Audit Report

Maryland Health Care Provider Rate Stabilization Fund

January 1, 2007 to December 31, 2007

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

March 10, 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:

As required by the Insurance Article, Section 19-808 of the Annotated Code of Maryland, we have audited the receipts and disbursements of the Maryland Health Care Provider Rate Stabilization Fund for the period beginning January 1, 2007 and ending December 31, 2007. The Fund is administered by the Commissioner of the Maryland Insurance Administration (MIA).

Our audit did not include procedures designed to verify the propriety of the subsidy payments made to medical professional liability insurers since State law requires MIA to conduct annual audits of each insurer for this purpose. At the time of our audit, MIA had not yet completed (including the issuance of audit reports) any audits under this requirement. Our audit also disclosed that delinquent premium taxes were not pursued on a timely basis.

A schedule of the Fund's financial activity for the 2007 calendar year is included in this report. As disclosed in that schedule, the Fund's cash balance was approximately $133 million as of December 31, 2007.

Respectfully submitted,

Bruce A. Myers, CPA
Legislative Auditor

Background Information

Establishment and Purpose of the Fund

The Insurance Article, Section 19-802 of the Annotated Code of Maryland established the Maryland Health Care Provider Rate Stabilization Fund effective April 1, 2005. The law provides that the Fund will serve several purposes, including retention of certain health care providers in the State by subsidizing their malpractice insurance premiums for a specified number of years, and by increasing fee-for-service rates paid to providers by the Maryland Medical Assistance program (Medicaid) and payments to managed care organizations that serve that program. The Fund is administered by the Commissioner of the Maryland Insurance Administration (MIA).

The Fund consists primarily of revenues generated by an annual premium tax imposed on health maintenance organizations and managed care organizations. All revenues are to be initially deposited into the Fund, and then allocated, in accordance with a schedule established in the law, to two accounts: the Rate Stabilization Account and the Medical Assistance Program Account. Amounts allocated to the Rate Stabilization Account are to be paid, in accordance with established criteria, to medical professional liability insurers who apply to MIA for rate subsidies on behalf of insured health care providers. Amounts allocated to the Medical Assistance Program Account are to be paid by MIA to the State's Department of Health and Mental Hygiene to increase payments to Medicaid providers and managed care organizations. The law provides that revenue allocations to the two accounts will continue through fiscal year 2009. Beginning in fiscal year 2010, all Fund revenues are to be allocated to the Medical Assistance Program Account.

Insurer Dividend Distributed to Fund

On September 12, 2007, the Board of Directors of the Medical Mutual Liability Insurance Society of Maryland, a medical professional liability insurer participating in the Fund, declared a dividend to its members in the amount of $68.6 million. Notice of the resolution adopted by the Board approving and implementing the dividend payment was provided to the Insurance Commissioner on the same date. Pursuant to the Society's participation in the Fund, as well as certain related statutory requirements, the Society proposed in its resolution distributing a portion of the dividend to the State (approximately $44.2 million), with the remainder being distributed to its policyholders in the form of a credit against their renewal premiums effective January 1, 2008.

As of December 12, 2007, the Society had received subsidies on behalf of its policyholders from the Fund totaling approximately $72.4 million, and was due an additional $11.7 million for calendar year 2007 for a total of $84.1 million. However, the law also provides certain conditions under which an insurer participating in the Fund must pay a portion of any dividend or similar distribution to the State. On September 13, 2007, the Insurance Commissioner issued an order to the Society to cease and desist from advertising, publicizing, implementing, or otherwise taking any action under or with respect to the dividend resolution adopted by the Society's Board of Directors. According to that order, a question existed as to the exact portion of the dividend to which the State was entitled. The Commissioner held public hearings on this matter, and on November 20, 2007, issued a final order requiring the Society to pay the entire dividend to the State for the benefit of the Fund. Payment was due within 30 days from the date of the order to allow parties from MIA and the Society to meet and determine if other alternatives to the Commissioner's order existed.

On December 12, 2007, the Board rescinded its original dividend declaration of $68.6 million and declared a new dividend in the amount of approximately $97.9 million. The Board proposed to divide the dividend between the Fund ($84.1 million) and the Society's policyholders ($13.8 million). On the same date, the Commissioner and the Society entered into a consent order agreeing to the terms in the Board's proposal. The Society also agreed that in 2008 it would not participate in the Fund nor would it receive any further disbursements. On December 19, 2007, the Society transferred $72.4 million ($84.1 million less $11.7 million due to the Society but not yet received) to MIA to be credited to the Fund's Rate Stabilization Account.

Financial Information

On page 5 is a summary of the receipts and disbursements for the Maryland Health Care Provider Rate Stabilization Fund for the period beginning January 1, 2007 and ending December 31, 2007, based on the State's accounting records. This summary is not intended to and does not provide the financial position and results of operations in accordance with generally accepted accounting principles. Specifically, certain financial statements and disclosures (for example, balance sheet, summary of significant accounting policies) have not been provided as would be required had this summary been prepared in accordance with generally accepted accounting principles.

SUMMARY OF FINANCIAL ACTIVITY

	January 1, 2007 to December 31, 2007
RECEIPTS:	
Premium taxes	$ 79,274,114
Premium tax exemption value [1]	9,170,192
Insurer dividend distributed to Fund [2]	72,419,650
Interest income	404,730
Total receipts	161,268,686
DISBURSEMENTS:	
Payments to medical professional liability insurers	23,911,651
Payments to Department of Health and Mental Hygiene	45,550,736
Administration expenses [3]	133,000
Total disbursements	69,595,387
EXCESS OF RECEIPTS OVER DISBURSEMENTS	91,673,299
FUND BALANCE (cash basis), December 31, 2006	40,913,598
FUND BALANCE (cash basis), December 31, 2007	$ 132,586,897

(1) Premium tax exemption value represents amounts paid by non-profit health maintenance organizations in lieu of premium taxes.

(2) See Background Information.

(3) The law provides for an annual allocation of up to $350,000 for costs incurred by the Commissioner to administer the Fund.

Findings and Recommendations

Audits

Finding 1
Required audits of applications submitted by insurers for subsidy payments were not completed on a timely basis.

Analysis
Required audits of application information submitted by medical professional liability insurers that applied for and received subsidies from the Fund were not completed on a timely basis. Such audits provide assurance that insurers properly calculated subsidy amounts due the insurers. We were advised that, as of February 20, 2008, the Maryland Insurance Administration (MIA) was in the process of completing audits of three of the four insurers who had applied for and received subsidy payments for subsidy year 2005. However, MIA had not yet held exit meetings to discuss the audit results with the insurers or issued audit reports, and MIA was uncertain as to when these actions would occur. We were further advised that an audit of the fourth insurer had just been started on February 15, 2008. Subsidy payments to insurers totaled $29.6 million, $42.3 million, and $23.9 million for calendar years 2005, 2006, and 2007, respectively.

The law requires the Commissioner (or designee) to conduct an annual audit to verify application information submitted by each medical professional liability insurer that applied for a subsidy payment from the Fund for an applicable subsidy year. Since all participating insurers do not implement rate changes on the same date and often renew policies on a staggered basis throughout the year, the subsidy year for each insurer will vary and may not end for months after the end of the related calendar year (for example, subsidy year activity may not be completed for more than a year after the related calendar year). MIA policy provides that audits will begin as soon as practicable after the end of the insurer's subsidy year. We believe that MIA should complete these audits on a timely basis.

Recommendation 1
We recommend that MIA complete audits of subsidy application information submitted by insurers on a timely basis, and take any appropriate follow-up action deemed necessary.

Delinquent Premium Taxes

Finding 2
MIA did not pursue delinquent premium taxes on a timely basis.

Analysis
MIA did not pursue delinquent premium taxes on a timely basis. Our review disclosed that, as of January 2008, one health maintenance organization (HMO) had not made required quarterly tax payments or filed the related tax forms for the last three quarters of calendar year 2007. Additionally, MIA had not taken any action to determine why the payments and forms, which were due June 15, September 15, and December 15 of 2007, had not been received. MIA advised us that the company owed approximately $2.9 million for these three quarters.

As previously mentioned, the Fund consists primarily of revenues generated by an annual tax imposed on premiums written by HMOs and managed care organizations (MCOs) for insurance business transacted in the State. The law requires all entities subject to the tax to make quarterly tax payments and file a corresponding tax declaration form. Although entities that do not submit premium taxes when due are subject to interest charges and penalties as provided for in the law, we believe that MIA should take appropriate follow-up action on a timely basis when required payments are not received. During calendar year 2007, the Fund received approximately $88 million in premium taxes or premium tax exempt values from a total of 14 HMOs and MCOs.

Recommendation 2
We recommend that, in the future, MIA pursue delinquent premium taxes on a timely basis. Specifically, we recommend that MIA contact applicable HMOs or MCOs within a reasonable period of time, such as 30 days, when a required tax form and/or payment is not received. We also recommend that MIA collect all taxes due from the HMO noted in our review, along with any applicable penalties and interest.

Audit Scope, Objectives, and Methodology

As required by the Insurance Article, Section 19-808 of the Annotated Code of Maryland, we have audited the receipts and disbursements of the Maryland Health Care Provider Rate Stabilization Fund for the period beginning January 1, 2007 and ending December 31, 2007. The Fund is administered by the Commissioner of the Maryland Insurance Administration (MIA). The audit was conducted in accordance with generally accepted government auditing standards.

The objectives of this audit were to examine the Fund's receipts and disbursements and related records and internal control, and to evaluate compliance with applicable State laws, rules, and regulations.

Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of the Fund's operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives.

MIA is required by law to annually audit each medical professional liability insurer that applied for a subsidy payment from the Fund to verify application information submitted by the insurer; accordingly, our audit did not include procedures designed to verify the propriety of the amounts requested by medical professional liability insurers and the disposition of such payments. As previously mentioned, at the time of our audit, MIA had not yet completed (including the issuance of audit reports) any audits under this requirement. Therefore, we will review the results of MIA's audits during subsequent audits of the Fund. In addition, we conducted a separate audit of the Medical Mutual Liability Insurance Society of Maryland as required by State law, for the period beginning January 1, 2005 and ending December 31, 2006. Our audit report on the Society was issued on February 25, 2008.

Our audit did not include certain support services provided to the Fund by MIA. These support services (such as maintenance of accounting records and related fiscal functions) are included within the scope of our audit of MIA.

MIA's management is responsible for establishing and maintaining effective internal control over the Fund. 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.

This report includes a finding relating to a condition that we consider to be a significant deficiency in the design or operation of internal control that could adversely affect MIA's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our report also includes a finding regarding a significant instance of noncompliance with applicable laws, rules, or regulations.

MIA's response to our findings and recommendations 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 MIA regarding the results of our review of its response.

APPENDIX

MARTIN O'MALLEY
Governor

ANTHONY G. BROWN
Lt. Governor

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RALPH S. TYLER
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BETH SAMMIS
Deputy Commissioner

March 7, 2008

Bruce A. Myers, CPA, Legislative Auditor
State of Maryland
Office of Legislative Audits
State Office Building, Room 1202
301 West Preston Street
Baltimore, Maryland 21201

Dear Mr. Myers:

Please find enclosed the Maryland Insurance Administration (MIA) response to the draft audit report on the Maryland Health Care Provider Rate Stabilization Fund January 1, 2007 to December 31, 2007.

In addition to the enclosed hard copy of the response, an electronic version was sent to response@ola.state.md.us.

If you have any questions or need additional information, please contact Lester C. Schott, Associate Commissioner. His direct telephone number is (410) 468-2119.

Sincerely,

Ralph S. Tyler
Commissioner

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Enclosure

MIA Response to
Findings and Recommendations

Finding 1
Required audits of applications submitted by insurers for subsidy payments were not completed on a timely basis.

Recommendation 1
We recommend that MIA complete audits of subsidy application information submitted by insurers on a timely basis, and take any appropriate follow-up action deemed necessary.

MIA Response:
The audits were initiated as soon as practicable after the end of the insurer's subsidy year as required by MIA's internal policy. Additionally the fieldwork is substantially complete for three of the four audits; however, finalization of the audits and issuance of the related reports has been delayed. These delays are primarily due to issues disclosed during these initial audits of the carriers' rate subsidy requests, which in several instances required review and advice of legal counsel to resolve. We agree the audits should be completed on a timely basis, and fully intend to do so.

We expect to conduct exit meetings with two of the insurers by March 31, 2008, and issue the final report by April 30, 2008. The fieldwork for the third 2005 subsidy year audit is scheduled for completion by March 31, 2008, with an exit meeting to be held in April 2008 and final report issuance in May 2008. The final 2005 subsidy year audit is expected to be completed in May 2008, with an exit meeting to be held in June 2008 and final report issuance in July 2008. Additionally, we intend to start the audits for the 2006 subsidy year for the carriers that are still participating in the rate subsidy program as soon as practicable after the end of their 2006 subsidy year activity.

Finding 2
MIA did not pursue delinquent premium taxes on a timely basis.

Recommendation 2
We recommend that, in the future, MIA pursue delinquent premium taxes on a timely basis. Specifically, we recommend that MIA contact applicable HMOs or MCOs within a reasonable period of time, such as 30 days, when a required tax form and/or payment is not received. We also recommend that MIA collect all taxes due from the HMO noted in our review, along with any applicable penalties and interest.

MIA Response:
The MIA does not pursue missing quarterly estimated tax payments, but rather, relies on the final return and audit of the return to detect missing or underpayments. As part of the final audit an underpayment of quarterly estimated taxes is assessed penalty and interest as provided for by statute. Our procedure is consistent with other federal and state taxing authorities. However, we recognize that the tax collected from health maintenance organizations (HMOs) and managed care organizations (MCOs) funds the rate stabilization fund, and the funding in each year is dependent upon a projected level of collections. Therefore, we agree to pursue missing quarterly estimated tax payments from HMOs and MCOs.

Regarding the tax owed by the one HMO that had not made estimated tax payments for the last three quarters of calendar year 2007, the MIA contacted the HMO and as of March 6, 2008, the HMO wired the estimated taxes due totaling $2,905,224 to the State. Any penalty and interest due as a result of the HMO's late payment of estimated taxes will be computed and assessed in conjunction with the audit of the annual premium tax return, which is due by March 15, 2008.

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