

**SPECIAL REPORT**

**WEST VIRGINIA PUBLIC EMPLOYEES INSURANCE AGENCY**

**FOR THE PERIOD**

**JULY 1, 1995 - APRIL 30, 1999**

WEST VIRGINIA LEGISLATURE  
*Joint Committee on Government and Finance*

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The Joint Committee on Government and Finance

In compliance with the provisions of the West Virginia Code, Chapter 4, Article 2, as amended, we have completed an examination of the Public Employees Insurance Agency.

Our examination covers the period July 1, 1995 through April 30, 1999. The results of this examination are set forth on the following pages of this report.

Respectfully submitted,

A handwritten signature in cursive script that reads "Theford L. Shanklin".

Theford L. Shanklin, CPA, Director  
Legislative Post Audit Division

May 21, 1999

Auditors: Michael E. Sizemore, CPA, Supervisor  
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WEST VIRGINIA PUBLIC EMPLOYEES INSURANCE AGENCY

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**WEST VIRGINIA PUBLIC EMPLOYEES INSURANCE AGENCY**

**EXIT CONFERENCE**

We held an exit conference on June 8, 1999 with the Controller of the Department of Administration and the Director of the West Virginia Public Employees Insurance Agency and all findings and recommendation were reviewed and discussed. The Directors' responses are included in italics in the Summary of Findings, Recommendation and Responses and after our recommendations in the General Remarks section of this report.

## WEST VIRGINIA PUBLIC EMPLOYEES INSURANCE AGENCY

### INTRODUCTION

The Public Employees Insurance Board was created by an Act of the First Extraordinary Session of the 1971 West Virginia Legislature, by an amendment to Chapter 5 of the West Virginia Code, 1931, as amended, by adding a new article, designated as Article 16, Section 1 through 16 known as the West Virginia Public Employees Insurance Act.

The Board was established to provide group hospital and surgical insurance, group major medical insurance and group life and accidental death insurance for all public employees. When the insurance program was originally established in 1971, participation was granted by the Legislature only to employees who worked regularly full-time in the service of the State. The 1972 Legislature granted participation privileges in the insurance program to full-time employees of county boards of education and Board of Regents. Again, in 1973, the Legislature granted participation privileges in the insurance program to include the following full-time employees of:

1. A county, city or town;
2. Any separate corporation or instrumentality established by one or more counties, cities or towns, as permitted by law;
3. Any corporation or instrumentality supported in the most part by counties, cities or towns;

4. Any public corporation charged by law with the performance of a governmental function and whose jurisdiction is coextensive with one or more counties, cities or towns;
5. Any agency or organization established by, or approved by, the former Department of Mental Health for the provision of community health or mental retardation services and which is supported in part by State, county or municipal funds; and
6. Any person who works regularly full-time in the service of a combined city-county health department created pursuant to Chapter 16, Article 2 of the West Virginia Code.

An Act of the 1988 Regular Session of the West Virginia Legislature changed the name of the spending unit to the "West Virginia Public Employees Insurance Agency" and made substantive changes to the program. The most dramatic change was one which allowed retiring employees to convert two days of accrued annual and sick leave for one month of paid insurance for single coverage and three days of accrued annual and sick leave for one month of paid insurance for family coverage. In the alternate, the employee may elect to apply the accrued annual and sick leave toward an increase in the employee's retirement benefits on the basis of two days of retirement service credit for each one day of accrued annual and sick leave.

Through the enactment of Chapter 7, of the 1990 Third Extraordinary Session of the West Virginia Legislature, the Public Employees Insurance Agency Finance Board was created. The Board was created to foster fiscal stability in the public employees'

insurance program through the development of an annual financial plan to meet the Public Employees Insurance Agency's estimated total financial requirements. The Finance Board is required to submit the annual financial plan each year by January 1, preceding the fiscal year after conducting the required public hearings.

In addition, the 1990 Third Extraordinary Session of the West Virginia Legislature created the Public Employees Insurance Agency Advisory Board consisting of 15 members who were responsible for advising and making recommendations in terms of group hospital and surgical insurance, group major medical insurance and group life and accidental death insurance to the Director of the Public Employees Insurance Agency in reference to the administration and management of the spending unit. However, such recommendations and advice are not binding on the Director. The Public Employees Insurance Agency Advisory Board was terminated effective July 1, 1997 per Chapter 4, Article 10, Section 5(2) of the West Virginia Code, as amended.

Since early 1990's, Public Employees Insurance Agency participants have been allowed to contract with Health Maintenance Organizations, (managed care plans) originally only two were licensed in West Virginia and operated in the northern panhandle region of the State. Public Employee Insurance Agency participants in that area were allowed to enroll in either of those organizations. In early 1995, the Public Employees Insurance

Agency expanded significantly its use of managed health care services. Currently, there are four Health Maintenance Organizations serving the Public Employees Insurance Agency participants. There are currently approximately 20,000 participants enrolled in Health Maintenance Organizations.



WEST VIRGINIA PUBLIC EMPLOYEES INSURANCE AGENCY

ADMINISTRATIVE OFFICERS AND STAFF

APRIL 30, 1999

During the period covered by the examination, the Public Employees Insurance Agency was under the following executive directors:

Russell W. Brown . . . . . May 1, 1995 - September 8, 1997  
Annette Castelle (Acting ) September 9, 1997 - January 12, 1998  
Robert A. Ayers . . . . . January 12, 1998 - Present

Staff

J. Michael Adkins . . . . . Deputy Director  
Kim Covert . . . . . Chief Financial Officer  
Larry Stover . . . . . Controller  
Fayette Bowen . . . . . Administration Coordinator  
Felice Joseph . . . . . Pharmacy Benefits Administrator  
Gloria Long . . . . . Benefits & Programs Manager  
Janice E. Long . . . . . Communications & Benefits Coordinator  
Mike Mullins . . . . . Information Services Manager

WEST VIRGINIA PUBLIC EMPLOYEES INSURANCE AGENCY

SUMMARY OF FINDINGS, RECOMMENDATIONS AND RESPONSES

Employee Insurance Administration System (EIAS)

1. The West Virginia Public Employees Insurance Agency (PEIA) began utilizing a new computerized system in early 1997 called the "Employee Insurance Administration System" (EIAS) to account for membership eligibility, billings and collections of employer and employee premiums, and accounting for the payments made to health care providers and reimbursements to PEIA insureds. We found the EIAS issued erroneous retroactive credits totaling \$2,854,507.92 of which \$89,479.00 was claimed by four different insured employers; a glitch in the EIAS programming can result in an improper re-activation of the coverage of previously insured employees under certain circumstances; the EIAS was not designed to account for the various collections of the PEIA in a manner which insures that the collections will only be used for their intended purposes; and, the EIAS does not properly age the outstanding accounts receivable of the PEIA making some accounts appear more current with their payments than is actually the case.

We recommend the PEIA take advantage of those remedies available under the contracts with Standard Data Corporation

and Mr. Jerone N. Deverman relating to the design and development of the EIAS system as may be available under the laws of the State of West Virginia to protect the best interests of PEIA, the State of West Virginia and its taxpayers.

**Agency's Response**

***We will comply with the audit recommendation. (See pages 14-29)***

**Prescription Drug Contract**

2. 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. The PEIA awarded the PBM agreement to PCS Health Systems, Inc. effective February 1, 1999; however, we believe the provisions of Chapter 5, Article 16, Section 9 of the West Virginia Code, as amended requiring competitive bidding for PEIA's professional services contracts were not followed.

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**

***PEIA is of the opinion that it violated no statute by making this award. (See pages 29-41)***

**Claims Audit Contract**

3. The PEIA awarded a \$35,000.00 contract to Wolcott & Associates, Inc. to perform an operational review and detailed claims audit and a Statement on Auditing Standards (SAS) 70 audit of the PEIA's third party administrator; however, we found the contract was poorly administered by PEIA, was not written in a way which effectively tested the PEIA's eligibility roles and did not appear to comply with the State Auditor's prescribed rules and regulations regarding requisitions for payment of contract invoices.

We recommend the PEIA comply with the requirements of Section 155-1-4.1.b of the State Auditor's rules and regulations governing invoices for services.

**Agency's Response**

***We are now in compliance with the audit recommendation. (See pages 41-43)***

**Poor Administration of Contracts**

4. The PEIA did not adequately administer their contracts which totaled millions of dollars including contracts for insurance coverage and the administration thereof and contracts for professional services such as audits and actuarial services in that contract ledgers detailing payments made on these contracts and tracking the remaining spending authority for the respective contracts were not maintained. Also, PEIA did not recoup at least \$25,488.73 of reimbursements due the agency relating to contracts where other State agencies received the benefit of PEIA contracts and had agreed to reimburse PEIA.

We recommend the PEIA comply with Chapter 5A, Article 8, Section 9 of the West Virginia Code, as amended and provide better monitoring of all contracts.

**Agency's Response**

***We are now in compliance with the audit recommendation. (See pages 43-48)***

**Overpayment of Former Employees' Final Pay**

5. We found two former employees of PEIA were overpaid a total of \$1,262.78. Specifically, according to the records available to us, the former Chief Financial Officer was overpaid a total of \$1,112.78 when his employment ended and

this amount has not been refunded. Also, the former Director of PEIA was overpaid a total of \$2,090.08; however, all of this amount except \$150.00 in savings account deposits have been refunded to PEIA by him.

We recommend the PEIA take the necessary steps to recover these overpayments from the affected ex-employees, if necessary take advantage of the remedies available under Chapter 14, Article 1 (CLAIMS DUE THE STATE) of the West Virginia Code, as amended.

**Agency's Response**

***We have taken appropriate action to comply with the audit recommendation. (See pages 49 and 50)***

**Retirement Withheld from Terminal Leave**

6. We found PEIA incorrectly withheld \$50.19 in retirement contributions from the terminal leave pay of a former employee and then incorrectly matched this amount with \$100.37 of PEIA funds.

We recommend the PEIA take the necessary steps to recover the overpayment of the matching funds from the Consolidated Public Retirement Board.

**Agency's Response**

***We have taken appropriate action to comply with the audit recommendation. (See pages 50-52)***

**Errors in Payment of Overtime Hours**

7. We found one employee was overpaid a total of 29 hours in overtime compensation at a cost of \$372.02 while another employee was overpaid for one hour amounting to \$14.80.

We recommend the PEIA comply with Chapter 12, Article 3, Section 13 of the West Virginia Code, as amended. Also, PEIA should collect the overpayment from the affected employees.

**Agency's Response**

***We have taken appropriate action to comply with the audit recommendation. (See pages 52 and 53)***

**Meal Periods Included in Overtime Calculations**

8. We noted PEIA paid overtime to employees after 37.5 hours actually worked in any week because PEIA was counting the employee's daily 30-minute lunch period as time worked. We determined the cost to PEIA during the period July 1, 1996 - June 30, 1998 of counting the lunch periods as time worked approximated \$3,187.00.

We recommend the PEIA comply with Section 441 of the Fair Labor Standards Act (FLSA) in determining hours worked for compensation of overtime.

**Agency's Response**

***PEIA's method of determining overtime hours is now consistent with State of West Virginia policy. (See pages 53 and 54)***



**WEST VIRGINIA PUBLIC EMPLOYEES INSURANCE AGENCY**

**GENERAL REMARKS**

**INTRODUCTION**

We have completed an examination of the Public Employees Insurance Agency. The examination covers the period July 1, 1995 to April 30, 1999.

**COMPLIANCE MATTERS**

Chapter 5, Article 16 of the West Virginia Code generally governs the West Virginia Public Employees Insurance Agency (PEIA). We tested applicable sections of the above, plus general State regulations and other applicable chapters, articles, and sections of the West Virginia Code as they pertain to fiscal matters. Our findings are discussed below.

**Employee Insurance Administration System (EIAS)**

In early January 1997, the West Virginia Public Employees Insurance Agency (PEIA) brought on line a new system which was supposed to be designed to account for membership eligibility in the PEIA Medical and Drug Insurance Program, billings and collections of employer and employee premiums, and accounting for the payments made to health care providers and reimbursements to PEIA insureds which was dubbed as the "**Employee Insurance Administration System**" (EIAS).

However, the new EIAS has been plagued by relatively poor performance from the implementation date and our work indicates continuing flaws in the various programs of the EIAS have continued through the completion of our current fieldwork (April 30, 1999). The problems which we became aware of during our work included the following:

1. The EIAS issued erroneous "retroactive credits" with regard to insurance premiums as of September 21, 1998 which totaled \$2,854,507.92. These improper retroactive credits resulted from EIAS' programming logic which applied changes in eligibility status which occurred subsequent to the launch of EIAS to premiums dating from January 1, 1997. Also, credits were located for some employees who never had a change in status since January 1, 1997. The Director of PEIA ordered his staff to evaluate the accounts which appeared to have received erroneous retroactive credits since January 1997 to determine whether any additional premiums were in fact due PEIA. The PEIA analyzed the payment patterns of the 48 largest employer accounts making up approximately 75% of the total monthly billings and which accounted for \$1,712,354.00 of the \$2,854,507.92 in erroneous credits. PEIA found that only \$89,479.00 of these \$1,712,354.00 in credits were actually taken by four of the 48 employers. PEIA billed and collected the \$89,479.00 in November 1998;
2. Our review of the maintenance of the eligibility system showed one instance where an insured terminated their employment with a Non-State participating employer on October 31, 1996; however, they were still being maintained as an eligible insured by PEIA in October 1998. At our request, PEIA reviewed their paid claims data and determined that no claims had been paid on behalf of this insured since October 31, 1996. Based on our discussions with PEIA staff, it appears the failure of this insured to be dropped from the eligibility roles is related to a "glitch" in the EIAS programming.

The EIAS system was designed to forward letters to employee dependents under certain circumstances for the purpose of verifying the dependent's full-time student status. We were told it had been discovered that changes in dependent status such as this was somehow prompting a re-activation of the previously terminated coverage of primary insureds.

The problem was identified as a system programming problem in the EIAS. Projecting the results of our examination of eligibility to the entire population of 69,583 active insureds as listed on PEIA's eligibility roles results in the possibility for as many as 1,459 insureds being on the eligibility roles and thereby, having access to health and drug benefits who are in fact not eligible for such benefits.

3. The EIAS allocates amounts paid by an agency to the oldest receivables without regard as to whether those receivables are health insurance premiums due, optional life insurance premiums due which are fully paid by employees (agency trust funds) or administrative expense fund payments. As a result, it appears the EIAS has inadvertently allocated some moneys collected to the wrong accounts. During our work, we became aware that PEIA staff attempt to compensate for the improper reporting by EIAS through the development of adjusting entries into the State of West Virginia's accounting system. However, the shortfall of funds available to pay optional life insurance premiums in January 1999 which required the transfer of \$1,002,561.61 from invested optional life premiums and \$3,267,026.13 from PEIA's Basic Insurance Premium Fund to cover the billing for optional life premiums is indicative that all of the needed adjustments have not been located.

The EIAS was not designed to account for the collection of various fees, premiums and agency trust funds in accordance with the requirements of the West Virginia Code. As a result, funds are not being separately accounted for by EIAS raising the likelihood for funds to be used for purposes other than those for which they are collected.

4. The EIAS module which performs the function of aging of accounts receivable due PEIA is not working properly based on our examination of billing statements relating to the Mount Olive Correctional Facility (MOCC). We analyzed the

aging schedule for MOCC as reflected on the monthly billing statement received by MOCC for August, September and October 1997. The aging schedule allocates PEIA's receivable from MOCC based on the following: 0 - 30 days old, 31 - 60 days old, 61 - 90 days old and over 90 days old. Our analysis showed the following differences:

AGING OF ACCOUNTS RECEIVABLE

<u>MONTH</u>	<u>DAYS</u>	<u>PEIA BILLING STATEMENT</u>	<u>AUDITED AMOUNT</u>	<u>DIFFERENCE OVER (UNDER)</u>
August 1997	0-30	\$247,690.70	\$118,028.09	\$129,662.61
	31-60	6,792.87	136,455.48	(129,662.61)
	61-90	115,068.52	115,068.52	0.00
	Over 90	<u>128,462.39</u>	<u>128,462.39</u>	<u>0.00</u>
		<u>\$498,014.48</u>	<u>\$498,014.48</u>	<u>\$ 0.00</u>
September 1997	0-30	\$238,732.56	\$121,056.47	\$117,676.09
	31-60	130,014.61	118,028.09	11,986.52
	61-90	6,792.87	136,455.48	(129,662.61)
	Over 90	<u>231,085.86</u>	<u>231,085.86</u>	<u>0.00</u>
		<u>\$606,625.90</u>	<u>\$606,625.90</u>	<u>\$ 0.00</u>
October 1997	0-30	\$240,811.95	\$119,755.48	\$121,056.47
	31-60	117,676.09	121,056.47	(3,380.38)
	61-90	48,937.82	118,028.09	(69,090.27)
	Over 90	<u>0.00</u>	<u>48,585.82</u>	<u>(48,585.82)</u>
		<u>\$407,425.86</u>	<u>\$407,425.86</u>	<u>\$ 0.00</u>

Based on our work, the EIAS' accounts receivable module does not always properly allocate payments received against the oldest receivables which has the effect of making PEIA's accounts receivable balance appear more current than is in fact the case. We believe these instances of incorrect aging of accounts receivable balances could affect management's decision making regarding the pursuit of outstanding premiums due the agency. We discussed our concerns with PEIA management and they confirmed our understanding of the shortcomings in the EIAS' ability to properly age accounts receivable.

The launching of the new EIAS culminated an almost five-year effort on the part of PEIA and consultants whose services were obtained by PEIA at a documented **development cost** of at least \$2,556,922.54 which was made up of \$ 2,030,801.08 paid to the selected vendor, Standard Data Corporation of New York, New York, and \$526,121.46 paid to a consultant, Mr. Jerone N. Deverman of Albuquerque, New Mexico, who was selected by PEIA to help coordinate the project with the selected vendor. The purposes of these contractual arrangements were to develop the programming software and select the computer hardware necessary to accomplish the stated objectives.

We examined the various contracts and related correspondence available in the records of the PEIA pertaining to the EIAS project. Our review of the available PEIA correspondence files revealed a July 29, 1997 letter from Mr. Russell W. Brown, then Director of PEIA to the Vice President of Standard Data Corporation which outlined four major problem areas as follows: 1. **Monthly activity and management reporting not**

accurate, consistent, dependable or existing; 2. Agencies refusing to honor retroactive billings as of June 30, 1997 due to errors; 3. Rate Table Changes Not Verified; and, 4. Response Time Is Unacceptable. The letter went on to say,

"The issues I have mentioned are major in nature and not what should be expected six months into operations. The continuing problems experienced in getting accurate billing generated and not having accurate, timely reporting has created an environment that is impacting the ability of PEIA to perform its statutory obligations as well as its reputation and relations with providers, insureds and other state agencies....

The established milestones of October 31, 1995, January 31, 1996, April 30, 1996 and July 31, 1996 were all met according to correspondence I had received ... Yet, the continuation of aforementioned problems raises questions regarding the accuracy of statements related to claims that system demonstration accurately and completely indicated design functionality as specified on July 31 and October 31, 1996.

Accordingly, I am asking for a full accounting of system functions per the previously mentioned benchmarks and why PEIA continues to experience problems of the magnitude it is if full functionality had been tested adequately ...

This situation is creating too many problems for PEIA as well as other State Agencies that depend on our reporting. It is clear that we are moving from inconveniences and frustration to actual damages occurring. Much has been accomplished since January and I truly recognize efforts extended, but I am left with the feeling we started much further behind the "8-ball" than anticipated."

We were not able to locate Standard Data Corporation's response to the PEIA Director's letter of July 29, 1997. However, other PEIA memoranda we obtained indicated numerous implementation

problems during the period between January and July 1997 which included retiree members whose eligibility in the PEIA program was improperly terminated resulting in their inability to have health and prescription claims honored. These memoranda indicate PEIA attempted to correct these problems on an individual basis by restoring the retiree's eligibility only to have the system fail again. Also, during the first few months of 1997, the Consolidated Public Retirement Board experienced difficulty in obtaining reliable information from PEIA which was needed for PEIA billing for retiree insurance premiums. While it is probably normal to have start-up difficulties in many new programming environments, our work and discussions with both agency personnel and employees of the Information Services and Communications Division (ISCD) of the West Virginia Department of Administration, who are currently working with PEIA in an effort to solve these difficulties, indicate a continuing problem with shortcomings in both the capabilities of the EIAS and the accuracy and reliability of information obtained from the EIAS.

In an effort to attempt to rectify these shortcomings, PEIA elected during 1998 to bring the EIAS back in-house and secure the services of ISCD in reviewing the functionality and reliability of the EIAS programming. The EIAS is designed for an IBM AS/400 operating environment while the ISCD personnel are more experienced in IBM Mainframes. This situation results in a

significant investment of additional time and money to rectify the problems in EIAS as the functionality of the programming logic must be verified while the ISCD personnel familiarize themselves with a relatively unfamiliar programming environment.

We met with ISCD's Manager of Planning and Control and Manager of Programming on September 28, 1998 to discuss the historical development of EIAS and to obtain a more thorough understanding of their thoughts on EIAS' shortcomings, as well as, possible time frames for correction of these shortcomings and cost estimates to make the needed corrections. We were told the earliest that PEIA could hope to move the EIAS back in-house with ISCD able to provide the needed support would be during the Summer of 1999 and they were not able to provide a cost estimate. Standard Data Corporation, who developed the EIAS, has been providing support for the system since the January 1997 launch at a cost of \$42,570.00 per month. As of April 30, 1999, this arrangement continues in place because the development of the necessary program documentation required to move these data processing operations from the vendor has not been fully accomplished. Our meeting with the ISCD confirmed our basic understanding of the historical development of the EIAS which follows below.

In the early 1990's, the West Virginia Public Employees Insurance Agency (PEIA) began to make preparations for the development of the new EIAS. In a June 1992 RFP, PEIA specifically



requested proposals for a "packaged system" which had already been developed by the vendor which would require only minor modifications in order to meet PEIA's requirements.

The June 1992 RFP specifically stated, "This solicitation is specifically not for a vendor to provide research, design and development of a custom EIAS. Rather, it is for a vendor who has a demonstrably proven EIAS which, with relatively minor modification, will satisfy PEIA's requirements, standards and expectations." The June 1992 RFP established the following time lines for vendor selection and anticipated implementation of the new EIAS:

<u>DATE OF COMPLETION</u>	<u>PROCEDURE</u>
On or Before August 28, 1992	EIAS Vendor Is Selected
On or Before January 4, 1993	Successful Vendor's EIAS Installed, Modified, Tested, Populated with Data and Ready For Live Operation
On or Before June 30, 1993	Billing and Premium Processing Modules Phased In for All Accounts

Following the unsuccessful June 1992 RFP, PEIA contracted with a consultant, Mr. Jerone N. Deverman, to work with PEIA staff to modify the RFP in an effort to achieve a better response from the vendor community. Therefore, the modified RFP which was issued in March 1993 stated,

"... In the current procurement effort certain time frames have been enlarged and certain specifications have been

restated to permit potential offerors more latitude to describe how their systems (would) achieve the needed functionality and/or propose alternatives that the offeror may wish to present ... Moreover, the Agency will also entertain offers from appropriately experienced and skillful custom software developers for delivery of a total custom design, development and implementation effort...."

In addition, the time lines for activation of the new system were modified as follows:

<u>DATE OF COMPLETION</u>	<u>PROCEDURE</u>
On or Before June 18, 1993	EIAS Vendor Is Selected
On or Before April 4, 1994	Successful Vendor's EIAS Installed, Modified, Tested, Populated with Data and Ready For Live Operation
On or Before July 1, 1994	Billing and Premium Processing Modules Phased In for All Accounts
On or Before October 3, 1994	Three Employers To Be On-Line With Employee Eligibility Data

Standard Data Corporation was selected as the successful vendor for the EIAS in June 1993 and ultimately, the project was designed in a way where the vendor would develop the programming specifications and staff from the Department of Administration's ISCD would develop the software needed for the EIAS. The design phase of EIAS commenced in October 1993 with the intention the programming specifications would be intended for use with the IBM

3090 Mainframe belonging to ISCD. The design phase was scheduled for completion in May 1994; however, the design phase was still not complete in early 1995, almost 1 ½ years after its start. Based on the correspondence available to us, many difficulties were encountered during the design phase which ultimately lead to a decision that ISCD would withdraw from the EIAS project around April 1995 due to "philosophical differences" between them, the EIAS vendor and PEIA staff.

During the time prior to their withdrawal, ISCD personnel had expressed concerns about the ultimate functionality of the EIAS based on the design specifications which were being developed. We obtained a copy of a March 17, 1995 position paper prepared by ISCD staff where they outlined several concerns regarding EIAS as follows:

- "1. The design document does not reflect adherence to standard rules for the following:
  - Business Requirements
  - Relational Database technology
  - DB2 methodology
  - Mainframe programming, especially consideration of system response time
  - CICS screen processing

Together, these are causing the system to be overly complicated-costing the State in excessive development, maintenance, and processing expense. IS&C can correct the platform and technology shortcomings, but needs adequate time and money to do so.

2. Delivery of the design spec is roughly a year late. It was to have been complete as of June 1994, in its entirety. The first 'third' was received March 2, 1995

with fundamental portions missing (security, system administration, record locking, etc.) The pattern of delivery thus far casts doubt on the achievement of a July 1996 implementation.

3. The first set of program specs have been provided for a portion of the system before the system design for that portion of the system has been completed, and are not programmer ready. Screen processing, security, table access, editing, and navigation are all presented separately. Additional analysis will be required to rewrite the specs so they can be assigned to the programming staff.
4. Adhoc reporting, performed by the user, will be virtually impossible due to the system's dependency on current time stamp as the primary selection criteria, and the removal of the Social Security number as the primary key."

With the withdrawal of ISCD in April 1995, those duties which were to be performed by them were assumed by Standard Data Corporation through acceptance by PEIA of a proposal dated April 18, 1995. Under the terms of the new contractual arrangement with Standard Data Corporation effective August 1, 1995, Standard Data Corporation would be responsible for both designing the EIAS, as well as, programming and testing of the EIAS, converting the existing PEIA database, actual implementation of the EIAS including system installation and user training, creating system documentation including a user manual and an on-line help function and operation of the EIAS for PEIA on an out-sourcing basis, with an option to bring the system under direct State control in the future. The contract for these various services, including subsequent change orders needed to pay for computer equipment,

required for the EIAS totaled \$1,150,000.00. We were able to identify \$1,119,872.87 in payments to Standard Data Corporation related to this contract prior to the January 6, 1997 launch date of EIAS with an additional \$910,928.21 paid to Standard Data Corporation for earlier services related to system development for a total of \$2,030,801.08. Under additional terms of the August 1, 1995 contract and subsequent change orders, Standard Data Corporation has received another \$1,327,237.58 through April 30, 1999 for services provided under the out-sourcing arrangement since the launch of the EIAS resulting in documented payments to the vendor of at least \$3,358,038.66 as of April 30, 1999. With the additional \$526,121.46 paid to Jerone N. Deverman to act as a consultant to PEIA for the EIAS design and development, the total outlays related to EIAS development, design and out-sourcing through April 30, 1999 totaled **\$3,884,160.12**.

We reviewed Mr. Deverman's contract to establish his responsibilities in relation to the EIAS design and development. We found his contract stated in part:

**"...1.3 Consultant shall advise the PEIA throughout the logical system design phase of the EIAS project, with the expectation by both parties that such phase, including prior phases of project start-up and requirements confirmation, will be concluded no earlier than three months after project start.**

**1.4 Consultant shall advise and assist the PEIA throughout the detail design phase of the EIAS project, with the expectation by both parties that such phase, including all prior phases and**

culminating in a complete set of system specifications to support subsequent coding of programs, will be concluded no earlier than nine months after project start.

- 1.5 Consultant shall advise the PEIA, throughout the development phase of the EIAS project, regarding procedures for user testing of system functionality, user and system documentation, and on user training for eventual operational use of the system...."

As stated earlier, the contract with Standard Data Corporation provided PEIA the right to move the EIAS' operation back in-house and PEIA management decided in 1998 to do so. As of April 30, 1999 the work of ISCD continues with respect to correction of the shortcomings in EIAS as a part of the effort to move the EIAS to the direct control of PEIA. The Director of PEIA told us that effort continues; however, as of April 30, 1999, ISCD still has not demonstrated the capability to adequately support the EIAS. As a result, the \$42,570.00 per month out-sourcing arrangement with the vendor will continue until such time as ISCD can demonstrate their ability to provide adequate support for the EIAS.

We recommend the PEIA take advantage of those remedies available under the contracts with Standard Data Corporation and Mr. Jerone N. Deverman relating to the design and development of the EIAS system as may be available under the laws of the State of West Virginia to protect the best interests of PEIA, the State of West Virginia and its taxpayers.

Agency's Response

As pointed out in this finding, the majority of the retrospective credits were not taken by the agency. Controls are in place to ensure timely reconciliation of accounts with PEIA. Payroll locations are trained and understand the retrospective billing process, and will on most occasions identify problems to PEIA.

Significant importance has been placed on identifying the "glitch" that causes this problem. As stated in the Legislative Auditor's Finding #1, most errors are caught before coverage or misuse occurs.

EIAS does not support the accounting of funds for PEIA. Manual processes are in place until an automated solution is found.

The EIAS accounting module was written without the benefit of review by knowledgeable users and lacks functionality in aging of accounts receivable. This has caused PEIA to perform manual controls (i.e. reviewing accounts for improper aging results). The use of manual controls is labor intensive and inconvenient, but has not adversely affected PEIA's ability to monitor accounts receivable. Currently, no significant amounts are owed PEIA that were inappropriately aged.

*PEIA is reviewing its options concerning both the design and implementation of the software. Additionally, PEIA staff is developing strategies to deal with the program's shortcomings and resulting effects on our operations.*

*PEIA fully intends to review all remedies afforded through its contracts. Additionally, we will explore every available option to protect the integrity of the system and the insureds in this process.*

#### 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:**

<b>Rebates to be Disbursed to PEIA during the <u>Quarter Expected</u></b>	<b>Amount of Termination Fee to be Withheld by <u>First Health</u></b>
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 State 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 2<sup>nd</sup> (PCS Health Systems, Inc.) and 3<sup>rd</sup> (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.*

Claims Audit Contract

The Public Employees Insurance Agency (PEIA) entered into a \$35,000.00 contract with Wolcott & Associates, Inc. to perform an operational review and detailed claims audit and a Statement on Auditing Standards Number 70 (SAS 70) audit of PEIA's third party claims administrator. This contract was accepted by PEIA on April 11, 1997. Wolcott & Associates, Inc. had conducted the two prior operational audits and the prior SAS 70 audit of PEIA's third party administrator. This contract is indicative of another contract poorly administered by PEIA.

Although the purchase order attached to this contract contains a service period of March 28, 1997 through March 27, 1998, the contract itself does not specify a beginning and ending service period. PEIA is exempt from the Department of Administration's Purchasing Division rules and regulations and, therefore, the purchase order attached to the contract was not a necessary item required of this contract. Therefore, we are unsure as to how PEIA arrived at a contract service period. The contract only mentions the period that the work of Wolcott & Associates, Inc. will address. The contract appears to be a copy of the previous contract performed by Wolcott & Associates with the periods of claims to be examined "whited out" and new dates typed over the old

dates. For instance, the date of the correspondence from Wolcott & Associates, Inc. to PEIA was dated March 25, 1995, but shown as being received by PEIA March 27, 1997. This letter appears to be the cover letter from Wolcott & Associates, Inc.'s prior proposal which was not fully updated for the current assignment relative to dates, etc.

Wolcott & Associates in their proposal relating to their audit of PEIA medical claims processed by the third party administrator (TPA) state on page three,

**"...As part of our test work to determine eligibility of claimants, we will verify that TPA records agree with records maintained by the PEIA and that the claimant is an employee, retiree or dependent of an employee/retiree or other qualified participant based on PEIA records at the time the claim was incurred...."**

PEIA implemented a new Employee Insurance Administration System (EIAS) on January 7, 1997. Our work on this system indicated that the system's eligibility roles were unreliable. We found system problems that would re-activate former insured who were no longer in the system. Therefore, the possibility exist that Wollcott & Associates, Inc. could have reported on claims paid that should not have been paid by PEIA.

The West Virginia State Auditor prescribed rules and regulation effective May 25, 1997 establishing standards for requisitions for payment made to the State Auditor issued by State

officers. Section 155-1-4.1.b. prescribes "Contract Invoice Requirements" This section states:

"The date(s) of service, if the item to be paid is service. The date(s) shall fall within the contract period."

The billing for Wolcott & Associates, Inc. contained a period that appeared to be the period of paid claims examined. The period on the billing was July 1, 1996 through April 30, 1997, a period that is out of the scope of any period indicated on the purchase order or contract. PEIA should require an itemization of costs on any of its contracts or billings.

We recommend the PEIA comply with the requirements of Section 155-1-4.1.b of the State Auditor's rules and regulations governing invoices for services.

**Agency's Response**

***Procedures are currently in place to ensure the contracts are maintained in accordance with statute and documented properly for payment through the Office of the State Auditor.***

**Poor Administration of Contracts**

Chapter 5A, Article 8, Section 9 of the West Virginia Code, as amended, states in part:

"The head of each agency shall: . . .  
(b) Make and maintain records containing adequate and proper documentation of . . . essential transactions of the agency designed to furnish information to protect the legal and financial rights of the state and of persons directly affected by the agency's activities."

The West Virginia Public Employees Insurance Agency (PEIA) is given exclusive statutory authority to execute contract(s) to carry out its mandate without having to satisfy the purchasing provisions of the Department of Administration's Purchasing Division. Chapter 5, Article 16, Section 9 of the West Virginia Code, as amended states in part:

"(a) The director is hereby given exclusive authorization to execute such contracts as are necessary to carry out the provisions of this article ..."

"(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..

The Public Employees Insurance Agency had entered into many contracts totaling millions of dollars during the audit period to provide insurance coverage and the administration thereof to its members and for various other types of professional services such as audits and actuarial services. During our audit of the PEIA contracts, we noted the PEIA did not maintain adequate records of the transactions affecting contracts made on their behalf. This situation was previously reported in our prior audit of the PEIA. While the PEIA maintained files containing the invoices paid against each contract, they did not maintain contract ledgers posting these invoices on the majority of contracts which would allow them to know the remaining balance of the spending authority

pertaining to each contract. The situation increases the probability for the authorized contract amount to be exceeded because billings could be forwarded to the State Auditor for payment even though the contract amount had been reached. We believe the PEIA is responsible for maintaining the records on all contracts of the Agency. Also, the PEIA is responsible for determining that, when invoices (under a particular contract) are submitted for payment, the remaining unpaid and unencumbered balance of the particular contract is sufficient to pay these obligations.

In some of the contracts (Pacific Health Policy Group; Health Economics Research, Inc.; and, Michael Madalena) other State agencies would join PEIA for the contracted services. It was explained to us that these other State agencies (West Virginia Department of Health and Human Resources, Bureau of Medical Services; Workers' Compensation Division of the Bureau of Employment Programs; Department of Insurance; and, Health Care Cost Review Authority) would "piggy-back" on the contracts with PEIA because PEIA contracts were not subject to Division of Purchasing regulations as noted above. With these contracts, PEIA would become the primary payor and the other agencies would reimburse PEIA for their portion of the services rendered.

Specifically, PEIA, as part of the council of representatives from the State's health care agencies, entered into



a contract with Pacific Health Policy Group to provide on-site expertise needed to coordinate a managed care initiative for the State's health care programs, and to further advise and recommend streamlining efforts to promote administrative simplification and savings. The Council includes, but is not limited to, the PEIA, Workers' Compensation Division and the Bureau of Medical Services ("Medicaid"). The Council agreed that the PEIA would enter into a contract for the specific services and the other State health care programs would reimburse the PEIA for their share of the Contractor's services through interagency agreements.

The contracted services were divided into two Phases, I and II. The Phase I contract including amendments was not to exceed \$253,000.00 and the Phase II contract including amendments was not to exceed \$1,421,188.00. For Phase I of the contract, PEIA entered into reimbursement agreements with each of the respective representatives of the Council indicating their share of the cost of the contract. Agreements were signed with each of the following State entities along with their respective share of the cost of the contracted services: the Health Care Cost Review Authority (6 2/3%); Bureau for Public Health (6 2/3%); Bureau of Medical Services (actual costs amounting to approximately 26% of the total cost); Workers' Compensation Division (26 2/3%); and, the Department of Insurance (6 2/3%). For Phase I of the contract, PEIA disbursed \$251,119.00 and was reimbursed approximately \$182,480.00 from the various entities listed above.

Under Phase II of the contract, the PEIA disbursed approximately \$537,431.00 and received no reimbursements. The agreements entered into between PEIA and the various entities listed above was only for Phase I. We were told by PEIA staff that PEIA and the other entities could not reach a consensus on the percentage of reimbursement amounts in Phase II; and, therefore no agreements were signed for Phase II and PEIA bore the total cost.

Also, some overpayments occurred as a result of PEIA paying the total due on the invoice when the invoice for current services included a past due balance from the previous month or the consultant requested payment for the same services on two different invoices. Specifically, overpayments made to Michael Madalena totaling \$41,840.06 were caused by PEIA incorrectly paying for past due amounts and were subsequently discovered by Mr. Madalena and repaid to PEIA. Also, Mr. Madalena received a duplicate payment of \$2,750.00 in February 1997 caused by his invoicing PEIA for the same services on two different invoices. This \$2,750.00 was repaid to PEIA in April 1997.

We noted PEIA had not requested reimbursement from Medicaid totaling \$22,597.30 for services provided in January through March 1998 by one of the "piggy back" consultants (Michael Madalena). Also, on another "piggy back" consultant contract (Health Economics Research, Inc.), PEIA had not requested reimbursement for expenditures totaling \$2,891.43 paid on behalf of Medicaid and the Workers' Compensation Division.

Also, the PEIA is required by the West Virginia Code to provide wellness programs and activities to its members and their dependents. The PEIA contracts with wellness providers to furnish these services to its insureds. For fiscal year 1998, expenditures for wellness programs totaled \$509,091.00, and \$503,285.00 through February 5, 1999, for fiscal year 1999. Most of the providers are to provide monthly or quarterly reports to PEIA indicating the services provided and the participants who took advantage of the services. When we requested these reports for the purpose of reviewing them, most of the reports could not be located at PEIA. The staff of the PEIA had to contact each provider to request copies of the respective reports. With PEIA being unable to provide us with the reports, we believe the reports were not being reviewed by the PEIA to assure that the contracted services were being provided and that the participants of the services were actually PEIA insureds or their dependents.

We recommend the PEIA comply with Chapter 5A, Article 8, Section 9 of the West Virginia Code, as amended, and provide better monitoring of all contracts.

**Agency's Response**

***Procedures are currently in place to ensure the contracts are maintained in accordance with statute and documented properly for payment through the Office of the State Auditor.***

Overpayment of Former Employees' Final Pay

We examined the final pay of employees who had terminated their employment with the Public Employees Insurance Agency (PEIA) during the audit. Two of the four employees examined were overpaid a total of \$1,262.78. Chapter 12, Article 3, Section 13 of the West Virginia Code, as amended, states:

"No money shall be drawn from the treasury to pay the salary of any officer or employee before his services have been rendered."

The Chief Financial Officer was overpaid a total of \$1,112.78 in his final pay upon his resignation. The Chief Financial Officer was paid a full semi-monthly salary and should have only been paid for the five days actually worked in the pay period.

The Previous Director of PEIA was overpaid a total of \$2,090.08 upon his resignation, effective September 8, 1997. With the exception of \$150.00 in savings deposits withheld from the duplicate checks issued to the Director in error, all of his overpayments have been redeposited. The overpayments occurred as a result of the Director remaining on PEIA's payroll for three pay periods following his resignation with each payroll check representing a duplicate payment of the six days actually worked in the first pay period of September. Each of the duplicate checks issued to the Director included a \$50.00 deduction deposited into the Director's personal saving account. The first check issued

September 30, 1997, was cashed by the Director and ultimately refunded to PEIA and deposited on January 8, 1998. A stop payment was issued for the October 16, 1997 check and the check was redeposited on November 13, 1997. The third check issued on October 31, 1997 was retained by PEIA and redeposited on December 4, 1997. The \$150.00 in savings deductions have never been recovered by PEIA.

PEIA's payroll is administered by the Department of Administration and we were told the above errors occurred due to the person administering the payroll being new to the position at the time of these resignations.

We recommend the PEIA take the necessary steps to recover these overpayments from the affected ex-employees, if necessary take advantage of the remedies available under Chapter 14, Article 1 (CLAIMS DUE THE STATE) of the West Virginia Code, as amended.

**Agency's Response**

***PEIA has taken appropriate action to recover overpayments from affected former employees.***

**Retirement Withheld from Terminal Leave**

Section 15.3(f)(1.) of the West Virginia Division of Personnel's Administrative Rule prohibits the deduction of retirement contributions from the payment of terminal leave. Section 15.03 states in part:

"(f) Separation of Employment - The appointing authority shall pay an employee who separates from employment for any reason for all accrued and unused annual leave. . .

2. Any eligible employee ... who is separated from employment by resignation, layoff, dismissal, retirement, death, or termination, may be paid in a lump sum, at his or her option, for accrued and unused annual leave... No deductions may be made for contributions toward retirement from the lump sum payment; ..."

In our review of the terminal pay of employees who had resigned their positions with PEIA, we noted one employee's retirement contributions were withheld from the employee's total lump sum payment and not on the pay for time actually worked during the pay period. PEIA withheld \$105.39 from the employee's final pay settlement. The amount that should have been deducted based on the time actually worked was \$55.20, therefore PEIA deducted \$50.19 in excess of the proper amount.

The other effect of this improper deduction is that the employer matches the employee's deduction by 9.5% of the total wages. Based on the amount that the employer reported as being withheld from the employee's pay, the employer, therefore, would have contributed \$210.78 and not \$110.41 based on the salary for time actually worked. An excess amount of \$100.37 was improperly contributed by the employer to the Consolidated Public Retirement Board.

We recommend the PEIA take the necessary steps to recover the overpayment of the matching funds from the Consolidated Public Retirement Board.

**Agency's Response**

***PEIA has taken appropriate action to recover overpayments from affected former employees.***

**Errors in Payment of Overtime Hours**

Chapter 12, Article 3, Section 13 of the West Virginia Code, as amended states:

"No money shall be drawn from the treasury to pay the salary of any officer or employee before his services have been rendered."

During our examination of overtime compensation, we noted on several occasions that the number of overtime hours worked as recorded on the "Request to Pay Overtime" and the number of overtime hours documented as being paid on the payroll register did not match. One employee was overpaid a total of 29 hours in overtime compensation at a cost of \$372.02. Another employee was overpaid one hour in overtime compensation at a cost of \$14.80.

For the first employee, the payroll register for the first payroll period in October 1996 indicated the employee was paid a total of 54.25 hours of overtime compensation, however, the "Request to Pay Overtime" only indicated a total of 25.25 hours. The employee was over compensated a total of 29 hours at a cost of \$372.02. For the second employee the payroll register for the second pay period in September 1996 indicated the employee was paid a total of seven hours of overtime compensation, however, the "Request to Pay Overtime" only indicated a total of six hours. The employee was over compensated one hour at a cost of \$14.80.

We recommend the PEIA comply with Chapter 12, Article 3, Section 13 of the West Virginia Code, as amended. Also, PEIA should collect the overpayment from the affected employees.

**Agency's Response**

***PEIA has taken appropriate action to recover overpayments from affected former employees.***

**Meal Periods Included in Overtime Calculations**

We noted the Public Employee's Insurance Agency (PEIA) paid overtime to its employee's after 37.5 hours worked per week during the period July 1, 1996 through June 30 1998. PEIA utilizes the full eight-hour workday when computing employees' compensation. During the period noted above, the PEIA employees' work schedule was an eight-hour work day, with one-half hour of paid lunch. We determined the employees examined by us were paid a total of \$50,655.01 in overtime pay during the period July 1, 1996 through June 30, 1998. We calculated \$3,187.47 in overtime paid these employees out of the total overtime payments of \$50,655.01 was due to the one-half hour lunch periods being treated as work time.

The Fair Labor Standards Act (FLSA) which governs public employees does not require compensation for meal time when the employee is completely relieved from duty. Certain tests determine when meal time is required to be compensable. Section 441 Bona Fide Meal Periods of the FLSA states in part:

"A bona fide meal time, when the employee is completely relieved from duty, is not worktime. Whether or not an employee's meal



periods can be excluded from compensable working time under the FLSA, depends upon the tests discussed below (29C.F.R. §785.19). . .

**Employee freedom meal test**

Unless all of the following three conditions are met, meal periods must be counted as hour worked:

- (1) The meal period generally must be at least 30 minutes, . . .
- (2) The employee must be completely relieved of all duties; . . .
- (3) The employee must be free to leave the duty post. . ."

Based on our testing, we believe approximately 6% of the overtime paid to employees during the period noted above was attributable to meal periods being used to compute employees' hours worked. Applying this percentage to the total overtime paid of \$83,799.00, we believe as much as \$5,028.00 was attributable to the method used by PEIA to compute the employees' countable work time.

We recommend the PEIA comply with Section 441 of the FLSA in determining hours worked for compensation of overtime.

**Agency's Response**

***PEIA's method for determining overtime hours is now consistent with State of West Virginia policy.***

STATE OF WEST VIRGINIA

OFFICE OF THE LEGISLATIVE AUDITOR, TO WIT:

I, Theford L. Shanklin, CPA, Director of the Legislative Post Audit Division, do hereby certify that the report appended hereto was made under my direction and supervision, under the provisions of the West Virginia Code, Chapter 4, Article 2, as amended, and that the same is a true and correct copy of said report.

Given under my hand this 20<sup>th</sup> day of June,  
1999.



Theford L. Shanklin, CPA, Director  
Legislative Post Audit Division

Copy forwarded to the Secretary of the Department of Administration to be filed as a public record. Copies forwarded to the Public Employees Insurance Agency; Governor; Attorney General; and, State Auditor.