STATE OF WEST VIRGINIA

PRELIMINARY PERFORMANCE REVIEW OF THE

PUBLIC EMPLOYEES INSURANCE AGENCY

Contract Administration Procedures
Unclear, Reactive and Need Improvement

OFFICE OF LEGISLATIVE AUDITOR
Performance Evaluation and Research Division
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JOINT COMMITTEE ON GOVERNMENT OPERATIONS

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WEST VIRGINIA LEGISLATURE

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John Sylvia
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February 11, 2001

The Honorable Edwin J. Bowman
State Senate
129 West Circle Drive
Weirton, West Virginia 26062

The Honorable Vicki V. Douglas
House of Delegates
Building 1, Room E-213
1900 Kanawha Boulevard, East
Charleston, West Virginia 25305-0470

Dear Chairs:

Pursuant to the West Virginia Sunset Law, we are transmitting a *Preliminary Performance Review of the Public Employees Insurance Agency*, which will be presented to the Joint Committee on Government Operations on Sunday, February 11, 2001. The issue covered herein is *"Contract Administration Procedures Unclear, Reactive and Need Improvement."*

We delivered a draft copy of the report to the PEIA February 6, 2001. We received the agency response on February 9, 2001.

Let me know if you have any questions.

Sincerely,

John Sylvia

JS/wsc

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EXECUTIVE SUMMARY

This review focuses on the performance of PEIA's administration and oversight of third party administrator (TPA) contracts. Over the past five and a half fiscal years, PEIA has spent $64 million for professional and contractual services. This amount represents 77% of administrative expenses over this time. With such a large percentage of administrative costs dedicated to outsourcing important administrative functions, PEIA needs to provide adequate oversight of these contracts to ensure customer satisfaction. The finding of this review is that although there is evidence that the PEIA monitors its contracts, in some respects the oversight is reactionary, undocumented, and unclear. The effect of this is that a reactionary approach allows poor performance to exist for relatively long periods of time. Undocumented oversight presents problems in resolving disputes with vendors which could become a more serious problem if the dispute goes to court. Unclear oversight creates a problem for the agency when an individual is absent or leaves the agency and the employees' responsibilities cannot be easily assumed by someone else.

Based on our review, the contracts appear to be the only written document by which the PEIA employees have guidance in monitoring contracts and vendor performance. The Legislative Auditor found there to be few individuals within the agency delegated to vendor performance monitoring and contract compliance assurance. There are only three individuals who are specifically assigned to contract administration of the four contracts reviewed. Their abilities to monitor TPA performance are hindered since they also handle tasks that range from plan development to customer service. For example, the person assigned to monitoring the Claims Administration contract is also responsible for customer service for claims, the Retiree Premium Assistance program, and Life Insurance. The person assigned to monitoring the Pharmacy Benefits contract is also responsible for answering correspondence concerning prescription drugs and benefits, customer service for drug benefits, attend fairs and hearings, and act as a liaison between PEIA and contractors.

Our review noted evidence of the results of contract monitoring. However, in some cases it is unclear the method in which these results were accomplished and additional supporting documentation was not available. The outcome is that PEIA's allegations of deficient TPA performance can and have been disputed. Concern also lies in whether these results were from diligent contract administration or after the fact customer complaints of the contractor's performance.

In addition to internal monitoring of contracts, PEIA requires its third party administrators (TPA) to have an independent review (SAS 70's) of their internal controls annually. These reports are provided following the fiscal year and review the TPA's multiple control procedures in regards to claims processing, rebate processing services, eligibility files, etc. However, the meaningfulness of SAS 70 reviews of contractors' internal controls depends on the effectiveness of PEIA's internal controls. The SAS 70's noted were performed on TPA's that are no longer contracted with the PEIA, and the reports were submitted to PEIA subsequent to the expiration of the contracts. Therefore, SAS 70 audit's effectiveness is contingent upon PEIA's controls and whether the terms of the contracts are for one or multiple years.

Review Scope and Methodology

This review focuses on the issue of the PEIA's administration and oversight of third party administrator (TPA) contracts, specificness of the contracts regarding expectations. In reviewing contract administration, the focus was on the PEIA's procedures to ensure the TPA is performing as contracts dictate and are within specific performance standards. Key personnel within the PEIA responsible for contract administration were interviewed to obtain an understanding of the process. All reports submitted by the TPA's for the PEIA's review were also obtained and reviewed. All audit reports dealing with PEIA's contract administration were obtained and reviewed.

A list was obtained of current vendors performing contracted services for PEIA. The PEIA currently has 16 different contracted vendors performing services (See Appendix B). This list was reviewed to determine the importance of the service performed in relation to the PEIA's mission and the cost. Based on this review, we selected four of the services performed by TPA's for the PEIA over the past 3 fiscal years including 2001. They were as follows:

Contracted Service	TPA Name	Contract Term
Claims Administration	Mountain State BlueCross and BlueShield, Inc.	07/01/96 to 06/30/00
	Acordia National, Inc.	07/01/00 to current
Utilization Management	Mountain State BlueCross and BlueShield, Inc.	07/01/96 to 06/30/00
	International Rehabilitation Services, Inc. (dba Intracorp)	07/01/00 to current
Pharmacy Benefits Management	PCS Health Systems, Inc.	02/01/99 to 06/30/00
	Merck-Medco Managed Care, LLC	07/01/00 to current
Wellness Services	Partners in Corporate Health, Inc.	07/01/97 to current

Issue Area 1: Contract Administration Procedures Unclear, Reactive and Need Improvement.

A primary outcome for the PEIA is to provide health insurance to eligible individuals with the objective of achieving high customer and provider satisfaction, and administrative efficiency. The PEIA out-sources many crucial functions of the agency to private vendors through legal contracts. Since most of the functions associated with providing health insurance are carried out by private contractors, the PEIA must provide adequate oversight of the performance of its contractors to achieve the desired outcome. **The finding of this review is that although there is evidence that the PEIA monitors its contracts, in some respects the oversight is reactionary, undocumented, and unclear.** The effect of this is that a reactionary approach allows poor performance to exist for relatively long periods of time. Undocumented oversight presents problems in resolving disputes with vendors which could become a more serious problem if the dispute goes to court. Unclear oversight creates a problem for the agency when an individual is absent or leaves the agency and the employees' responsibilities cannot be easily assumed by someone else.

Over the past five and a half fiscal years, the PEIA has spent $64 million for professional and contractual services. This amount represents 77% of administrative expenses over this time (see Figure 1). In fiscal year 2000 for example, the PEIA reported $14.5 million in administrative and other operating expenses with contractual and professional payments representing $12.5 million of this amount. This calculation does not include claim expenses or pass through expenses for healthcare management organizations and life insurance premiums. This accentuates the importance of proper contract language, administration and oversight of vendor performance.

Overview of PEIA's Contract Administration

Based on our review, the contracts appear to be the only written document by which the PEIA employees have guidance in monitoring contracts and vendor performance. This is expected since the contracts drive what standards the vendor must adhere to and the expectations of all parties involved. However, these contracts are sometimes voluminous, full of legal jargon, and involve complicated calculations. The Legislative Auditor found there to be few individuals within the agency delegated to vendor performance monitoring and contract compliance assurance. There are only three individuals who are specifically assigned to contract administration of the four contracts reviewed. The task of contract administration is made more difficult because they also have other duties. They handle tasks that range from plan development to customer service. For example, the person assigned to monitoring the Claims Administration contract is also responsible for customer service for claims, the Retiree Premium Assistance program, and Life Insurance. The person assigned to monitoring the Pharmacy Benefits contract is also responsible for answering correspondence concerning prescription drugs and benefits, customer service for drug benefits, attend fairs and hearings, and act as a liaison between PEIA and contractors.

Our review noted evidence of the results of contract monitoring. Such evidence included the following:

1) A letter placing a vendor on notice of termination because of an unacceptably high backlog of claims.
2) A letter indicating that a guaranteed savings had not been fulfilled as required in the contract and the vendor still owed PEIA over $3 million.
3) A letter from the Pharmacy Benefits Administrator to the Chief Financial Officer ordering that a penalty be imposed on the vendor by not paying it half of the administrative fees due the contractor.
4) A document indicating termination of another contractor for alleged lack of adequate reporting, administrative guarantees were not made available, software not installed within the specified timeframe, and inadequate customer service.

However, in some cases it is unclear the method in which these results were accomplished and some supporting documentation was not available. Furthermore, in some cases the deficient performance of a vendor can be impacted by its predecessor, or the performance of another vendor for which it receives data. The result is that PEIA's claims of deficient performance can and have been disputed. Concern also lies in whether these results were from diligent contract administration or after the fact customer complaints of the contractor's performance. The latter is in the Legislative Auditor's opinion unacceptable. Table 1 below summarizes main concerns regarding contract administration within PEIA. We noted customer service satisfaction surveys were a part of one contract reviewed but the PEIA does not conduct them on their own.

Table 1 Concerns Regarding PEIA Contract Administration	
Concern	Benefits
Lack of agency wide, consistently applied written procedures for contract administration	▸ Further accountability with clearer summarized contract review guidelines ▸ Less risk of poor vendor performance unnoticed ▸ Record retention and organization ▸ Information management and utilization ▸ Pro active control vs. reactive ▸ No stop in contract oversight during personnel absence. ▸ Cross training for personnel when necessary
Lack of scheduling information received from Vendors	▸ To verify information received is timely, accurate and in compliance with contract stipulations. ▸ Allows for data storage for sorting, queries and trend development when necessary.
No verification procedures when providing TPA's crucial data	▸ Would assure the TPA is receiving correct information and reduce the risk that the PEIA is at fault when there are data problems. ▸ Reduce the risk of policyholders not receiving necessary coverage due to incorrect PEIA data.
Only one customer satisfaction survey conducted by PEIA in October 1996.	▸ This would provide insight as to customer satisfaction with TPA's service to compare with surveys conducted by TPA's

In addition to internal monitoring of contracts, PEIA requires its third party administrators (TPA) to have an independent review (SAS 70's) of their internal controls annually. The term "SAS 70" refers to the American Institute of Certified Public Accountants Statement on Auditing Standard number 70, "*Reports on the Processing of Transactions by Service Organizations*". These reports are provided following the fiscal year and review the TPA's multiple control procedures in regards to claims processing, rebate processing services, eligibility files, etc. However, the meaningfulness of SAS 70 reviews of contractors' internal controls depends on the effectiveness of PEIA's internal controls. The following passages are qualifying statements from two SAS 70's:

> *It is the customers responsibility, together with their auditors, to evaluate this information in relation to procedures in place at their organizations in order to assess the total operation of the controls. Further, if effective controls are not in place at the customer location, PCS' controls may not compensate for such*

weakness.[1]

The relative effectiveness and significance of specific controls at MSBCBC and MMO and their effect on assessments of control risk at the PEIA ***are dependent on their interaction with controls and other factors present at the PEIA.*** *We have performed no procedures to evaluate the effectiveness of controls at the PEIA.*[2]

Based on the above statements from the respective reports, it appears there is much required on the part of the user organization, PEIA. That is, PEIA must have sufficient controls to ensure the service organizations' controls reviewed in the reports are effective.

The passages above are noted because of problems experienced with the PEIA's eligibility system, the employee information administrative system (EIAS), and the TPA's systems. Specifically, TPA's claim their information systems have trouble interpreting EIAS data. This results in inaccuracies in plan membership. Based on our review, the PEIA did not have a procedure to assure their eligibility information was correct before submission to the TPA's. The "SAS 70" report performed on the PBM vendor had a section specifically testing the eligibility controls at the service entity. Within this section we noted the following which pertains to the PEIA:

User Control Considerations

Users are responsible for ensuring that transactions initiated by the user are appropriately authorized, complete, and accurate.

Users are responsible for ensuring that output reports received from PCS, are reviewed by appropriate user personnel for completeness and accuracy.

However, the only procedure noted at the PEIA for data accuracy was one in retrospect when policyholders or billed agency notifies PEIA of errors. In effect this makes the "SAS 70" less effective because, as the "SAS 70" stated, the controls in place at the service organization are reliant upon controls within the user's organization, PEIA. Also, in regards to the SAS 70 audits, it should be noted that these audits are performed at the end of a fiscal year. The SAS 70's noted above were performed on TPA's that are no longer contracted with the PEIA, and the reports were submitted to PEIA **subsequent to the expiration of the contracts.** Therefore, SAS 70 audit's effectiveness are contingent upon PEIA's controls and the terms of the contracts being multiple year. This is not to infer the reports aren't useful for single year plans, just less effective since modifications implemented due to audit findings would be of no value to the PEIA.

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[1] *PCS Health Systems, Service Auditor's Report Claims and Rebate Processing Review for the period July 1, 1999 to June 30, 2000*

[2] *Mountain State Blue Cross Blue Shield, PEIA Claims Processing System, Report on Controls Placed in Operation and Tests of Operating Effectiveness, for the period May 1, 1999 to April 30, 2000.*

Specific Examples of Contract Monitoring

As mentioned previously in the methodology section, the Legislative Auditor's Office reviewed contract monitoring for Pharmacy Benefits Management, Claims Administration, Utilization Management, and Wellness Services. The following sections are broken down per service contract type denoting key issues noted during the review.

Pharmacy Benefit Management (PBM)

Merck Medco, Inc. (Merck) Contract - July 1, 2000 to Current

The PBM performs the crucial role of providing prescription drug benefits to PEIA preferred provider benefit plan policyholders. These contracts tend to be of a very complicated nature due to the fact that there are many contingencies involved based on drug ingredient costs, manufacturer rebates and formularies.

Based on our review, it appears the contract for this service is specifically written to allow for specific performance measures to be monitored. Everything from what reports are to be provided and when, claim accuracy rates, response rates to inquiries and customer service telephone average speed of answer. However, what we were unable to observe was how PEIA tracked these.

Merck was awarded the PBM contract based on the PEIA's competitive bidding process as of July 1, 2000. Due to the short tenure of Merck as the PBM, the scope was limited. Additionally, the performance standards are based on annual performance. The performance standards in this contract are broken down in Table 2 below.

Table 2 **Performance Penalties**
$25,000 for a Contract Year if Telepaid System Availability Rate averages less than 99.5% for a Contract Year.
$25,000 for a Contract Year if Dispensing Accuracy Rate averages less than 99.99% for a Contract Year.
$25,000 for a Contract Year if Rx Services fails to meet the dispensing time period standards set forth in Section 5.5 of the Agreement measured on a Contract Year basis. The maximum penalty pursuant to this Section 10.1.3 is $25,000 per Contract Year.
$25,000 for a Contract Year if the Maintenance Identification Card Response Rate set forth in Section 5.7 of the Agreement is not met measured on a Contract Year basis.

Table 2 Performance Penalties
$25,000 for a Contract Year if the direct reimbursement paper claims' response rates of Section 5.11 of the Agreement are not met, measured on a Contract Year basis, subject to a maximum penalty pursuant to this Section 10.1.5 of $25,000 per Contract Year.
$25,000 for a Contract Year if the ASA of the customer service telephone line for any Contract Year averages more than thirty seconds measured on a Contract Year basis.
$25,000 for a Contract Year if the Telephone Abandonment Rate for a Contract Year averages more than 5% measured on a Contract Year basis.
$25,000 for a Contract Year if the Claims Adjudication Accuracy Rate averages less than 98% measured on a Contract Year basis.
$25,000 for a Contract Year if the Program Satisfaction Rate set forth in Section 5.13 of the Agreement is not met.
$25,000 for a Contract Year if the written correspondence response rates set forth in Sectio 5.9 is not met, measured on a Contract Year basis. The maximum penalty pursuant to this Section 10.1.10 is $25,000 per Contract Year.
$25,000 for each of the four most important implementation tasks (as agreed to by PEIA and PAID, in writing) which are not completed by the scheduled completion dates mutually agreed to by PEIA and PAID, in writing, provided PEIA and any applicable third party fully comply with all related implementation requirements, subject to a maximum penalty of $100,000.
$250 for each report which is not mailed within the applicable time periods set forth in Section 5.6 of the Agreement, subject to a maximum penalty of $10,000 per Contract Year.
$250 for each processable host to host, tape or floppy disc not processed by PAID within the time period set forth in Section 5.8 of the Agreement, subject to a maximum penalty of $10,000 per Contract Year.
$25,000 for a Contract Year that the retail pharmacy access guarantee of Section 5.14 is not met.

For this contract the focus was on the procedures to confirm receipt of information and monitor performance. We obtained the reports submitted by Merck and requested a description of how they were utilized and any supporting documentation. The PEIA had all reports submitted by Merck, but there was no documentation such as schedules showing whether these reports complied with the contract, were timely submitted and within contract parameters. Also, it was unclear how these reports are utilized by the Agency other than they were reviewed for any spikes in data and other specific items. The following items are reviewed by the PEIA monthly upon receipt of reports:

Total drug cost
PEIA paid amount
Member paid amount
Number of claims
Number of members
Amount paid per member
Plan cost share
Member cost share
Single-source, multi source, and generic distribution by claims and dollars
Retail usage
Mail order usage
Retail maintenance network usage

Once reviewed, any concerns are relayed to the PBM. It was disclosed to us that performance monitoring of the PBM is not a priority at this point since the performance standards are based on annual performance. However, the Legislative Auditor does not believe this relieves the PEIA from performance monitoring early in the contract. For instance, the bolded items within the Table 2 are items in which the PEIA can currently monitor the vendor's performance. This is especially true since this is a new PBM and there could be transitional problems that should be noted due to pro-active controls rather than reactive ones from customer or pharmacy (providers) complaints. Merck Medco meets regularly with PEIA and also attend the PEIA Finance Board Meetings.

Pharmacy Benefit Management (PBM)
PCS Health Systems, Inc. - February 1, 1999 to June 30, 2000

The PBM First Health, Inc.'s contract was bought out by PEIA for $550,000 in January 1999 with 33 months still remaining on the contract. First Health had been the PBM since 1991. This situation was covered at length by the Legislative Auditor's Office Post-audit Division in its May 21, 1999 PEIA Special Report (See Appendix B). In summary, PEIA bought out the contract because it believed it could save money with another TPA and receive better performance. This led to the contract being awarded to PCS in an "emergency award" since PCS was second in the contract bidding to First Health.

It was noted that the new PCS contract had a savings guarantee. This guarantee was stated as follows:

> For the 12 month period beginning February 1, 1999 (the "Guarantee Period"), **PCS Health Systems guarantees to the Customer a six million ($6,000,000) savings (the "Guarantee Amount") from the Sixty-eight million dollar ($68,000,000) the Agency projected to spend during the Guarantee Period, based on the Agency's current plan design and level of clinical management, and the assumptions set forth below**. PCS will reimburse the Agency for any non-administrative net plan cost, calculated as Customer's total drug spend for the Guarantee Period minus

deductibles minus copays minus Customer's Rebate share (the "Drug Spend"), which exceeds sixty-two million dollars ($62,000,000), dollar for dollar not to exceed the Guarantee Amount.

This contract with PCS ended June 30, 2000, yet there is still debate between the PEIA and PCS as to whether this guarantee had been fulfilled. This is due to the fact that the PEIA, subsequent to the initiation of the contract, made changes to the PEIA benefits plan. One change that caused problems was the amount of copays for policyholders. The original guarantee was for a plan with a $40 copay and the change made it a $25 copay. This created a problem because it changed how much was left to be paid by the PEIA affecting the drug spend amount and the guarantee.

PCS is of the opinion that it met the guarantee and the PEIA is of the opinion they did not. PEIA's actuary has made calculations to refute PCS' claims that the guarantee was met. Based on information assembled by the PEIA actuary, PCS still owes PEIA $3,072,586 in guaranteed savings. Per PCS however, it believes it covered the spending guarantee by $3,615,546.

The matters causing debate are due to actuarial adjustments for change in membership and the adjustment for plan changes initiated by PEIA July, September and November of 1999. PEIA has submitted it's actuarial adjustments to PCS to substantiate its claim. As of January 24, 2001, the matter is still being discussed. The guaranteed savings portion of the contract appears to disclose the necessary specifics as to how the reconciliation would be performed. PCS was to provide an estimated reconciliation prior to April 1, 2000 and a final reconciliation prior to September 1, 2000.

During our review of PCS reports there were no performance results reports from the TPA. This is in light of the contract having specific performance standards by which they must adhere. Table 3 discloses these below.

Table 3 PCS Contract Performance Guarantees
All Performance Penalties are 10% of Administrative Fees not to exceed 50% of total administrative fees for the plan year.
RECAP Help Desk - Telephone inquiries form contracted pharmacies will be answered, on average, in (45) seconds or less. 2% or less of all telephone inquiries will be abandoned. 2% or less of all telephone inquiries will be blocked.
PCS Mail Service Shipping - Prescriptions Not Requiring Intervention - 95% of all pharmacist-approved prescriptions requiring no Intervention will be shipped within 2 Business Days.
Client Services Administration Calls- Telephone inquiries during Normal Business Hours from customers will be answered on average in 30 seconds. Abandonment rate will be less than 4%.
Client Services Administration Implementation - PCS will implement customers on PCS' system as of the effective date of the agreement provided that PCS receives, within the time frames reasonably requested by PCS, complete and accurate implementation information from its customers, including, without limitation, any documents signed by its customers that PCS may reasonably request.
Claims Processing - Standard RECAP Processing - 100% of the claims submitted electronically through the RECAP System will be priced in accordance with customers plan guidelines.

Oddly enough, reporting deficiencies was one reason stated by the PEIA for buying out the previous PBM contract. At any rate, we were however provided with documentation stating that the performance penalty of half the annual administrative fee due PCS would be enforced because of multiple reasons (See Appendix C). This indicates there was some oversight of the TPA's performance, but the method it was accomplished, or determined is not known. **Although some items would have been difficult to document, the supporting documentation of these asserted performance problems was not provided. Additionally, the PEIA never made the information available to support these administrative fees were in fact withheld.** It is not our position that we do not believe these matters of performance assertions to be true. But, in the event legal action would be necessary against TPA's, we see inadequate documentation being a possible weakness in the States case.

We were able to confirm receipt of formulary rebates from the TPA and trace them to confirm deposit into a State fund. During fiscal year 2000, the PEIA received $2,477,873 in formulary rebates. Formulary rebates are kickbacks from drug manufacturers passed onto the customers by the PBM. It was noted that the PEIA controller tracked these rebates by making estimated receivables based on estimated receivable amounts provided. The PBM made formulary

rebate estimates known to the PEIA approximately a quarter of a year prior to the actual payment of the rebate.

Pharmacy Benefit Management Conclusion

The PEIA showed evidence of contract administration such as:

- Assertion that they had not received the correct guaranteed savings amounts
- Alleged enforcement of penalties upon the PBM
- Retention of PBM reports
- Independent SAS 70 audits required
- Receipt and deposit of formulary rebates.

However, there remain control weaknesses and areas for improvement in the PBM contract administration as far as performance monitoring. One cause for this in the opinion of the Legislative Auditor is the multiple responsibilities assigned to one individual. It was disclosed to us by the PEIA that during the 17 month term of the PCS contract, much of the time spent by the individual responsible for contract administration was devoted to developing a request for proposal for the next PBM bid process.

This task left little time for the necessary clerical work to assure the current PBM was performing up to standards. In addition, the work performed by the controller in contract administration is in addition to monthly production of the Agencies financial statements and other essential Agency accounting functions. Thus, the only individuals assigned to PBM contract administration appear to have plenty of duties already assigned which mostly have priority over tasks noted as lacking by this report.

At this time though, it would be highly difficult for the PEIA to efficiently place someone else in the position to handle these tasks. This is because there are no basic guidelines or procedures in which they could follow. The skill set for someone to come in and handle the current contracts without procedures would not be wise cost benefit management.

Additionally, due to the time necessary to develop an RFP subsequent to the emergency award, problems with PCS in lack of reporting and failure to obtain the guaranteed savings, it appears the contract buyout of First Health may not have been a sound decision. Especially since First Health made claims that PEIA's claims against their performance were unfounded. This would have saved the state the buyout money and the transitional problems resulting from the multiple PBM's in the past three years such as data exchange problems. It would also have allowed more time to develop the PBM RFP.

Claims Administration and Management

Mountain State Blue Cross Blue Cross Blue Shield (July 1, 1996-June 30, 2000)

The claims management TPA provides medical claims processing services for the PEIA Plan.

The contract for claims management stipulates performance measures for the TPA which are monitored by PEIA. The contract itself addresses that weekly, monthly and quarterly standard reports on the performance quality of the TPA duties are to be delivered from the TPA to PEIA. The content of the reports include such information as interest accumulation to providers, performance standards, physician payments and claims. **No consistent and permanent controls are currently in place monitoring claims management TPA's duties.**

In July 1996, PEIA contracted Mountain State Blue Cross Blue Shield to provide claims processing and utilization review for the agency. In July 2000, this contract was terminated and Acordia was contracted for claims processing and Intracorp was separately contracted for utilization review.

The contract for claims management TPAs is constructed establishing formulas for penalties and deadlines for reports due to PEIA. These reports and compliance standards from the TPA ensure that performance is accomplished. The agency personnel conclude that the MSBCBS contract was monitored through the contract language itself. However, the contract for MSBCBS does not provide procedural guidelines for PEIA personnel to follow in order to monitor the contract. The contract does not explain contract administration procedures for PEIA staff to maintain penalty controls and checklists for report/financial deadlines.

The MSBCBS contract stated specific performance standards. If these performance standards were not followed, a penalty was applied to MSBCBS (see Table 4).

Table 4 Penalty Calculations

Performance Measurements	Performance Standards	Rating	Penalty	Rating	Penalty
Financially Correct Claims Percentage (Q1)	98%	96%-98%	$0.35	less than 96%	$0.50
Financial Accuracy Percent (Q2)	At least 99.5%	96%-98%	$0.35	less than 96%	$0.50
Percent of Claims Finalized in 12 Working Days (T1)	At least 92%				$0.50
Telephone Calls Abandonment Percentage (A1)	2% or less				$0.25
Average Speed of Answer in Seconds (S1)	30 seconds or less				$0.25
Blockage Percentage on Calls (B1)	1% or less				$0.25

*Penalty amount is determined by multiplying the average number of members during the quarter by the rates described above.

If these performance standards were not met monthly, MSBCBS provided a penalty amount to PEIA which was deducted out of the administrative costs. For example, compliance reports and invoices indicate that for the months of April and May 1998 penalties totaling $15,418 were deducted from FY 1999 administrative expenses to MSBCBS for inadequate TPA performance of T1 (Timeliness Standard) and Q2 (Financial Accuracy Amount). The administration of these penalties included the manager of the MSBCBS contract sending correspondence to MSBCBS informing them of the penalty, a copy of which was sent to the PEIA finance entity to alert them of reduction in administration expenses for MSBCBS. PEIA was not able to provide the Legislative Auditor with FY 2000 penalty invoices. Moreover, there were no consistently applied checks in place to establish that these penalties were enforced and no communication between the financial entity of PEIA to the MSBCBS contract manger to confirm that financial penalties are enforced. With no written procedures in place describing how to monitor the penalty process or to ensure performance standards, there remains the possibility that MSBCBS was not charged correctly or at all for penalties. The lack of organization and controls over performance standards left PEIA with the possibility of MSBCBS providing poor performance without MSBCBS being penalized.

In December 1998, PEIA amended the contract with MSBCBS concerning penalties. The contract was amended to include incentives for MSBCBS on performance standards. This included the same performance standards that were set forth for penalties including Q1, Q2, T1, A1, S1 and B1. It was determined that PEIA would pay MSBCBS quarterly incentives for fulfilling these standards, whereas MSBCBS would pay PEIA quarterly penalties for not accomplishing the performance standards. This amendment is puzzling because MSBCBS should be doing its contracted performance of the contract to fulfill the contract and accept its end of the agreement for which they are being paid to do. The concept that MSBCBS was rewarded further through an incentive in the contract for a standard they should have done through the contract itself appears to be flawed. Invoices obtained by the Legislative Auditor show that for FY 2000 PEIA paid MSBCBS $336,724.73 in incentives. The PEIA did not provide invoices or evidence to prove whether or not the penalties inflicted on MSBCBS lesson or equaled the amount of incentives paid back to MSBCBS because PEIA cannot account for penalties charges to MSBCBS for FY 2000. The incentive performance standard provision was eliminated when Acordia was contracted in July 2000.

It is important to note that the contract manager for this contract has kept all performance standard reports from MSBCBS up to FY 1999 and provides spreadsheets to evaluate and document their performance. This system of contract documentation is developed and catered by the contract manager. This method works efficiently when the contract manager is present. However, at the time of this review, the contract manager was on leave. Because no written procedures exist on how to monitor the contract, the PEIA staff was at a loss to find contract documentation, reports and operational controls after FY 1999 for the contract. The staff was also unable to locate or provide information on performance standards for S1 (Speed of Answer) and B1 (Blockage Percentage on Calls). This individualization of contract controls leaves the agency in a position of vulnerability if the contract administrator absents the position.

MSBCBS was responsible for providing reports other than performance standards. The PEIA filed these reports. Examples include MSBCBS interest reports documenting interest paid to

providers from MSBCBS after the 65 day claim period and MSBCBS/PEIA operations weekly inventory reports detailing days payable for claims and billed charges. Utilization review, another contracted duty of MSBCBS was reviewed for performance by PEIA through MSBCBS Utilization Management Reports. These reports were filed and received by PEIA in accordance with the contract. However, there is no documentation showing how these reports were utilized by PEIA. The PEIA does not show documentation of whether the reports were submitted within timeliness or standard parameters set in the contract.

Acordia National, Inc. (July 1, 2000-present)

The PEIA awarded Acordia the claims management through the competitive bidding process effective July 1, 2000. The contract for Acordia is similar to the MSBCBS contract with the exception of utilization management. Due to the short period in which PEIA has obtained Acordia as the claims management TPA the scope was limited. The focus on the Acordia contract is limited to the monitoring procedures for transition between claims management TPAs.

The PEIA alleges that due to the transition between contracted TPAs, PEIA has not received reports necessary to review Acordia's performance to date. The explanation given by PEIA for lack of reporting is that Acordia has given most of their resources and staffing to deal with claims backlog. The PEIA has not received the reports data in order to evaluate Acordia's performance or apply penalties. (See Table 4 for performance and penalty standards.) This situation is being handled between Acordia and PEIA through weekly meetings to discuss claims backlog, customer service issues and reporting status from Acordia to PEIA. Acordia currently produces their monthly procedure claim reports and phone statistics for customer service. This appears to be the only documented monitoring procedures in place implemented by PEIA to manage the transition period.

There is evidence that PEIA has not been satisfied with Acordia's performance. The former director of the PEIA issued a letter to Acordia in November 27, 2000 providing notice that if Acordia did not resolve compliance issues set in the contract within sixty days then action would be taken *to protect the insureds of this program and taxpayers of the state of West Virginia.* This notice outlined a number of concerns over Acordia's performance including unacceptable claims backlog, no establishment of acceptable Eastern panhandle out-of-state network and member confusion over network providers. The PEIA was not able to provide the Legislative Auditor documentation confirming that Acordia is not meeting these requirements. The Acordia contract may be monitored retroactively through consumer complaints brought to PEIAs customer service. This is a plausible conclusion to make since there is no documentation of Acordia's performance. The monitoring of Acordia does not appear to be established pro-actively but rather in a reactive manner. It should be considered that PEIA come up with procedures to monitor and enforce the Acordia contract in order to provide performance standards, savings and quality due to PEIA when Acordia does not reach their contract requirements.

Wellness Program Contract

The PEIA is charged with the responsibility of providing a wellness program per §5-16-8(9) of the West Virginia Code. The wellness program is required to include plan incentives to discourage tobacco use, alcohol and chemical abuse and an educational program to encourage proper diet. This section also requires the PEIA to contract with county boards of education for the use of facilities, equipment or any service related to the wellness program. It was noted the PEIA had not contracted with any county boards of education for facility use. The PEIA received a glowing accommodation for its innovative program. This came in the way of an article in Business & Health (See Appendix C). The program is known as "Pathways to Wellness".

Partners in Corporate Health - July 1, 1997 to Current

PEIA contracted with Partners in Corporate Health to administer the wellness program. We obtained reports submitted by Partners in Corporate Health (PCH) that outline the accomplishments, goals, and effectiveness of the program. The Pathways website was also visited and all but two links on the site were functional and therefore operating effectively. PCH provides quarterly reports complete with handouts given at worksite activities, examples of the newsletters sent to the PEIA policyholders homes, various flyers, newsletters and brochures for various programs. These are kept on hand at the PEIA and the president meets with the PEIA weekly and makes presentations to the PEIA Finance Board on the programs accomplishments.

The Pathways to Wellness program provides a website, worksite activities such as health screenings, blood pressure screenings and other health promoting activities. The program conducts satisfaction surveys, compiles membership claim data and vital statistics. This information is then used to produce return on investment data to help evaluate the effectiveness of the program. It is also helpful in determining the average claim cost for low risk vs. high risk members. It was noted during the review of reports that PCH reported during Phase III the Pathways project was honored with the "Exemplary Public Worksite Wellness Program" Award by the National Association of Public Worksite Health Promotion.

The evolution of the PEIA wellness program has went through four phases since its inception in 1992. Phase IV was recently completed and although the final evaluation report hasn't been completed, PCH disclosed that there are now over 126 worksites as of January 2001 and over 10,000 enrolled. The worksites will soon total 230 in Phase V.

The program has also implemented a smokers cessation program that over it's time has had 3,590 medicaid enrollees and 827 PEIA enrollees. There is a telephone number that policyholders can reach the Pathways smokers cessation program by dialing 1-877-Y NOT-QUIT. The program also tabulates any prescriptions issued to aid in quitting. As of September 2000 the formal evaluation for the YNOTQUIT program had just begun. As of December 2000, the Quarterly Report had no mention of evaluation results for the smokers cessation program.

Wellness Contract Conclusion

The program is highly capable of producing numbers showing the programs activity, productivity and effectiveness. The Legislative Auditor inquired with the PEIA as to what procedures were in place to oversee this program and validate the program's figures in effectiveness. We also interviewed with a representative of PCH to gain further understanding of the evaluation process of the program. Outside of the reports submitted and the regular meetings it was disclosed to us there were no other means of verifying validity.

However, all reports submitted do include an example of an actual sign in sheet of an activity performed at worksites and an example of a survey form which had been performed, etc. So there is some proof of activities submitted in reports. The Legislative Auditor requested examples of source documents such as sign in sheets for activities and smoker cessation enrollment directly from PCH. PCH obliged our request and submitted these documents without delay along with explanations as to how they arrive at their ROI numbers. This is one method that takes little time to perform and is effective in making sample confirmations as to activity number verification.

The PEIA's smoker cessation program cost share for the 2000 program that extends to June 30, 2001 estimated costs total $203,473. The current Phase IV program for January 1, 2000 to June 30, 2001 will cost the State $977,922 in fixed cost and there will variable costs in addition to this based on activities performed by PCH not to exceed $190,000. In the event the Pathways program reaches the maximum allowable variable costing, there will be a total of $1,371,395 spent on these programs. Based on these budgeted cost figures, it appears validation procedures would be warranted.

Utilization Management Contracts

Utilization management is a crucial aspect of claims processing. This is the step in which certain medical procedures are scrutinized prior to application to determine the necessity and if this is the best procedure to perform. Medical care providers are given a list of procedures or situations that require prior review before it can be administered and honored by the PEIA. This process is known as pre-certification. Utilization management is a cost saving measure based on reducing unnecessary utilization of plan benefits. A segment of the section titled Duties of Intracorp in the contract states:

> *In exercising its responsibilities under this Agreement, Intracorp shall use its best efforts to assure that health care is provided to insureds with the least costly combination of services which are actually medically necessary without compromising or diminishing the quality of the health care or outcomes resulting from the health care delivered to the insureds.*

Intracorp - July 1, 2000 to current

Intracorp was awarded the utilization management through the competitive bidding process

as of July 1, 2000. The contract has specific performance measures, services and what reports are to be provided. In providing its service to the PEIA Intracorp utilizes licensed, board certified or eligible physicians, psychologists and counselors with graduate degrees in their specialties, and registered nurses employed or engaged by Intracorp. Intracorp performs its services in compliance with the PEIA plan document which is an attachment to the contract.

Based on our review, all reports were provided as dictated by the contract. The reports denoted any cost saving incurred by the PEIA due to utilization management. All performance reports were also provided.

It was disclosed to us verbally that the PEIA utilizes these reports by monitoring the percentage of approval for reviewed procedures. If, for example, a certain procedure is approved 100% of the time there is no need to continue reviewing this procedure. But, we weren't sure of this procedure's purpose since the current contract's billing is based on the number of eligible members and not per utilization review.

As with other contracts handled by the PEIA, Intracorp meets frequently with the PEIA staff. These meetings also include representatives of Acordia. This is due to the fact that there is a necessary relationship between the two entities. It is necessary for Acordia to sometimes wait for Intracorp's approval before some claims can be paid by Acordia. Since all current contracts were issued on the same day, July 1, 2000, there have many transitional problems occurring. It was noted that Acordia notes one of its reasons for high claim backlogs is due to the required interaction with Intracorp.

Mountain State BlueCross and BlueShield (MSBCBS) - July 1, 1996 to June 30, 2000

MSBCBS handled utilization review along with claims administration. We were able to obtain utilization reports for the period of July 1997 to December 1999. These reports were much more limited than the current utilization management vendor but did break down savings for the PEIA. The PEIA had a plan compliance review performed on MSBCBS for the period of January 1, 1998 to June 30, 1999.

One item focused on during this review was the utilization pre-certification process and other utilization processes performed by MSBCBS. This review noted exceptions in this process. For example, the review noted 16 claims submitted for claims processing were assigned a different diagnosis related group (DRG) category by the MSBCBS CAPS claims processing system than the DRG category assigned by the MSBCBS pre-certification system. The reviewing auditor's concern regarding this matter was that there was not a procedure in place during the precertification process to confirm the discharge DRG and communicate to the claims processors the appropriate DRG category to utilize during payment. Basically, the reviewing auditor's had concern regarding the effectiveness of the MSBCBS's utilization review.

Utilization Management Conclusion

Based on our review of the utilization management contract administration, the PEIA used an independent review of the utilization management vendor to monitor performance. This review was effective in helping determine that there were issues regarding the utilization management performed by MSBCBS and acted accordingly. MSBCBS did not specialize in this function and the PEIA now retains the services of a vendor that does in fact specializes in this field. Hopefully PEIA will in fact save the state money by making this move.

Internally however, the PEIA does not appear to have procedures for monitoring utilization management vendors other than the retention of reports submitted by the vendor. Utilization management is a crucial cost saving tool which could be used to help develop future cost efficient insurance plans if data received is utilized. Also, there were no procedures to verify all reports were received, timely and in accordance with the contracts.

Recommendation 1:

The PEIA should develop written procedures to monitor the performance of it's TPA's.

Recommendation 2:

The PEIA should reallocate personnel resources within the current PEIA staff to assist current personnel assigned contract administration. The position would assure all required data is received, performance standards met and maintain contact with finance and benefits administration personnel.

Recommendation 3:

The PEIA should develop procedures to ensure proper data transmissions with TPA's.

APPENDIX A

Transmittal Letter to Agency

WEST VIRGINIA LEGISLATURE

Performance Evaluation and Research Division

Building 1, Room W-314
1900 Kanawha Boulevard, East
Charleston, West Virginia 25305-0610
(304) 347-4890
(304) 347-4939 FAX

John Sylvia
Director

February 6, 2001

Tom Susman, Director
Public Employees Insurance Agency
Building 5, Room 1001
1900 Kanawha Blvd., East
Charleston, WV 25305

Dear Mr Susman:

Enclosed is the report on the PEIA which will be presented at the February Legislative Interims on February 11, 2001. I will inform you on the time and location of the interim meeting. Please review the enclosed report and contact us to schedule an exit conference for next week to discuss any concerns or factual errors.

Please provide your written response by noon Friday, February 9, 2001. If you have any questions give me a call.

Sincerely,

John Sylvia

John Sylvia

Joint Committee on Government and Finance

APPENDIX B

TPA Table

VENDOR NAME	DESCRIPTION OF SERVICES	AMOUNT SPENT AS OF DECEMBER 31, 2000
ACORDIA NATIONAL	HEALTH CLAIMS TPA SERVICES	$4,004,180
AIM HEALTHCARE	HOSPITAL AUDITS	48,347
BEACON RECOVERY GROUP	SUBROGATION SERVICES	33,119
BUREAU FOR MEDICAL SERVICES	HER SERVICES	8,791
CONSULTEC	ELECTRONIC CLAIM SUBMISSION	3,929
ERNST & YOUNG	FINANCIAL AUDIT	46,710
ERNST & YOUNG	ACTUARIAL SERVICES	119,923
INTRACORP	PRE-CERTIFICATION	1,164,794
KAY CASTO & CHANEY PLLC	LEGAL REPRESENTATION	633
M&M MAILING	MAILING SERVICES	5,897
MERCK-MEDCO	DRUG CLAIMS TPA SERVICES	416,062
MIKE MADALENA	DATABASE MGMT SERVICES	57,470
MOUNTAIN STATE BC/BS	HEALTH CLAIMS TPA SERVICES	162,343
NANCY LYNCH	TEMPORARY SERVICES	8,160
PARTNERS IN CORPORATE HEALTH	WELLNESS SERVICES	627,018
SUTTLE & STALNAKER	REVIEW OF PEIA PLAN DOC	61,500

APPENDIX C

Prescription Drug Contract

Prescription Drug Contract

During our examination, we learned that on January 13, 1999, PEIA terminated the prescription benefit management (PBM) agreement with their prescription claims processor, First Health Services Corporation (First Health) effective January 31, 1999 with provision for the payment of a "termination fee" totaling $550,000.00. Effective February 1, 1999, the prescription claims processor is PCS Health Systems, Inc.; however, our review of this contract and related correspondence indicate this agreement was awarded as an "emergency contract" and was not subject to competitive bidding in violation of Chapter 5, Article 16, Section 9 of the West Virginia Code, as amended, dealing with the authority of the PEIA to contract, which states in part,

> "...(e) The provisions of article three [§ 5A-3-1 et seq.], chapter five-a of this code, relating to the division of purchases of the department of finance and administration, shall not apply to any contracts for any

insurance coverage or professional services authorized to be executed under the provisions of this article. **Before entering into any contract for any insurance coverage, as herein authorized, said director shall invite competent bids from all qualified and licensed insurance companies or carriers, who may wish to offer plans for the insurance coverage desired....**" (Emphasis added)

We believe the provisions of Chapter 5, Article 16, Section 9 of the West Virginia Code, as amended, required PEIA to utilize competitive bidding with respect to any termination of the PBM contract and the awarding of a new contract for prescription claims processing. Therefore, any awarding of a contract for professional services without the benefit of solicitation of competent bids as required by the aforementioned provisions would in our opinion be in noncompliance with State law.

Our review shows the termination agreement with First Health stated in part,

"In consideration of the early termination of the PBM Agreement, PEIA agrees to pay to First Health (in addition to the Administrative Fee) the sum of Five Hundred Fifty Thousand Dollars and 00/100 (550,000) (the "Termination Fee"). As a primary source of payment of the Termination Fee, First Health shall make deductions from the portion of rebates otherwise due to PEIA in accordance with following schedule:

Rebates to be Disbursed to PEIA during the Quarter Expected	Amount of Termination Fee to be Withheld by First Health
April 1999	$ 82,500 (15%)
July 1999	$110,000 (20%)
October 1999	$247,500 (45%)
January 2000	$110,000 (20%)

The parties agree that rebates shall not be the exclusive source for payment of the Termination Fee. In the event the portion of rebates otherwise payable to PEIA for any above payment interval is insufficient to cover the amount due First Health as part of the termination fee, then First Health may invoice PEIA for the difference, which PEIA shall pay within forty-five (45) days of receipt of invoice."

We discussed with the Director of PEIA the method of making the payments to First Health under the termination agreement which basically called for First Health to withhold the scheduled payments in the first instance from rebates otherwise due PEIA. As a result, these payments would effectively be netted against revenues and would not be disclosed in the accounting records of the State of West Virginia nor subject to review by the State Auditor prior to payment. Following our discussions, the Director of PEIA contacted First Health to tell them any payments under the termination agreement would be required to be invoiced to PEIA by them. The President of First Health responded in her letter of May 5, 1999 to the Director of PEIA as follows:

"This is to confirm our conversation today relating to PEIA's invoice requirements for administrative fees payable to First Health pursuant to the Termination Agreement dated January 13, 1999. We agree that, approximately 30 to 45 days prior to the anticipated rebate distribution dates included in the schedule in Section 3 of the Termination Agreement, First Health will invoice PEIA for the amount of administrative fee shown in the schedule as due for the quarter. Upon receipt of payment from PEIA, we will promptly distribute the rebates payable to PEIA without any reduction for the administrative fee."

Initially, we believed the termination agreement itself may have violated State law because no apparent additional services were being given to the Sate of West Virginia in return for the $550,000.00 termination fee. However, a review by legal staff from the Legislative Services Division indicates their belief that the termination agreement is probably a valid agreement. Their response to our inquiry stated in part,

> **"...it is the opinion of the attorneys in this office...that the termination agreement is probably a valid agreement...Also, as to your question about WVC §12-3-10, it appears to us that services were and continue to be provided by First Health which would plausibly justify the financial terms of the termination agreement. In addition to the ongoing services provided under the agreement, First Health presumably incurred substantial start up costs and other expenses in setting up the prescription benefit management program with the expectation of recouping that investment over the life of the initial agreement. It is thus plausible that First Health would have received compensation for those additional expenses incurred as a result of the early termination of the agreement."**

The PEIA entered into the subsequently terminated contract with First Health on September 30, 1997, to be effective February 1, 1998 for the purpose of processing prescription claims for insureds. First Health Services Corporation (First Health) of Richmond, VA was the successful bidder in a second round of competitive bidding which began with PEIA's Request for Proposals (RFP's) dated July 24, 1997. First Health successfully challenged the results of the initial bidding which resulted in the selection on January 16, 1997 of PCS Health Systems, Inc. (PCS) as the

prescription claims processor. First Health had held the prescription claim processing contract since January 1, 1991.

During 1996, PEIA began preparations for solicitation of RFP's for the awarding of a new contract for the processing of prescription claims. Originally, the contract with First Health was scheduled to end on December 31, 1996. However, a decision was made to extend this contract an additional year to allow PEIA more time to develop changes in the drug benefit program and to solicit competitive bids for the implementation of those changes. According to the minutes of the meeting of the PEIA Finance Board held on February 19, 1997, Mr. Russell W. Brown, then Director of the PEIA, informed the Board the new prescription contract had been awarded to PCS on January 16, 1997; however, First Health immediately challenged PEIA's decision. Thereafter, PEIA sought assistance from consultants with Coopers & Lybrand in developing a more systematic way of scoring the RFP's solicited in the second round of bidding which commenced with the July 24, 1997 RFP.

On September 8, 1997, the contract was awarded to First Health; however, PCS Health Systems, Inc. initially challenged this contract award but later withdrew their challenge allowing the PBM contract with First Health to commence on February 1, 1998. We observed a memorandum from the PEIA legal counsel to the new Director of PEIA dated April 1, 1998, which we believe to be the legal counsel's response to the PEIA Director's inquiry as to what conditions would allow PEIA to terminate the First Health contract.

Almost immediately, commencing on April 7, 1998, we observed a series of correspondence between the PEIA Director and other PEIA officials with various high-ranking officers of First Health where several different issues of alleged material breach of the PBM contract are set out. **Among these issues which PEIA considered indicative of material breach of contract are the failure of First Health to provide a $1,000,000.00 performance bond in conformity with the PBM agreement by November 1, 1997; First Health's alleged failure to have Rxpert (First Health's prescription claims processing software) installed at First Health's Charleston Office and the PEIA by May 1, 1998; certain reports needed to document First Health's compliance with claims payment, customer service, and administration guarantees were allegedly not made available to PEIA; and, First Health's alleged failure to provide PEIA a certificate of insurance of general and professional liability in the amount of $5,000.00 per occurrence.** In the series of correspondence which followed, we noted First Health's President and other corporate officers responded and, as a general rule, refuted each of the PEIA claims, except for the supplying of the performance bond. A performance bond conforming to the specifications of the PBM contract was not received by PEIA until July 2, 1998.

At some point in the round of discussions with First Health, PEIA got in contact with the two firms which had been rated as 2nd (PCS Health Systems, Inc.) and 3rd (Merck-Medco) in the scoring of the July 24, 1997 RFP's for the purpose of determining these respective firms' capabilities to assume the PBM contract in the event the issues with First Health could not be resolved to the satisfaction of PEIA. The first written correspondence between PEIA, PCS Health Systems, Inc. and Merck-Medco occurred as early as late May 1998 which is almost four months before a formal offer was made by First Health to reach a mutually agreeable termination arrangement regarding the PBM contract. Finally, a September 23, 1998 letter to the PEIA Director from the President of First Health states in part,

> **"As is perfectly clear from the above responses to your unfounded claims, every issue you have raised is either (i) not required by the contract, or (ii) is not a material breach of it. However, for those not part of the current contract, you attempt in your letter to make an "end-run", unilateral modification to the contract by stipulating in your letter that First Health Services' response becomes part of the contract ... Your actions are perfectly consistent with the widespread rumors and the confirmation you gave me in an earlier phone conversation that you have been meeting with First Health Services' competitors for some time and fully intend to find a way to remove us as PEIA's pharmacy benefit manager ... Alternately, if you wish to meet to discuss the terms under which a mutually agreed termination of the contract would be acceptable to First Health Services, we are quite willing to do so...."**

In response to this letter, the Director of PEIA wrote a September 25, 1998 letter to the President of First Health which states in part,

> " ... **After reviewing your response to my correspondence of September 15, 1998, it is apparent to me that we will not be able to reach a consensus with regard to the continuation of this contract. . . Thereafter, it is my intent to contact you to discuss an agreeable termination. Once we have the ground work covered, we will work with you to draft the necessary documents....**"

After a series of follow-up letters, PEIA and First Health reached agreement on a $550,000.00 termination agreement which is set forth in a November 20, 1998 letter from the Director of PEIA to the President of First Health.

We discussed the decision to terminate the First Health PBM agreement with the Director of PEIA. He told us he was made aware of numerous complaints from PEIA insureds relating to First Health's performance as the prescription claims processor. We reviewed the written complaints made available and determined some of the complaints appeared to criticize First Health's administration of the PBM agreement. Other complaints could have been the result of eligibility problems created for insureds by the earlier mentioned EIAS system. In addition, he told us PEIA was unable to reach a consensus with First Health regarding the full implementation of the terms of the agreement and, further, PEIA was not achieving the cost savings contemplated under this agreement. After discussions with PCS and Merck-Medco and the submission of

cost proposals by these firms, PEIA elected to enter into an agreement with PCS for prescription claims processing. The Director of PEIA told us his decision to award this contract to PCS was based on certain estimates provided him in their letter of September 22, 1998 which stated that under the PBM agreement effective February 1, 1998, PEIA would have saved $8,264,000 in retail dispensing fees and ingredient cost, $900,000 in the retail intervention program, and $600,000 through use of academic detailing. Further, PCS in their December 4, 1998 letter to the PEIA Director stated,

> " ... **PCS will guarantee savings of Six million dollars ($6,000,000) in calendar year 1999, based on the Agency's current plan design and level of clinical management....PCS will reimburse the Agency for any non-administrative net plan cost over Sixty-two million dollars ($62,000,000) dollar for dollar to a maximum of Six million dollars ($6,000,000)....**"

In reviewing the PCS' letter of September 22, 1998, we noted the estimated savings in retail dispensing fees, ingredient cost, the retail intervention program and the use of academic detailing were calculated by comparing PEIA's prescription claim data for the period April 1, 1997 - March 31, 1998 with what those costs would have been using the PBM agreement which did not become effective until February 1, 1998. We made this determination based on the following statements contained in the September 22, 1998 letter,

> " ... **The analysis was completed using data from the time period April 1997 - March 1998 ... I believe you will agree**

that PCS' programs can produce significant savings to the PEIA by truly managing your prescription drug program. All savings are based upon mirroring the current plan design...."

In effect, ten months of the claims data used was accumulated under the prior PBM agreement. We noted changes in the PBM agreement effective February 1, 1998 as compared to those contained in the prior PBM agreement which became effective on January 1, 1991 which should have acted and were intended to contain costs. In short, we believe the analysis of savings done by PCS as set forth in their September 22, 1998 letter while clearly explained would probably not result in a true comparison of the capabilities of any two possible prescription claims processors to manage the PBM contract during the period April 1, 1997 - March 31, 1998, because the agreement under which ten months of the cost data was accumulated was not the same as the agreement controlling costs the last two months of the period evaluated.

We recommend the PEIA comply with the provisions of Chapter 5, Article 16, Section 9 of the West Virginia Code, as amended, dealing with the requirement for competitive bidding for professional services contracts.

Agency's Response

The cancellation of the First Health Services Corporation/PEIA contract has been discussed at numerous meetings of Legislative Interim Committees and the PEIA Finance Board.

In January 1998, PEIA was asked by both legislative bodies to review and provide information on the contracts administered by PEIA. During the review of the First Health contract, it became clear that significant deliverables were not being met:

- *PEIA lost $3 million as a result of First Health's inability to provide an edit capability*
- *in May 1998, no management reports had been received for the months of February, March, and April 1998*
- *coordination of benefits (COB) was poorly implemented: letters were sent to Medicare recipients in error and the overall effort was not timely*

PEIA attempted to resolve these issues with First Health, but after some time it became apparent that continuing the contract would seriously impact the financial performance of our financial plan.

Because PEIA had just completed an RFP process for prescription services, a process that took almost fourteen months to complete, and was only in the third month of a thirty-six month contract, PEIA's management team decided to negotiate a contract with the second place vendor of the bidding process. However, to ensure that pricing had not changed in the market, we asked the number two and number three vendors from the bid to provide updated cost estimates. This process was to protect the interests of the agency and the State. After a thorough review, PEIA awarded an abbreviated seventeen-month contract to PCS, the second place

vendor in the RFP process. As stated, because of the emergency need to have these services available and the potential large losses (a projected $1.75 million) that would be borne by the Plan by continuing the contract with First Health, PEIA awarded an emergency short-term contract to PCS. The contract period was chosen to correspond with the end of the policy year and to allow time for a new RFP and award process to occur.

As for the termination agreement, PEIA requested the assistance of legal counsel from within the Department of Administration and the State Attorney General's Office. Both suggested a mutual termination of the contract. PEIA accepted the advice of counsel and ended the contract through a termination agreement.

In addition, the finding asserts that the $6 million in savings guaranteed by the second vendor "would probably not result in a true comparison" because different agreements were in effect, while in fact, the same benefits were in place. Had older data been used, the savings calculation would have exceeded $6 million because the trends had increased the total cost.

In summary, PEIA is of the opinion that it violated no statute by making this award. PEIA made an award based on the RFP's submitted. Had the contractor requested termination of the contract, our process to secure the contracted services would have

been the same: the second vendor would have been chosen. We acted completely within the mandates of applicable statutes.

APPENDIX D

Memo - Performance Guarantees

MEMORANDUM

TO: Kim Covert
Chief Financial Officer

FROM: Felice B. Joseph
Pharmacy Benefits Administrator

DATE: July 23, 1999

RE: Performance Guarantees

Please let this memo serve as my request for you to withhold fifty percent of the annual Administrative Fees owed to PCS due to the following guarantees having not been met. Unless PEIA receives reports stating the contrary, PCS has not fulfilled the issues outlined below.

- **Recap Help Desk.** Incorrect information, long wait times, and constant referrals to PEIA and Mountain State Blue Cross & Blue Shield consistently continue, as of this date, to occur. This has been occurring since February 1, 1999 as noted in Concerns with Service, attached.

- **PCS Mail Service Shipping – Prescription Not Requiring Intervention.** Members regularly call PEIA because they have not received their medication and cannot get through to talk to a PCS representative in under thirty minutes. This has been a problem issue since February 1, 1999.

- **Client Services Administration Calls.** PEIA staff does not get timely answers to inquiries or requests. This is evidenced in Concerns with Service, attached. PEIA has repeatedly reported this problem since February 1, 1999.

- **Client Services Administration Implementation.** For both February 1, 1999 and July 1, 1999, PCS had difficulty in meeting PEIA's requirements for the eligibility tape layout. Thus, members did not get added to PCS' eligibility and were denied prescription coverage at the pharmacy. For July 1, 1999, correct ID cards and the customized brochure did not begin mailing until July 22, 1999, despite assurances that this would occur during the last week of June and the first week of July.

- **Standard Recap Processing.** Claims have been incorrectly processed since February 1, 1999. Impact reports and associated reimbursements have not been received by PEIA for incorrect co-pays of two and three dollars, an inadvertent no limitation on Viagra approvals, as well as the new pricing problem which began July 1, 1999. The 7-day emergency supply provision, which was to be in place February 1, 1999 is still not available. The maintenance list was incorrectly coded for February 1, 1999 implementation on certain drugs. Some of the same medications (e.g., diabetic drugs and supplies) got incorrectly coded again for the July 1, 1999 implementation.

FBJ:trs

cc: Robert Ayers

I:\felice\memo to kim covert re pcs. 723

CONCERNS WITH SERVICE
(June 16, 1999)

1. Mail order: 4/30/99 Michelle told member 90 days only available at mail order
   6/15/99 Daniel told member 90 days only available at mail order
   5/6/99 Karen (supervisor at m-o) told member no 90 day supply available
   6/4/99 Ray (at client services) told PEIA CSR no 90 days supply available
   6/16/99 SS# 236-40-0684 Pam (at m-o) incorrectly quoted copayments even though managed access on profile.

2. Incorrect copayments of $2.00 (for up to 34 day) and $3.00 (for up to 90 day) for all claims with a DAW of 1, 2, or 7. PEIA expects an impact report run on these claims.

3. Copayments charged with MAC penalty even though a managed access on member #233-80-9483 on Elavil and Klonopin.

4. PCS incorrectly entered managed access for SS# 234-60-3636 by putting a person code of 16 instead of 02. When the R.Ph. called the help desk, they were instructed to call PEIA to change code from 16 to 02 instead of correcting their own problem.

5. PCS paid 6 claims on Xenical totaling (about $374) before the exclusion went into place. Even though PEIA excludes all anorectic agents, I contacted Toni about this on 4/30/99 and was assured we would not cover any claims. The actual exclusion did not go in effect until 5/6/99 due to some question about Xenical's classification. PEIA expects an impact report run on these claims.

6. First requested On Demand access for CHIP program on 5/12/99. I was assured I would have access on 5/24/99. As of today, I still do not. CHIP invoices must be accompanied by a claim detail report. The invoice dated 5/21/99 has still not been paid, even though future invoices have, because we still do not have the detail for it.

7. As of 4/30/99 PCS still telling some members only Accu-Chek products covered and not BAYER. This has subsided from 2/1/99, but still isolated occurrences.

8. CHIP effective date of 4/1/99 still appearing on cards. Thus, MSBCBS has some appeals where physicians billed before actual effective date since card says 4/1/99. Began speaking with Ann Pilgrim 5/5/99. Mike Mullins was to hear from their programmers on 5/11/99 to see if eff. date (month and year) could be passed in GP fields. To this date no such call has occurred.

9. Still waiting to hear if I could send Chris the Medicaid Recovery Billings for PCS to deny and require electronic submission. I am still holding these claims.

10. SS# 233-48-3727 received MAC penalties in March, April, and possibly May. I first spoke with Chris on 5/11/99 so that PCS would calculate her refund. To this date I have still not heard any solution on this issue.

11. Member service told an insured (who was questioning their copayment) that it is priced that way because PEIA has the hard coding of "care level K pricing" on 5/14/99. Chris agreed this was far too technical because the member called PEIA asking what that meant. I did not know as I had never heard of it before.

12. On 5/14/99 SS# 236-74-5887 order 90 day supply of Coumadin. PCS incorrectly entered the managed access on 5/3/99. Thus, mail order only sent him a 34 day supply. Once the problem was identified PCS was to mail the remaining 56 and charge the difference. Again, the member received 34. Finally, on 6/9/99 PCS shipped remaining amount. I was only notified because I inquired about the status of this problem.

13. PEIA has a dummy group number for direct pays of 0098. I started receiving CHIP 0098 eligibility reports. I first faxed this to Chris on 5/21/99—still no answer. We also get "dependent not found" reject reports when the members are termed and should not be there. I first faxed this to Ann on 5/17/99—still no answer. We believe these are PEIA members.

14. Where is PEIA 7 day emergency supply for prior authorization drugs? No one seems to know about it. It should definitely be in and remain in our benefit design.

15. Auditor's Office needs a detail page with the AT &T bill and also an itemization on managed access charges on the invoices for Admin. Fees. I have talked with Michael Messick as well as Chris Burns at PCS—still no details. Thus, payment has not been released.

16. Verified that the anti-ulcer edits are working correctly for PEIA because they MUST remain in place for CHIP after 7/1/99.

17. Asked about prior authorization for Benzodiazepines, Ultram, and non-sedating antihistamines that are going into place 7/1/99. We still do not have these. PCS is still developing these as they are not routine ones with them.

18. Asked if DUR letters could be sent to physicians in advance on patients they have on any drugs PEIA is placing limitations or prior authorizations. This way we could notify them in advance of the limits running out or the next refill.

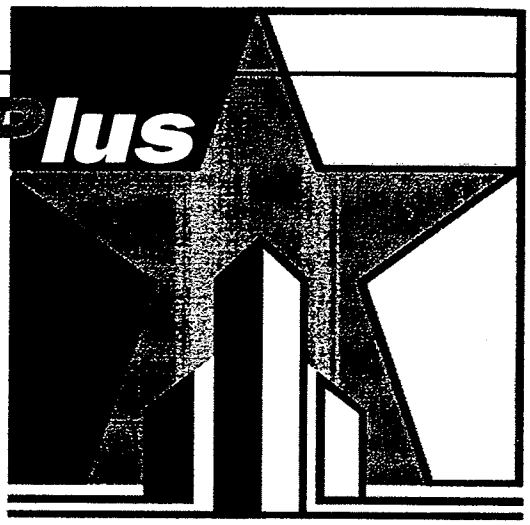
APPENDIX E

Article from Business and Health

Business & Health
KEYS TO WORKFORCE PRODUCTIVITY

Productivity*Plus*

Pathways to wellness



By Chad Abresch MEd, Craig Johnson and Bo Abresch

The data you collect is one thing. The way you look at it is far more important. The Wellness Councils of America reports on an innovative program in a state where bad health behaviors abound.

This edition of Productivity*Plus* highlights one of the most important and innovative programs in the country. Important because it operates in a state notorious for being unhealthy and deals with a population that has been largely forgotten. Innovative because it takes a comprehensive research-based approach to changing health behavior. The West Virginia Public Employees Insurance Agency (PEIA) collects and uses data like few other programs. In addition, it routinely has an impact on the bottom line.

As the largest insurer in the state, PEIA covers approximately 212,000 lives in over 96,000 households. The pool of insured lives is made up of active and retired public employees at 126 different public worksites plus their dependents.

The health woes of West Virginia—and the consequent challenges PEIA faced—are well documented. In 1995, the state had the third highest prevalence of smoking and the second highest occurrence of both heart disease and cancer. The overall health of the population was ranked 48th in the nation by the ReliaStar State Health Rankings.

Faced with such a monumental undertaking, PEIA turned to Partners in Corporate Health Inc. to help research, plan and operate a wellness initiative that became known as "Pathways to Wellness" and in just a few short years has become enormously successful. But before we get to the measures that quantify this success, let's discuss how they go about promoting and improving the health of their population.

First principles

The Pathways program does more than offer wellness activities; it manages the health of the population. Following a fundamental set of health promotion principles, PEIA first assesses the needs of its insured population. Second, it uses the information to target specific areas for intervention. Finally, it continuously evaluates with an eye toward program improvement.

Population assessment. Like few other programs in the field, Pathways collects, stores and even cross-references employee health data in a comprehensive in-house database. This prolific database and software program were specifically designed to safeguard confidentiality of participants while giving all involved access to information that would drive the program.

Admittedly, database development is not all that unusual. In fact, a handful of wellness programs have developed similar tools that track activities and administrative processes such as delivery and participation. What's unique here is a modular structure and relational theme, plus the ability to capture and relate two additional modules of information:

1. Comprehensive health risk assessment and behavior modification data;
2. Data related to medical claims analysis and other economic indicators.

The three modules allow for computation of various indicators that show, for example, how the presence of a risk factor relates to participation in a program or how medical claims expenditures relate to common health behaviors.

The logistics of the database are straightforward: All participants must first complete an enrollment form consisting of basic demographic and health data. They also are assigned a member tracking number. Additionally, all programs and services require the completion of pre- and post-program evaluation forms. These forms incorporate assessments on the readiness of participants to change with more standard satisfaction and outcome measures.

This is where Pathways parts company with other programs. The data listed above is merged with medical claims data to quantify changes in health care costs and utilization. PEIA's evolution into population health management is no less than groundbreaking.

Chad Abresch is WELCOA's senior staff writer for consumer and organizational publications. Craig Johnson, a health promotion specialist and staff writer for WELCOA, also manages the national Well Workplace Awards Initiative. Bo Abresch is the communications specialist for WELCOA.

Targeting the bottom line. This database has imparted two critical lessons that reiterate and confirm what health professionals have known all along: High-risk employees are exceedingly costly to business, and worksite efforts can significantly reduce risk and lower costs.

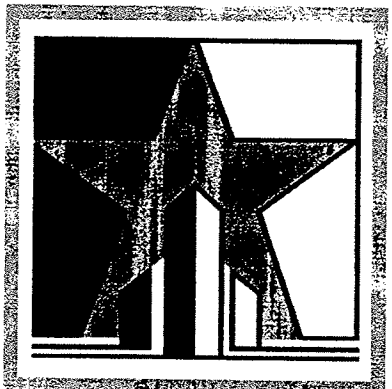
For instance, comprehensive pre- and post-program evaluations showed that those at high risk for cardiovascular disease cost significantly more per year to insure than those at low risk. PEIA then measured and compared expenditures for high- and low-risk groups for various individual cardiovascular risks like blood glucose and sedentary lifestyles. Not surprisingly, both of these risk factors were correlated with increased expenditure.

Now for the million-dollar question: "Could PEIA reduce these risk factors and in turn reduce its payouts?" The answer was Yes. Using the expenditure data to target programs to specific risks, Pathways was more than marginally successful.

For example, PEIA was able to move 43 percent of high-risk blood glucose participants to low-risk. Even more important, 99 percent of low-risk participants stayed that way. How does that translate in dollar signs? It made a difference of $125 per employee per year.

Need more evidence? Consider PEIA's work with those at high risk in the sedentary lifestyle category. Through previous research, program administrators knew that those who exercised regularly were less of a drain on the company's pocketbook than were their couch potato counterparts. One year after targeting this risk factor, the percentage of those exercising in excess of one hour per week more than doubled—up from 17 percent to 35 percent. In other words, the program was successful to the tune of $268 per person annually.

Eye on the prize. Pathways holds to a very high operating standard, Continuous Quality Improvement (CQI), which uses program assessments to tailor offerings to the needs of the insured. The process relies upon several strategies.



Participants are constantly surveyed about their needs and interests, and the results are thoroughly disseminated via semiannual presentations to the agency's finance and governing board and newsletters to worksite administrators. Worksite coordinators receive 10 interactive newsletters a year. Quarterly evaluation reports add to the flow of information.

Face-to-face meetings turn data into decisions. Regional coordinators and central administration have quarterly planning retreats. Twice a year, they're joined by worksite coordinators and the sponsoring agency. There are also quarterly meetings on data collection with six outside researchers and strategic allies.

This close collaboration has fueled continuous growth in funding and participation. In fact, worksite participation has doubled in each of the last three years.

Final question

The Goliaths of the business world might well use this model, but will it work for the Davids as well? To be sure, there will be significant challenges in implementing such a comprehensive system in any business setting, small or large, and any investment in such a project will be scrutinized for its potential return.

Logic would argue that the exemplary efforts of PEIA could be mimicked. Certainly any company might implement some of the ideals found in CQI. Furthermore, the database is essentially a tool for population health management. It allows for the planning, assessment and subsequent refinement of programs and interventions. These steps can be taken without gigantic expenditures on more basic yet effective terms.

PEIA has charted new ground for identifying strategic areas of health, implementing programs and bringing about change. Where PEIA goes, others will follow. □

About WELCOA

For over a decade, The Wellness Councils of America has partnered with corporations, hospitals, universities and governmental agencies to design and deliver comprehensive wellness initiatives that address employee health and well-being, productivity, safety and work and family issues.

WELCOA has more than 2,000 member organizations located throughout North America and 10 locally-affiliated community Wellness Councils.

Approximately 400 companies and three cities nationwide have met rigid criteria and received WELCOA's Well Workplace and Well City awards for quality and excellence in worksite health promotion.

For more information about the Wellness Councils of America:

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APPENDIX F

Agency Response

Bob Wise
Governor

Tom Susman
Director

WV Toll-free: 1-888-680-PEIA • Phone: 1-304-558-7850 • Fax: 1-304-558-2516 • Internet: www.peia.state.wv.us

February 9, 2001

Mr. John Sylvia
West Virginia Legislature
Performance Evaluation and Research Division
Building 1, Room W-314
1900 Kanawha Boulevard, East
Charleston, WV 25305

Dear Mr. Sylvia:

I have read the audit prepared by your agency as it relates to the operation of the Public Employees Insurance Agency (Agency). Having been appointed Director, less than a month ago, the concerns expressed in your report reflect many of the same conditions that I have uncovered during my short tenure. It is apparent to me, that for the last several years, the contractors have been managing the Agency instead of the Agency managing its contractors.

Because of this lack of management, the PEIA has lost the opportunity to engage in an effective methodology that would have protected the resources of the taxpayers and the policyholders. An indication of this is the conversion from one claims processor to another. No in depth analysis of provider adequacy of the Third Party Administrator (TPA) along the bordering counties was performed, to my knowledge, by members of the current PEIA staff. Therefore, the residents of the Eastern Panhandle enrolled with the PEIA PPB plan have encountered a significant access problem. I began to address this situation with the TPA as soon as I arrived.

The reporting package and data compatibility issues were not dealt with before conversion. As a result, we are seven months into the contract and we still lack many of the needed reports to effectively manage our health claims. Currently, the TPA has a backlog of nearly 100,000 claims. This number should be in the 65,000 range. A significant number of these claims are several months old. This is another situation I am addressing.

In addition, upon coming to the Agency, the new administration learned that our independent auditor performed the SAS 70 audit for our TPA, as well as their independent auditor. This same company also serves as our actuary and as the independent auditor for one of our largest managed care contractors. The PEIA Management Team has decided to put the independent audit out to bid

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and preclude the current firm from participating. This change of independent auditors will eliminate a conflict of interest.

In terms of contract management the Agency will employ a Contract Compliance Administrator. This person will have the responsibility to develop procedures and to monitor all Agency contracts in order to ensure compliance with the terms. A monitoring calendar will also be established.

Under existing practices, the Agency did not place major Requests for Proposals (RFP) in the State Purchasing Bulletin. I have altered this policy and have canceled a bid for a life insurance administrator that I didn't believe was proper. A directive has been issued that, in the future, all major RFPs will be published in the State Purchasing Bulletin.

The Agency will review all Pathways to Wellness (PTW) contracts before contracts come up for renewal this summer. Part of this review is to determine if we can communicate more effectively with our insureds. Currently, PEIA sends a quarterly newsletter to its members. In addition, PTW sends a newsletter to all PEIA members on a bi-monthly basis and a separate contractor also sends a quarterly newsletter to a segment of the Agency's membership. It will be our intent to combine the efforts and adapt the content of the newsletters to be more appropriate for the policyholders.

We will implement the recommendations set forth in your report. Within the next month we will provide you with a timetable for compliance. The input from your audits has proved helpful and instructive to the Agency and myself as we transition from one administration to another.

If you have any further questions or would like further information, please do not hesitate to contact me at 304-558-6244, ext. 225.

Yours truly,

Tom Susman
Director

TS:tr