

**STATE OFFICE OF RISK MANAGEMENT**  
Austin, Texas

**ANNUAL INTERNAL AUDIT REPORT**

Fiscal Year 2013



STATE OFFICE OF RISK MANAGEMENT  
Austin, Texas

Annual Internal Audit Report  
Fiscal Year 2013

TABLE OF CONTENTS

	Page <u>No.</u>
Internal Auditor's Report .....	1
Introduction .....	2
Internal Audit Objectives .....	3
Executive Summary	
Medical Cost Containment Unit	
Background .....	4-6
Audit Scope/Objective .....	7
I. Compliance with House Bill 16: Posting the Internal Audit Plan, Internal Audit Annual Reports and Other Audit Information on SORM's website.....	8
II. Internal Audit Plan for Fiscal Year 2013.....	8-9
III. Consulting and Nonaudit Services Completed.....	9
IV. External Quality Assurance Review .....	9
V. Observations/Findings and Recommendations .....	10-12
VI. Proposed Internal Audit Plan for Fiscal Year 2014 .....	12
VII. External Audit Services Procured in Fiscal Year 2013.....	13
VIII. Reporting Suspected Fraud and Abuse .....	13
IX. Organizational Chart .....	13

# Garza/Gonzalez & Associates

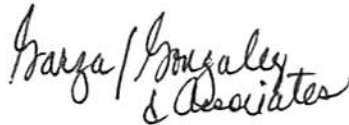
CERTIFIED PUBLIC ACCOUNTANTS

Audit Committee and Board Members  
State Office of Risk Management  
Austin, Texas

We performed tests of management's assertion about the effectiveness and efficiency of the internal control structure over the Medical Cost Containment Unit (MCCU) of the State Office of Risk Management (SORM) and its compliance with applicable state requirements and SORM's established policies and procedures for the year ended August 31, 2013.

The results of our tests disclosed that such controls were adequate and no material instances of noncompliance were noted; however, we noted a certain matter, which is included in this report, that is an opportunity for strengthening internal controls and operating efficiency; and, ensuring compliance with state requirements and SORM's established policies and procedures. We also performed a follow-up of the findings that were presented in the prior year annual internal audit report and this report reflects the implementation status of those matters; and, includes all information required for the Annual Internal Audit Report.

We have discussed the comment and recommendations from the MCCU audit; and, the implementation status from the follow-up performed, with various SORM personnel; and, will be pleased to discuss them in further detail; to perform an additional study of these matters; or, to assist you in implementing the recommendations.



June 28, 2013

**STATE OFFICE OF RISK MANAGEMENT**  
Annual Internal Audit Report  
Fiscal Year 2013

---

INTRODUCTION

The State Office of Risk Management (SORM) was created by House Bill 2133, 75<sup>th</sup> Legislature and became a state agency effective September 1, 1997. SORM was created from the merger of the Workers' Compensation Division of the Office of the Attorney General (OAG) and the Risk Management Division of the Texas Workers' Compensation Commission (TWCC), now the Division of Workers' Compensation at the Texas Department of Insurance (TDI).

SORM is charged by Texas Labor Code §412.011 to administer state risks and insurance services obtained by state agencies, including the government employees workers' compensation insurance program and the state risk management programs.

Some of SORM's statutory objectives and key functions are to:

- administer the workers' compensation insurance program for state employees established under Chapter 501;
- operate as a full-service risk manager and insurance manager for state agencies;
- maintain and review records of property, casualty, or liability insurance coverage purchased by or for state agencies;
- administer the program for the purchase of surety bonds for state officers and employees; and,
- review, verify, monitor, and approve risk management programs adopted by state agencies.

SORM's operations are governed by the Texas Labor Code, Chapters 412 and 501; and, by a five-member board, appointed by the Governor, that serves staggered terms.

**Internal Audit Plan for Fiscal Year 2013**

Following are the internal audits and other functions performed, as identified in SORM's approved 2013 Internal Audit Plan:

- Medical Cost Containment Unit
- Follow-up of Prior Year Internal Audits
- Other Tasks as Assigned by the Board or Audit Committee

This report contains the results of our audit of the Medical Cost Containment Unit area, reflects the follow-up performed in the current year, and meets the Annual Internal Audit Report requirements.

## STATE OFFICE OF RISK MANAGEMENT

Annual Internal Audit Report

Fiscal Year 2013

---

### INTERNAL AUDIT OBJECTIVES

In accordance with the **International Standards for the Professional Practice of Internal Auditing**, the audit scope encompassed the examination and evaluation of the adequacy and effectiveness of SORM's system of internal control and the quality of performance in carrying out assigned responsibilities. The audit scope included the following objectives:

- **Reliability and Integrity of Financial and Operational Information** – Review the reliability and integrity of financial and operating information and the means used to identify, measure, classify, and report such information.
- **Compliance with Policies, Procedures, Laws, Regulations, and Contracts** – Review the systems established to ensure compliance with those policies, procedures, laws, regulations, and contracts which could have a significant impact on operations and reports, and determine whether the organization is in compliance.
- **Safeguarding of Assets** – Review the means of safeguarding assets and, as appropriate, verify the existence of such assets.
- **Effectiveness and Efficiency of Operations and Programs** – Appraise the effectiveness and efficiency with which resources are employed.
- **Achievement of the Organization's Strategic Objectives** – Review operations or programs to ascertain whether results are consistent with established objectives and goals and whether the operations or programs are being carried out as planned.

## **STATE OFFICE OF RISK MANAGEMENT**

Annual Internal Audit Report

Fiscal Year 2013

---

### EXECUTIVE SUMMARY

#### **Medical Cost Containment Unit (MCCU)**

##### **Background**

The Claims Operations Division of the State Office of Risk Management (SORM) is comprised of claims units, the Customer Service Call Center, Quality Assurance Unit and the MCCU. The MCCU oversees the processing of medical and pharmacy bills on behalf of injured state employees. The scope of this audit was limited to the MCCU and the processing of medical bills.

The MCCU is managed by a Supervisor who reports to the Director of the Claims Operations Division. The MCCU is comprised of 4 Manual Adjudicators (Auditors); 2 Quality Assurers (QA); and one Administrative Supporter. All personnel in the MCCU are licensed claim adjusters who are also Official Disability Guidelines (ODG) Certified.

The MCCU is responsible for auditing and releasing funds for medical reimbursement claims (bills) in accordance with Title 28, Part 2, §133-134 of the Texas Administrative Code (TAC). These Chapters of the TAC are inclusive of the applicable Texas Insurance and Texas Labor codes which also govern the MCCU's practices.

SORM contracts with a cost containment vendor (CCV) to assist the MCCU in auditing and processing medical bills submitted for reimbursement. Medical bills are processed and reviewed within the Claims Maintenance System (CMS), which has built-in internal control edit checks that flag possible errors for review by the MCCU staff.

##### **Bill Process**

Bills may be received electronically, via mail, or facsimile and are reviewed by the Data Processing Unit (DPU) to ensure they are complete, according to the listing of required items, and a duplicate does not exist. The DPU will create a trailer sheet with an assigned SORM bill control number (SBCN) and scan all related documents (e.g. medical records) into the imaging system. This information is then prepared in a batch and prepared to be sent to the CCV. The trailer sheet, along with the medical bill and scanned documents are uploaded to a File Transfer Protocol (FTP) site which is used to transmit data to the CCV nightly.

The CCV performs its duties in auditing and processing the bill according to its contract. These duties include applying the appropriate fee schedule and treatment analysis. After the CCV has performed its review, it transmits the reviewed bills to the MCCU, who then imports the batched file into CMS.

## STATE OFFICE OF RISK MANAGEMENT

Annual Internal Audit Report

Fiscal Year 2013

---

Approximately 50 to 60 bills, which represent 30% of the bills, will 'error out' daily. Bills will automatically 'error out' based on built-in CMS edit checks that are programmed to detect bills with potential problems and require additional review by the MCCU auditors. For example, if information related to a bill corresponds to a previous bill within the claimant's file, it will automatically 'error out' since it could potentially be a duplicate item. Other common reasons for bills to automatically 'error out' include the following:

- Claimant's file is in "Inactive Status".
- The medical provider's profile has been flagged for close monitoring due to unusual billing patterns.
- The claimant's file has special instructions.
- A bill is \$5,000 or more.
- Total costs for the claim have exceeded the estimated amount.
- Barcodes or data do not match.

The bills that 'error out' are listed on an error report that is generated by CMS at the beginning of the day. The bills on the error report are listed in date order, from the oldest to the most recent, from the bill receipt date. The MCCU monitors these dates to ensure compliance with TAC §133.240 and §133.250, which requires that a new bill or a bill for reconsideration be processed within 45 and 30 days, respectively, from the respective claim date.

The 'error out' bills are assigned to the auditors, who perform an extensive review, research the potential error(s), and address them in accordance with written policies and procedures. Upon completion of their review of the bill and support documentation, the auditor will determine whether to pay or deny the bill. Should the auditor confirm an error or find discrepancies within the bill, the bill is either denied or further research will be conducted until a resolution is reached. To have the bill paid, the auditor enters the applicable override code(s), makes applicable notes in the claimant's file to ensure that the bill will not 'error out' again, and places the bill in 'ready to pay' (RTP) status. Once a bill is in RTP status, it is transmitted to the State Comptroller for payment, which generally occurs within 2 days. Currently, new bills take an average of 17 days to process (with a maximum time of 45 days) while reconsiderations take an average of 9 days (with a maximum time of 30 days).

### Quality Assurance (Post Error) Reviews

The MCCU quality assurance staff strives to conduct audit reviews on 20% of the bills that typically 'error out'. This audit review is referred to as the 'post error' review, which consists of the QAs reviewing the entire bill and support documentation to ensure the following:

- The appropriate action was taken by the MCCU auditors.
- The correct amount was disbursed according to the applicable fee schedules and treatment analysis.
- Treatment relatedness and necessity reported in CMS agrees with the bill support documentation.
- A SORM claims adjuster authorized the disbursement.
- The required auditing and processing controls were executed and documented.

Once the QAs complete their review, the results are documented in a Microsoft Access housed Audit Review Checklist and their findings are forwarded to the attention of the person responsible for the post error review. QAs monitor the respective bill until final action is taken.

## STATE OFFICE OF RISK MANAGEMENT

Annual Internal Audit Report

Fiscal Year 2013

---

Additionally, the QAs have a goal to conduct audit reviews on 30% of the bills that do not 'error out', which usually occurs after a bill has been paid.

### Monitoring Performance

Using Microsoft Excel, the QAs monitor the results from their audit reviews. Examples of results or data that are accumulated; include, error history patterns, overpayments, underpayments, work load allocation, bill processing turnover, and audit accuracy. The MCCU supervisor uses this information to generate an internal unit quarterly report that includes charts and graphs to reflect the MCCU's performance. This quarterly report also serves as an indicator for determining if core objectives of the MCCU are being met and for the supervisor to set goals for the following quarter.

During the period September 1, 2012 through June 30, 2013, QA staff performed 8,658 post audit reviews (i.e. bills that did not 'error out'). From these post audit reviews, QAs found \$114,161 in overpayments to health care providers. Once an overpayment has been identified, the MCCU staff will notify the healthcare provider of the overpayment and seek a refund. The healthcare provider will either repay the overpayment or file an appeal. If neither an appeal nor repayment occurs, the MCCU files a complaint with the TDI-DWC seeking their assistance in obtaining the refund.

### Fee and Medical Guidelines

The MCCU staff utilize fee schedules to compute one bill and ensure it agrees to the billed amount. Applicable fee schedules are posted online on the Medicare/Medicaid Services websites, or on the Texas Department of Insurance Division of Workers Compensation website.

The Official Disability Guidelines (ODG) is a catalog listing of numerous injuries that could typically occur in a workplace. For each injury listed in the ODG is a description of the injury, a benchmark of medical absence, other subsequent injuries associated, medical procedures and common treatments used to respond to those injuries.

SORM staff use the fee schedules and the ODG to measure and determine the following:

- Relatedness of injuries to the treatments itemized on the bill.
- Necessity of the treatment itemized on the bill.
- Necessity of pre-authorization for bills that include injuries not listed in the ODG.



## **STATE OFFICE OF RISK MANAGEMENT**

Annual Internal Audit Report

Fiscal Year 2013

---

### **Audit Scope/Objective**

The scope of our audit was the Medical Cost Containment Unit (MCCU) of the State Office of Risk Management (SORM). The objective of our audit was to gain an understanding of how the MCCU oversees and processes medical bills to determine whether the applicable statutes, rules, policies, and procedures are consistently applied.

The procedures performed to achieve the objective of our audit were as follows:

1. Reviewed and obtained an understanding of state requirements applicable to the MCCU; such as, those provided by the Texas Administrative Code and the Texas Department of Insurance, Division of Workers' Compensation.
2. Obtained and reviewed the MCCU's written policies and procedures, collected available documentation, and conducted interviews to document both formal and informal processes and controls.
3. Observed the performance of how the MCCU staff processes and audits a medical bill by performing the following:
  - a. Gained an understanding of the computer systems the MCCU uses to process a medical bill and how to generate specific information, data, or support documentation.
  - b. Reviewed the MS Access Checklist that Quality Assurers use to document their findings after their audit review.
  - c. Observed examples of how the MCCU staff obtains and applies fee schedules to compute and agree the billing amount on a bill.
4. Observed MCCU's process of ensuring the cost containment vendor's (Forte) compliance with significant contract terms and conditions.

## STATE OFFICE OF RISK MANAGEMENT

Annual Internal Audit Report

Fiscal Year 2013

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### I. Compliance with House Bill 16: Posting the Internal Audit Plan, Internal Audit Annual Report, and Other Audit Information on SORM's Website

To comply with the provisions of House Bill 16, within 30 days of approval by SORM's Board, SORM will post the following information on its website:

- An approved fiscal year 2014 audit plan, as provided by Texas Government Code, Section 2102.008.
- A fiscal year 2013 internal audit annual report, as required by Texas Government Code, Section 2102.009.

The internal audit annual report includes any weaknesses, deficiencies, wrongdoings, or other concerns raised by internal audits and other functions performed by the internal auditor as well as the summary of the action taken by SORM to address such concerns.

### II. Internal Audit Plan for Fiscal Year 2013

The Internal Audit Plan (Plan) included one audit to be performed during the 2013 fiscal year. The Plan also included a follow-up of the prior year audit recommendations, as applicable, other tasks as may be assigned by the Board or Audit Committee, and preparation of the Annual Internal Audit Report for fiscal year 2013.

#### Risk Assessment

Utilizing information obtained through the inquiries and background information reviewed, 15 audit areas were identified as potential audit topics. A risk analysis utilizing our 8 risk factors was completed for each individual audit topic and then compiled to develop an overall risk assessment.

Following are the results of the risk assessment performed for the 15 potential audit topics identified:

HIGH RISK	MODERATE RISK	LOW RISK
Medical Cost Containment Unit Information Resources	Lost Time Teams Unit Customer Service/Intake Unit Internal/External Training Procurement/HUB Compliance/Travel Payroll/Human Resources Fund Accounting Capital Assets	General Counsel Risk Management and Insurance Services Quality Assurance Unit Document Management/Records Retention Interagency Contract Assessments Performance Measures

## STATE OFFICE OF RISK MANAGEMENT

Annual Internal Audit Report

Fiscal Year 2013

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The area recommended for internal audit and other functions to be performed for fiscal year 2013 were as follows:

<u>Report No.</u>	<u>Audits/Report Titles</u>	<u>Completion Date</u>
1.	Medical Cost Containment Unit (MCCU)	6/28/2013
	Follow-Up of Prior Year Internal Audits	6/28/2013
	Other Tasks Assigned by the Board of Audit Committee	None

In the prior 3 years, the internal auditor performed the following audits and functions:

Fiscal Year 2012:

- Follow up of Prior Year Audit Recommendations
- Preparation of the Annual Internal Audit Report

Fiscal Year 2011:

- Subrogation Unit Audit

Fiscal Year 2010:

- Information Resources Audit

### III. Consulting and Nonaudit Services Completed

The internal auditor did not perform any consulting services, as defined in the Institute of Internal Audit Auditors' *International Standards for the Professional Practice of Internal Auditing* or any non-audit services, as defined in the *Government Auditing Standards, December 2011 Revision*, Sections 3.33-3.58.

### IV. External Quality Assurance Review

The internal audit department's most recent *System Review Report*, dated October 26, 2012, indicates that its system of quality control has been suitably designed and conforms with applicable professional standards in all material respects.

**STATE OFFICE OF RISK MANAGEMENT**  
 Annual Internal Audit Report  
 Fiscal Year 2013

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**V. Observations/Findings and Recommendations**

Report No.	Report Date	Name of Report	Observations/ Findings and Recommendations	Current Status (Fully Implemented, Substantially Implemented, Incomplete/ Ongoing, or Not Implemented) with brief description if not yet implemented	Fiscal Impact/Other Impact
1	6/28/2013	Medical Cost Containment Unit	<p><u>Managing Overpayments</u></p> <p>1. For the period September 1, 2012 through June 30, 2013, there were 333 overpayments to health care providers totaling \$114,161. Of the 333 overpayments that occurred during this period, 45 were recovered while 66 were filed as complaints with the Texas Department of Insurance. Recovery of overpayments during this period totaled \$17,776, which may have resulted from overpayments during this period or from prior periods.</p> <p>These overpayments are generally discovered by the 2 MCCU quality assurance staff, whose goal is to review approximately 30% of non-error claims after payment has been made. However, the estimated percentage reviewed, was closer to 15% as a result having only one quality assurance staff person for half the year.</p> <p><b>Recommendation</b>          We recommend the MCCU determine the total amount of outstanding overpayments and consider the following to increase the efficiency and effectiveness in managing overpayments:</p> <ul style="list-style-type: none"> <li>• Cross-train MCCU personnel to audit a greater percentage of bills, which could result in additional cost savings.</li> <li>• Integrate a system into CMS that will track outstanding overpayment receivables, or utilize an alternate method to monitor the aging of outstanding overpayment receivables to increase the likelihood of recovery by the 45<sup>th</sup> day from the (SORM) refund request date.</li> <li>• File complaints more frequently with the TDI-DWC in an effort to receive refunds in a more timely manner.</li> </ul>		Increase the amount of recoupment for overpayments.

**STATE OFFICE OF RISK MANAGEMENT**  
 Annual Internal Audit Report  
 Fiscal Year 2013

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Report No.	Report Date	Name of Report	Observations/ Findings and Recommendations	Current Status (Fully Implemented, Substantially Implemented, Incomplete/ Ongoing, or Not Implemented) with brief description if not yet implemented	Fiscal Impact/Other Impact
1	6/28/2013	Medical Cost Containment Unit	<p><b>Management's Response</b></p> <ul style="list-style-type: none"> <li>• SORM has hired an additional staff member to assist in post-payment bill review. Additional self-identified structural and process improvements under analysis for future implementation.</li> <li>• SORM is currently in the early stages of re-designing and updating the Claims Management System. SORM will explore the feasibility of including a tracking system as described.</li> <li>• The number of complaints filed against health care providers that do not issue timely refunds has been increased. Additional self-identified structural and process improvements under analysis for future implementation.</li> </ul>		

**STATE OFFICE OF RISK MANAGEMENT**  
 Annual Internal Audit Report  
 Fiscal Year 2013

Report No.	Report Date	Name of Report	Observations/ Findings and Recommendations	Current Status (Fully Implemented, Substantially Implemented, Incomplete/Ongoing, or Not Implemented) with brief description if not yet implemented	Fiscal Impact/Other Impact
	6/28/2013	2013 Follow-Up	<p><u>Follow-Up of Prior Year Audits</u></p> <p>Following is the status of the recommendations made in previous fiscal years that had not been fully implemented.</p> <p><u>Document Management/Records Retention</u></p> <p>1. Records Retention</p> <ul style="list-style-type: none"> <li>• Perform a comprehensive inventory of records generated and maintained, both onsite and offsite, and revise the Schedule accordingly.</li> <li>• Develop a process, to include a disposition log/form, to ensure records maintained and stored, in any medium; such as, microfilmed and the Filenet data system, are disposed in accordance with the Schedule.</li> </ul> <p><u>Information Resources (IR)</u></p> <p>1. Policies and Procedures</p> <p>Perform a comparison of the security policies recommended by the TAC to SORM's written policies and procedures to ensure that sufficient written policies and procedures are documented and implemented.</p>	<p><b>Incomplete/Ongoing</b></p> <p>Primary inventory and schedule revisions complete. Policy and procedures revised and in implementation phase.</p> <p><b>Substantially Implemented</b></p> <p>The IR department has reviewed and updated all IR policies and procedures and is in the process of comparing the security policies recommended by the TAC to the existing SORM policies.</p>	<p>Comprehensive Records Retention Schedule and compliance with Records Retention program requirements.</p> <p>Ensure that policies and procedures are adequately documented.</p>

**VI. Proposed Internal Audit Plan for Fiscal Year 2014**

The risk assessment performed during the 2013 fiscal year was used to identify the following *proposed* areas and functions that are recommended for inclusion in the internal audit plan for fiscal year 2014. The Internal Audit Plan for fiscal year 2014 will be developed and presented to the Audit Committee and Board at a meeting to be determined at a later date.

- Procurement/HUB Compliance/Travel
- Follow-up of Prior Year Internal Audits
- Other Tasks Assigned by the Audit Committee or Board

**VII. External Audit Services Procured in Fiscal Year 2013**

SORM procured the internal audit services documented in the Internal Audit Plan for fiscal year 2013.

**VIII. Reporting Suspected Fraud and Abuse**

SORM has provided information on its home page on how to report suspected fraud, waste, and abuse to the State Auditor’s Office (SAO) by posting a link to the SAO’s fraud hotline. SORM has also developed a Fraud Policy that provides information on how to report suspected fraud, waste, and abuse to the SAO.

**IX. Organizational Chart**

