A Report on the MDCH Audit Agency
Review of Administrative Outreach Program (AOP) Cost Reports
For the Quarters Ended March 31 and June 30, 2006

Executive Summary

Objectives:
The primary objective of our review was to identify and contact school districts that were incorrectly reporting estimated salaries rather than actual earnings as required by MDCH policy. Any apparent clerical errors within cost reports were also noted.

Conclusions:
We believe all school districts in Michigan are now correctly reporting actual salaries on their AOP cost reports. Additionally, only a few isolated clerical errors were discovered during the review. The small number and types of errors found did not provide a basis for recommending improvements at this time.

We confirmed that three of the (approximately) 700 school districts in Michigan did not report the actual salaries paid during the quarter ended March 31, 2006. All have agreed to report actual salaries on future cost reports. Due to materiality, we did not confirm estimates were used in five additional districts that may have improperly reported salaries. Those five districts had only one or two AOP employees and the potential effect on Medicaid claims was insignificant. We sent a letter asking those districts to begin reporting the actual salaries paid if their reports were based on estimates. No follow-up was made to determine if corrections were deemed necessary.

Three clerical errors were found in approximately 1,400 cost reports reviewed. Two revisions were sent to the AOP claims processing contractor (PCG). The third error was relatively insignificant. The small number and types of errors found did not provide a basis for recommending improvements at this time.

Background:
Prior audits found the salaries reported on AOP cost reports submitted by two local school districts were based on estimates. In each instance the school districts reported their employees' contracted salaries divided by four on quarterly AOP cost reports. However, employees were actually paid every two weeks.

Bi-weekly payrolls result in six pay periods during two fiscal quarters, alternating with seven pay periods in the other two quarters. The two schools that used budget estimates reported an amount equal to (26 pay periods / 4 quarters per year =) 6 ½ payments each quarter.

MDCH policy requires school districts to report actual salaries on their AOP cost reports. This requirement provides some assurance the employees worked during the report period, whereas using estimates based on salary contracts signed at the beginning of a school year does not. Use of contracted salaries provides no assurance the employees did not leave the district early for

medical reasons, dismissal, layoffs or other reasons. Actual salaries on cost reports begin an audit trail to the payroll documents which provide the added assurance that work was performed.

None of the estimated staff salaries on AOP cost reports could be accepted during our audits, even though the estimates for an entire school year should be similar to the actual salaries earned the same year. As described above, the estimates violated MDCH policy and provided no audit trail to payroll records. The estimates also resulted in incorrect Medicaid claims because certain allocation rates developed for a specific fiscal quarter would be applied to salary costs that were not paid in the same quarter. When the unallowable estimates were found during AOP audits, a school district could either (1) prepare all new cost reports suitable for audit, using actual salaries and fringe benefits, or (2) lose reimbursement for all the estimated costs found during the audit. School districts have elected to correct their cost reports for our audits rather than lose their Medicaid reimbursement. The administrative costs for schools to prepare new cost reports and for auditors to review the revised reports are significant when compared to the differences in allowable costs.

Our prior audits also found a few clerical errors that had not been discovered by PCG's review procedures. One error over-stated an employee's salary by more than one million dollars.

Purpose and Methodology

The primary purpose of our review was to identify school districts that may be reporting estimates of AOP salaries, based on budgets or their employees' contracts, rather than the amounts actually paid to the employees. Our objective was to have all school districts report the actual staff salaries earned. This objective brings future cost reports into compliance with MDCH policy, allows for the proper calculation of allowable Medicaid costs and eliminates the administrative costs of preparing corrected cost reports for future audits.

To accomplish our objective we compared the salaries reported for individual employees in the quarter ended March 2006 to the salaries reported for the same employees in the quarter ended June 2006. Because most schools pay their employees bi-weekly, most employees received pay for six pay periods in one quarter and pay for seven periods in the next quarter. Districts that reported nearly identical salaries for each employee in the two consecutive quarters were possibly reporting annual salaries divided by four. These districts were identified for further review.

We were able to eliminate some districts from additional review by extending our salary comparisons to a third cost report. School employees in some districts did not receive pay during summer vacation. If the school year ended early in June, the employees were paid for only six of the seven possible pay periods in the QE June 30. A district could properly report identical salaries earned for six pays in both the March and June quarters. These were eliminated from further review if the salaries reported for the QE December 31, 2005 were different than the (identical) salaries reported for the March and June 2006 quarters.

It was also possible that certain districts properly reported identical salaries in several consecutive quarters because that was the amount the employees actually earned each quarter. Employees in a few districts are paid monthly, or twice a month, making their salaries identical for any three month period during a school year. We therefore contacted each school district that reported identical, or nearly identical, salaries on three consecutive cost reports.

Our contact with small districts was limited to a letter passed through their ISD instructing them to begin reporting actual salaries if they are currently reporting estimates. Even if a small district continues to report estimated amounts, the effect on Medicaid claims will be minor. Also, identifying one employee's actual salary for future audits should be administratively simple in any district.

Large districts that reported similar salary amounts on three consecutive cost reports were also contacted by letters sent through their ISDs. However, letters to large districts requested they contact the MDCH auditor. In that way we were able to assess any explanation, answer any questions about what is required or why, and offer our assistance in preparing correct cost reports. When a district offered to correct future cost reports, we requested they send us a copy of the report sent to PCG. In our opinion these actions provide adequate assurance that all large districts in Michigan will report actual salaries rather than estimates on their cost reports.

The objective of our clerical error review was to assess the effectiveness of PCG's review for clerical errors. Their quality assurance procedures include reviews for staff that exceed salary thresholds and for fringe benefits that are an unusually high percentage of salaries. Our prior audits found a few salaries and fringe benefits that exceeded PCG's review parameters and yet were included in Medicaid claim calculations. Since we needed to compare the salaries listed on about 1,400 cost reports while searching for schools reporting estimated salaries, we also noted any salaries or fringe benefits that seemed too high.

Results

Reporting Estimates:

We believe all school districts in Michigan are now reporting actual salaries on their AOP cost reports. Two districts that reported estimated salaries have agreed to start reporting actual costs. Our contact with a third district found they used estimates only during our review period, before a new employee was properly trained. Five small districts may have reported estimated salaries; we reminded each of these districts and their ISDs that actual salaries paid must be used for AOP cost reports.

Clerical Errors:

We confirmed three clerical errors were not identified and corrected by PCG's review procedures. After allocations, we estimate FFP was over-claimed by less than $1,000 during our six month review period as a result of the errors. Revised claims for the significant errors were submitted to PCG.

One $109,000 error should have been identified by PCG's quality assurance procedures. Their procedures state that line items are flagged when participant costs exceed a ratio of 55% benefits to salary. We found one AOP participant that had a $28,186 salary reported with $121,032 of fringe benefits, clearly exceeding PCG's 55% review parameter. The school district confirmed for us that an extra "1" was inadvertently typed in the report. The correct amount was $12,032.

The other two errors found in our review would not have been caught by PCG's review procedures, but they were relatively minor. One district reported about $17,000 of support worker salaries in the "Name" column of their cost report. PCG has no review procedure designed to spot such unexpected errors. Another district reported more fringe benefit cost than salary for one of their four support workers. We confirmed the benefits reported were overstated by $2,500. PCG has no review of support worker benefits in districts that list fewer than 30 support workers.

The small number and the types of errors we found in the 1,400 reports reviewed do not provide a basis for any recommendation(s) for improvement. Because MDCH policy does not require PCG to report the number of errors they find through reviews, we can not determine whether the small number is from careful preparation by school districts or from PCG reviews. Additionally, the isolated errors that were identified were not systematic and may be the types of errors that can occur in most systems.