Department of Health and Human Services

OFFICE OF INSPECTOR GENERAL

ILLINOIS' FEDERAL MEDICAID WITHDRAWALS WERE SUPPORTED BY NET EXPENDITURES FOR FISCAL YEARS 2010 THROUGH 2012

Inquiries about this report may be addressed to the Office of Public Affairs at Public.Affairs@oig.hhs.gov.

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Regional Inspector General
for Audit Services

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Office of Inspector General

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EXECUTIVE SUMMARY

For Federal fiscal years 2010 through 2012, the Federal funds that Illinois obtained were supported by net expenditures. However, Illinois overdrew Medicaid funds for most quarters and could not immediately pay back overdrawn funds.

WHY WE DID THIS REVIEW

To fund their Medicaid programs, States receive Federal grant awards that pay for the Federal share of their Medicaid medical and administrative expenditures. An external audit of the Federal fiscal year (FY) 2011 financial statements for the Centers for Medicare & Medicaid Services (CMS) determined that State Medicaid programs owed $1.3 billion to the Federal Government. This review is part of a series related to States' Federal Medicaid withdrawals.

The objective of this review was to determine whether Federal Medicaid funds that the Illinois Department of Healthcare and Family Services (State agency) obtained for FYs 2010 through 2012 were supported by net expenditures.

BACKGROUND

Before each quarter, States estimate their Medicaid expenditures. CMS uses the estimates to determine the initial grant awards, which are the Federal fund amounts that will be available to States during the quarter. If a State underestimates the amount of funds it will need during a quarter, it may request additional funds through a supplemental grant award.

The Payment Management System (PMS) is used to account for Medicaid financial activity. Throughout a quarter, States withdraw Federal funds from the PMS accounts to pay the Federal share of Medicaid expenditures. After the end of each quarter, States report expenditures and the associated Federal share on the Quarterly Medicaid Statement of Expenditures for the Medical Assistance Program (CMS-64 report). CMS calculates a finalized grant award amount for each State by comparing the initial and supplemental grant awards for the quarter to both the expenditures reported on the CMS-64 report and adjustments to those expenditures that were not included on the CMS-64 report.

After each quarter, the State agency performs a reconciliation to compare the total Federal funds withdrawn with the Federal share of net expenditures. If total Federal funds withdrawn are less than expenditures, the State agency increases future withdrawals. Conversely, if total Federal funds withdrawn exceed expenditures, the State agency reduces future withdrawals by the difference.

WHAT WE FOUND

The Federal funds totaling $23,303,834,479 that the State agency obtained for FYs 2010 through 2012 were supported by net expenditures. However, the State agency overdrew Medicaid funds from its main Medicaid PMS accounts for most quarters because its withdrawal methodology was imprecise. The State agency could not immediately repay the overdrawn amounts because the funds were used for purposes other than Medicaid. Rather, the State agency repaid the overdrawn amounts 2 to 6 months later. As a result, the Federal Government could have lost as much as $792,000 in interest.

Additionally, the State agency did not withdraw Federal funds from the appropriate PMS accounts because of a faulty procedure and other misclassifications. The withdrawals caused the balances in the accounts to be wrong, so the State agency had to transfer large amounts of Federal funds to correct those balances.

WHAT WE RECOMMEND

We recommend that the State agency:

- adjust its withdrawal methodology to ensure that Medicaid funds are withdrawn only for the Federal share of actual Medicaid expenditures and

- ensure that it withdraws funds from the appropriate PMS account.

STATE AGENCY COMMENTS

The State agency concurred with our recommendations.

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INTRODUCTION

WHY WE DID THIS REVIEW

To fund their Medicaid programs, States receive Federal grant awards that pay for the Federal share of their Medicaid medical and administrative expenditures. Before Federal fiscal year (FY) 2010, States had grant award accounts that combined the Medicaid funds from every year. Consequently, yearly balances were not distinguished. Beginning in FY 2010, the Centers for Medicare & Medicaid Services (CMS) implemented annualized accounts for grant awards that had beginning and ending balances to improve the transparency of Medicaid funding. As a part of the *CMS Financial Report Fiscal Year 2011,* an external audit of CMS's financial statements determined that State Medicaid programs owed $1.3 billion to the Federal Government.[1] This review is part of a series related to States' Federal Medicaid withdrawals.

OBJECTIVE

Our objective was to determine whether Federal Medicaid funds that the Illinois Department of Healthcare and Family Services (State agency) obtained for FYs 2010 through 2012 were supported by net expenditures.

BACKGROUND

Medicaid Program

The Medicaid program provides medical assistance to low-income individuals and individuals with disabilities. The Federal and State Governments jointly fund and administer the Medicaid program. At the Federal level, CMS administers the program. Each State administers its Medicaid program in accordance with a CMS-approved State plan. In Illinois, the State agency administers the Medicaid program. Although the State agency has considerable flexibility in designing and operating its Medicaid program, it must comply with applicable Federal requirements. The Federal Government pays its share of a State's Medicaid expenditures based on the Federal medical assistance percentage (FMAP), which varies depending on the State's relative per capita income.

Medicaid Funding Process

Before each quarter, States estimate their Medicaid expenditures and report the estimates to CMS on the quarterly Medicaid Program Budget Report (CMS-37 report). CMS uses the estimates to determine the initial grant awards, which are the Federal fund amounts that will be available to States during the quarter. If a State underestimates the amount of funds it will need during a quarter, it may request additional funds by submitting a revised CMS-37 report. The resulting increase in Federal funds is known as a supplemental grant award.

CMS provides the grant award amounts to the Division of Payment Management (DPM), a division within the U.S. Department of Health and Human Services, which operates as CMS's

[1] CMS, *CMS Financial Report Fiscal Year 2011*, Financial Section, Audit Reports, page 121.

fiscal intermediary. DPM uses the Payment Management System (PMS) to account for Medicaid financial activity, such as recording grant award amounts and processing the States' withdrawals. Beginning in FY 2010, CMS implemented annualized PMS accounts for the grant awards. As a result, each State has PMS accounts for each FY rather than combining the funds for multiple FYs.

Throughout a quarter, States withdraw Federal funds from the PMS accounts to pay the Federal share of Medicaid expenditures. Within 30 days after the end of each quarter, States report to CMS expenditures and the associated Federal share on the Quarterly Medicaid Statement of Expenditures for the Medical Assistance Program (CMS-64 report). The amounts that States report must represent actual expenditures.

CMS calculates a finalized grant award amount for each State by comparing the initial and supplemental grant awards for the quarter with expenditures reported on the CMS-64 report. CMS also includes in its calculation adjustments to expenditures that were not included on the CMS-64 report, such as interest due to CMS and expenditures that CMS disallowed. If a State's initial and supplemental grant awards are less than its expenditures, CMS increases the State's grant award. Conversely, if a State's initial and supplemental grant awards exceed its expenditures, CMS decreases the State's grant award by the difference.

The State Agency's Method for Withdrawing Federal Medicaid Funds

The State agency gathered actual and estimated expenditures for all of its programs, including Medicaid, the Children's Health Insurance Program, and solely State-funded programs. The State agency then withdrew funds for the actual and estimated expenditures from its main Medicaid PMS account. In an attempt to compensate for withdrawing for non-Medicaid expenditures, the State agency used lower estimated Federal share percentages, which ranged from 47.10 percent to 49.16 percent, rather than its actual FMAPs of 50 percent to 50.20 percent. The State agency deposited most withdrawn Federal Medicaid funds directly into the State's General Revenue Fund (GRF), which also included funds for such things as transportation, education, and pensions.

After each quarter, the State agency performed a reconciliation to compare the total Federal Medicaid funds withdrawn with the Federal share of net expenditures and identify any differences. If total Federal funds withdrawn were less than expenditures, the State agency increased future withdrawals to obtain the difference. Conversely, if total Federal funds withdrawn exceeded expenditures, the State agency reduced future withdrawals to return the difference.

HOW WE CONDUCTED THIS REVIEW

The State agency obtained $23,303,834,479 in Federal Medicaid funds for FYs 2010 through 2012 (i.e., October 1, 2009, through September 30, 2012). We compared the amounts that the State agency withdrew with the final amounts that CMS awarded for expenditures and reviewed the State agency's quarterly reconciliations.

We conducted this performance audit 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.

Appendix A contains the details of our audit scope and methodology.

FINDINGS

The Federal funds totaling $23,303,834,479 that the State agency obtained for FYs 2010 through 2012 were supported by net expenditures. However, the State agency overdrew Medicaid funds from its main Medicaid PMS accounts for most quarters because its withdrawal methodology was imprecise. The State agency could not immediately repay the overdrawn amounts because the funds were used for purposes other than Medicaid. Rather, the State agency repaid the overdrawn amounts 2 to 6 months later. As a result, the Federal Government could have lost as much as $792,000 in interest.

Additionally, the State agency did not withdraw Federal funds from the appropriate PMS accounts because of a faulty procedure and other misclassifications. The withdrawals caused the balances in the accounts to be wrong, so the State agency had to transfer large amounts of Federal funds to correct those balances.

THE STATE AGENCY CONSISTENTLY OVERDREW ITS NET EXPENDITURES

Sections 1903(a)(1) and (a)(7) of the Social Security Act make Federal financial participation available only for the total amount expended as medical assistance and for the proper and efficient administration of a CMS-approved State plan. Additionally, 42 CFR § 430.30(d)(3) authorizes the State to withdraw Federal funds as needed to pay the Federal share of Medicaid disbursements.

Also, a State must minimize the time that elapses between the transfer of funds from the United States Treasury and the State’s payout of funds for Federal assistance program purposes and limit the amount of funds transferred to the minimum required to meet a State’s actual and immediate cash needs (31 CFR §§ 205.11(a) and (b)).

The State agency consistently withdrew more Medicaid funds than were supported by net expenditures from its main Medicaid PMS accounts. During the 3 years we reviewed, the State agency’s withdrawals exceeded its expenditures by an average of $60 million a quarter, ranging from an underdrawn amount in one quarter of $28.6 million to an overdrawn amount in another quarter of $193.7 million. The following table shows the underdrawn or overdrawn amounts by quarter.

Table: Underdrawn or Overdrawn Amounts

FY	Quarter	Underdrawn or Overdrawn Amount[2]
2010	1st	$16,094,144
2010	2nd	(28,648,274)
2010	3rd	(12,730,470)
2010	4th	4,235,817
2011	1st	77,037,715
2011	2nd	79,310,273
2011	3rd	(6,755,407)
2011	4th	193,748,785
2012	1st	151,936,696
2012	2nd	85,006,236
2012	3rd	13,254,015
2012	4th	$146,909,486

The overdraws occurred because of the State agency's imprecise withdrawal methodology, which included withdrawing Medicaid funds for non-Medicaid expenditures, calculating the Federal share to be withdrawn on the basis of estimated Federal share percentages, and estimating some Medicaid expenditures.

The State agency recognized that it had overdrawn funds in its quarterly reconciliations. However, the State agency could not repay the overdrawn amounts immediately because the overdrawn funds were no longer in the GRF. According to a State agency official, the Illinois Comptroller spends all funds in the GRF without regard to matching revenues to expenditures. Therefore, the Illinois Comptroller used the overdrawn Medicaid funds to pay non-Medicaid expenditures because funds in the GRF were commingled.

Consequently, the State agency repaid the overdrawn amounts by decreasing Medicaid withdrawals from 2 to 6 months after the overdraws occurred. However, the State agency calculated the withdrawals that it decreased using the same imprecise withdrawal methodology. Therefore, the State agency continued to overdraw, while attempting to repay previously overdrawn funds. This created a perpetual "treadmill effect" because the State agency was usually in an overdrawn condition.

Because the funds were used for purposes other than Medicaid, the Federal Government lost the use of overdrawn funds. Additionally, the State agency was not required to pay interest on the

[2] Underdrawn amounts are shown in parentheses.

funds that it held for extended periods of time. For example purposes, we calculated the possible interest the Federal Government lost, which could have been as much as $792,000.[3]

THE STATE AGENCY DID NOT WITHDRAW FUNDS FROM THE APPROPRIATE ACCOUNTS

According to a CMS program official, States should withdraw funds from or return funds to the appropriate PMS account (i.e., the account for the FY in which the associated expenditures were reported).

The State agency did not always withdraw funds from the appropriate PMS accounts because of a faulty procedure and other misclassifications. On multiple occasions, the State agency withdrew Federal funds from 1 year's account to pay for a different year's expenditures. The following are descriptions of the misclassifications:

- The State agency adjusted for a quarter's reconciliation difference in a later quarter, so the adjustment for the last quarter in a FY was made using funds from the following FY's account.

- After the end of each FY, the State agency continued to withdraw funds from the previous year's accounts for expenditures reported in the new FY. CMS had not finalized the funds in the previous year's accounts, so the funds were still available.

- The State agency corrected errors made in its quarterly reconciliations when it discovered them. Many times, the discovery occurred after the close of the FY, and the State agency made those corrections in the following FY's account.

Although the withdrawals caused the account balances to be wrong, they did not result in monetary effects because the expenditures were simply misclassified. However, to correct those balances, the State agency had to transfer large amounts of Federal funds among its PMS accounts.

RECOMMENDATIONS

We recommend that the State agency:

- adjust its withdrawal methodology to ensure that Medicaid funds are withdrawn only for the Federal share of actual Medicaid expenditures and

- ensure that it withdraws funds from the appropriate PMS account.

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[3] We used annualized interest rates published by the U.S. Department of the Treasury (available online at www.fms.treas.gov/cmia/interest-13.html; accessed on April 25, 2014). Those rates ranged from 0.05 percent to 0.12 percent. The interest amount reflects only the possible interest lost because of the State agency's delayed return of overdrawn funds in its main Medicaid PMS accounts.

STATE AGENCY COMMENTS

The State agency concurred with our recommendations and described corrective actions that it had taken or planned to take. The State agency's comments appear in their entirety as Appendix B.

APPENDIX A: AUDIT SCOPE AND METHODOLOGY

SCOPE

The State agency obtained $23,303,834,479 in Federal Medicaid funds for FYs 2010 through 2012 (i.e., October 1, 2009, through September 30, 2012).

We limited our review of supporting documentation to records supporting the State agency's withdrawing of Federal funds; we did not evaluate the accuracy of the expenditures that the State agency reported on its CMS-64 report. Our objective did not require a review of the State agency's overall internal control structure. Therefore, we limited our internal control review to the State agency's procedures for withdrawing Federal Medicaid funds.

We conducted fieldwork at the State agency's offices in Springfield, Illinois.

METHODOLOGY

To accomplish our objective, we:

- reviewed applicable Federal laws and regulations;
- held discussions with CMS officials to gain an understanding of CMS guidance furnished to the State agency concerning the withdrawing of Federal funds;
- interviewed State agency officials to obtain an understanding of the State agency's policies and procedures for withdrawing Federal funds;
- analyzed the State agency's procedures for conducting quarterly reconciliations and reviewed those reconciliations;
- obtained and analyzed the PMS account detail, including grant award amounts and actual withdrawals that the State agency made;
- compared the grant award amounts in the PMS for each quarter with Medicaid grant award documents to ensure the accuracy of the PMS data;
- traced the amounts that CMS used to calculate the final grant award amounts for each quarter to the CMS-64 report;
- compared the State agency's documentation supporting its Federal Medicaid fund withdrawals to the withdrawals in the PMS;
- calculated the possible interest lost to the Federal Government; and
- discussed our results with the State agency.

We conducted this performance audit 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.

APPENDIX B: STATE AGENCY COMMENTS

ILLINOIS DEPARTMENT OF
Healthcare and
Family Services

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July 30, 2014

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Attn: Patricia Wheeler, Regional Inspector General for Audit Services
1100 Commerce Street, Room 632
Dallas, Texas 75242

Re: Draft Audit Report A-06-13-00032

Dear Ms. Wheeler:

Thank you for providing the opportunity to comment on your draft audit report entitled *"Illinois' Federal Medicaid Withdrawals Were Supported by Net Expenditures for Fiscal Years 2010 through 2012."*

The Department concurs with the recommendation. HFS is currently analyzing and reviewing our draw processes for FFY15 to reduce the amounts of overdraws and underdraws of federal Medicaid funds. The migration of a larger percentage of Medicaid recipients to managed care should allow for more consistent payment cycles and better estimates of the federal share of payments. Development of a new MMIS that will provide system generated federal share calculations is on-going. The expected date of implementation of the new MMIS is the fourth quarter of calendar 2017.

HFS modified our quarterly reconciliation process starting in FFY13 which should reduce the issues that led to the incorrect PMS accounts being used.

We appreciate the work completed by your audit team. If you have any questions or comments about our response to the audit, please contact Amy Lyons, External Audit Liaison, at (217) 557-0576 or through email at amy.lyons@illinois.gov.

Sincerely,

Julie Hamos
Director

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