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United States General Accounting Office
Washington, DC 20548

Office of Special Investigations

B-284400

April 4, 2000

The Honorable William V. Roth, Jr.
Chairman
The Honorable Daniel Patrick Moynihan
Ranking Minority Member
Committee on Finance
United States Senate

Subject: Procurement of Michigan School-Based Medicaid Consulting Services

Under Medicaid, a joint federal-state program, the federal government pays a share of the costs incurred by the states in providing health care to 41 million low-income beneficiaries, including 13 million school-aged children. States may use their Medicaid programs to pay for certain healthcare services that schools provide to eligible children. School districts often contract with private firms who act as consultants and billing agents on their behalf to prepare and submit claims to seek reimbursement for school-based Medicaid services.

At your request, we investigated the circumstances surrounding the process used by a consortium of eight intermediate school districts in the state of Michigan to contract for consulting and billing services. The procurement at issue was conducted on behalf of the consortium by a committee consisting of school district officials and led by a chairperson from one of the school districts. At the end of the process, however, each of the school districts entered into its own contract with Deloitte Consulting LLC, (Deloitte). The procurement process was completed in October 1998, and contracts were signed shortly thereafter for services to be provided beginning in the following year. You specifically requested that we determine whether the process used by the school districts complied with U.S. Department of Health and Human Services (HHS) procurement regulations.¹

To perform our investigation, we interviewed officials of the school districts, the state of Michigan, the Health Care Financing Administration (HCFA), Deloitte, and other consulting firms that had competed for the contracts. We also reviewed pertinent documents from these sources and HHS regulations.

In brief, we determined that the procurement for the 1998 contracts to Deloitte did not adhere to standards in the HHS regulations. These standards are applicable to

¹ 45 C.F.R. § 74.40.

the procurement for these services only if the state claims the costs as a cost of the Medicaid program in order to receive federal matching funds.

Although the school districts included this fee in their claims to the state of Michigan, the state has yet to formally submit the claims to HCFA as a cost of the Medicaid program. The state of Michigan requested an opinion from HCFA as to whether such a claim would be allowable. In response, the HCFA regional office rendered an opinion that Deloitte's fee under the contracts would not be an allowable cost because the procedures used to select Deloitte did not meet the HHS procurement regulations. The state then requested that HCFA's central office reconsider the regional office decision. HCFA is waiting for the results of our investigation before taking further action.

Background

In 1993 and 1996, the school districts awarded contracts to Deloitte to prepare and submit claims to the state for reimbursement of school-based Medicaid services. The contracts' services include conducting outreach activities to enroll children in Medicaid; providing eligibility determination assistance, program information, and referrals; and training and follow-on technical assistance to school district personnel. Officials from the school districts stated that the procurements for 1993 and 1996 were not competed. HHS procurement regulations were not applicable to these contracts because the fees paid to Deloitte under these contracts were not claimed for federal matching funds.

The 1998 Procurement

The school districts' 1996 contracts with Deloitte were due to expire in January 1999. On December 26, 1997, Medbill Corp., Deloitte's chief competitor in Michigan, wrote to one of the school districts, expressing interest in bidding in its next contract award cycle. On January 23, 1998, a school district official invited Medbill to give a presentation to a meeting of the school district committee on February 24, 1998. Although no solicitation was ever issued, the school district committee received expressions of interest from other potential vendors. These vendors did not pursue the contracts, however, leaving Deloitte and Medbill as the two leading competitors for the contracts.

Also on February 24, 1998, Deloitte provided an "Analytical Comparison" that Deloitte had prepared, apparently in response to a request by members of the school district committee that Deloitte compare its performance with that of Medbill. According to the Deloitte document containing the analysis, this comparison—of Deloitte's performance under its contract and Medbill's performance under Medbill contracts with other Michigan school districts for similar services—was requested by "various members" of the committee at Deloitte's prior meeting with the committee.

On March 16, 1998, Medbill offered to lower its fee 1 percentage point. Sometime after March 16, 1998, a member of the school district committee advised Deloitte of Medbill's new lower rate and asked Deloitte to update its "Analytical Comparison"

concerning Medbill. On August 11, 1998, Deloitte provided to the school district committee its "Updated Analytical Comparison." The comparison's stated purpose was to update the "analytical cost performance comparisons to reflect the new price quotations of the two respective firms, and...to cost out known variations in the claim development methodologies of the two firms."

Decisions were reached in the October to December 1998 time period to award the 1998 contracts to Deloitte. Our interviews determined that at least three of the school district committee members considered or relied on Deloitte's analytical comparisons. There is no other documentation of a cost or price analysis.²

State of Michigan's Procurement Guidance

On July 15, 1998, the Michigan Department of Community Health issued a bulletin effective August 15, 1998, that required contracts for billing agents, accounting firms, service bureaus, or other consultants for school-based services to be competitively bid. According to interpretive guidelines issued by the department, the basic principles of competitive bidding are as follows:

"Institute and maintain a notification process that informs all potential vendors of the intent to solicit bids for services related to the administration of School Based Services."

"Provide all pertinent information to all the potential vendors regarding the specifications and criteria for the services being sought such that the same information is presented to all potential bidders."

"Select the billing agents/accounting firm/service bureau and/or consultants for services related to the administration of School Based Services, using an objective evaluation process that incorporates consideration of the technical merits and quality as well as the price presented."³

Following the issuance of these principles, the school district committee sought assurances from the state of Michigan that the procurement process for the 1998 procurement met the principles. The committee provided the state with a chronology of the process used and a letter outlining why the committee believed that the procurement met the principles. Although the school district committee had not completed its selection process, in September 1998 the Michigan Director, Bureau of Plan Administration and Customer Services, Department of Community Health, determined that "the consortium [of school districts] appears" to meet the basic procurement principles issued by the state. This determination was based upon the representations of the school district committee.

² The school district committee, in response to a request from HCFA, provided Deloitte's analytical comparisons to HCFA as evidence that a cost/price analysis had been performed.

³ Subsequent guidance from the state instructed school districts to determine the "specific and detailed procedures by which competitive bidding will be conducted." State of Michigan, Medical Services Administration, "Summary and Response, School Based Services Policy Clarifications," Project Number 03-98-07, Aug. 31, 1998.

Procurement Standards in HHS Regulations

HHS regulations apply to grants and agreements, and any subawards under such grants and agreements, awarded to carry out certain entitlement programs, including Medicaid. (45 C.F.R. § § 74.1, 92.4(a)(3)(v).)

The HHS regulations include procurement standards that apply in situations where the state claims the cost of the contract as a direct cost of the Medicaid program. (See 45 C.F.R. § 74.40.) These standards include the following:

“Solicitations shall clearly set forth all requirements that the bidder or offeror shall fulfill in order for the bid or offer to be evaluated by the recipient.” (45 C.F.R. § 74.43.)

“The recipient shall be alert to organizational conflicts of interest....” (45 C.F.R. § 74.43.)

“Some form of cost or price analysis shall be made and documented in the procurement files in connection with every procurement action. Price analysis may be accomplished in various ways including the comparison of price quotations submitted, market prices and similar indicia, together with discounts.” (45 C.F.R. § 74.45.)

The School District’s Failure to Adhere to HHS Procurement Standards

Based on our investigation, we determined that the 1998 contract awards to Deloitte by the school districts in Michigan failed to adhere to the procurement standards set forth in the HHS regulations.

The standards were not met in the following areas:

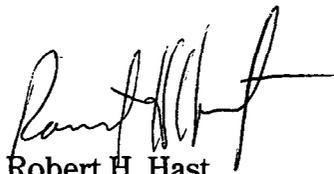
- The school districts did not prepare a solicitation setting forth the requirements that bidders must fulfill. However, we are unaware of any potential vendor who might have competed for these contracts but was not advised of the school districts’ requirements.
- The school districts failed to be alert to organizational conflicts of interest. Although not specifically defined in the HHS regulations, guidance for this term may be obtained from the Federal Acquisition Regulations (FAR). (48 C.F.R. Ch. 1.) The FAR states that an organizational conflict of interest arises when “because of activities or relationships with other persons, a person is unable or potentially unable to render impartial assistance or advice to the Government....” (FAR § 9.501.) Deloitte, as the incumbent contractor and competitor for the follow-on contracts with the school districts, was unable or potentially unable to render impartial assistance or advice to the school district committee concerning which vendor, Medbill or Deloitte itself, would provide the best value to the school districts. Nevertheless, the school districts responsible for making the selection of the contractor requested and considered Deloitte’s two analyses comparing Medbill’s expected performance and revenue production with Deloitte’s own. Moreover, rather than being alert to the organizational conflict of interest, the school district committee officials provided Deloitte with Medbill’s

proposed fee, a figure that was not publicly available, in order to obtain the second Deloitte analysis.

- The school districts failed to perform and document a cost or price analysis, other than the analyses prepared by Deloitte which, as discussed, were tainted by the failure to be alert to an organizational conflict of interest.⁴

We conducted our investigation from September 1999 through February 2000 in Michigan. It was performed in accordance with quality standards for investigations as set forth by the President's Council on Integrity and Efficiency.

If you have any questions regarding this letter, please feel free to contact me at (202) 512-7455 or Assistant Director Steven Iannucci at (202) 512-6722. Richard Burkard, William Hamel, and Andrew O'Connell were key contributors to this investigation.



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⁴We note that the state of Michigan official concluded that the school districts appeared to meet the state's basic procurement principles related to notifying vendors and providing pertinent information to vendors. The state official, however, was unaware of the facts supporting our conclusion that there was a failure to be alert to an organizational conflict of interest. In addition, since the school districts had not completed their selections when the state official made the determination that the principles appeared to have been met, the official could not have been aware that no cost or price analysis would be prepared, other than the ones performed by Deloitte.