



New York State Office of the State Comptroller

Office of Budget and Policy Analysis

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December 2006

New York State Replacement Medicaid System eMedNY Project

Summary

During an effort to improve the system used to process and pay Medicaid claims, poor contract oversight practices resulted in the Department of Health (Department) paying the same vendor to operate and improve the existing payment system while implementation of the new system was delayed. While negotiations were underway to remedy excess payments and improve contract terms, the same vendor threatened to terminate all Medicaid payments should issues regarding a proposed extension to its contract not be resolved to its satisfaction. Instead of rejecting these threats, representatives of the Department drafted letters that would transmit the threat to Medicaid service providers, potentially disrupting the provision of medical care to New Yorkers who rely on Medicaid.

Given the risks associated with an interruption in payments, the Office of the State Comptroller was forced to approve a contract amendment including terms it had previously rejected. Instead of resolving outstanding issues, the implementation of this amendment raises questions about the vulnerability of the Medicaid payment system to weak oversight by the Department, as well as inadequate contingency planning for such actions by vendors.

Computer Sciences Corporation (CSC) was selected through a competitive procurement process conducted by the Department to develop, implement and operate a replacement of the Legacy Medicaid claims processing and payment system. The new system, which was required to comply with provisions of the federal Health Insurance Portability and Accountability Act (HIPAA), was slated for full implementation July 1, 2002, 26 months after the contract start date. It was projected that the "eMedNY" system would cost \$357 million to develop, deploy and operate. The cost of the investment was justified by an expectation that savings would accrue from better controls on inappropriate payments and provisions built into the system to deter fraud.

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Development and deployment of the system faced substantial delays. In fact, not one of the three major project components was implemented on time. Phase I of the project, which included a new eligibility verification system, drug utilization review, pharmacy claims capture and service authorization, was 17 months late. Phase II of the project, which incorporated the remainder of claims processing and reporting functions of the eMedNY system, was implemented 33 months late and the data warehouse, a comprehensive data repository and analytical reporting system, was implemented 23 months late.

An audit of the eMedNY system by the Office of the State Comptroller (*Implementation of eMedNY Contract C014305, 2005-R-3*) found that two important contract deliverables were not fully implemented: access for authorized personnel to the adjudicated claims file and, more importantly within the context of other State initiatives, the fraud detection and prevention program. While the Department responded that it later implemented the components, the Office of the State Comptroller maintains that they were not implemented in accordance with the contract and as agreed upon by CSC.

Office of the State Comptroller audits issued during calendar year 2006 have identified nearly \$52 million in inappropriate payments that should have been detected by the system and prevented.ⁱ

CSC benefited significantly from the delays as a result of its dual roles in the project, accruing \$138.1 million in payments for changes to and operation of the Legacy system during the time when the eMedNY system should have been running.ⁱⁱ Delays in the development of the eMedNY system, and other factors contributing to cost overruns, increased the gross value of the original contract by \$179.7 million. The Department negotiated an amendment to the original contract with CSC and took other actions to reduce cost overruns to \$85.8 million, or 24 percent, more than the original project cost estimate. Of this amount, CSC will receive \$66.2 million, or 19 percent, more than originally projected for total contract payments of \$414.8 million.ⁱⁱⁱ

Under the contract extension approved in June 2006, CSC will operate the eMedNY system through June 30, 2009 for an additional \$278.1 million. The Department provided no justification as to how the 62 percent pricing increase for the first year of the three-year extension was necessary. The amendment brings the total eMedNY project cost to \$720.9 million, \$363.9 million (102 percent) over the original estimated cost.

The contract extension includes provisions previously rejected by the Office of the State Comptroller. Furthermore, the Department waived the State's contractual rights to refuse to pay CSC for certain excess project costs and failed to provide sufficient evidence supporting the negotiated closeout with CSC. Specifically, in rejecting the closeout, the Office of the State

Comptroller had expressed concern about the piecemeal approach to negotiation and the absence of a comprehensive pricing mechanism to provide fair and equitable pricing based on revised implementation dates. These issues were not resolved by the Department, yet it chose to bundle the negotiated closeout with the contract extension and present a single package for approval by the Office of the State Comptroller. Worse, it requested this approval in the context of the threat by CSC that it would stop making Medicaid payments if the agreement and three-year contract extension were not in place by June 30, 2006.

The Office of the State Comptroller saw no alternative but to approve the settlement and contract extension. Since approval of the extension, the Office of the State Comptroller has continued to closely monitor the project. For example, the Office of the State Comptroller has preaudited and processed 22 related payments, totaling nearly \$29 million since July 2006. In addition, the Office of the State Comptroller has urged the Department to initiate a new procurement that might result in the replacement of CSC as operator of the eMedNY system. Action is needed to ensure that the people who rely on Medicaid to meet their health care needs are not at the mercy of a single vendor and a Department of Health that appears unwilling to use all available resources to hold the vendor accountable.

Background

In the 1970s, the first major state level effort in social service information system development focused on Medicaid management information systems designed for billing and payment of Medicaid claims to providers.^{iv} In 1973, Public Law 92-603, which provided for 90 percent Federal Financial Participation (FFP) for design, development and installation of Medicaid management information systems in addition to 75 percent FFP for ongoing operational costs, was enacted.^v In the fall of 1977, New York State implemented its own Medicaid Management Information System (MMIS). In the past, claims were paid at the county level, requiring monthly reconciliations of advances received and payments made.^{vi} MMIS provided a method of centralizing claims processing and a system for storing, managing and retrieving Medicaid data.

Historically, the State's Medicaid program was administered and managed by various agencies. When the Department of Health (Department) took full responsibility for the program in 1997, it recognized the need for system improvements.^{vii} The functionality of MMIS was customized to meet State specific laws and policies. Over time, numerous system changes to reflect changes in law and policy left MMIS a patchwork system, and fundamental components of an integrated MMIS were lacking. For example, eligibility, provider and reference data maintenance functions were performed on separate New York State systems operated by the New York State Human Services Application Services Center. In addition to system inefficiencies, states were mandated to update their systems to comply with new federal regulations. The Health Insurance Portability and Accountability Act (HIPAA) of 1996 requires states to comply with electronic data interchange

standards, and federal reporting requirements under the Balanced Budget Act of 1997 mandate states to submit data to the Centers for Medicare and Medicaid under the Medicaid Statistical Information System.

To create an integrated claims processing system providing updated technologies and achieve compliance with federal requirements, the Department procured services to design, develop, implement and operate a replacement Medicaid system. The new system would: in Phase I, replace the old Electronic Medicaid Eligibility Verification System (EMEVS); in Phase II, replace the Legacy MMIS; and finally, augment the system with the addition of a data warehouse and a fraud detection and prevention program. The new system, known as “eMedNY,” was required to both meet and enhance the functionality of the Legacy MMIS and EMEVS.

eMedNY

In 1998, the contract for design, development and implementation of the replacement Medicaid system, named eMedNY, was awarded to CSC, the same firm that held the contract for the aging Legacy claims processing system.^{viii} The contract was slated to begin in September 1998. However, contract negotiations between CSC and the Department changed the scope of work and timetable. As a result, the Office of the State Comptroller required the Department to request a best and final offer ensuring that all firms that had competed or had been interested in competing for the contract were given a fair chance to bid on the revised project. Once again, CSC was selected as the responsible vendor. The material changes delayed the actual start to the contract by 20 months, to May 1, 2000. The Office of the State Comptroller approved the contract on March 29, 2000. The initial value of the eMedNY contract was \$340.3 million with all system functionality scheduled for implementation July 1, 2002, 26 months from the start date.^{ix}

In addition to contracting with CSC, the Department entered into a contract with Bearing Point (formerly KPMG) to provide quality assurance oversight of the eMedNY project.^x The initial value of this contract was approximately \$5.6 million and was approved by the Office of the State Comptroller in August 2000. The Bearing Point contract raised the overall costs of the eMedNY project to \$345.9 million. In house, the Department developed a structure to oversee and manage the contract with CSC. The Steering Committee, made up of representatives from the Department, the Division of the Budget, the Office for Technology and other entities, led project management, with the help of a Project Management Team. The Project Management Team included a contract liaison and was supported by a Core Team of 20-plus staff members.^{xi}

During the transition to full operation of eMedNY, the contract costs of Legacy MMIS claims processing and Legacy eligibility verification must be considered in total project cost.^{xii} The contract with CSC for operation of the Medicaid Legacy system for three months after final eMedNY

Office of the State Comptroller Monitoring of the eMedNY Project

implementation was valued at \$8.3 million, and the contract with eFunds for eligibility operations was valued at nearly \$2.8 million.^{xiii} Factoring these costs into the project raised the original estimated total project cost to be spent via contracts to \$357 million. Additionally, there are other significant costs to the State related to this project which have not been determined, such as the cost to maintain the Department's Project Management Team, the Steering Committee and the Department's Medicaid operations staff that have been involved in the project.

Recognizing the importance of the system to the State's healthcare industry and the potential implications should this long-term project get off track, the Office of the State Comptroller has closely monitored the eMedNY project from the early stages of the procurement right through to the recent contract extension. The Office of the State Comptroller's Division of State Services, Bureau of Contracts has expended significant resources in its contract approval role. As the delays arose, there were numerous contract amendments reviewed and approved by the Office of the State Comptroller. Many of the amendments resulted in expensive modifications to the Legacy system. There were significant concerns by the Office of the State Comptroller about the financial benefit to CSC as a result of its dual roles in the project as the developer and operator of the new system and operator of the Legacy system. The Office of the State Comptroller provided timely feedback to the Department as far back as March 2003 seeking important information from the Department on topics such as:

- Whether the Department had made a determination as to the responsibility for the delays and assessed liquidated damages against CSC as provided for in the eMedNY contract,
- Documentation of negotiated changes in the scope of work to be performed, which was needed for Office of the State Comptroller approval and the Procurement Record,
- How delays in system components would impact negotiations of future amendments, and
- A comprehensive assessment of the delays and evidence that the Department had a plan in place to control costs going forward.

The Department was often unresponsive in providing this information and when information was provided, it was often in a piecemeal manner, which demonstrated that despite its project management and oversight structures, the Department did not have a formal plan.^{xiv} As the costs continued to increase, the anticipated savings of the new system was eroded.

The Office of the State Comptroller also monitored the development and implementation of the eMedNY system itself. This was done by the Division of State Services, State Audit Bureau (SAB). SAB maintains an onsite staff at the location where CSC operates the Medicaid claims processing and payment system. This staff provided ongoing monitoring of both the new system as it was being developed and the Legacy system. Over several years, SAB staff worked to ensure that the new system had appropriate controls over payments and information, and provided valuable feedback to the Department, CSC and other related contractors.

Most recently, SAB completed an audit of the implementation of the eMedNY contract (*Implementation of eMedNY Contract C014305, 2005-R-3*) with audit objectives of determining whether eMedNY contract deliverables were provided on time and within budget, whether contract-related payments were supported and appropriate, and whether the Department provided adequate oversight of CSC. The audit found that while two of the major contract deliverables—the replacement Medicaid system and the data warehouse—had been implemented after long delays and considerable unanticipated costs, two significant contract deliverables, a fraud detection and prevention program, and read and copy access by authorized personnel to the adjudicated claims file, were not implemented in accordance with the contract and as agreed to by CSC. The audit tested 13 invoices of fixed and variable payments, valued at \$51 million, and found that invoices for fixed payments were accurate and supported, but the Department had only received limited support documentation for the variable payments. The audit concluded that the Department's oversight practices need improvement and that future contracts should require monthly financial reporting in a format that enables the Department to assess the reasonableness of fixed fees.

Federal Monitoring

The results of the Office of the State Comptroller audit related to the eMedNY fraud detection and prevention component are also important in the context of a recent federal review of the State's Medicaid program integrity procedures.^{xv} The review was requested by federal and State lawmakers after a series of articles in the *New York Times* in July 2006 revealed serious weaknesses with the Department's Medicaid fraud and abuse activities.^{xvi} In addition to assessing program compliance with federal statutory and regulatory requirements, the November 2005 review by the CMS assessed the Department's activities in identifying, receiving and using information about potential fraud and abuse of State Medicaid providers. The review confirmed many of the concerns raised in the *Times* articles, noting the following key problems:

- Inadequate Staffing - From 1998 to federal fiscal year 2004, both Department and contractual program integrity staff combined decreased from about 950 to 584, 60 percent. In contrast, during that same time, Medicaid program expenditures increased 55 percent. The number of

program integrity staff in the Department is somewhat misleading as it includes several units, such as third-party liability, drug rebate and drug utilization review, which are not considered within the program integrity function by other states. Further, as the Department has decreased its program integrity staff over the years, it has increased the number of contract staff by 40 percent, from 114 to 160.

- Diminished Audit Collections - In SFY 2004-05, the Department was at a four-year low for fee-for-service audit recoveries—\$29.1 million, dropping more than 50 percent compared to the average for the previous three years. While the Department experienced a higher return on investment with rate-based audits, it decreased the number of these audits by 35 percent, from 247 to 160.
- Insufficient Referral to the Attorney General's Medicaid Fraud Control Unit - In calendar year 2005, the Department made 77 referrals to the Attorney General's Medicaid Fraud Control Unit (MFCU), which investigates and prosecutes Medicaid fraud and abuse. While this represents an 80 percent improvement over the Department's prior four-year average, it is quite low and CMS questioned why the Department was not able to generate a significantly higher number of referrals.
- Insufficient Provider Sanction Activity - While the number of Department provider reviews and investigations has increased significantly, more than doubling over the last three years (SFY 2002-03 through 2004-05), the number of provider exclusions/terminations and related activities have remained steady. Given the number of enrolled providers and the increased activities, CMS questioned why it did not result in identifying more than 260 providers for contract termination and only 61 providers meriting payment withholds. Also of concern is that the Department's average savings per provider review and investigation dropped 62 percent over the same three-year period.

From not ensuring that CSC develops a fraud and prevention program in accordance with the contract to the disappointing results of its fraud and abuse, and program integrity activities, the results of both the federal review and the audit by the Office of the State Comptroller show a pattern by the Department that calls into question its ability to act in the best interests of the State.

eMedNY Project Components

The development portion of the eMedNY project included three major components: Phase I - development of eligibility verification, drug utilization review, pharmacy claims capture and service authorization; Phase II - development of the remainder of the claims processing, claims payment and reporting functions; and the third component, implementation of a data warehouse, comprehensive data repository, analytical reporting

system, and fraud detection and prevention system. Once implemented, CSC was responsible for operating the new system.

The development and implementation of the three eMedNY components experienced significant delays attributed to CSC, the Department and some external factors, such as the September 11, 2001 terrorist attacks. Phase I was required to be implemented within 14 months of the contract start (May 1, 2000).^{xvii} However, this phase was not implemented until November 2002, 31 months after the contract start and 17 months late. The data warehouse was required to be implemented within 18 months of the contract start, but was not implemented until September 2003, taking 41 months to implement, 23 months longer than anticipated.^{xviii} Phase II experienced the lengthiest delays, with implementation taking 59 months from the contract start, 33 months longer than the 26 months provided for in the contract.^{xix} In the recent contract extension amendment, the Department and CSC changed the contracted implementation dates of the three eMedNY components above to the date the component was delivered late.^{xx}

eMedNY Delay of Contract Deliverables

Component	Months Provided by Contract to Implement	Original Contract Operation Date	Actual Operation Date	Actual Months to Operation	Months Late
Phase I	14	07/01/2001	11/16/2002	31	17
Phase II	26	07/01/2002	03/24/2005	59	33
Data Warehouse	18	11/01/2001	09/22/2003	41	23

Note: Contract start date - May 1, 2000.

The Department received final approval of the eMedNY system from the federal government on April 26, 2006, allowing the Department to claim 75 percent Federal Financial Participation retroactive to April 1, 2005 for costs associated with the operation of the certified eMedNY system.

Phase I

Phase I of the project incorporated replacing the old EMEVS, which performed eligibility verification, drug utilization review, pharmacy claims capture and service authorization. The Department contracted with eFunds to operate EMEVS in April 1991 for a five-year term, which was extended several times. The new EMEVS was required to receive all claims electronically in compliance with HIPAA. The original date of implementation was 14 months after the start of the contract, or July 1, 2001.^{xxi} However, the implementation date was delayed four separate times, and Phase I was implemented nearly 17 months late. The delays resulted in extending the period for which eFunds needed to continue running EMEVS from the original three months ending September 30, 2001, costing \$2.8 million, to an additional 15 months, costing an additional \$12.4 million for a total cost of \$15.2 million.

Phase I was delayed primarily due to a change in project management at CSC. The new CSC project management team conducted an assessment of the Phase I implementation and unilaterally determined that it was not ready for implementation. Phase I was further delayed by the September 11, 2001 terrorist attacks, when Department resources were directed to support the Medicaid Disaster Relief effort.^{xxii} The final agreed upon date of implementation between the Department and CSC was February 16, 2002.

On February 17, 2002, when CSC failed to implement Phase I, the Department sent a letter informing CSC that it was in breach of the contract. However, the letter stated that, “without waiving any of its rights, the Department wishes to continue to work with CSC to promote CSC’s timely satisfaction of all future contract obligations.” Phase I was finally implemented nine months later, on November 16, 2002. As a result of significant delays in implementing and operating the replacement Medicaid system, the Department had no choice but to extend the contract for the Legacy system with the incumbent contractor, CSC, to maintain an operational system during the implementation of Phases I and II.^{xxiii}

Phase II

Phase II of the contract incorporated the remainder of claims processing, claims payment and reporting functions of the eMedNY system. The original contract specified that Phase II was to be implemented 26 months after contract start on July 1, 2002.^{xxiv} Phase II was primarily delayed due to Phase I setbacks, such as CSC’s change in project management noted above. In addition, this phase was delayed because of evolution updates to the Legacy system, which necessitated ongoing changes to the eMedNY system (Legacy gap). The importance of continuing a functional Legacy system, while simultaneously procuring and transitioning to eMedNY, required the Department to bring the Legacy system under compliance with federal guidelines. These updates were incorporated into the eMedNY design at an extra expense (Legacy gap costs) totaling nearly \$7.7 million. Legacy gap items also added another nine months to the project, pushing projected implementation to July 1, 2003.^{xxv} When CSC failed to implement Phase II on July 1, 2003, the Department sent another breach of contract letter to CSC. Again, the Department continued to work with CSC to satisfy the contract. Phase II was eventually implemented on March 24, 2005, after a 33-month delay.^{xxvi}

Data Warehouse

Another stage of the contract was the implementation of a data warehouse. The warehouse serves as a comprehensive data repository and analytical reporting system. According to the original contract, the data warehouse was to be implemented 18 months after contract start, or November 1, 2001.^{xxvii} The Department and CSC mutually agreed to delay the

implementation of the data warehouse component to allow additional time for testing. The final implementation of the data warehouse was delayed 23 months. As of September 22, 2003, the warehouse was in place and fully operational.^{xxviii}

Fraud Detection and Prevention

One of the most significant changes to New York's replacement Medicaid system was the addition of a fraud detection and prevention component. Two fraud elements, one required and one optional, were incorporated into

the contract for the replacement Medicaid system.^{xxix} Due to the growth of health care fraud, the Department required the contractor to design, develop and implement a fraud detection and prevention program, which included the random selection of claims, prepayment aggregate monitoring tools, measurement systems and methodologies, and relationships between fraud control teams and claims. The contract required that during development, the contractor coordinate with the Medicaid Fraud Control Unit of the Office of the Attorney General (MFCU), the Department's provider audit units and the Office of the State Comptroller. The contract required the vendor to submit its program within 30 calendar days after start of full replacement Medicaid system operations for Department and State review and approval.^{xxx} The contract further specified that the vendor shall report on a quarterly basis the results of its fraud detection and prevention activities.

The Department also included an optional, separately priced fraud component, which would be implemented at the discretion of the Department. The optional component is a front-end electronic fraud, waste and abuse prevention module. The Legacy MMIS system edits are designed to ensure that claims are paid in accordance with law and regulations. A front-end module would detect fraud and or abuse by using statistical methods to profile providers that fall into suspicious patterns or represent anomalies from normal patterns. Provider profiles would then be used to audit claims for actual fraud and abuse.

As noted above, a recent Office of the State Comptroller audit on the *Implementation of eMedNY (Contract C014305, 2005-R-3)* determined that the required fraud and detection prevention component, which should have been in place by the end of April 2005, was still being developed during audit fieldwork (Fall 2005). During development of the fraud component, CSC did not coordinate the activities with the Office of the State Comptroller and MFCU as specifically required by the contract. Instead, CSC was working exclusively with the Department in developing the fraud component. Additionally, the audit found that no quarterly reporting had been initiated. During the audit, Department officials stated that they were working with CSC to develop and implement the fraud component and to

determine the type of quarterly reporting the Department was interested in receiving. However, the Department had no documentation to support this assertion.

The draft audit report recommended the Department ensure the fraud detection and prevention program, and associated reporting, be developed and implemented as soon as possible and in compliance with contract terms. The draft audit also recommended that the Department determine whether damages against CSC were warranted for failing to implement the component as required and assess damages as appropriate. In contrast to what the audit found during fieldwork, the Department responded to the draft audit report by stating that it disagreed with these recommendations and stating that the fraud detection component was implemented as required, and only the formal documentation describing the component was late, but had been delivered in January 2006. Again, as with the other delays of the eMedNY project, despite contract provisions allowing it to assess damages against CSC, the Department stated that no damages were warranted. The lack of the Department's taking such actions raises concerns that it may not be acting aggressively enough in the best interests of the State.

The final audit report notes that while some progress had been made toward developing the fraud and detection program, it had not been fully developed and implemented in accordance with the contract and as agreed to by CSC. For example, had this been the case, the fraud program would have been submitted to the Office of the State Comptroller for review and approval which, as of the time of the audit, it had not.

Cost Overruns Due to Delays

CSC has operated the Legacy claims processing system since 1991 and received \$350.3 million prior to the scheduled transition to the new eMedNY system. Simultaneous with operating the Legacy system, CSC worked to develop eMedNY, benefiting financially from both contracts. The eMedNY project delays resulted in significant corresponding cost overruns and necessitated unplanned continued operation and changes to the Legacy system. CSC, as the operator of the Legacy system, had little incentive to assure a timely completion of the project as it would continue to be paid for operating the Legacy system, while it simultaneously developed eMedNY.

Development costs of the eligibility and claims processing eMedNY components increased \$8.7 million (16 percent) to \$64.6 million.^{xxxi} CSC benefited from continuous operation of the Legacy system, accruing \$138.1 million in payments due to the delays. Further, these Legacy costs were priced at regular operation cost rates, while CSC was also accruing payments for the delayed eMedNY system. Therefore, the State was essentially paying for two systems at the same time. The increase in Legacy costs is associated with the following:

- Extended operation of the Legacy system from November 1, 2002 through June 30, 2005, while operation of the eMedNY system was delayed, \$97.1 million,^{xxxii} and
- By terms of the contract, eMedNY is to be HIPAA compliant, whereas the Legacy system was not. Since these delays resulted in the Legacy system remaining in operation after implementation of HIPAA requirements, significant modifications were needed to bring the system into compliance with HIPAA, totaling \$41 million.

All told, accrued payments to CSC (including the delays) through June 30, 2006 were \$495.4 million, \$146.8 million (42 percent) over the original estimate.^{xxxiii} The delays also caused an increase in the Bearing Point quality assurance oversight contract by \$7.2 million (129 percent) to \$12.8 million and an increase in the eFunds contract for eligibility services by \$12.4 million (443 percent) to nearly \$15.2 million. In total, due to the delays, the entire eMedNY project was now estimated to cost \$523.4 million, \$166.4 million (47 percent) over the original estimate of \$357 million.

Impact of Delays on eMedNY Project Cost
(in millions)

Contractor/Component	Original Estimate	Delay Cost	Estimate with Delays
CSC:			
eMedNY - Development, Eligibility and Claims Processing	\$55.9	\$8.7	\$64.6
eMedNY - Development, Data Warehouse	\$23.5	\$0.0	\$23.5
eMedNY - Operations	\$260.9	\$0.0	\$260.9
Legacy - Ops/Extensions	\$8.3	\$97.1	\$105.4
Legacy - HIPAA	\$0.0	\$41.0	\$41.0
CSC Total	\$348.6	\$146.8	\$495.4
Bearing Point (eMedNY)	\$5.6	\$7.2	\$12.8
eFunds (Legacy)	\$2.8	\$12.4	\$15.2
TOTAL	\$357.0	\$166.4	\$523.4

**Negotiated
Closeout
Associated with
Implementation
Delays**

eMedNY

The contract with CSC provided for consequential and liquidated damages for not meeting the eMedNY implementation deadlines.^{xxxiv} The Department, however, waived such rights, instead choosing to negotiate a closeout associated with the delays in implementation.^{xxxv} The Department did not base the closeout pricing on actual costs incurred by CSC during the delay period nor solely on the fixed costs contained within the pricing

originally bid and actually incurred by CSC, but rather on a recalculation of the fixed fees for operations based upon a simplified percentage allocation of responsibility for the delays.^{xxxvi} The negotiated closeout has raised several concerns:

- The closeout is the very same closeout that was returned to the Department unapproved for a lack of justification by the Office of the State Comptroller in June 2004,
- The waiver of the consequential and liquidated damages for not meeting the eMedNY implementation deadlines has not been justified by the Department,
- The closeout was bundled with a three-year extension of the CSC contract calling for a 62 percent increase in annual operation costs for the first year of the extension (see below),
- The closeout may be an effort by the Department to prevent the negative financial effects for CSC of the additional costs incurred to implement the system and/or for bidding an initial price that was too low,^{xxxvii} and
- Under the closeout and extension, CSC may be unjustly enriched given its responsibility for a portion of the delay in implementation.

The Department claims that in developing the closeout, it analyzed each delay period and assessed responsibility to CSC, itself or both. For delays in which there was shared responsibility between the Department and CSC, the Department planned to reimburse CSC for half of its fixed costs. When CSC was found to be fully at fault, the Department determined it would not reimburse any of CSC's fixed costs. For delays in which the Department claimed full responsibility, there were no adjustments to CSC.^{xxxviii}

Pursuant to the Department's negotiations, the closeout adjustments to fixed operating costs provided for annual operating costs when the eMedNY system was not yet operational. The operational pricing adjustments, which were not based on actual costs, totaled a \$90.6 million reduction and comprised fixed administrative fee - \$66.2 million, evolution - \$16.4 million, fixed fee data warehouse - \$5.9 million and nearly \$2.1 million related to transaction fees.

eMedNY Closeout Adjustments
(in millions)

Operational Component	Original Contract Amount ^{xxxix}	Negotiated Amount ^{xi}	Reduction Amount
Fixed Administrative Fee	\$187.6	\$121.4	\$66.2
Evolution	\$26.8	\$10.4	\$16.4
Fixed Data Warehouse	\$39.9	\$34.0	\$5.9
Transaction Fees	\$6.6	\$4.5	\$2.1
Total	\$260.9	\$170.3	\$90.6

Legacy System

The Department also negotiated a closeout amendment to the CSC Legacy contract extension from April 1 - June 30, 2005. The contract had been extended to allow continued claims processing for those providers not yet ready for electronic claims processing through eMedNY. The extension was valued at \$7.6 million.^{xli} The closeout amendment value was determined by an agreement to pay CSC the fixed fee for claims processing for the month of April (despite claim volume falling below the level to which fixed price was applicable) and adjust pricing for May and June based on actual costs incurred plus corporate allocation and markup, as provided for by the contract when claim volume fell below a certain level. The value of the adjustment made to CSC for the month of April in order to provide continued Legacy claims processing was \$1.4 million. As a result, the Legacy contract value was reduced by \$3.3 million, from \$7.6 million to \$4.3 million.^{xlii}

Total Closeout Adjustment Impact

Combining the closeout adjustments for eMedNY and the Legacy systems from above results in a total closeout adjustment of \$93.9 million. After consideration of an additional \$13.3 million in implementation and operations costs that were not associated with the delays, the net project payments accrued to CSC are \$414.8 million. The net \$66.2 million (19 percent) increase in reimbursement that CSC will receive over the original project amount represents the benefit to CSC from its dual roles of developing the eMedNY system while operating the Legacy system. An undetermined amount of the CSC payments represents duplicate payments as there appear to have been some shared resources between the Legacy and eMedNY systems. The State did not benefit from this sharing of resources. Again, it is important to note that CSC had little incentive to complete eMedNY in a timely manner as doing so would end its payments for operating the Legacy system. In the end, the closeout adjustments (and added costs not related to the delays) reduce total estimated project cost from \$523.4 million to \$442.8 million, \$85.8 million (24 percent) over the original eMedNY project estimate.

eMedNY Total Project Cost
(in millions)

Contractor/Component	Original Estimate	Delay Cost	Estimated Total with Delays	Increase Not Attributed to Delays	Negotiated Closeout	Net Total Cost	Net Increase Over Original Estimate
CSC:							
eMedNY - Development, Eligibility and Claims Processing	\$55.9	\$8.7	\$64.6	\$10.6	\$0.0	\$75.2	\$19.3
eMedNY - Development, Data Warehouse	\$23.5	\$0.0	\$23.5	\$0.0	\$0.0	\$23.5	\$0.0
eMedNY - Operations	\$260.9	\$0.0	\$260.9	\$2.7	(\$90.6)	\$173.0	(\$87.9)
Legacy - Ops/Extensions	\$8.3	\$97.1	\$105.4	\$0.0	(\$3.3)	\$102.1	\$93.8
Legacy - HIPAA	\$0.0	\$41.0	\$41.0	\$0.0	\$0.0	\$41.0	\$41.0
CSC Total	\$348.6	\$146.8	\$495.4	\$13.3	(\$93.9)	\$414.8	\$66.2
Bearing Point (eMedNY)	\$5.6	\$7.2	\$12.8	\$0.0	\$0.0	\$12.8	\$7.2
eFunds (Legacy)	\$2.8	\$12.4	\$15.2	\$0.0	\$0.0	\$15.2	\$12.4
TOTAL	\$357.0	\$166.4	\$523.4	\$13.3	(\$93.9)	\$442.8	\$85.8

Three-Year Contract Extension

The original eMedNY contract with CSC provided a six-year term with the possibility for a two-year extension and six one-month extensions. Rather than exercise the available two-year contract extension, on February 16, 2006, the Department submitted an amendment extending the CSC eMedNY contract for the three-year period July 1, 2006 through June 30, 2009. The amendment established the potential for six one-month extensions. On April 24, 2006, the Office of the State Comptroller returned the amendment to the Department unapproved due to a lack of sufficient information for its support. In May 2006, the Department resubmitted the extension request along with a partial response to some of the Office of the State Comptroller's questions.

Late in its review of the amendment, the Office of the State Comptroller learned of CSC's intent to not continue to provide services beyond June 30, 2006 without an approved extension. Such a situation endangered the continuity of the State's Medicaid program, raising the real potential of the need for contingency planning and the development of alternative payment issuance mechanisms.

As stated above, the contract extension was bundled with the negotiated closeout for the implementation period. CSC was unwilling to unbundle the closeout from the contract extension, demonstrating a take it or leave it attitude. The three-year extension is valued at \$278.1 million and would bring the total cost of the eMedNY project to \$720.9 million, \$363.9 million (102 percent) over the original estimate.^{xliii} The extension significantly increased the annual cost of the contract. For example, in the first year of

the extension (contract year 7), the annual cost increases \$34.1 million (62 percent) from \$54.5 million (contract year 6) to \$88.6 million.^{xliv} These increases continue in the subsequent years of the extension as well, with the cost in the second year of the extension (contract year 8) increasing \$3.5 million (4 percent) to \$92.1 million and the cost in the third year of the extension (contract year 9) increasing \$5.4 million (6 percent) to \$97.5 million.

Despite specific requests by the Office of the State Comptroller, the Department provided no justification as to how an increase of this magnitude was fair and equitable on top of the closeout pricing (previously returned unapproved by the Office of the State Comptroller). Without documentation justifying the increase, the Office of the State Comptroller has no assurance that the extension pricing is reasonable. Of additional concern is approving an extension with a contractor that has demonstrated serious performance problems during the current contract, coupled with the contractor's placing the State's Medicaid program, its providers and recipients in jeopardy by threatening to refuse to continue to operate after June 30, 2006, if the Office of the State Comptroller would not approve the extension by that time.

Proposed Contract Extension
July 1, 2006 - June 30, 2009
(in millions)

Cost Component	Amendment Period			
	Current Contract Year 6	Contract Year 7	Contract Year 8	Contract Year 9
Operations - Data Warehouse Fixed Fee	\$8.8	\$8.7	\$ 8.9	\$9.1
Operations - Fixed Admin.*	\$38.6	\$63.4	\$66.0	\$70.5
Operations - Fixed Fee Per Transaction	\$1.5	\$6.3	\$6.3	\$6.3
Operations - Evolution and User Support Staff	\$5.6	\$9.4	\$10.2	\$10.9
Business Reengineering Studies (3/year)	Inc. in fixed Admin.	\$0.7	\$0.7	\$0.7
Total Price	\$54.5	\$88.5	\$92.1	\$97.5

* - CSC staffing increased by 114.

On June 6, 2006, the Office of the State Comptroller, essentially faced with no other option based on the representation made by the Department that CSC would not continue to provide services beyond June 30, 2006 without an approved extension, approved this extension. The decision allowed the needs of program recipients and providers to take precedence, but left the

State with many unanswered questions and in a position where it must now continue to do business with a questionable contractor. To underscore the points made in the context of the Office of the State Comptroller's reluctant approval of this amendment, First Deputy Comptroller Thomas Sanzillo sent a letter to the Department of Health Executive Deputy Commissioner Dennis Whalen on June 13, 2006.

The State's experience with this contractor has served as an excellent example of how poor project management combined with a poor contract performer can expose the State to unnecessary vulnerability and expense. Had the Department been better at planning and managing, it would have had a viable backup plan in place so that when CSC threatened to shut down its Medicaid operations, the State could have executed the plan instead of rewarding CSC through an extension and exorbitant long-term price increases. The Department needs to devote appropriate resources to ensure that procurement of a new Medicaid fiscal agent is conducted in as timely a manner as possible and incorporates a backup plan so the State does not find itself in this same position again.

ⁱ Office of the State Comptroller, Department of Health, "Multiple Medicaid Payments for Managed Care Recipients, Report 2004-S-48," February 2006; Office of the State Comptroller, Department of Health, "Duplicate Medicaid Payments to Fulton County Ambulance, Report 2006-S-30," July 2006; Office of the State Comptroller, Department of Health, "Medicaid Claims Processing Activity, Report 2005-S-31," August 2006; Office of the State Comptroller, Department of Health, "Duplicate Medicaid Payments to Clinics, Report 2006-S-35," September 2006; and Office of the State Comptroller, Department of Health, "Medicaid Payments for HIV Pre-Test Counseling Services, Report 2006-S-34," September 2006.

ⁱⁱ Computer Sciences Corporation (CSC) has operated the Legacy system since 1991 and, through October 31, 2002, received payments totaling \$358.6 million for providing this service.

ⁱⁱⁱ The balance of the cost increases includes \$7.2 million for Bearing Point's quality assessment of the eMedNY project and \$12.4 million for the eFunds initiative associated with the Legacy Medicaid system.

^{iv} Maxwell, Terrence. *Information Federalism*. 1999. The Nelson A. Rockefeller Institute of Government.

^v *Ibid.*

^{vi} <<http://www.osc.state.ny.us/agencies/accmanual/policies/IV-4.htm>>.

^{vii} NASCIO 2004 Recognition Awards. *Using the Enterprise Data Warehouse to Transform the Management of Medicaid and Improve the Delivery of Health Care Services*. 2004. New York State Department of Health.

^{viii} Contract C014305.

^{ix} Contract C014305, Appendix F, 6.

^x Contract C014303.

^{xi} Letter from Dennis Whalen, Executive Deputy Commissioner, Department of Health to Thomas Sanzillo, First Deputy Comptroller, Office of the State Comptroller, September 11, 2003.

^{xii} Contract C013653.

^{xiii} Contract C013652.

^{xiv} Letter from Dennis Whalen, Executive Deputy Commissioner, Department of Health to Thomas Sanzillo, First Deputy Comptroller, Office of the State Comptroller, September 11, 2003. (The value of these savings was not provided to the Office of the State Comptroller.)

^{xv} Department of Health and Human Services Centers for Medicare and Medicaid Services. *Medicaid Integrity Program Review of Program Integrity Procedures Final Report – State of New York*. May 2006.

^{xvi} "Medicaid Fraud May Reach Into Billions," *New York Times*, CJ Levy, M Luo, July 18, 2005 and "As Medicaid Balloons, Watchdog Force Shrinks," *New York Times*, M Luo, CJ Levy. July 19, 2005.

^{xvii} Contract C014305, Appendix F, 1 and Appendix K, Amendment No. 6, K-1.

^{xviii} *Ibid.*

^{xix} *Ibid.*

^{xx} Contract C014305, Appendix K, Amendment No. 6, K-1.

^{xxi} Contract C014305, Appendix F, 1.

^{xxii} Letter from Dennis Whalen, Executive Deputy Commissioner, Department of Health to Thomas Sanzillo, First Deputy Comptroller, Office of the State Comptroller, November 14, 2003.

^{xxiii} Letter from Dennis Whalen, Executive Deputy Commissioner, Department of Health to Thomas Sanzillo, First Deputy Comptroller, Office of the State Comptroller, September 11, 2003.

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- ^{xxiv} Contract C014305, Appendix F, 1.
- ^{xxv} Letter from Dennis Whalen, Executive Deputy Commissioner, Department of Health to Thomas Sanzillo, First Deputy Comptroller, Office of the State Comptroller, November 14, 2003.
- ^{xxvi} Contract C014305, Appendix K, Amendment No. 6, K-1, Paragraph 4.
- ^{xxvii} Contract C014305, Appendix F, 1.
- ^{xxviii} Letter from Dennis Whalen, Executive Deputy Commissioner, Department of Health to Thomas Sanzillo, First Deputy Comptroller, Office of the State Comptroller, November 14, 2003.
- ^{xxix} Request for Proposal, Section 3.4.2.
- ^{xxx} Request for Proposal, Amendment No. 1, Section 3.
- ^{xxxi} This amount does not include \$10.6 million in added implementation costs that are not attributable to the delays.
- ^{xxxii} C014305, Amendments 15, 16, 17, 18 and 19.
- ^{xxxiii} These figures do not include \$13.3 million in added implementation and operation costs that are not attributable to the delays.
- ^{xxxiv} Contract C014305, Section 43.
- ^{xxxv} Contract C014305, Appendix K, Amendment No. 6, K-1.
- ^{xxxvi} Contract C014305, Appendix K, Amendment No. 6, K-6.
- ^{xxxvii} Profit and loss data submitted by CSC indicates that CSC was losing money monthly on the contract even after eMedNY was fully operational. This suggests that CSC underestimated the cost to implement and operate the system. On the Legacy side, CSC's profit and loss statement for the MMIS Legacy project was not provided, making it impossible to determine whether CSC was actually losing money on New York State's Medicaid program.
- ^{xxxviii} Letter from Mary Beth Hefner, Assistant Director, Bureau of Accounts Management, Department of Health to John Moriarty, Director, Bureau of Contracts, Office of the State Comptroller, May 10, 2006.
- ^{xxxix} Contract C014305, Appendix F, 6.
- ^{xl} Contract C014305, Appendix K, Amendment No. 6, K-6.
- ^{xli} Contract 013653, Amendments 17, 18 and 19.
- ^{xlii} Contract C013653, Attachment A, Closeout Amendment Calculations.
- ^{xliii} Contract C014305, Appendix K, Amendment No. 6, K-6.
- ^{xliv} Comparison of Contract C014305, Appendix K, Amendment No. 6, K-6 to Appendix F, 6.

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