

Calendar Year 2019 California Health & Wellness Mainstream Rate Development Template

Auditor's Report

California Department of Health Care Services

January 17, 2023

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Section 1

Executive Summary

Pursuant to federal requirements under Title 42 of the Code of Federal Regulations 438.602(e), the State of California Department of Health Care Services (DHCS) must periodically, but no less frequently than once every three years, conduct, or contract for the conduct of, an independent audit of the accuracy, truthfulness, and completeness of the encounter and financial data submitted by, or on behalf of each managed care organization (MCO). DHCS contracted with Mercer Government Human Services Consulting (Mercer), part of Mercer Health & Benefits LLC, to fulfill this requirement for the financial data submitted in the Medi-Cal rate development template (RDT) for calendar year (CY) 2019 by California Health & Wellness (CHW). Mercer designed and DHCS approved procedures to test the accuracy, truthfulness, and completeness of self-reported financial data in the RDT.

The specific financial schedules selected for testing are used by Mercer as a critical part of the base data development process for capitation rate development related to the CY 2022 rating period. The RDT tested was the final version, including any revisions stemming from resubmissions as a result of the RDT Question and Answer discussion guide process with the MCO.

The key schedules subject to testing from the RDT include, but were not limited to:

- Schedule 1 — Utilization and Cost Experience
- Schedule 1A — Global Subcontracted Health Plan Information
- Schedule 1C — Base Period Enrollment by Month
- Schedule 1U — Utilization Management/Quality Assurance/Care Coordination (UM/QA/CC)
- Schedule 5 — Large Claims Report
- Schedules 6a and 6b — Financial Reports
- Schedule 7 — Lag Payment Information

The data collected in the RDT is reported on a modified accrual (incurred) basis for CY 2019 and does not follow generally accepted accounting principles with regards to retroactivity from prior year activity, including claim or capitation accruals, retroactive enrollment, or termination of enrollment of members from prior years. The data provided is designed to report only financial and enrollment activity incurred for the CY reported.

The procedures and results of the test work are enumerated in Table 1 of Section 2.

Section 2

Procedures and Results

Mercer has performed the procedures enumerated in Table 1 below, which were designed by Mercer and were reviewed and agreed to by DHCS, solely to test the completeness, accuracy, and truthfulness of information reported in the Medi-Cal RDT from CHW for the CY 2019. CHW's management is responsible for the content of the RDT and responded timely to all requests for information.

Table 1: Procedures

| Category | Description | Results |
|------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Fee-for-Service (FFS) Medical Expense | <p>Mercer reviewed all paid claims data for each category of service (COS) to verify control totals, verify eligibility and enrollment in the Mainstream Medi-Cal program, confirm the COS grouping was correct, confirm the year reported was correct, and confirm enrollment with CHW for date of service.</p> <p>Mercer compared detailed lag tables for each major COS (Inpatient, Outpatient, Physician, Pharmacy, Facility-LTC, and All Others) created from the paid claims data files provided by CHW and compared the information reported in Schedule 7. Mercer compared the paid claims amounts from Schedule 7, line 35 and the incurred but not reported (IBNR) amount from Schedule 7 line 40 to total paid claims data as provided by CHW. Allowable absolute value</p> | <ul style="list-style-type: none"> Control totals: No variance noted. Eligibility: No unexplained variances noted. COS Map: No variance noted. Service Year: No variance noted. <p>Variance: RDT Overall FFS expenses over/(understated):</p> <ul style="list-style-type: none"> Inpatient 0.57% Outpatient 2.56% LTC (4.26%) Physician 0.19% Pharmacy (0.08%) All Other 13.04% <p>In Total 1.47% or \$8,317,730</p> |

| Category | Description | Results |
|-------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------|
| | variances were deemed to be not greater than 2% for inpatient claims and 1% for all other COS. | |
| | Using data files (paid claims files) provided by CHW, Mercer sampled and tested 60 transactions across each major COS (Inpatient, Outpatient, Physician, Pharmacy, Facility-LTC, and All Others) and traced sample transactions through CHW's claims processing system, the payment remittance advice, and the bank statements. | No variance noted. |
| Sub-capitated Medical Expense | Mercer requested overall non-global subcapitation supporting detail. Mercer compared the support provided to the amounts reported in Schedule 7. The total of the detail provided agreed to the amounts reported in the RDT. | No variance noted. |
| | Mercer reviewed a sample of the five highest provider payments and ten random payments, reviewed the related contractual arrangements, and recalculated the total payment amounts by sub-capitated provider using roster information provided by CHW. | Variance: RDT Sub-capitated Medical Expense overstated by 0.08%, or \$2,400. |
| | Mercer observed proof of payments via relevant bank statements, clearing house documentation or | No variance noted. |

| Category | Description | Results |
|---------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| | <p>other online financial institution support for the sampled sub-capitated provider payments in the previous step.</p> <p>Mercer obtained roster information for the sampled provider payments and verified eligibility of members, confirmed enrollment with CHW, and analyzed claims to verify none of the FFS claims paid should have been covered by the sub-capitated arrangement.</p> <p>If applicable, Mercer reviewed full-dual COA subcontracted per member per month (PMPM) payment rates to determine if the amount(s) are at a reduced rate as compared to the non-full dual COAs.</p> <p>Mercer reviewed the sampled sub-capitated contracts to determine delegated administrative duties. Using this information, Mercer then reviewed the amount of administrative dollars reported in the RDT as compared to the delegated administrative functions.</p> | <p>No variance noted.</p> <p>All rates as expected.</p> <p>Per CHW, their sub-capitated contracts do not have an administrative component, therefore none reported in the RDT. However, based on Mercer's review of the sampled sub-capitated contracts, Community Care, IPA and Optima/Envolve both contain administrative functions. See Appendix A for details.</p> |
| Utilization and Cost Experience | Mercer compared summarized total net cost data from amounts | No variance noted. |

| Category | Description | Results |
|---------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Member Months | <p>reported in Schedule 1 to Direct Medi-Cal COS totals from Schedule 6a and to total incurred claims by COS for Schedule 7 for consistency.</p> <p>Mercer compared MCO-reported member months from Schedule 1C to eligibility and enrollment information provided by the State. Mercer's procedures are to request explanations for any member months with greater than 0.5% variance in total or greater than 1.0% variance by major COA.</p> | Variance: RDT overstated by 0.28% in total. |
| Provider Incentive Arrangements | <p>Mercer requested a listing of all provider incentive arrangements, by provider, by month and compared the amounts to Schedule 6a, lines 34–36.</p> <p>From the listing of provider incentive payments, Mercer sampled the highest two payment amounts and one random payment. Mercer observed proof of payments for the sampled provider incentive payments. The proof of payment information agreed to the supporting detail provided for the sampled provider incentive payments. As a result of the review of the Imperial County arrangement not</p> | <p>Variance: RDT Provider Incentive Expense is overstated by 4.73%, or \$282,232 after removing the amount paid to Imperial County noted below. This amount represents 0.05% of total medical expense.</p> <p>Variance: CHW reported \$1.03 million in incentives paid to Imperial County that have the parameters of a revenue sharing arrangement rather than a true incentive arrangement with specific quality or other measures to meet. Therefore, this amount was disallowed as an incentive amount/medical expense and is excluded from the support used in the variance calculation reported above.</p> |

| Category | Description | Results |
|-------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------|
| | meeting allowable incentive guidelines (noted in the results column), Mercer sampled three additional incentive arrangements. The resulting complete sample tested represents 48.25% of the total incentive amount reported on Schedule 6a. | |
| | Mercer reviewed the listing of provider incentive payments for any payments to related parties. If the review of the provider incentive payment listing showed payments to related parties, and the sample selection in the previous step did not include related party arrangements, Mercer selected the two highest related party provider incentive payments. Mercer observed proof of payments for the sampled related party provider incentive payments. | No related party incentives paid. |
| | If related party provider incentive payments were noted, Mercer reviewed the incentive terms to determine if the terms align with similar arrangements for non-related parties. | N/A. |
| Reinsurance | Mercer reviewed the reinsurance contract and compared the amount on the RDT to the requested supporting schedule. | No variance noted. |

| Category | Description | Results |
|-------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Settlements | Mercer recalculated reinsurance premiums, based on 2019 RDT reported membership, to compare to reported amounts. | No material variance noted. However, per the reinsurance agreement provided, CHW pays the minimum premium but is subject to periodic adjustments. For CY 2019, CHW was charged the maximum premium. CHW's premium is based on block pricing with its affiliates/parent, thus the experience of the group caused the increase to the maximum premium, even though no recoveries were incurred for CHW. The entire reinsurance premium, however, represents only 0.06% of total medical expense. |
| | Mercer recalculated recoveries for a sample of five members. | No cases exceeded the reinsurance threshold. |
| | Mercer compared the amount of reinsurance recoveries as compared to the information in Schedule 5 for reasonableness. | Reported amounts in Schedule 5 are consistent with zero recoveries based on review of the reinsurance threshold. |
| | Mercer inquired of CHW if they incurred any settlement amounts with providers related to CY 2019 dates of service. If settlements exist, Mercer noted whether the amounts are actual or estimates based on the status of the settlements and where the amount(s) are reported in the RDT. | Variance: RDT Settlements are understated by 513.27%, or \$2,362,030. This amount is only 0.38% of total medical expenses. The entire settlement is related to Sutter Health and is based on disputed claims submitted by Sutter Health. Of this amount, \$1,627,213 had been paid by CHW as of the time of the audit. |

| Category | Description | Results |
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| Third Party Liability (TPL) | Mercer reviewed TPL as a PMPM and as a percentage of medical expense on Schedule 6a line 39 as compared to benchmark information across those plans reporting a value for TPL. | The benchmark TPL percentage was 0.04%. CHW did not report any TPL in the RDT. |
| Administrative Expenses | <p>Mercer benchmarked administrative expenses as a percentage of net revenue across all Two-Plan/GMC plans and compared to the amount reported in Schedule 6a, taking into consideration the membership size of the plan under review when reviewing the results.</p> <p>Mercer compared detailed line items from the plan's trial balance mapped to line items in Schedule 6a and Schedule 6b for reasonableness. Mercer reviewed allocation methodologies and recalculated for reasonableness.</p> | <p>The benchmark administrative percentage was 6.07% and CHW reported 13.16%, primarily driven by higher than average Compensation and Outside Services (on a PMPM basis). It should be noted that 88.64% of the administrative expenses are with Centene Management Company, LLC (Centene), a related party. CHW pays Centene 12% of capitation premiums for administrative services, which is significantly more than the benchmark administrative percentage derived from all other Two-Plan/GMC plans.</p> <p>Variance: RDT Administrative Expenses are overstated by 2.24%, or \$1,942,982. The entire variance is due to an administrative to claims reclassification reported in the trial balance, but not reported on line 53 "Admin to Claims Reclass" on the RDT.</p> |

| Category | Description | Results |
|----------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Taxes | Mercer reviewed to ensure proper reporting of federal, state, and local taxes on line 59 of Schedule 6a. | Variance: RDT reported income taxes correctly. |
| Related Party Transactions | Mercer obtained related party agreements and reviewed to determine if the terms are at fair market value. Mercer compared the terms (e.g., PMPM or other payment rate amounts) to other similar non-related party terms for reasonableness. | <p>There were no significant related party arrangements for medical services with the exception of Pharmacy. Envolve Pharmacy Solutions accounts for approximately 93% of the pharmacy spend. This amount includes spread pricing of \$3.50 million for the period January 2019–March 2019. The remainder of 2019 was paid on pass-through pricing only. This spread pricing represents an overstatement of allowable medical expenses of \$3.50 million, or 0.57% of total medical expenditures.</p> <p>The pharmacy benefits manager (PBM) expense related to Envolve Pharmacy Solutions was \$3.31 million, which is reasonable and is appropriately included in administrative costs.</p> <p>CHW is charged 12% of capitation revenue by Centene, a related party for management fees. This exceeds an acceptable range for industry standards as well as compared to the</p> |

| Category | Description | Results |
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| | | benchmark for similar Medi-Cal plans as noted. |
| | If related party contracts are a material portion of the related medical COS, Mercer also reviewed any allocation methodologies for reasonableness. | No material related party arrangements for medical services other than pharmacy, as outlined above. |
| | Mercer reviews that all services included in the related party agreements are allowable for Medicaid rate setting. | As noted within, pharmacy spread pricing and excessive administrative expense allocation were included within the RDT. These findings have been noted and results reported as appropriate. |
| | When applicable, Mercer obtained related party corporate allocation methodologies for administrative services. Where significant, Mercer recalculated the amounts for reasonableness. | CHW reported \$76.65 million in management fees paid to Centene. This amount equates to approximately 12% of net premium revenue, consistent with the terms of the arrangement. Again, as noted previously, this fee is considered excessive as compared to the Two-Plan/GMC benchmark of just 6.07%. |
| UM/QA/CCs | Mercer benchmarked UM/QA/CC expenses as a percentage of total medical expense across all Two-Plan/GMC plans and compared to the amount reported on Schedule 6a, taking into consideration the membership size of the plan under review when reviewing the results. | The benchmark UM/QA/CC percentage was 1.57% and CHW reported 2.42%, which is within an acceptable range. |
| | Mercer compared detailed line items from the plan | No variance noted. |

| Category | Description | Results |
|--------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------|
| | mapped to line items in Schedule 1-U for reasonableness. Mercer reviewed allocation methodologies and recalculated for reasonableness. | |
| | Mercer interviewed financial management to determine how health care quality improvement activities such as care coordination are isolated from general administrative expenses in the general ledger. Confirmed with CHW management via interview that UM/QA/CC costs were not also included in general administrative expenses. | Confirmed. |
| Pharmacy | Mercer confirmed and observed pharmacy benefit manager fees were recorded as administrative expenses and not included in pharmacy claims expenses in the RDT. | As referenced above, the PBM fees are appropriately reported as administrative costs but as noted were paid to Envolve Pharmacy Solutions, a related party. |
| | Mercer benchmarked pharmacy rebate expenses as a percentage of pharmacy spend and on a PMPM basis across all Two-Plan/GMC plans and compared to the amount reported on Schedule 7. | The benchmark pharmacy rebate PMPM was (\$1.39) and CHW reported (\$2.04), which is within a reasonable range. |
| Capitation Revenue | Mercer compared capitation amounts reported in Schedule 6a with the CAPMAN file received from DHCS. The CAPMAN file contains all | RDT is higher than the CAPMAN amount by 4.55%, or \$29,753,870. Most of the difference is due to the appropriate accrual of HQAF for the second half of CY2019 |

| Category | Description | Results |
|--------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Interest and Investment Income | <p>amounts paid to the health plan by DHCS.</p> <p>Mercer requested interest and investment income for the MCO entity as a whole and information regarding how the income provided in Schedule 6a was allocated to the Medi-Cal line of business.</p> | <p>which was not paid by DHCS prior to the RDT submission, therefore accrued by CHW.</p> <p>No variance noted.</p> |
| Other Information | <p>Mercer reviewed the audited financial statements for the plan for the CY 2019 for a clean audit opinion or identification of significant deficiencies or material weaknesses.</p> <p>Mercer compared reported expenses, including IBNR and administrative expenses, to audited financial statements for consistency.</p> <p>Mercer inquired how hospital-acquired conditions (HACs) were</p> | <p>No concerns noted.</p> <p>Significant differences from the RDT reported medical, administrative and income tax expenses as compared to the audited financial statements. Per reconciliation from CHW, the majority of these variances appropriately relate to the treatment and/or restatement of Hospital Directed Payments, Intergovernmental Transfers, HQAF, Prop 56, MCO Tax, Premium Deficiency Reserves and prior period adjustments.</p> <p>CHW performs a thorough review for HACs using various tools and appropriately excludes any</p> |

| Category | Description | Results |
|----------|----------------------------------------------|------------------------------------------|
| | treated in the RDT and policies for payment. | related expenditures from RDT reporting. |

Section 3

Summary of Findings

Based on the procedures performed, the total amount of gross medical expenditures in the RDT were overstated by \$9,901,872 or 1.60% of total medical expenditures in the CY 2019 RDT. Of this amount, \$3,503,543 relates to pharmacy spread pricing that should be excluded from RDT reporting, as well as \$1,031,554 of physician incentive expense that has been deemed a revenue sharing arrangement, thus also should be excluded. Excluding the pharmacy spread pricing and physician incentive issues, the overall results would be an overstatement of \$5,366,775 or 0.87% of total medical expense.

Based on the procedures performed, administrative expenditures in the CY 2019 RDT were overstated by 1,942,982 or 2.24%. In addition, to that overstatement, the 12% administrative fee paid to the parent company Centene is significantly more than the benchmark average of 6.07% for all Two-Plan/GMC health plans.

In addition, it was observed that certain sub-capitated arrangements contained delegated administrative functions. However, the administrative component was not removed from the related sub-capitated medical costs and reclassified as administrative costs. This adjustment would further increase the amount of administrative costs included in the RDT and would have reduced the amount of medical expenditures included in the RDT.

Based on the defined variance threshold, the overall variance results of the medical expenditures audit are determined to be immaterial and do not warrant corrective action.

The audit results of the administrative expenditures, however, warrant additional attention. CHW should estimate or determine the value of the administrative component of all sub-capitated arrangements and report those amounts in the administrative section of the RDT, while excluding that amount from their medical expenses. In addition, the high level of administrative expenditures paid to Centene will be reviewed in future rating periods to determine a reasonable level to allow for rate setting purposes.

CHW reviewed this report and had no comments.

Appendix A

Administrative Duties in Sub-capitated Arrangements

| Administrative Task | Community Care, IPA | OptiCare/Envolve |
|------------------------------------------------------------------------------------------------|---------------------|------------------|
| Case Management | X | |
| Claims Adjudication and Payment | X | X |
| Joint Operating Committee | X | |
| Member Grievances | X | X |
| Member Services | X | |
| Network Adequacy Maintenance | X | X |
| Pharmacy Benefit Manager Services (paid for separately and included in Administrative Expense) | | X |
| Provider Credentialing | | X |
| Provider Services | X | |
| Quality Management | X | X |
| Quality Measure Tracking | X | X |
| Utilization Management | X | X |



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