Audit Report

Department of Health and Mental Hygiene
Maryland Health Regulatory Commissions

November 2008

OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Karl S. Aro
Executive Director

Bruce A. Myers, CPA
Legislative Auditor

November 6, 2008

Senator Verna L. Jones, Co-Chair, Joint Audit Committee
Delegate Steven J. DeBoy, Sr., Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland

Ladies and Gentlemen:

We have audited the Health Regulatory Commissions of the Department of Health and Mental Hygiene for the period beginning September 26, 2005 and ending April 30, 2008. These three independent commissions are responsible for health-related functions, such as directing and administering the State's health planning functions, developing health care cost-containment strategies, reviewing and approving hospital rates, and increasing health care access for low-income, underinsured, and uninsured Marylanders.

Our audit disclosed that the Commissions had not resolved a finding from our two preceding audits. Specifically, the Maryland Health Care Commission had not recalculated its 2002 user fees, which were not determined in accordance with a change in State law, resulting in an improper allocation of fees among regulated health care industries and practitioners. We were advised that, as of July 2008, this matter was under legal review.

State law requires that user fees assessed by two of the commissions be used to cover the commissions' actual costs. These fees and expenditures are recorded in special non-lapsing funds. Similarly, the Maryland Trauma Physician Services Fund—which is maintained by these two commissions and which was established to reimburse trauma physicians and centers for certain costs—is funded by a surcharge on Maryland vehicle registrations. As of June 30, 2007, the commissions' fund balances had accumulated to $4.6 million and the Maryland Trauma Physician Services Fund balance had accumulated to $20.6 million.

The Department of Health and Mental Hygiene's response to this audit, on behalf of the Commissions, is included as an appendix to this report. We wish to acknowledge the cooperation extended to us during the course of this audit by the Commissions.

Respectfully submitted,

Bruce A. Myers, CPA
Legislative Auditor

Background Information

Agency Responsibilities

The Health Regulatory Commissions is a budgetary unit that comprises three independent commissions established by law: the Maryland Health Care Commission, the Health Services Cost Review Commission, and the Community Health Resources Commission.

The Maryland Health Care Commission (MHCC) is responsible for directing and administering the State's health planning functions, developing health care cost-containment strategies, and maintaining a database on all non-hospital health care services. The Health Services Cost Review Commission (HSCRC) is responsible for reviewing and approving hospital rates, collecting data on hospital utilization, and administering the Hospital Uncompensated Care Fund. The MHCC and HSCRC are jointly responsible for administering the Maryland Trauma Physician Services Fund. Chapter 280, Laws of Maryland 2005, effective October 1, 2005, created the Community Health Resources Commission (CHRC). The CHRC is responsible for increasing health care access for low-income, underinsured, and uninsured Marylanders by providing support to community health resources.

According to the State's records, fiscal year 2007 expenditures for the Commissions totaled approximately $101 million, of which approximately $70 million was paid to hospitals from the Hospital Uncompensated Care Fund.

Fund Balances

State law requires user fees assessed by the MHCC and the HSCRC to be used to cover the actual costs of fulfilling the statutory duties of these two commissions. A special non-lapsing fund to record these user fees was established for each commission. According to the Commissions' records, MHCC had a fund balance of approximately $3.5 million at June 30, 2007, representing 36 percent of its fiscal year 2007 general administration appropriation. Similarly, HSCRC had a fund balance of approximately $1.1 million, representing 34 percent of its fiscal year 2007 general administration appropriation. These fund balances indicate that the cumulative amount of user fees collected for these commissions have exceeded the costs of their operations.

The Department of Legislative Services' (DLS) analyses of the operating budgets for the Commissions have included comments that the balances of the aforementioned MHCC and HSCRC special non-lapsing funds exceeded the target level of 10 percent of annual general administration appropriations, and

indicated that these commissions should reduce these fund balances accordingly. This target level, which was intended to cover unanticipated costs or legislative mandates, was recommended in Sunset reviews conducted by the DLS in November 2000, and again in December 2005. Although the commissions took certain measures to reduce the fund balances (such as reducing HSCRC fiscal year 2007 user fee assessments by approximately 18 percent), the fund balances continue to exceed the target level.

Maryland Trauma Physician Services Fund

Chapter 385, Laws of Maryland, 2003, effective July 1, 2003, established the Maryland Trauma Physician Services Fund with the intent of stabilizing the trauma system in Maryland by reimbursing trauma physicians for costs associated with treating certain trauma patients, and by reimbursing trauma centers for costs to maintain trauma physicians on call. This special non-lapsing Fund is financed through a $2.50 annual surcharge on all Maryland vehicle registrations, and is overseen and administered by MHCC and HSCRC. According to the State's accounting records, the Fund's balance was approximately $20.6 million as of June 30, 2008, representing an increase of $2 million from its September 30, 2005 balance of $18.6 million.

Because the level of Fund expenditures anticipated by the initial legislation has not been met, legislation passed during the 2006 Legislative Session increased the compensation available to trauma centers and expanded the authorized uses of the Maryland Trauma Physician Services Fund. However, these changes had only a limited impact on the Fund's balance. Subsequent legislation (Chapter 627, Laws of Maryland, 2007) required the MHCC and HSCRC to include options for reducing the Fund's balance in the Fund's fiscal year 2007 annual report. For example, these options were to include (1) identification of one-time-only uses for eliminating the large surplus that accumulated in the early years of the Fund, and (2) ongoing uses of the Fund that would align annual expenditures with annual revenues. In their 2007 annual Fund report, the Commissions identified a number of options for reducing the balance in the Fund (such as expanding the specialties eligible for on-call reimbursement). Moreover, these options were included in legislation that was passed during the 2008 Legislative Session. Based on a review of the options included in the 2008 legislation, the Department of Legislative Services – Office of Policy Analysis determined that a reduction in the Fund balance was expected beginning in fiscal year 2009.

Status of Findings From Preceding Audit Report

Our audit included a review to determine the status of the two findings contained in our preceding audit report dated March 7, 2006. We determined that the Commissions had satisfactorily addressed one of the findings. The remaining finding is repeated in this report.

Findings and Recommendations

User Fees

Finding 1
As noted during our two preceding audits, MHCC did not assess fiscal year 2002 user fees in accordance with a new State law, resulting in an improper allocation of fees among regulated industries; MHCC has not resolved this issue.

Analysis
In our two preceding audit reports, we noted that MHCC had not assessed fiscal year 2002 user fees, which funded the MHCC's operations and totaled approximately $8.2 million, in accordance with State law. Specifically, a law change, effective July 1, 2001, required MHCC, in assessing user fees to each of its four regulated industries, to use a methodology that considers the amount of MHCC's workload attributable to each industry. The new legislation also required MHCC to assess user fees to certain health care practitioners (such as dentists) that had not previously been assessed user fees, and introduced a new waiver process. Although MHCC formally adopted a revised user fee assessment methodology at its December 2000 meeting, MHCC management advised that there was not enough time to fully implement all provisions of the new legislation before fiscal year 2002 fees were assessed. As a result, the fiscal year 2002 user fees were based on the percentages that existed prior to the law change and the newly identified health care practitioners were not assessed fees as required. The allocation method used did not affect the total amount of user fees assessed; rather, each regulated industry was either over-assessed or under-assessed. For example, hospitals were over-assessed $611,000 and nursing homes were under-assessed $652,000. Subsequent user fees have been based on the law changes.

We recommended in our preceding audit report that MHCC consult with the Office of the Attorney General (OAG) on this matter, which MHCC agreed to do. MHCC management personnel advised us that it contacted the OAG during the summer of 2008 and, as of July 2008, was awaiting its decision.

Recommendation 1
We recommend that, upon receipt of the OAG's decision, MHCC take the recommended action to resolve this matter.

Audit Scope, Objectives, and Methodology

We have audited the Health Regulatory Commissions of the Department of Health and Mental Hygiene for the period beginning September 26, 2005 and ending April 30, 2008. The audit was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine the Commissions' financial transactions, records and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations. We also determined the status of the findings contained in our preceding audit report.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of materiality and risk. Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of the Commissions' operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives. Data provided in this report for background or informational purposes were deemed reasonable, but were not independently verified.

Our audit did not include certain support services provided to the Commissions by the Department of Health and Mental Hygiene's Office of the Secretary and related units. These support services (such as payroll, purchasing, maintenance of accounting records, and related fiscal functions) are within the scope of our audit of the Office of the Secretary.

The Commissions' management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

Our audit did not disclose any conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect the Commissions' ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. This report includes a finding regarding a significant instance of noncompliance with applicable laws, rules, or regulations. Another less significant finding was communicated to the Commissions that did not warrant inclusion in this report.

The response from the Department of Health and Mental Hygiene, on behalf of the Commissions, is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise the Department regarding the results of our review of its response.

APPENDIX

STATE OF MARYLAND

DHMH

Maryland Department of Health and Mental Hygiene
201 W. Preston Street • Baltimore, Maryland 21201
Martin O'Malley, Governor – Anthony G. Brown, Lt. Governor – John M. Colmers, Secretary

November 3, 2008

Mr. Bruce Myers, CPA
Legislative Auditor
Office of Legislative Audits
301 West Preston Street
Baltimore, MD 21201

Dear Mr. Myers:

Thank you for your letter regarding the draft audit report of the Department of Health and Mental Hygiene – Maryland Health Regulatory Commissions for the period beginning September 26, 2005 and ending April 30, 2008. Enclosed you will find the Department's response and plan of correction that addresses the audit recommendation.

I will work with the appropriate Directors of Administration, Program Directors, and Deputy Secretary to promptly address the audit exception. In addition, the Division of Internal Audits will follow-up on the recommendation to ensure compliance.

If you have any questions or require additional information, please do not hesitate to contact me at 410-767-4639 or Thomas Russell, Inspector General, of my staff at 410-767-5862.

Sincerely,

John M. Colmers
Secretary

Enclosure

cc: James Johnson, Deputy Secretary for Operations
Rex M. Cowdry, M.D., Executive Director, Maryland Health Care Commission
Robert Murray, Executive Director, Health Services Cost Review Commission
Grace S. Zaczek, Executive Director, Maryland Community Health Resources
Ellwood L. Hall, Assistant Inspector General, Audits, DHMH
Thomas Russell, Inspector General, DHMH

Maryland Health Care Commission
Response to the Legislative Audit Report
Findings and Recommendations

Legislative Audit Finding 1:
As noted during our two preceding audits, MHCC did not assess fiscal year 2002 user fees in accordance with a new State law, resulting in an improper allocation of fees among regulated industries; MHCC has not resolved this issue.

Legislative Auditor's Recommendation:
We recommend that, upon receipt of the OAG's decision, MHCC take the recommended action to resolve this matter.

Administration's Response:
The Commission disagrees with the auditor's findings as the Commission believes that the FY 2002 assessments were properly determined in June 2001, using the methodology set forth in the law that was in effect when the required notifications were timely given. The General Assembly was aware that the implementation of the legislation would require both a process of consultation with the affected Boards and the promulgation of new regulations. This process was initiated promptly, the regulations became effective during the fiscal year, and notifications of resulting assessments were made in June 2002 for the next fiscal year.

The Commission has consulted with the Office of the Attorney General and is awaiting a decision**.** If the Office of the Attorney General determines the assessment should be recalculated, the Commission at this time would be unable to comply with their decision. For example Nursing Homes, Health Occupational Practitioners, Insurance Companies and Hospitals pay their fees per facility or per licensee. The process of reallocation would increase or decrease the amount owed to the Commission. We would be unable to collect or refund money to facilities that are no longer in business or to Health Occupational Practitioners who have no longer renewed their licenses.

Because the Commission is special funded, the recalculation of the assessments for Fiscal Year 2002 suggested by the audit, would not bring additional revenue to the State. As a practical matter, a recalculation for the Health Occupation Boards would require the State to reissue checks to approximately 50,000 board licensees for around .94 cents each. [1]

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[1] **Auditor's Comment:**
During our preceding audit, we obtained correspondence from the Chief Counsel for the Opinions and Advice of the Office of the Attorney General which concurred with our position that fiscal year 2002 user fees were not properly assessed, and stated that the law provided for no discretion on the timing of implementation of the law. In the event the pending decision of the Office concludes that the assessments should be recalculated and reassessed, we would suggest that the Commission, in consultation with the Office, develop an appropriate methodology for reassessment of the fiscal year 2002 user fees that addresses the concerns expressed in the Department's response.

Background Information

During the 1999 session of the General Assembly, House Bill 995 was merged with the Health Resources Planning Commission and the Health Care Access and Cost Commission to create the Maryland Health Care Commission. The Maryland Health Care Commission is a special funded agency supported by an assessment on four categories of payers, insurance companies, hospitals, nursing homes, and the health occupational licensing boards. House Bill 995 requires that, by June 30th of each year, the Commission give notification to each assessed entity of the amount of their fee (for the upcoming fiscal year). House Bill 995 also required the Commission to complete a workload distribution study, to make recommendations on the percentage of the budget to be paid by each industry, and to determine whether the current budgetary cap of $8.25 million would be sufficient to sustain forecasted expenditures.

The Commission completed the required study and presented several recommendations to the Commission at its December 2000 meeting which included: 1) raise the current cap from $8.25 million to $10 million; 2) keep an assessment apportionment in place for four years; 3) conduct a workload distribution study every four years; and, 4) seek to remove the apportionment formula from the statute and replace it with an apportionment formula promulgated through regulation(s), based on the workload distribution study. The Commission adopted staff's recommendations and the report was forwarded to the General Assembly on January 1, 2001, as required. The Commission then submitted legislation to implement these recommendations through Senate Bill 786 – The Maryland Health Care Commission – Modifications and Clarifications.

At the time the 2001 legislation was introduced, the Commission assessed only some of the Health Occupation Boards. Several of the Boards felt that all health care practitioners should be assessed and lobbied for their inclusion. Senate Bill 786, as adopted, included all health care practitioners in the assessment, but contained language directing the Commission to create a waiver process allowing those practitioners making wages that were "substantially" less than other providers to be exempted from the fee. The effective date of the bill was set as July 1, 2001, solely because the budget required an increase in the statutory ceiling to $10 million at the beginning of the fiscal year. It is important to note that the Commission was required to notify the Boards of their allocations for FY 2002 by June 30, 2001, before the effective date of the new legislation. As a practical matter, notifications have to go out well before the required notification deadline.

Implementation of the bill in fact involved much more that mere notification. The Commission also had to promulgate regulations setting forth both a process to determine which occupations would be exempted and the new allocations across industries. Even before the effective date of the legislation, the Commission began the work necessary to develop a method for determining exemptions for certain practitioners and to make necessary changes to the Commission's regulations.

This process included:

- determining the average annual wages across professions in order to establish which professions would be eligible for a waiver. This required the Commission to match each health occupation profession within the State personnel classification system in order to determine a representative average hourly wage;
- establishing an average annual wage below which professions would be exempted from the allocation;
- attending meetings of each of the Health Occupation Boards to review the law, to describe the scope of work, and to discuss the process for allocating and collecting the fees; and
- drafting, proposing, and adopting regulations to implement the new law.

After the above was done, the Commission:

- determined the base number of practitioners for the assessed health occupations boards, set the fee per practitioner, and, in June, notified the Boards of their status and assessments for the following fiscal year;
- surveyed each hospital and nursing home for admissions and revenue from the previous calendar year and, in June, notified each facility of its assessment for the following fiscal year; and
- surveyed each insurance company for earned premiums and, in June, notified each of its assessment for the following fiscal year.

AUDIT TEAM

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