recommendation 1

We again recommend that MIA complete audits of subsidy application information submitted by insurers on a timely basis, and take any appropriate follow-up action deemed necessary.

MIA Response:

We agree with the auditor's recommendation that the audits be completed timely, and that appropriate follow-up action be taken.

Section 19-805(i) of the Insurance Article requires an annual audit to verify information submitted by a medical professional liability insurer applying for reimbursement from the Rate Stabilization Account. However, the law does not specify that the audits be conducted annually, or that the audits be conducted on any specific timeframe. As a practical matter, the audits cannot be efficiently conducted until all activity for a given subsidy year is complete. As the auditor acknowledges, the subsidy year for each insurer will vary, and may not end for months, or in some instances, more than a year after the end of related calendar year. It is our documented policy to start the audits of an insurer as soon as practicable after the end of the insurer's subsidy year. We intend to continue to follow our policy. Regarding subsidy year 2006, it is not practicable to start the audits for three of the insurers. As of February 10, 2009, these three insurers project that in the aggregate, they will be requesting additional subsidy year 2006 reimbursements totaling approximately \$127,000.¹

¹ **Auditor's Comment:** MIA acknowledges that audits should be completed timely but does not consider its audits of medical professional liability insurers to be untimely based on its audit policy. We question MIA's contention that audits cannot be efficiently conducted until all activity for a given subsidy year is complete. Since there is no specific deadline for insurers to request additional subsidies for a given year, the audits may be delayed for an undetermined period, regardless of how significant the additional requests might be as compared to amounts previously reimbursed. In the case cited by MIA, further 2006 subsidy reimbursement requests of \$127,000 are possible as compared to reimbursements already paid totaling \$13.3 million. Given the lack of a deadline, we believe MIA should not wait to initiate audits until all subsidy activity concludes.

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