

REVISED CONDITIONAL FISCAL IMPACT

(replaces fiscal note dated May 1, 2010)

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Date: May 7, 2010

Prime Sponsor(s): Rep. Vaad
Sen. Mitchell

Bill Status: Senate Second Reading

Fiscal Analyst: Ron Kirk (303-866-4785)

TITLE: CONCERNING RECOVERY AUDITS FOR GOVERNMENT OVERPAYMENTS OF TAX DOLLARS.

Fiscal Impact Summary	FY 2010-11	FY 2011-2012	FY 2012-2013
State Revenue General Fund			up to \$805,000
State Expenditures General Fund*	\$161,643	\$235,374	
FTE Position Change	2.1 FTE	3.3 FTE	
Effective Date: Upon signature of the Governor, or upon becoming law without his signature, but, only if HB10-1338 passes with savings sufficient to fund this bill.			
Appropriation Summary for FY 2010-2011: See State Appropriations section.			
Local Government Impact: None.			

*General Fund expenditures may be reimbursed from savings in HB10-1338.

Summary of Legislation

As amended in the **Senate Appropriations Committee**, this bill requires the Office of the State Controller to contract with a third party to perform an audit of state executive agencies to determine whether overpayments to individuals, vendors, and others occur as a result of pricing errors, neglected rebates, discounts, unclaimed refunds, or other related general errors. The bill applies to state executive agencies that spend more than \$25 million annually and authorizes the Office of the State Controller to retain a portion of any amount recovered due to an audit to defray the administrative costs incurred in contracting for and providing oversight of the recovery audit. General Fund expenditures will be reimbursed from the savings related to the Department of Corrections identified in the fiscal note for FY 2010-11 and FY 2011-12 in **HB10-1338**.

The Office of the State Controller must begin contracting with third party auditors for recovery audits no later than January 1, 2011, to conduct recovery audits for FY 2007-08, FY 2008-09, and FY 2009-10.

The Office of the State Controller must promulgate rules, provide a report to the Office of the State Auditor, Legislative Audit Committee, and Joint Budget Committee by October 1, 2010, regarding exemptions from the recovery audit process. In addition, the Office of the State Controller is required to provide a written report to the General Assembly by December 31, 2011, summarizing the contents of all reports contracted for pursuant to the provisions of this bill.

Background

Detailed recovery audit outcome data for four states (Texas, Missouri, Virginia, and North Carolina) were evaluated for purposes of this fiscal note. All of these states contracted out the audit work and paid the audit firm using proceeds from the recovered funds. Of the four states evaluated, the contingency rate (cost) for auditors was up to 20 percent of the funds recovered (Virginia). The recovery rate ranged from 0.0025 percent in Virginia to 0.0954 percent in Missouri, for an average of 0.0279 percent.

A variety of techniques can be employed to identify and collect recoverable funds. Under typical recovery audit programs, the state provides access to various sources of information including accounting systems, purchasing systems, receiving charts, vendor files, and client files. The recovery audit firm then reviews these records using proprietary software to reveal duplicate payments, pricing errors, and payments for goods or services not received.

State Revenue

As amended in the **Senate Finance Committee**, this bill requires the Office of the State Controller to contract for recovery audits conducted for a three-year period rather than a one-year period identified in the April 29, 2010 fiscal note. State General Fund revenue will increase by up to \$805,000 in FY 2012-13. This revenue estimate uses recovery rates that assume that less money will be identified, and less money will be **collected**, from recovery audits conducted in FY 2007-08 than in FY 2009-10.

In addition, over time, as errors are identified and corrected through the audit process, revenue recovered from the program will decrease in future years if audits were to be conducted in years beyond FY 2009-10. This bill does not require the Office of the State Controller to contract for recovery audits beyond FY 2009-10.

The Office of the State Controller must begin contracting with third party auditors for recovery audits no later than January 1, 2011. But no recovery money is expected until at least 24 months after the contracting process begins. In addition, other states requiring recovery audits have collected only about 50 percent of money identified in audits as duplicative or erroneous payments.

In Colorado, several state agencies already have similar audit programs in place that identify overpayments between the given agency and vendor or individual. These agencies — Education, Higher Education, Health Care Policy and Financing, Human Services, Transportation, and the Governor's Office of Information Technology (OIT) — have been excluded from this analysis. As an example, OIT has programs in place that identify overpayments and has previously contracted for such audit/recovery functions associated with state billings for services from third party telecommunications vendors.

A total of \$2.7 billion of the state's budget in FY 2010-11 is expected to be subject to audit as a result of this bill. A recovery rate of 0.0279 percent, or the average of the recovery rates realized by Texas, Missouri, Virginia, and North Carolina, was assumed for the most recent audit year in the bill (FY 2009-10). A lower recovery rate was used for FY 2007-08 and FY 2008-09.

State Expenditures

General Fund expenditures will increase \$161,643 and 2.1 FTE in FY 2010-11 and \$235,374 and 3.3 FTE in FY 2011-12. General Fund expenditures will be reimbursed from the savings related to the Department of Corrections identified in the fiscal note for FY 2010-11 and FY 2011-12 in **HB10-1338**. With the exception of the Department of Local Affairs, expenditures incurred by state agencies to comply with the provisions of this bill will be reimbursed by money collected from recovery audits in FY 2012-13.

Office of the State Controller: \$134,716 General Fund in FY 2010-11 and \$208,447 in FY 2011-12. Costs for the state controller are expected to increase \$134,716 and 1.8 FTE in FY 2010-11 for one contract administrator and one support person to promulgate rules, contract with consultants to conduct recovery audits, manage vendor contracts, and ensure that vendors receive appropriate information. In FY 2011-12, an additional person will be needed to assist in the negotiation and execution of contracts and serve in the role as an arbitrator to any disagreements between the recovery auditor and the individual departments. Of the costs identified above, \$2,000 will be reappropriated each year to the Department of Law to review any rules promulgated.

Department of Local Affairs: \$26,927 General Fund in FY 2010-11 and FY 2011-12. Costs for the department are expected to increase \$26,927 and 0.3 FTE in FY 2010-11. These costs include an estimated 576 hours in staff time to provide programmatic details to the contractor for each of 24 affected programs and copying costs for 16,500 payment vouchers that meet the \$25 million threshold requirement in the bill.

Other state agencies: unknown. All agencies were canvassed for purposes of this fiscal note, but not all agencies were able to respond with complete information. It is assumed that for state agencies required to comply with the provisions of this bill, additional expenditures will be incurred. These expenditures will be realized in terms of increased staff time to compile three years of agency transaction data that will need to be evaluated and submitted to third party auditors. The total expenditure impact for these agencies is unknown.

Table 1. Expenditures Under HB 10-1176		
Office of the State Controller		
Cost Components	FY 2010-11	FY 2011-12
Personal Services	\$114,194	\$177,635
FTE	1.8	3.0
Operating Expenses and Capital Outlay	18,522	28,812
Department of Law	\$2,000	\$2,000
Subtotal	\$134,716	\$208,447
Department of Local Affairs		
Personal Services	\$20,327	\$20,327
FTE	0.3	0.3
Copying Expenses	\$6,600	\$6,600
Subtotal	\$26,927	\$26,927
Other State Agencies		
Personal Services	Unknown	
FTE	Unknown	
Copying Expenses	Unknown	
Total FTE	2.1	3.3
Total Expenditures	\$161,643	\$235,374

State Appropriations

The Office of the State Controller requires an appropriation of \$134,716 and 1.8 FTE in FY 2010-11, of which \$2,000 will be reappropriated to the Department of Law. The Department of Local Affairs requires an appropriation of \$26,927 and 0.3 FTE in FY 2010-11. These appropriations should be from the General Fund.

Departments Contacted

All Departments