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**Department of Health and Senior Services
Division of Senior Benefits and
Utilization Management
Medical Services for the Aged
Nursing Homes**

July 1, 2007 to December 31, 2008

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President of the Senate

The Honorable Joseph J. Roberts, Jr.
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Enclosed is our report on the audit of the Department of Health and Senior Services, Division of Senior Benefits and Utilization Management, Medical Services for the Aged, Nursing Homes for the period of July 1, 2007 to December 31, 2008. If you would like a personal briefing, please call me at (609) 292-3700.

A handwritten signature in cursive script that reads "Stephen M. Eells".

Stephen M. Eells
Assistant State Auditor
March 31, 2009

Table of Contents

	Page
Scope	1
Objectives	1
Methodology	2
Conclusions	2
Findings and Recommendations	
Acuity Audits	4
Cost Recoveries	5
Rate Setting	6
Provider Relations	8
Potential Cost Savings	
Therapeutic Leave	10
Auditee Response	11

**Department of Health and Senior Services
Division of Senior Benefits and Utilization Management
Medical Services for the Aged
Nursing Homes**

Scope

We have completed an audit of the Department of Health and Senior Services, Division of Senior Benefits and Utilization Management, Medical Services for the Aged, Nursing Homes for the period July 1, 2007 to December 31, 2008. The audit included financial activities accounted for in the state's General Fund. Expenditures are funded by the federal government and recoveries are shared with the federal government at a 50 percent rate. The fiscal year 2008 state and federal expenditures for this program were \$1.7 billion.

The mission of the department is to foster accessible health and senior services of the highest quality for all people in New Jersey to ensure optimal health, dignity, and independence. Our scope included payments made to nursing homes for Medicaid eligible patient days. Claims are submitted to a vendor which serves as the state's Medicaid fiscal agent. Most claims are submitted electronically. Payments are based upon a per diem rate that is calculated annually by the division's rate setting unit on an Excel application that was developed in-house. Although we did not review this system to determine the accuracy of the rate calculation, we did review components of the calculation.

Objectives

The objective of our audit was to determine the propriety of payments to nursing homes by reviewing components reported to the division for use in calculating the nursing home per diem rates. We also tested for resolution of significant conditions noted in our prior report dated October 24, 2002.

This audit was conducted pursuant to the State Auditor's responsibilities as set forth in Article VII, Section I, Paragraph 6 of the State

Constitution and Title 52 of the New Jersey Statutes.

Methodology

Our audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Additional guidance for conduct of the audit was provided by Control Objectives for Information and Related Technology (CobiT) issued by the Information System Audit and Control Foundation.

In preparation for our testing, we studied legislation, administrative code, and policies and procedures of the agency. Provisions that we considered significant were documented and compliance with those requirements was verified by interview, observation, and through our samples of financial transactions. We also read the budget message, reviewed financial trends, and interviewed agency personnel to obtain an understanding of the program and internal controls.

A nonstatistical sampling approach was used. Our samples of financial transactions were designed to provide conclusions about the validity of transactions as well as internal control and compliance attributes. Transactions were judgmentally selected for testing. The components of the rate setting calculation reviewed and tested included the acuties reported by nursing homes and the Medicaid occupancy level which is used to determine if a reduced per diem rate is applicable.

To ascertain the status of findings included in our prior report, we identified corrective action taken by the division and walked through or performed tests on the system to determine if the corrective action was effective.

Conclusions

We found that the payments to the nursing homes included in our testing were related to the division's program, were reasonable, and were re-

corded properly in the accounting system. In making this determination, we noted internal control weaknesses related to components of the per diem rate calculation, cost recoveries, and Provider Relations activities meriting management's attention. We also found that the agency has resolved the significant issues noted in our prior report.

Acuity Audits

**The division should
reinstate the acuity audit
function.**

Additional nursing services, commonly referred to as acuities, are provided when a patient requires trachea tubes, intravenous therapy, wound care, oxygen therapy, and tube feeding or additional care due to head trauma or respiratory condition. The numbers of acuities for a calendar year are reported to the division and ultimately are reflected in the nursing home's subsequent year per diem calculation. In the past, audits of a nursing home's reported acuity services had been performed by the professional nursing staff of the department as part of a cost report audit. Agency personnel stated that these audits had resulted in the greatest amounts recovered due to overstatement of acuities. Due to the vacancy in the nursing staff position these audits have not been performed by the department since 2005. The only records the division could provide were from fiscal year 2005 when eight acuity audits were performed. Four of these audits identified overpayments totaling \$424,000 for an average of \$53,000 per audit.

We performed two acuity tests at 11 nursing homes. The first test consisted of reviewing the support for all acuities for one month. The second test involved selecting individuals that had started and then completed the acuity treatment during a subsequent month. Our objective was to verify that the nursing homes had followed the regulations (N.J.A.C. 8:85-3.9) for inclusion of an acuity on their cost report. We found a seven percent error rate on our first test and a 26 percent error rate on the second. If the department had a nursing professional on staff performing these same tests, the error rates may even be higher because their expertise could identify and disallow additional services. We had the rate setting unit perform a recalculation on the two nursing homes with the largest error rates using our sample results which resulted in

overpayments of \$114,000 and \$48,000. Based on the department's information and our current acuity tests, it is important to resume the acuity audits since it is likely that they will result in significant recoveries.

Recommendation

We recommend that the division seek the professional staffing necessary to perform acuity audits.

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Cost Recoveries

Increased efforts are needed to reduce the recalculation backlog.

Each year there are 40 full and 100 focus audits performed on nursing homes by a contract vendor. Audit adjustments may result in a reduction in a facility's per diem reimbursement rate. A recalculation of the per diem rate and the recovery calculation is performed by the rate setting unit and forwarded to the financial unit for recovery. Our review noted that due to a vacancy that existed in the unit there was a backlog in performing these per diem and recovery recalculations. The unit has begun the process of calculating recoveries, but as of December 2008 there were 125 to be completed. We estimate this to be a six to nine month backlog at the current processing rate. The average recovery from the last eight months of recalculations is \$29,000. Applying this average to the remaining 125 to be recalculated would result in \$3.5 million in recoveries.

Procedures to strengthen internal controls should be implemented.

Our examination of the recovery process also disclosed internal control weaknesses. One individual is responsible for notifying the nursing home of their overpayment and maintaining a manual log of the notices. This person is also responsible for processing documentation to offset subsequent payments on the state's Medicaid fiscal agent system to recover the overpayment or receive checks if the nursing

home chooses this method of repayment. A report is prepared by this individual that identifies those homes which have satisfied their overpayment. The unit supervisor uses this report to relieve an informal accounts receivable report. However, during our review we noted that the accounts receivable report is incomplete. In addition, there is no independent reconciliation of the amount received to the calculated recovery.

Recommendation

We recommend that additional staff be trained to perform the recalculation function to alleviate the backlog and expedite the recovery process. A formal accounts receivable process should be established to facilitate an independent reconciliation of the amount to be recovered to collections.

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Rate Setting

The division needs to document the rate calculation process.

New Jersey reimburses nursing homes based on annual facility specific prospective per diem rates. In accordance with N.J.A.C. 8:85-3.2, nursing homes submit annual cost reports to the department's rate setting unit. These reports provide the information necessary to establish per diem rates. The fiscal year 2008 rates were calculated using calendar year 2006 cost reports. We did not perform a test of the rate calculation, although we did evaluate access and system controls.

The rate setting unit developed an Excel spreadsheet entitled the Excel Nursing Home Cost Report Workbook (ENHCRW) to perform the calculation beginning in fiscal year 2007. Our review disclosed that no supporting explanatory documentation as to how the formulas were developed or changed exists. This lack of documentation increases the risk that necessary changes to the ENHCRW or recovery of the application due to a disaster could not be

accomplished if the one individual currently responsible for the application was unavailable. Control Objectives for Information and Related Technology (CobiT) requires detailed system documentation be created during the development and maintenance process for all applications. The additional time and resources that would be needed to replace or upgrade an undocumented application could be greater than the time spent documenting the system.

The calculation errors should be corrected and resulting overpayments recovered.

Our audit noted several errors in the rate calculation that need to be corrected. The rate calculation includes an evaluation of the occupancy level of a nursing home to determine if they achieved 85 percent Medicaid occupancy. If the nursing home was below this occupancy level it would fall into a penalty phase which may result in a lower per diem rate. The ENHCRW did not correctly apply this penalty phase to the per diem rate calculation. Upon discovery of this problem, the rate setting unit recalculated the rates of those nursing homes affected resulting in a \$1.2 million recovery for fiscal year 2008. The division should review fiscal year 2007 and recalculate the effect of the penalty phase for those calculations.

In addition, we noted an input error in which the acuities were vastly overrecorded for one facility. This error resulted in a higher per diem rate which caused an overpayment of \$485,000. If there were edit checks for reasonableness in the ENHCRW the overrecorded acuities would have been identified.

Recommendation

We recommend the division develop documentation for the rate setting calculation (ENHCRW). The documentation should include information about the flow of data, descriptions of calculations in the ENHCRW, and other pertinent data. The ENHCRW should be corrected for the penalty phase condition and reasonableness edit checks should be

implemented to identify errors. The division should pursue any recoveries for any resulting overpayments.



Provider Relations

Procedures to strengthen internal controls should be implemented. The division should investigate the cost benefit of the system changes.

Provider Relations is responsible for collecting voluntary and change of ownership (CHOW) reimbursements. Voluntary reimbursements occur when a nursing home resident receives funds which would cause them to be ineligible to receive Medicaid benefits. The resident or their representative can make a voluntary reimbursement to the state which is used to offset Medicaid claims previously paid on their behalf. In most cases Provider Relations is contacted prior to any reimbursement and it researches the claims that have been paid by Medicaid for the resident. However, in some instances voluntary reimbursements arrive at Provider Relations without prior notice. The resident's claim file on the state's Medicaid fiscal agent system is not updated to reflect this reimbursement of previously paid Medicaid claims. This could lead to faulty research of claims in the event of subsequent voluntary reimbursements.

CHOW reimbursements are necessary due to the time it takes the licensing unit to establish a new provider number when a facility is sold. During this period, the new owner must operate and submit claims under the previous owner's number. Once a new provider number is established all claims submitted under the old number are voided. These claims are resubmitted under the new provider number which generates a second payment for the previously paid, now voided, claims. The state's Medicaid fiscal agent system does not recognize these as duplicates since the original claims are voided. However, the new owner has received payment twice.

Provider Relations maintains an accounts receivable for the voided claims and the new owner must make a reimbursement for those claims.

Voluntary and CHOW reimbursements are collected and deposited to state and federal accounts by Provider Relations. The unit has not developed sufficient procedures for these collections. They maintain a check log, but no reconciliations are performed. Procedures should ensure the safety of state and federal assets through regular reconciliations to confirm that all funds are properly deposited.

In fiscal year 2008 Provider Relations recorded \$3.5 million in voluntary reimbursements. We tested all of these deposits and found \$81,425 in errors that could have been identified and corrected if regular reconciliations were performed. Provider Relations recorded \$2.9 million in CHOW reimbursements. We were able to verify these deposits.

Recommendations

We recommend voluntary and change of ownership reimbursements be reconciled regularly. We also recommend that the unit research the deposit errors to ensure that they are deposited to the correct accounts. The department should consult with the state's Medicaid fiscal agent to determine if it is cost beneficial to upgrade the system to reflect voluntary reimbursements of Medicaid payments and eliminate the need for duplicate payments during the change of ownership process.

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Potential Cost Savings Therapeutic Leave

The division should consider treating therapeutic leave days the same as bed hold days.

Therapeutic leave, as per N.J.A.C. 8:85-1.14, is therapeutic or rehabilitative home and community visits with relatives and friends. Residents are permitted to take up to 24 days per year of therapy leave for which Medicaid pays the full per diem rate to the nursing home. During our field visits we found one facility was not recording the therapy days on the system billing documents. Their rationale was that they are paid at the same full daily rate anyway. Other facilities may be underreporting as well. Bed hold days, per appropriations language, are paid at 50 percent of the per diem rate if the facility meets the 90 percent Medicaid occupancy level. The therapy day payment could be reduced by \$1.4 million annually if they were paid at the same 50 percent rate.

Recommendations

We recommend the division investigate the effects of treating therapeutic days the same as bed holds for the purpose of payments to nursing homes and seek Centers for Medicare and Medicaid Services approval to implement this change.

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HEATHER HOWARD
Commissioner

March 30, 2009

Stephen M. Eells
Assistant State Auditor
Office of Legislative Services
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125 South Warren Street
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Dear Mr. Eells:

Thank you for the opportunity to submit comments on the audit report of the Department of Health and Senior Services, Division of Senior Benefits and Utilization Management, Medical Services for the Aged, Nursing Home Audit. I will submit the Department's comments in the order listed in your report.

Acuity Audits

State Auditor Recommendation: We recommend that the division seek professional staffing necessary to perform acuity audits.

DHSS Response: Staffing in the Nursing Facility Rate setting unit dropped from twenty-four (24) employees in January, 2006 to eleven (11) employees by January, 2008 (the period of this audit). Clinicians are needed to review charts and records to determine appropriate client acuity reporting. The State hiring freeze and the nursing shortage necessitated that the Department prioritize efforts towards core public health functions. Therefore DHSS chose to utilize the limited number of nursing staff for critical functions (such as facility inspections and complaints); as a result, the Department has been unable to continue to perform acuity audits. However, the Department is in the process of contracting with a private accounting firm, who will employ nurses, to perform acuity audits. The Department will then recalculate the nursing home rates and recover from nursing homes any additional Medicaid reimbursement for nursing costs that were overpaid as a result of inaccurate reporting of patient acuities.

Cost Recoveries

State Auditor Recommendation: We recommend that additional staff be trained to perform the recalculation function to alleviate the backlog and expedite the recovery process. A formal accounts receivable process should be established to facilitate an independent reconciliation of the amount to be recovered to collections.

DHSS Response: As noted previously, the Nursing Facility Rate Setting Unit had been operating with less than half staff during part of the time that is covered by this audit. Nursing home rates were not rebased in FY'09 which provided staff time to do recalculations over the last few months. As a result, the number of rates to be recalculated has dropped from 125 as of December 31, 2008 to 11 as of March 31, 2009. All 11 of the remaining facilities have extenuating circumstances for the delay at this point, including appraisals and open appeal issues. The open issues are anticipated to be resolved within 60 days. Funds recovered from rate recalculations FY'09 to date total \$3.2 million which is an increase from \$2.5 million in State Fiscal Year 2008.

The Department has implemented a procedural change which formalized the accounts receivable process and recommended reconciliation in accordance with OMB Circular 06-03 OMB State Non-tax Collection and Write-off.

Rate Setting

State Auditor Recommendation: We recommend the division develop documentation for the rate setting calculation (ENHCRW). The documentation should include information about the flow of data, descriptions of calculations in the ENHCRW, and other pertinent data. The ENHCRW should be corrected for the penalty phase condition and reasonableness edit checks should be implemented to identify errors. The division should pursue any recoveries for any resulting overpayments.

DHSS Response: This recommendation is not consistent with DHSS' long term strategy for managing nursing home rate setting. The utilization of the ENHCRW will be substantially reduced since nursing home rates will not be rebased in FY'09 or FY'10. A contractor has been hired to develop a new rate setting system and calculate rates effective FY'11. System documentation will be the responsibility of the new rate setting contractor. Therefore, it would not be an efficient use of DHSS' limited resources to hire the new staff that would be required to implement this recommendation.

Provider Relations

State Auditor Recommendation: We recommend voluntary and change of ownership reimbursements be reconciled regularly. We also recommend that the unit research the deposit errors to ensure that they are deposited to the correct accounts. The department should consult with the state's Medicaid fiscal agent to determine if it is cost beneficial to upgrade the system to reflect voluntary reimbursements of Medicaid payments during the change of ownership process.

DHSS Response: Staff reductions will make this difficult to accomplish, but reorganization of duties has already begun to address this issue. The Medicaid fiscal agent will be consulted for a cost estimate for the change of ownership process.

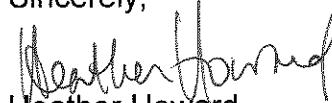
Potential Cost Savings Therapeutic Leave

State Auditor Recommendation: We recommend the division investigate the effects of treating therapeutic days the same as bed holds for the purpose of payments to nursing homes and seek Centers for Medicare and Medicaid Services approval to implement this change.

DHSS Response: The Department agrees with this State Auditor Recommendation and has determined that this initiative could generate approximately \$1.25 million (State and federal) in savings, but statutory authority is required for implementation.

I appreciate the opportunity to submit our DHSS Response to the audit State Auditor Recommendations. If you need further clarification, please feel free to contact me.

Sincerely,



Heather Howard
Commissioner