

# **PACE FINANCIAL REQUIREMENTS**

This list is intended to assist applicants in completing Chapter 3 of the federal CMS PACE application while also meeting the State of California financial requirements for new PACE Organizations.

## **FEDERAL REQUIREMENTS**

### **I. FISCAL SOUNDNESS (§460.80(a))**

- A. Describe any reserve requirements and other financial requirements set by the State in which the PACE Organization operates and demonstrate how the entity meets these requirements. Include any supporting documentation, as necessary.
- B. In the Documents section, provide independently certified audited financial statements for the three most recent fiscal year periods or, if operational for a shorter period of time, for each operational fiscal year. If the PACE program is a line of business of the applicant, it should provide audited statements relating to the legal entity. Audits are to include:
  - 1. Opinion of a certified public accountant.
  - 2. Statement of revenues and expenses.
  - 3. Balance sheet.
  - 4. Statement of cash flows.
  - 5. Explanatory notes.
  - 6. Management letters.
  - 7. Statements of changes in net worth.
  - 8. Actuarially certified statement of incurred but not reported claims. (If required by State licensure.)
- C. In the Documents section, provide a copy of the most recent year-to-date unaudited financial statement of the entity.
- D. In the Documents section, provide independently certified audited financial statements of guarantors, and lenders (organizations providing loans, letters of credit or other similar financing arrangements, excluding banks).

If the entity is a public corporation or subsidiary of a public corporation, provide in the Documents section the most recent Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934, Form 10-K.

## II. FINANCIAL PROJECTIONS<sup>1</sup>

In the Documents section, provide financial projections for a minimum of one year from the date of the latest submitted financial statement. Give projections from this date through one year beyond break-even. Describe financing arrangements and include all documents supporting these arrangements for any projected deficits. There must be evidence of financing arrangements for any projected deficit. (If the PACE organization has reached break-even, provide projections from this date until one year from anticipated date of execution of contract.)

Financial projections should be prepared using the accrual method of accounting in conformity with generally accepted accounting principles (GAAP). Prepare projections using the pro-forma financial statement methodology. For a line of business, assumptions need only be submitted to support the projections of the line. Projections must include the following:

Quarterly balance sheets for the applicant, using accrual accounting in conformity with GAAP. The National Association of Insurance Commissioners (NAIC) Financial Report #1 format may be used if also required for State licensure.

Quarterly statements of revenues and expenses for the legal entity. In cases where the plan is a line of business, the applicant should also complete a statement of revenue and expenses for the line-of-business. Give projections in gross dollars as well as on a per member per month basis. Quarters should be consistent with standard calendar year quarters. Include year end totals. If an organization has a category of revenue and/or expense that is not included in the present definitions, provide an explanation.

### Quarterly Statements of Cash Flows

Statement and Justification of Assumptions - State major assumptions in sufficient detail to allow an independent financial analyst to reconstruct projected figures using only the stated assumptions. Include operating and capital budget breakdowns.

Stated assumptions should address all periods for which projections are made and include inflation assumptions. Details of minor assumptions will be verified on site. Justify assumptions to the extent that a knowledgeable reviewer would be convinced that they are reasonable. Base justification on such factors as the

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<sup>1</sup> See the reference in the Introduction for the sources for purchasing the NAIC report forms and the instructions for completing the forms. This information is extracted from the CMS Application located at [http://www.cms.hhs.gov/PACE/06\\_ProviderApplicationandRelatedResources.asp](http://www.cms.hhs.gov/PACE/06_ProviderApplicationandRelatedResources.asp)

applicant's experience, the experience of other health plans. Describe hospital and health professional costs and utilization in detail.

III. INSOLVENCY (§460.80(b))

A. Describe the PACE Organization's provisions for the event of insolvency that include:

1. The continuation of benefits for the duration of the period for which capitation payment has been made;
2. Continuation of benefits to participants who are confined in a hospital on the date of insolvency until their discharge; and
3. Protection of participants from liability for payment of fees that are the legal obligation of the PACE Organization.

B. Provide documents in the Documents section that demonstrate the PACE Organization can, in the event it becomes insolvent, cover expenses of at least the sum of one month's total capitation revenue to cover expenses the month prior to insolvency and one month's average payment to all contractors, based on the prior quarter's average payment, to cover expenses the month after the date insolvency is declared or operations cease. (Arrangements to cover expenses may include, but are not limited to, insolvency insurance or reinsurance, hold harmless arrangements, letters of credit, guarantees, net worth, restricted state reserves or State law provisions.)

IV. FINANCIAL RISK

Insurance Protection: Use the Insurance Table to summarize insurance or other arrangements for major types of loss and liability. Complete the table `paceinsu.doc` in its file on the disk and place the hard copy in the Documents section.

V. FINANCIAL RECORD KEEPING AND REPORTING (§460.204-208)

A. Describe how the PACE Organization's financial records and reports meet the regulatory requirements.

B. How does the PACE Organization ensure that it will submit quarterly and annual certified financial statements in a format acceptable to CMS and the State.

## STATE REQUIREMENTS

1. An attestation that the plan is prepared to increase its financial security deposit to accommodate the projected increase in enrollments.
2. Contractor shall demonstrate financial viability/standards compliance to CDHS satisfaction for each of the following Elements:
  - A. Tangible Net Equity – Contractor shall maintain a tangible net equity equal to one month's capitation.
  - B. Administrative Costs – Contractor's administrative costs shall not exceed 25%, unless otherwise authorized in writing by CDHS after the submission of appropriate justification by the Contractor.
  - C. Contractor shall maintain an organizational structure sufficient to conduct the proposed operations and ensure that its financial resources are sufficient for sound business operations.
  - D. If the organization conducting the day-to-day operations of the program is a subsidiary entity within a larger parent company, a separation of duties must be clearly established between the two entities in the Contractor's operating policies and procedures and its financial record keeping. A separate financial statement must be maintained for this entity, which includes but is not limited to the balance and income statements. The financial reserve requirements specified in the CDHS contract must be held in a separate bank account clearly designated as the specific program reserve account. The funds in this account shall not be commingled with the reserves for any other program.
  - E. Working Capital and current ratio of one of the following:
    - Contractor shall demonstrate to CDHS that Contractor is now meeting financial obligations on a timely basis and has been doing so for at least the preceding two years; **OR**
    - Contractor shall provide evidence that sufficient noncurrent assets, which are readily convertible to cash, are available to achieve an equivalent working capital ratio of 1:1, if the noncurrent assets are considered current.
  - F. The Contractor shall ensure that an annual audit is performed according to Section 14459 Welfare and Institutions Code (WIC). Combined financial statements shall be prepared to show the financial position of overall related health care delivery system when deliver of care or other services is dependent upon Affiliates. Financial Statements shall be presented in a form that clearly shows the financial position of the Contractor separately from the combined

totals. Inter-entity transactions and profits shall be eliminated if combined statements are prepared. The Contractor shall have separate certified Financial Statements prepared if an independent accountant decides that preparation of combined statements is inappropriate.

- The independent accountant shall state in writing reasons for not preparing combined Financial Statements.
- The Contractor shall provide supplemental schedules that clearly reflect all inter-entity transactions and eliminations necessary to enable CDHS to analyze the overall financial status of the entire health care delivery system.
- In addition to annual certified Financial Statements Contractor shall complete the entire 1989 HMO Financial Report of Affairs and Conditions Format, commonly known as the "Orange Blank". The Certified Public Accountant's (CPA) audited Financial Statements and the "Orange Blank" report shall be submitted to CDHS no later than 120 calendar days after the close of Contractor's Fiscal Year.
- Contractor shall submit to CDHS within forty-five (45) calendar days after the close of Contractor's fiscal quarter financial reports required by Title 22, CCR, Section 53312. The required quarterly financial reports shall be prepared on the "Orange Blank" format and shall include, at a minimum, the following reports/schedules:
  - Jurat
  - Report 1A and 1B: Balance Sheet
  - Report 2: Statement of Revenue, Expenses, and Net Worth Statement of Cash Flow, prepared in accordance with Financial Accounting Standards Board Statement #95 – this statement is prepared in lieu of Report #3: Statement of Changes in Financial Position for Generally Accepted Accounting Principles (GAAP) compliance.
  - Report 4: Enrollment and Utilization Table.
  - Schedule F: Unpaid Claims Analysis. Appropriate footnote disclosures in accordance with the GAAP.

G. The Contractor shall authorize the independent accountant to allow representatives of CDHS, upon written request, to inspect any and all working papers related to the preparation of the audit report.

- H. The Contractor shall submit to CDHS all financial reports relevant to Affiliates as specified in T22, CCR, Section 53330 (a) (1).
- I. The Contractor shall submit to CDHS copies of any financial reports submitted to other public or private organizations as specified in T22, CCR, Section 53324(d).
- J. The Contractor may be required to file monthly Financial Statements at CDHS' request during the first year in operations and then on a quarterly basis, thereafter.
- K. The Contractor shall cooperate with CDHS' own independent audits annually or as necessary for good cause, at the discretion of CDHS.
- L. The Contractor shall prepare financial information requested in accordance with GAAP and where Financial Statements/Projections are requested, these statements/projections should be prepared on the 1989 HMO Reporting Format (commonly known as the "Orange Blank").