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**New York State Office of the State Comptroller**  
Thomas P. DiNapoli

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Division of State Government Accountability

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## **Empire BlueCross BlueShield: Controls Over Payments for Special Items**

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### **New York State Health Insurance Program**

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Report 2016-S-57

June 2017

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## Executive Summary

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### Purpose

To determine if Empire BlueCross BlueShield: implemented sufficient controls over the identification and recovery of overpayments made to hospitals for special medical items; and took sufficient steps to minimize the State's risk of excessive payments resulting from contracts with hospitals that do not include language that limits the reimbursement of special medical items. The audit covered the period January 1, 2013 through December 31, 2016.

### Background

The New York State Health Insurance Program (NYSHIP) provides health insurance coverage to about 1.2 million active and retired State, participating local government, and school district employees, and their dependents. The Empire Plan is the primary health benefits plan for NYSHIP, serving about 1.1 million members. The Empire Plan covers a comprehensive range of services including, but not limited to, hospital services, office visits, home care, medical equipment, mental health services, and prescription drugs. The State Department of Civil Service (Department) administers NYSHIP. In carrying out its responsibilities, the Department contracts with Empire BlueCross BlueShield (Empire) to administer the Empire Plan's hospitalization program.

Empire's contracts with member hospitals include reimbursement rate schedules for the payment of inpatient and outpatient hospital services. Empire's hospital contracts also allow certain special items, such as implants, drugs, and blood, to be paid over and above the standard rate schedule amounts. Contracts with many of Empire's member hospitals limit payment amounts for special items; however, some contracts do not have similar limitations. As of December 31, 2016, Empire had contracts with 162 member hospitals: 117 had contract provisions that limited the reimbursement of special items; 29 based the reimbursement of special items on the hospitals' gross charges (i.e., no limit); and 16 did not allow for additional reimbursement of special items. During the four-year audit period, Empire paid the hospitals \$636 million for special items.

From 2009 through 2012, the Office of the State Comptroller (OSC) completed 21 audits of Empire's payments for special items. Systemic problems in Empire's controls over these payments were identified, as was about \$10 million in payments that exceeded reimbursement limits according to Empire's hospital contracts, and another \$2.2 million in excessive payments that were not recoverable due to limitations in Empire's hospital contracts. To correct the issues identified in OSC's prior audits, Empire contracted with two companies to review payments for special items (implants and drugs). In addition, Empire expressed a commitment to ensure all hospital contracts contained provisions to limit the reimbursement of special items.

### Key Findings

- In response to our prior audits, Empire improved its controls over the identification and recovery of overpayments for special items. As a result of Empire's efforts, including contracts with two vendors, Empire recovered overpayments totaling \$6,313,534 for special items. Nonetheless, we concluded that Empire needs to further enhance its reviews of special item payments by incorporating steps and techniques that result in additional recoveries.

- Since 2016, Empire's recoveries of overpayments for certain special items have decreased. Effective January 1, 2016, Empire assumed responsibility for reviewing special item payments for implants, having ended its corresponding vendor contract. For special item implant claims processed during the 18-month period July 1, 2015 to December 31, 2016, Empire recovered \$208,993 for payments exceeding hospital contract-based reimbursement limits. In contrast, OSC's prior audit of 200 special item payments, for the one-year period January 1, 2012 through December 31, 2012, identified implant overpayments totaling \$894,315 (over 300 percent more than the \$208,993 that Empire recovered).
- Not all hospital contracts include language that limits payments for special items. As of December 31, 2016, Empire's contracts with 29 hospitals did not include provisions that limited the reimbursement of special items, and another 16 hospitals had contracts that only limited reimbursement for certain types of special items. During the audit period, January 1, 2013 through December 31, 2016, Empire paid hospitals about \$145.7 million for special items that were not subject to reimbursement limits. Based on our prior audits, there is a high risk that many of these payments were excessive. For example, in a prior audit (Report 2009-S-99), we found that Empire paid a hospital \$1,115,745 for 50 special items that actually cost only \$230,065. Thus, the hospital generated surpluses totaling \$885,680 for the items (or a 385 percent profit margin).

## Key Recommendations

- Enhance internal controls designed to ensure payments for special items are made in accordance with hospital contracts.
- Continue efforts to ensure all hospital contracts include language that defines and limits reimbursement for all special items and expands audit look-back periods.

## Other Related Audits/Reports of Interest

[New York State Health Insurance Program: Empire BlueCross BlueShield - Payments Made to Hudson Valley Hospital Center \(2009-S-99\)](#)

[New York State Health Insurance Program: Empire BlueCross BlueShield - Selected Payments for Special Items for the Period July 1, 2011 Through December 1, 2011 \(2012-S-3\)](#)

[New York State Health Insurance Program: Empire BlueCross BlueShield - Selected Payments for Special Items for the Period January 1, 2012 Through July 31, 2012 \(2012-S-132\)](#)

[New York State Health Insurance Program: Empire BlueCross BlueShield - Selected Payments for Special Items for the Period July 1, 2012 Through December 31, 2012 \(2013-S-28\)](#)

[New York State Health Insurance Program: Empire BlueCross BlueShield - Selected Payments for Special Items for the Period January 1, 2012 Through July 31, 2012, Follow-Up \(2015-F-21\)](#)

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**State of New York**  
**Office of the State Comptroller**

**Division of State Government Accountability**

June 22, 2017

Mr. Jason O'Malley  
Director, New York State Empire Plan  
Empire BlueCross BlueShield  
11 Corporate Woods Boulevard  
Albany, NY 12211

Dear Mr. O'Malley:

The Office of the State Comptroller is committed to helping State agencies, public authorities, and local government agencies manage government resources efficiently and effectively and, by so doing, providing accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of State agencies, public authorities, and local government agencies, as well as their compliance with relevant statutes and their observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations. Audits can also identify strategies for reducing costs and strengthening controls that are intended to safeguard assets.

Following is a report of our audit of the New York State Health Insurance Program entitled *Empire BlueCross BlueShield: Controls Over Payments for Special Items*. This audit was performed pursuant to the State Comptroller's authority under Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law.

This audit's results and recommendations are resources for you to use in effectively managing your operations and in meeting the expectations of taxpayers. If you have any questions about this report, please feel free to contact us.

Respectfully submitted,

*Office of the State Comptroller*  
*Division of State Government Accountability*

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This report is also available on our website at: [www.osc.state.ny.us](http://www.osc.state.ny.us)

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## Background

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The New York State Health Insurance Program (NYSHIP) provides health insurance coverage to approximately 1.2 million active and retired State, participating local government, and school district employees, as well as their dependents. The Empire Plan is the primary health benefits plan for NYSHIP, serving about 1.1 million of these members. The Empire Plan covers a comprehensive range of services including, but not limited to, hospital services, outpatient surgery, office visits, home care services, infertility services, medical equipment and supplies, mental health and substance abuse services, and prescription drugs.

The State Department of Civil Service (Department) administers NYSHIP. In carrying out its responsibilities, the Department contracts with Empire BlueCross BlueShield (Empire) to administer the hospitalization portion of the Empire Plan. Empire processes claims for hospital services according to contracts it negotiates with member hospitals that are located in Empire's region, which covers the 28 eastern and southeastern counties of New York State. Empire also processes claims for services provided outside of Empire's region. These claims are submitted by hospitals to their local health insurance plans for payment. Empire then reimburses these local plans.

As of December 31, 2016, Empire had contracts with 162 member hospitals. Empire's hospital contracts include reimbursement rate schedules for the payment of inpatient and outpatient hospital services. Empire's contracts with 146 of the 162 member hospitals provided that certain special items, such as implants, drugs, and blood, were allowed payments over and above the standard rate schedule amounts: 117 of the 146 contracts contained provisions that limited reimbursement for certain special items; and 29 of the 146 contracts did not contain provisions limiting reimbursement for certain special items. Empire's contracts with the remaining 16 of the 162 hospitals did not allow for additional reimbursement for special items. During our audit period, January 1, 2013 through December 31, 2016, Empire paid hospitals a total of \$636 million for special items: \$340 million for implants, \$274 million for drugs, and \$22 million for blood. We limited our audit analysis to Empire's payments for implants and drugs, which accounted for \$614 million (or 97 percent) of Empire's \$636 million in payments for special items.

From 2009 through 2012, the Office of the State Comptroller (OSC) completed 21 audits of Empire's payments for special items. We found systemic problems with Empire's controls, and we identified about \$10 million in overpayments that resulted from payments that exceeded the reimbursement limit provisions in Empire's hospital contracts. We also identified \$2.2 million in excessive payments that were not recoverable due to limitations in Empire's hospital contracts (for instance, some contracts did not include provisions that limited the reimbursement of special items).

As a result of OSC's audit findings and recommendations, in 2013 Empire's top executive management met with officials from OSC and the Department and Empire's management expressed a strong commitment to address and correct the issues identified in our prior audits. To accomplish this, Empire contracted with two companies to review payments for special items:

Company A reviewed special item payments for implants and Company B reviewed special item payments for drugs. In addition, Empire expressed a commitment to continue its efforts to ensure all hospital contracts contained provisions to limit reimbursements of special items, and contained audit look-back periods of at least six years.



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# Audit Findings and Recommendations

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## Special Item Payment Controls

We found that Empire improved its controls over the identification and recovery of overpayments for special items. As a result of Empire's contracts with two vendors, Empire recovered overpayments totaling \$6,313,534 for special items. These actions represented a significant step in addressing the problems identified in our prior audits. However, we found that Empire should further enhance its efforts to cover more member hospitals and incorporate risk assessment methodologies to better target high-risk payments.

We also found that Empire needs to continue efforts to ensure all hospital contracts specify reimbursement limits for special items, expand audit look-back periods, and require hospitals to provide appropriate supporting documentation upon request.

## Payment Controls for Implants

Empire contracted with Company A to review special item payments for implants. Company A developed a proprietary computer algorithm that established cost parameters for implants based on the type of service provided. Claims exceeding the algorithm's cost parameters were flagged for review, adjustment, and recovery. Based on Company A's work, Empire recovered \$3,359,532 in overpayments.

Empire's contract with Company A ended on September 15, 2015. Effective January 1, 2016, Empire assumed responsibility for reviewing special item payments for implants. Empire's internal review included claims processed on or after July 1, 2015. As of December 31, 2016, Empire had recovered \$208,993, about two-tenths of 1 percent of the \$96 million that Empire paid the 104 hospitals that had contract-based reimbursement limits for implants. In addition, Empire's recoveries related to just three of the 104 hospitals. In contrast, our prior audit of 200 special item payments for the one-year period January 1, 2012 through December 31, 2012 identified special item implant overpayments totaling \$894,315 (over 300 percent more, in six fewer months, than the \$208,993 that Empire recovered) made to 30 hospitals.

Empire also recovered \$1,798,639 for supplies that were incorrectly billed by hospitals as implants. (Empire's hospital contracts do not provide for additional payments, over Empire's rate schedule payments, for supplies, such as surgical gloves and sponges.) Empire identified these incorrect implant billings using additional information that was not readily identifiable on claim submissions. As noted by Empire in response to our preliminary findings, identifying special item implant overpayments can be labor intensive and time consuming, as it requires requesting and reviewing additional documentation from hospitals.

Despite Empire's efforts, based on our analysis and our prior audit findings, we believe Empire should expand its review of claim payments for special item implants. Also, Empire should incorporate more risk-based approaches to select hospitals and payments for review. For



example, we used data mining techniques to segregate payments into similar groupings, and identified certain payments that fell outside the normal range. This may be an indication of materially increased risk for overpayment. In addition, Empire should consider using statistical sampling, including extrapolation techniques, to supplement its identification and recovery of overpayments. Statistical techniques are recognized and accepted audit methodologies, and provide an efficient and effective method to cover voluminous amounts of transactions with limited resources.

In response to our preliminary audit findings, Empire stated its intention is to audit a larger sample of claims, and to incorporate a more risk-based analysis to move to a more targeted audit approach. Empire also noted additional recoveries related to our audit period may still be obtained as some recovery efforts are ongoing.

## Payment Controls for Drugs

Empire contracted with Company B to review special item payments for drugs. As a result of the contract, Empire recovered \$946,371 for special item drug overpayments (of this amount, \$710,892 from 15 hospitals related to claims incurred during our four-year audit period of January 2013 through December 2016). Nonetheless, Empire did not recover overpayments from any of the remaining 102 (or 87 percent) of the 117 hospitals that had contract-based reimbursement limits for drugs. Given the materiality of Empire's special item payments for drugs, we recommend that Empire enhance its review to cover a broader range of payments and hospitals.

In response to our preliminary audit findings, Empire stated Company B uses a global review of drug charges, and does not rely solely on the amount billed. During our four-year audit period, Empire's payments for special item drugs to the 117 hospitals with contract-based reimbursement limits totaled \$126.6 million, and Empire's recoveries totaled \$689,933, an average of about \$172,000 per year. In our prior audit of 200 special item payments made during the one-year period January 1, 2012 to December 31, 2012, we relied primarily on payment amounts to select claims for audit. We identified special item drug overpayments totaling \$375,026 made to 20 hospitals. Given the materiality of Empire's special item payments for drugs, and the amount of our prior audit findings, Empire should enhance the review of special item drug payments to cover a broader range of payments and hospitals and, as previously stated, should consider including the use of statistical techniques.

## Hospital Contracts

Empire processes and pays claims according to the contracts they negotiate with member hospitals. Empire's contracts with many, but not all, of its member hospitals limit payments for special items. As of December 31, 2016, Empire's contracts with 29 hospitals did not limit payments for special items. In addition, Empire's contracts with another 16 hospitals only limited payments for certain types of special items. Empire reimburses hospital claims for special items that are not subject to reimbursement limits based on the hospitals' gross charges. During our audit period of January 1, 2013 through December 31, 2016, Empire paid hospitals \$145.7 million

for special items that were not subject to contract-based reimbursement limits.

Empire does not review or monitor special item payments that are not subject to reimbursement limits. Our prior audits have shown that hospitals without contract-based reimbursement limits routinely made excessive profits on special items. For example, in one prior audit (Report 2009-S-99), we found that Empire paid Hudson Valley Hospital Center \$1,115,745 for 50 special items that actually cost Hudson Valley Hospital Center only \$230,065. Thus, the hospital generated surpluses totaling \$885,680 for the 50 items (or a 385 percent profit margin). We concluded this profit margin was unreasonable and excessive.

In another prior audit (Report 2012-S-3), we analyzed Empire's payments for certain implantable cardiac devices, which were among the most common special items claimed by hospitals. We determined that hospitals without contract-based reimbursement limits submitted charge amounts for special items that were significantly more than hospitals with such limits. We found that Empire's average payment to hospitals with reimbursement limits exceeded the hospitals' costs for implantable cardiac devices by \$2,818. However, for hospitals without reimbursement limits, Empire's average payment exceeded the hospitals' costs by \$13,140 – over four times the amount for hospitals with reimbursement limits. Thus, we concluded that contract-based reimbursement limits are crucial to controlling the State's costs for these items.

Additionally, we found that hospital contracts had limited audit look-back periods; for instance, many only had two-year look-back periods. As a result, during our prior audits, certain hospitals refused to provide supporting documentation (including invoices) for payments beyond the two-year period.

In response to our preliminary report, Empire stated the inclusion of language limiting the reimbursement of special items is always one of the primary goals in contract negotiations. Empire noted the number of facilities without limiting language or without expanded audit look-back periods is decreasing. During our follow-up of one of our prior audits (Report 2015-F-21), we found that, as of August 5, 2015, Empire's contracts with 35 hospitals did not contain contract-based reimbursement limits for special items. As of December 31, 2016, Empire had reduced the number of hospitals without contract-based reimbursement limits for special items to 29.

Nevertheless, during our four-year audit period, January 2013 through December 2016, Empire paid hospitals \$145.7 million for special items that were not subject to contract-based reimbursement limits. Based on our prior audits, we believe many of Empire's payments for special items to these hospitals resulted in excessive profits for the hospitals. Consequently, Empire needs to continue efforts to include language in all hospital contracts that limits these reimbursements.

## **Overpayment Recoveries**

When Empire identifies overpayments made to a hospital, Empire should credit the Department for any overpayment recoveries. According to Empire, they recovered special item overpayments totaling \$6,313,534. We reviewed various claim transaction files to verify that all recoveries were included as credit transactions. We then reconciled the claim transaction files to annual financial

reports obtained from the Department. Based on our testing, we concluded Empire credited the Department for the \$6,313,534.

## Recommendations

1. Enhance internal controls designed to ensure payments for special items are made in accordance with hospital contracts. Such efforts should include reviews of a greater number of hospitals and payments, and could incorporate statistical sampling (including extrapolation techniques) as well as risk-based approaches to better target high-risk payments.
2. Continue efforts to ensure all hospital contracts include language that: defines and limits reimbursement for all special items; expands audit look-back periods; and requires hospitals to provide appropriate supporting documentation (including invoices) upon request.

## Audit Scope, Objectives, and Methodology

The objectives of our audit were to determine if Empire: implemented sufficient controls over the identification and recovery of overpayments made to hospitals for special medical items; and took sufficient steps to minimize the State's risk of excessive payments resulting from contracts with hospitals that do not include language that limits the reimbursement of special medical items. The audit covered the period January 1, 2013 through December 31, 2016.

To accomplish our objectives, and assess internal controls related to our objectives, we obtained and analyzed a listing of claim overpayments identified by Empire, and verified that overpayments were credited to the Department. We obtained and reviewed a listing of Empire's hospital contracts and the status of each contract, and we reviewed selected hospital contracts to verify the accuracy of Empire's listing. We also interviewed Empire officials to gain an understanding of their internal controls.

We conducted our performance audit 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.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions, and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these functions do not affect our ability to conduct independent audits of program performance.

## Authority

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The audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law.

## Reporting Requirements

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We provided preliminary copies of the matters contained in this report to Empire officials for their review and comment. Their comments were considered in preparing this report.

Within 90 days of the final release of this report, we request that Empire officials report to the State Comptroller advising what steps were taken to implement the recommendations included in this report.

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## Contributors to This Report

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### Vision

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### Mission

To improve government operations by conducting independent audits, reviews and evaluations of New York State and New York City taxpayer financed programs.