STATE OF ARIZONA

Joint Legislative Budget Committee

STATE SENATE

1716 WEST ADAMS
PHOENIX, ARIZONA 85007

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http://www.azleg.gov/jlbc.htm

HOUSE OF REPRESENTATIVES

**** R E V I S E D ****

JOINT LEGISLATIVE BUDGET COMMITTEE
Tuesday, October 29, 2013
1:00 P.M.
House Hearing Room 4

MEETING NOTICE

- Call to Order

- Approval of Minutes of August 20, 2013.

- DIRECTOR'S REPORT (if necessary).

- EXECUTIVE SESSION
  A. Arizona Department of Administration, Risk Management Services - Consideration of Proposed Settlements under Rule 14.
  B. Arizona Department of Administration - Risk Management Annual Report.

1. ARIZONA DEPARTMENT OF ADMINISTRATION - Automation Projects Fund
   A. ADOA - Review of ASET Projects.
   B. ADOA/DOR - Review of DOR Information Technology Projects.
   C. ADOA/DEQ - Review of Department of Environmental Quality Phase I.
   D. ADOA/ADE - Review of Arizona Education Learning and Accountability System (AELAS).

2. AHCCCS/DEPARTMENT OF ECONOMIC SECURITY/DEPARTMENT OF HEALTH SERVICES - Review of Proposed Capitation Rate Changes.

3. AUTOMOBILE THEFT AUTHORITY - Review of the Proposed Expenditures from the Reimbursables Program Special Line Item.

4. DEPARTMENT OF PUBLIC SAFETY - Review of Expenditure Plan for the Gang and Immigration Intelligence Team Enforcement Mission (GIITEM) Fund Border Security and Law Enforcement Subaccount.

5. JLBC STAFF - Review of Agency Legal Services Charges.

6. ARIZONA DEPARTMENT OF ADMINISTRATION - Review of the Arizona Public Safety Communication Advisory Commission.

The Chairman reserves the right to set the order of the agenda.
~~10/22/13~~
10/24/13
lm

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STATE OF ARIZONA

Joint Legislative Budget Committee

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HOUSE OF
REPRESENTATIVES

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STEFANIE MACH
JUSTIN OLSON
MICHELLE UGENTI

MINUTES OF THE MEETING

JOINT LEGISLATIVE BUDGET COMMITTEE

August 20, 2013

The Chairman called the meeting to order at 1:02 p.m., Tuesday, August 20, 2013, in House Hearing Room 4. The following were present:

Members:	Representative Kavanagh, Chairman	Senator Shooter, Vice-Chairman
	Representative Gowan	Senator Cajero Bedford
	Representative Kwasman	Senator Griffin
	Representative Lesko	Senator McComish
	Representative Olson	Senator Melvin
	Representative Ugenti	Senator Pancrazi
		Senator Tovar
Absent:	Representative Alston	Senator Yarbrough
	Representative Mach	

APPROVAL OF MINUTES

Hearing no objections from the members of the Committee to the minutes of June 11, 2013, Chairman John Kavanagh stated that the minutes would stand approved.

ARIZONA DEPARTMENT OF ADMINISTRATION (ADOA) - Automation Projects Fund

A. ADOA - Review of ASET Projects.

Mr. Ben Henderson, JLBC Staff, stated that this item is for review of a $3.5 million expenditure plan from the Automation Projects Fund for information technology (IT) projects for the Arizona Strategic Enterprise Technology (ASET) Office in ADOA.

Mr. Aaron Sandeen, Deputy Director, Arizona Department of Administration addressed the Committee.

Senator Shooter moved that the Committee give a favorable review of the FY 2014 $3.5 million expenditure plan from the Automation Projects Fund for information technology (IT) projects for the Arizona Strategic Enterprise Technology (ASET) Office in ADOA. The $3.5 million includes:

(Continued)

- *Project Management* — *$1,700,000*
- *Security, Privacy and Risk* — *$900,000*
- *Enterprise Architecture* — *$600,000*
- *E-Government* — *$325,000*

The motion carried.

B. ADOA/Arizona Department of Corrections - Review of Adult Inmate Management System.

Mr. Ben Henderson, JLBC Staff, stated that this item is for review of an $8.0 million expenditure plan from the Automation Projects Fund for information technology (IT) projects to replace the Adult Inmate Management System at the Arizona Department of Corrections.

Mr. Aaron Sandeen, Deputy Director, Arizona Department of Administration responded to Committee questions.

Mr. Michael Kearns, Administrative Director, Department of Corrections, responded to Committee questions.

Mr. Jonathan Taylor, Vice President, Public Consulting Group, responded to Committee questions.

Senator Shooter moved *that the Committee give a favorable review of the $8.0 million FY 2014 expenditures from the Automation Projects Fund for information technology (IT) projects to replace the Adult Inmate Management System at ADC with the following provisions:*

1. *The Request for Proposal (RFP) for the proposed system shall only be issued upon agreement between ADC and ASET regarding the technology requirements and evaluation process identified in the Statement of Work.*

2. *ADC may not award the solicitation until an updated Project Investment Justification (PIJ) reflecting the results of its evaluation, including the selected technology approach, scope of work, implementation schedule, and detailed itemization of the development and operational costs for the project, has been submitted for review to ASET and approved by the Information Technology Authorization Committee (ITAC), in Executive Session if applicable.*

3. *ADC shall retain the services of the vendor currently engaged as an Independent Advisory Consultant (IAC) to assist in the development of the RFP, for the duration of the solicitation process. Costs to retain the current vendor, or other qualified vendor, as an IAC for the duration of the project, must be reflected in the updated PIJ.*

The motion carried.

C. ADOA/Arizona Department of Education (ADE) - Review of Arizona Education Learning and Accountability System.

Mr. Ben Henderson, JLBC Staff, stated that this item is for review of a $3.4 million expenditure plan from the Automation Projects Fund for 3 projects related to the Arizona Learning and Accountability System (AELAS) at the ADE.

Senator Shooter moved *that the Committee give a favorable review of the $3.4 million FY 2014 expenditure plan from the Automation Projects Fund for 3 projects related to the development of AELAS at ADE. The 3 projects include:*

(Continued)

- *AELAS - Education Data Fidelity (Ed-Fi)* *$1,600,000*
- *Program Support Office* *$1,000,000*
- *AELAS - School Finance Automation* *$800,000*

In addition, the Committee added the following provisions as part of its review:

1. *ADE may proceed with the assessment phase of the AELAS "Education Data Fidelity" project to determine the data collection requirements, business processes, technical approach, and legal requirements to implement a compliant student data store. Costs are not to exceed $630,000 for the assessment phase, and ADE may not proceed with additional development efforts, until a full PIJ reflecting the technology, scope of work, costs and implementation schedule for the proposed solution has been submitted to ASET and ITAC for review and approval.*

2. *ADE must present information to ITAC regarding an upcoming Organization Entity Management PIJ, as a component of the AELAS Education Data Fidelity initiative, prior to proceeding beyond an assessment phase which is not expected to exceed $90,000 in cost.*

3. *ADE shall return to the Committee for additional review of the "Education Data Fidelity" project if ASET raises serious concerns when reviewing its upcoming full PIJ for the $920,000 development cost.*

4. *ADE may proceed with the design, development and implementation of the proposed solution related to the AELAS School Finance automation project; however, should there be significant differences in the scope of work, costs, implementation schedule, or proposed technology, ADE must amend the PIJ for the project to reflect the changes and submit it to the ASET office for review and approval prior to further expenditure of funds.*

5. *ADE shall present results of the pending third party analysis of AELAS for review at the next Committee meeting.*

The motion carried.

ARIZONA DEPARTMENT OF CORRECTIONS - Review of FY 2013 Bed Capacity Report.

Ms. Micaela Larkin, JLBC Staff, stated that this is for a review of the Arizona Department of Corrections (ADC) FY 2013 bed capacity report. The JLBC Staff presented options to the Committee and answered questions from members.

Mr. Chuck Ryan, Director, ADC, responded to member questions.

Senator Shooter moved *that the Committee give a favorable review of the FY 2013 bed capacity report.* The motion carried.

ATTORNEY GENERAL - Review of FY 2011 and FY 2012 Uncollectible Debts.

Mr. Matt Gress, JLBC Staff, stated that the Attorney General's (AG) office is requesting review of their uncollectible debts report. After a period of time the Attorney General determines that some debts that are owed to the state are uncollectible and upon the Committee's review these can be removed from the state accounting system. The Attorney General identified $17.2 million of uncollectible debt in FY 2011 and $30.4 million in FY 2012.

The JLBC Staff presented options to the Committee.

(Continued)

Representative Gowan moved that the Committee give a favorable review of the FY 2011 and FY 2012 listings of uncollectible debts referred to the AG by state agencies for collection. The uncollectible debt listings total $17.2 million for FY 2011 and $30.4 million for FY 2012. The motion carried.

ARIZONA BOARD OF REGENTS - Review of FY 2014 Tuition Revenues.

Mr. Art Smith, JLBC Staff, stated that Arizona Board of Regents (ABOR) requests Committee review of its expenditure plan for tuition revenue amounts greater than the amounts appropriated by the Legislature, and all non-appropriated tuition and fee revenue expenditures for the current fiscal year.

The JLBC Staff presented options to the Committee.

Senator Shooter moved that the Committee give a favorable review of ABOR's expenditure plan. The motion carried.

DEPARTMENT OF ENVIRONMENTAL QUALITY - Review of Vehicle Emissions Contract Modification.

Ms. Micaela Larkin, JLBC Staff, stated that the Department of Environmental Quality (DEQ) requests Committee review of proposed modifications or amendments to the Vehicle Emissions Inspection Contract with a private vendor.

Mr. Trevor Baggiore, Deputy Director, Air Quality Division, Department of Environmental Quality responded to member questions.

Senator Shooter moved that the Committee give a favorable review to the Vehicle Emissions Inspection contract modifications. The motion carried.

EXECUTIVE SESSION

Senator Shooter moved that the Committee go into Executive Session. The motion carried.

At 2:10 p.m. the Joint Legislative Budget Committee went into Executive Session.

Senator Shooter moved that the Committee reconvene into open session. The motion carried.

At 2:38 p.m. the Committee reconvened into open session.

Senator Shooter moved that the Committee approve the recommended settlements proposed by the Attorney General's office in the cases of:

- *Van den Berg* v. *Arizona Board of Regents, et al.*
- *Nieves v. State of Arizona, et al.*

The motion carried.

(Continued)

Without objection, the meeting adjourned at 2:40 p.m.

Respectfully submitted:

Tera Scherer, Secretary

Richard Stavneak

Richard Stavneak, Director

Representative John Kavanagh, Chairman

NOTE: A full audio recording of this meeting is available at the JLBC Staff Office, 1716 W. Adams. A full video recording of this meeting is available at http://www.azleg.gov/jlbc/meeting.htm.

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Joint Legislative Budget Committee

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PHOENIX, ARIZONA 85007

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http://www.azleg.gov/jlbc.htm

DATE: October 22, 2013

TO: Representative John Kavanagh, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director RS

FROM: Ben Henderson, Fiscal Analyst BH

SUBJECT: Arizona Department of Administration - Review of ASET Projects (Automation Projects Fund)

Request

Pursuant to A.R.S. § 41-714, the Arizona Department of Administration (ADOA) has requested that the Committee review $18.8 million in proposed FY 2014 expenditures from the Automation Projects Fund for information technology (IT) projects. This memo addresses the $3.5 million for the Arizona Strategic Enterprise Technology (ASET) Office in ADOA. The remainder of the $18.8 million request is addressed in Agenda Items 1B, 1C, and 1D.

Recommendation

The Committee has at least the following 2 options:

1. A favorable review.
2. An unfavorable review.

All projects have received relevant approvals from ASET staff through the Project Investment Justification (PIJ) process. For the 2 projects regarding security, privacy, and risk, ASET's approval included the following condition:

A) Should there be significant changes in the proposed costs, technology approach, scope of work, or implementation schedule, as a result of the evaluation and selection process, the Security, Privacy, and Risk (SPR) team within ADOA-ASET must amend the PIJ to reflect the changes and submit the updated PIJ to the ADOA-ASET Strategic Oversight team for review, and approval as necessary.

The project regarding the web portal transition is the only ADOA project that requires Information Technology Authorization Committee (ITAC) approval. As of this writing, ITAC approval was pending based on a review that will occur on October 23rd, 2013.

(Continued)

The JLBC Staff recommends that the JLBC consider adopting the ITAC/ASET provision as part of its review.

Analysis

Background
The FY 2013 Government Budget Reconciliation Bill (BRB) (Laws 2012, Chapter 298) established the Automation Projects Fund, consisting of monies appropriated by the Legislature and administered by ADOA. The FY 2014 Budget Procedures BRB (Laws 2013, 1st Special Session, Chapter 6) subjected the Automation Projects Fund to legislative appropriation, retroactive to June 30, 2013. The fund is exempt from lapsing. Monies in the fund are to be used to implement, upgrade or maintain automation and IT projects for any state agency. Pursuant to A.R.S. § 41-714, before monies are expended from the fund, ADOA must submit an expenditure plan to the JLBC for review.

The financing of the Automation Projects Fund is described in more detail in *Attachment A*.

Automation Project Oversight
In addition to the JLBC review of Automation Projects Fund expenditures, all IT projects over $25,000 are reviewed by ASET through the Project Investment Justification (PIJ) process. If an IT project exceeds $1,000,000, statute requires additional approval by ITAC. ITAC consists of members from both the public and private sectors and is staffed by ADOA. If a project funds internal staff or training, neither ITAC nor ASET approval is required.

Current Request
ADOA is requesting a review of $18.8 million from the Automation Projects Fund for FY 2014 projects at ADOA, the Arizona Department of Revenue (DOR), the Arizona Department of Environmental Quality (DEQ), and the Arizona Department of Education (ADE), as follows:

- ADOA – ASET Initiatives $3.5 million
- DOR – Data Security and Encryption $4.9 million
- DOR – Business Reengineering and Integrated Tax System (BRITS) $1.7 million
- DEQ – E-Licensing $5.0 million
- ADE – Arizona Education and Learning Accountability System (AELAS) $3.7 million

A total of $14.9 million of Automation Project Fund expenditures were reviewed by this committee during the August 20th meeting. Following the review of this $18.8 million request, $4.5 million of total FY 2014 IT funding will remain to be reviewed by JLBC at a later date, following the necessary PIJ and ITAC approvals.

ADOA – ASET Initiatives
ADOA is currently proposing an expenditure plan totaling $3.5 million from the Automation Projects Fund for projects to enhance the state's IT infrastructure, including:

- Web Portal Transition $1,530,000
- Security, Privacy, and Risk $1,075,000
- Project Management $450,000
- Enterprise Architecture $400,000

Web Portal Transition
Since 2007, the state's web portal has been operated and maintained exclusively by a third-party vendor. This contract expired on June 26, 2013. Due to the fact that this contract gave exclusive rights and ownership of many aspects of the state web portal to the vendor, ADOA has extended the contract to provide state web portal services for a transitionary phase not to exceed June 26, 2014. ADOA has chosen 4 vendors to rebuild the state's web portal. A single vendor has been chosen to operate the web

(Continued)

portal. Under the new structure, however, ADOA will assume responsibility and ownership of the web portal, including infrastructure, application source code, licensing, and the customer service desk.

The FY 2014 General Appropriation Act appropriated $1,975,000 to ADOA for costs associated with this transition to a new web portal structure. ADOA is currently requesting review of $1,530,000, which consists of $1,149,000 to be spent on development and operational costs to transition from the old vendor to the new vendor, in addition to 4,000 hours of Professional and Outside Services at a total cost of $381,000.

These projects have received relevant PIJ approvals. As of this writing, ITAC approval was pending based on a review that is scheduled to occur on October 23rd, 2013. ASET anticipates returning to this committee at a later date for review of the remaining FY 2014 appropriation, a total of $445,000.

Security, Privacy, and Risk
ADOA's ASET Office is responsible for directing and training state agencies in regards to information security and protection against cyber-attacks. The FY 2014 General Appropriation Act appropriated $3.1 million to ADOA for projects related to security privacy and risk. This committee has previously given a favorable review to $900,000 of this amount. ADOA is currently requesting review of projects totaling $1,075,000. Following this review, $1,100,000 of the FY 2014 appropriation remains to be reviewed by this committee for projects related to security, privacy, and risk.

The current $1,075,000 request would fund 2 projects. The first project would cost $350,000 and would fund efforts to track the location of sensitive data across the state's IT infrastructure, as well as require users to undergo a multi-faceted authentication system whenever accessing sensitive data.

The second project would cost $725,000 and would increase security measures in the State Data Center, including increased monitoring of State internet connections, assist in creating a dashboard of the State's cybersecurity threat situation, and would expand upon security services currently provided by the U.S. Department of Homeland Security.

Both projects have received PIJ approval, with the following condition:

- Should there be significant changes in the proposed costs, technology approach, scope of work, or implementation schedule, as a result of the evaluation and selection process, the Security, Privacy, and Risk (SPR) team within ADOA-ASET must amend the PIJ to reflect the changes and submit the updated PIJ to the ADOA-ASET Strategic Oversight team for review, and approval as necessary.

Neither project requires ITAC approval. The JLBC Staff recommends that the JLBC consider adopting the PIJ provisions as part of its review.

Project Management
ADOA's ASET Office is responsible for approving and tracking all IT projects over $25,000 through the PIJ process, and to assist state agencies with management and oversight of their various IT projects.

The FY 2014 General Appropriation Act appropriated $2.5 million to ADOA for project management. This committee has previously given a favorable review to $1.7 million of this amount. ADOA is currently requesting review of 1 project totaling $450,000. Following this review, $300,000 of the FY 2014 appropriation remains to be reviewed by this committee for project management, following any necessary PIJ approvals. The current $450,000 request would fund additional FTE positions to implement ASET's various initiatives.

This project has not received any independent review, as it does not meet the requirements for PIJ or ITAC approval.

(Continued)

Enterprise Architecture
Enterprise Architecture focuses on creating proper guidelines, frameworks, and policies that ensure reliable implementation and maintenance of IT systems.

The FY 2014 General Appropriation Act appropriated $1.0 million to ADOA for enterprise architecture. This committee has previously given a favorable review to $600,000 of this amount. ADOA is currently requesting review of 1 project for $400,000, the remainder of the FY 2014 appropriation. This amount would fund an assessment of ASET's services, assets and resources. This assessment is intended to assist in establishing a new pricing model for the State Data Center, as well as other ASET services, and would include implementation of dashboards for financial management and reporting.

This project has not received any independent review, as it does not meet the requirements for PIJ or ITAC approval.

Further Review
The FY 2014 General Appropriation Act appropriated $11.5 million to ADOA for ASET Projects. This committee has previously given a favorable review to $3.5 million of this amount. Following the current request to review an additional $3.5 million, $4.5 million for ASET projects will remain to be reviewed by JLBC at a later date, following the necessary PIJ and ITAC approvals, as follows:

• State Data Center	$2.7 million
• Security, Privacy, and Risk	$1.1 million
• Project Management	$300,000
• Web Portal Transition	$445,000

RS:BHe/ts

Attachment A – Automation Projects Fund Background

The FY 2013 General Appropriation Act (Laws 2012, Chapter 294, Section 124) appropriated a total of $91,100,000 over 4 years for deposit into the Automation Projects Fund, primarily for the replacement of the state's financial and accounting system, the Arizona Financial Information System (AFIS). In the 2013 Legislative Session, the Legislature enacted a plan to allocate a portion of AFIS replacement costs to non-General Fund sources. As a result, the FY 2014 General Appropriation Act (Laws 2013, 1st Special Session, Chapter 1) reduced the Chapter 294 General Fund appropriation by $16,998,000 over 4 years and replaced it with a one-time transfer totaling $17,013,600 charged to other appropriated and non-appropriated funds for the replacement of AFIS. This charge represents a proportional contribution from the General Fund and all other funds, at an estimated 0.72% of FY 2014 expenditures. *Table 1* delineates the change in the Chapter 294 General Fund appropriation.

Table 1

Change in 4-year Chapter 294 General Fund Appropriation
($ in thousands)

	Chapter 294	Chapter 1	Difference
FY 2013	16,800	16,800	0
FY 2014	20,000	18,400	(1,600)
FY 2015	20,000	18,400	(1,600)
FY 2016	23,000	9,202	(13,798)
Total	**79,800**	**62,802**	**(16,998)**

Automation Projects Fund Revenues

Chapter 1 made additional transfers into the Automation Projects Fund in FY 2014 for various IT projects in ADOA, the Arizona Department of Corrections (ADC), the Arizona Department of Education (ADE), the Department of Environmental Quality (DEQ), and the Department of Revenue (DOR). These transfers totaled $34,175,000, as shown in *Table 2*.

Table 2

Automation Projects Fund
($ in thousands)

	FY 2013	FY 2014	FY 2015	FY 2016
Beginning Balance		5,225.1	8,075.7	(57.3)
Revenues				
General Fund Appropriation	16,800.0	18,400.0	18,400.0	9,202.0
General Fund Transfer		7,100.0		
Automation Charges		17,013.6		
ADOA Automation Operations Fund	4,200.0	8,130.0		
ADOA State Web Portal Fund	5,600.0	4,000.0		
ADOA Information Technology Fund	1,500.0	345.0		
ADC Inmate Store Proceeds Fund		5,500.0		
State DOC Revolving Fund		2,500.0		
DEQ Emissions Inspection Fund		5,000.0		
ADE Education Learning and Accountability Fund 1/		1,600.0		
Total Funds Available	**28,100.0**	**74,813.7**	**26,475.7**	**9,144.7**
Total Expenditures	**22,874.9**	**66,738.0**	**26,533.0**	**9,202.0**
Ending Balance	**5,225.1**	**8,075.7**	**(57.3)**	**(57.3)**

1/ In addition to $1.6 million, the FY14 General Appropriation Act transferred all remaining balances in the Education Learning and Accountability Fund as of June 30, 2013, into the Automation Projects Fund for ADE's AELAS project.

Janice K. Brewer
Governor

Brian C. McNeil
Director

ARIZONA DEPARTMENT OF ADMINISTRATION

OFFICE OF THE DIRECTOR

100 NORTH FIFTEENTH AVENUE • SUITE 401
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RECEIVED
OCT 08 2013
JOINT BUDGET COMMITTEE

October 8, 2013

The Honorable John Kavanagh, Chairman
Joint Legislative Budget Committee
Arizona House of Representatives
1700 West Washington Street
Phoenix, Arizona 85007

The Honorable Don Shooter, Vice-Chairman
Joint Legislative Budget Committee
Arizona State Senate
1700 West Washington Street
Phoenix, Arizona 85007

Dear Representative Kavanagh and Senator Shooter:

In accordance with Arizona Revised Statutes § 41-714, the Arizona Department of Administration (ADOA) is submitting this request for review of fiscal year 2014 Automation Projects Fund (APF) projects. Monies to support the expenditure plan have already been appropriated to the Automation Projects Fund.

The attached document contains a detailed explanation of each proposed project. We will be happy to meet with your staff to provide further explanation as appropriate.

Sincerely,

Brian C. McNeil
Director

Attachment

cc: Richard Stavneak
Ben Henderson
Clark Partridge
Mike Smarik
John Arnold
Ken Matthews
Aaron Sandeen
Paul Shannon

Fiscal Year 2014 Automation Projects Fund (APF) Joint Legislative Budget Committee (JLBC) 2nd Review – October 29, 2013

Requesting Agencies:
Arizona Department of Administration (ADOA)
Arizona Department of Revenue (ADOR)
Arizona Department of Corrections (ADC)
Arizona Department of Environmental Quality (ADEQ)
Arizona Department of Education (ADE)

Prepared By: Arizona Department of Administration (ADOA) – Arizona Strategic Enterprise Technology (ASET)

Date Submitted: October 8, 2013

Executive Summary

"In 2013, we are framing the future and assembling a solid infrastructure for economic prosperity. When the transformation of State Government is complete, we will have created an enduring model of effective and responsible governance." – Janice K. Brewer, Governor - 'The Four Cornerstones of Reform: Building a Framework of Effective and Responsible Governance' - http://azgovernor.gov/dms/upload/GS_011413_FCRBuildingFramework.pdf.

Fiscal Year 2014 – Automation Projects

The following transformation initiatives were prioritized by the Governor in her plan, proposed in her budget and finalized by the legislature in Laws 2013, 1st Special Session, Chapter 1, Section 115:

Agency-Division	Project		FY 14 Amount	JLBC Review	PIJ / ITAC Approval
ADOA	ERP - AFIS Replacement	$	28,638,000	Complete	Approved
ADOA-ASET	State Data Center (SDC) Improvements & Maintenance	$	2,675,000	TBD	Pending
ADOA-ASET	Statewide Security Enhancements	$	3,075,000	August 20 - $900,000 Approved **October 29 - $1,075,000 Request**	Approved Approved
ADOA-ASET	Enterprise Architecture Enhancements	$	1,000,000	August 20 - $600,000 Approved **October 29 - $400,000 Request**	Not Required Not Required
ADOA-ASET	Statewide Automation & IT Project Management	$	2,450,000	August 20 - $1,700,000 Approved **October 29 - $450,000 Request**	Not Required Not Required
ADOA-ASET	E-government Agency Website Platform	$	325,000	August 20 - $325,000 Approved	Approved
ADOA-ASET	Web Portal Transition	$	1,975,000	**October 29 - $1,530,000 Request**	Approved
ADOR	Taxpayer Accounting System Refresh	$	1,700,000	**October 29 - $1,700,000 Request**	Approved
ADOR	Data Security and Encryption	$	4,900,000	**October 29 - $4,900,000 Request**	Approved
ADC	Adult Information Management System (AIMS) Upgrade	$	8,000,000	August 20 - $8,000,000 Approved	Approved
ADEQ	E-Licensing System	$	5,000,000	**October 29 - $5,000,000 Request**	Approved
ADE	Student Longitudinal Data System (SLDS) and Education Learning and Accountability System (ELAS)	$	7,000,000	August 20 - $3,350,000 Approved **October 29 - $3,650,000 Request**	Approved Approved
	Total	**$**	**66,738,000**		

Oversight and Transparency

ADOA-ASET currently has three oversight resources who work with all State agencies to develop Project Investment Justifications (PIJs). All IT projects over $25,000 have to go through the PIJ process and receive approval from the State Chief Information Officer (CIO). All IT Projects over $1,000,000 have to go through an additional checkpoint. These large projects require agencies to present and receive approval from the Information Technology Authorization Committee (ITAC), chaired by the State CIO.

Because of the size and complexity of the projects associated with the Automation Projects Fund (APF), JLBC and OSPB have made it possible for ADOA-ASET to expand oversight services in Fiscal Year 2014. In the ADOA-ASET 'Statewide Automation & IT Project Management' project, ADOA-ASET has been allocated $1,700,000 to accomplish the following objectives:

- Assist agencies in business case development, project planning, risk mitigation planning, oversight, reporting, communication and finance
- Develop templates, processes and tools

- Provide oversight training
- Monitor and coordinate financial reporting

With a Favorable Review of this project, ADOA-ASET is prepared to grow the oversight team and provide these services to all the agencies working on strategic initiatives funded in the APF. ADOA-ASET understands and assumes that continued funding for this team is dependent on the success of these services and the success of the Automation Projects.

Quarterly Reporting

When the Joint Legislative Budget Committee (JLBC) reviewed the Fiscal Year 2013 Automation Projects Fund (APF) projects in June 2012, a condition to provide a quarterly report on the last day of the month following the end of a quarter was applied to all projects funded through the Automation Projects Fund. Since then ADOA has partnered with JLBC and the Governor's Office of Strategic Planning and Budgeting (OSPB) to refine the report and its details.

The 2013 legislative session codified the reporting process as follows:

> Laws 2013, 1st Special Session, Chapter 1, Section 115, I. The department of administration shall **submit to the joint legislative budget committee quarterly reports on or before the last day of each calendar** quarter on the implementation of projects described in this section, including the projects' deliverables, timeline for completion and current status.

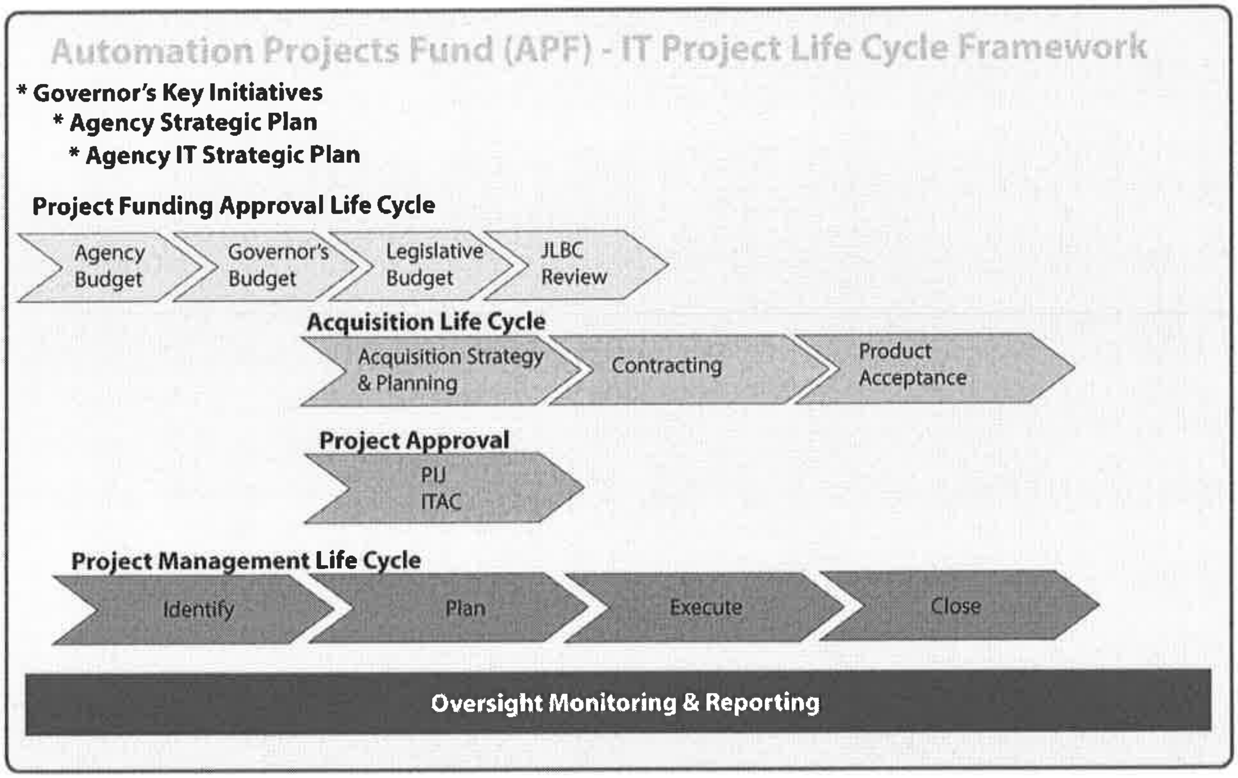
ADOA-ASET recognizes the change in the law and will prepare and submit quarterly reports on or before the last day of each quarter. JLBC has suggested that each quarterly report reflect the last month of the previous quarter and the first two months of the current quarter. For example;

- Fiscal Year 2014, Quarter 1 report would be due on or before September 30 and would contain data for July and August 2013.
- Fiscal Year 2014, Quarter 2 report would be due on or before December 31 and would contain data for September, October and November 2013.

ADOA-ASET finds this option reasonable and would like to formally make a request to have this included in the Favorable Review.

APF - IT Project Life Cycle

ADOA-ASET has defined the following Automation Projects Fund (APF) – IT Project Life Cycle Framework:



This framework provides guidance for the overall project life cycle: ensure project sponsorship; clearly define the business problem(s) to be solved; identify funding streams; develop and manage acquisition strategy; assure compliance with project approval process; execute the project and end-to-end monitoring and reporting.

State agencies are responsible for developing strategic plans and IT plans aligned with the Governor's key initiatives. Agencies are also responsible for developing their budgets (working with OSPB and the legislature), acquisition plans (in alignment with the State Procurement Office (SPO)), and Project Investment Justification Document (PIJ); presenting to the Information Technology Authorization Committee (ITAC), where necessary; and executing the projects and providing oversight reporting.

ADOA-ASET facilitates the PIJ and ITAC processes for project approval. ADOA-ASET also provides some standards and best practices around project management and is responsible for end-to-end oversight and reporting on IT projects.

IT projects funded by the APF must receive a Favorable Review from JLBC to proceed. ADOA-ASET works with all agencies that have projects funded through the APF to develop an initial report that can be used to review the projects approved in the budget. ADOA-ASET utilizes this initial report as the foundation for the APF quarterly report.

Request for Favorable Review

This Initial Review document describes the strategic IT programs for ADOR, ADC, ADEQ, ADE and ADOA for Fiscal Year 2014. Each program and their projects are at various stages of the IT Project Lifecycle. Each agency has identified projects to be reviewed on October 29, 2013, for a Favorable Review in order to move forward on the execution phase. All of the agencies understand the process and are committed to managing these projects successfully.

ADOA-ASET - State Data Center (SDC) Improvements & Maintenance - $2,675,000

ADOA-ASET's core mission is to ensure the continuity of mission-critical and essential systems of our customers. The State Data Center (SDC) currently hosts more than one hundred customers and processes multiple billions of dollars of transactions per year. In Fiscal Year 2013, ADOA-ASET completed many projects in the SDC including replacing multiple Power Distribution Units (PDUs), expanding a building to house an Automatic Transfer Switch (ATS) and to add an additional Uninterruptible Power Source (UPS), updated wiring and many other projects. ADOA-ASET is in the final stages of replacing the 17+ year old UPS with two new UPS units.

In Fiscal Year 2014 (FY14), ADOA-ASET will finalize the UPS installations, implement a monitoring and notification system and begin to address disaster recovery solutions for the open systems line of services. ADOA-ASET has developed a comprehensive plan to address critical disaster recovery needs and move applicable services to cloud offerings.

SDC Projects

Project Name	FY14 Description	Project Budget
State Data Center (SDC) Disaster Recovery Site Storage Solution	- Implement shared area network (SAN) director - Implement disaster recovery (DR) tape library - Implement virtual storage platform - Implement synchronization software & hardware	$ 800,000
SDC Disaster Recovery Shared Services Platform	- Implement failover blade server infrastructure - Implement in-rack PDUs - Implement failover and virtual machine software	$ 1,700,000
SDC Facilities Enhancement	- Enhance network cabling and connectivity management in SDC	$ 175,000
Total SDC		**$ 2,675,000**

SDC Projects – Favorable Review Requests – October 29

There are no Favorable Review requests for SDC projects pending at this time.

ADOA-ASET - Statewide Security Enhancements - $3,075,000

Over the past two years several states including Utah, South Carolina and Alabama have incurred serious data breaches. The complexity and ferocity of the attacks continue to increase. Basic security "hygiene," day-to-day operational basics, can address a significant portion of risks but not all. The ADOA-ASET Security Privacy and Risk (SPR) team has developed a comprehensive Security Strategy that will systematically address potential gaps.

Security Projects

Project Name	FY14 Description	Project Budget
Secure Data Protection Pilots	- Implement solution to discover, track and protect sensitive data - Implement end user solution with supporting hardware and software capabilities - Expand email data loss prevention (DLP), encryption, and spam filter - Encrypt critical end user laptops - Encrypt critical databases - Implement two-factor authentication system *Reoccurring maintenance needs to be factored in	$ 350,000

Project Name	FY14 Description	Project Budget
Data Center Network Managing/Monitoring	- Identify mission critical, at-risk web applications that use personally identifiable information (PII), personal health information (PHI) or sensitive data for service delivery - Implement perimeter firewalls - Identify at-risk agencies and implement perimeter firewall protection - Implement web application filtering to aid in the prevention of SQL injection attacks	$ 500,000
Security Assessment	- Complete penetration testing of the State's most critical applications - Address vulnerabilities and security problems identified - Address critical issues identified in Penetration Testing *Agency resources required to address vulnerabilities - funds for testing only	$ 450,000
Central Security Management	- Form multi-agency working group to assess cloud encryption offerings - Conduct Proof of Concept (POC) - Implement solution determined by POC - Implement web content filtering to remove malicious and unwanted sites - Implement server encryption solution	$ 650,000
Incident Response	- Implement solution to protect SDC customers from external distributed denial-of-service (DDoS) attacks	$ 150,000
Security Awareness	- Provide multi-agency security training classes - Continue in-person presentations to key staff - Conduct multi-agency security exercise(s)	$ 250,000
Data Center Security Management	- Purchase additional licensing to provide alert capabilities when unexpected server configuration changes are made - Implement intrusion detection to identify malicious activities or policy violations for the SDC - Add network time appliance to SDC - Increase patch management compliance licensing	$ 725,000
Total SPR		**$ 3,075,000**

Security Projects – Favorable Review Requests – August 20

Project Name	FY14 Description	Total Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Security Assessment	- Complete penetration testing of the State's most critical applications - Address vulnerabilities and security problems identified - Address critical issues identified in Penetration Testing *Agency resources required to address vulnerabilities - funds for testing only	$ 450,000	$ 450,000	PIJ Approved	Approved
Incident Response	- Implement solution to protect SDC customers from external distributed denial-of-service (DDoS) attacks	$ 150,000	$ 150,000	FY13 Existing PIJ - Amendment Approved	Approved
Security Awareness	- Provide multi-agency security training classes - Continue in-person presentations to key staff - Conduct multi-agency security exercise(s)	$ 250,000	$ 250,000	PIJ Not Required	Approved
Total SPR			**$ 900,000**		

Security Project – Favorable Review Request – October 29

Project Name	FY14 Description	Total Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Secure Data Protection Pilots	- Implement solution to discover, track and protect sensitive data - Implement end user solution with supporting hardware and software capabilities - Expand email data loss prevention (DLP), encryption, and spam filter - Encrypt critical end user laptops - Encrypt critical databases - Implement two-factor authentication system *Reoccurring maintenance needs to be factored in	$ 350,000	$ 350,000	PIJ Approved	Pending
Data Center Security Management	- Purchase additional licensing to provide alert capabilities when unexpected server configuration changes are made - Implement intrusion detection to identify malicious activities or policy violations for the SDC - Add network time appliance to SDC - Increase patch management compliance licensing	$ 725,000	$ 725,000	PIJ Approved	Pending
Total SPR			**$ 1,075,000**		

ADOA-ASET - Enterprise Architecture Enhancements - $1,000,000

Enterprise Architecture (EA) is a disciplined approach to long-term Business Information Technology planning. ADOA-ASET's EA objective is to:

> Increase enterprise agility through leadership, strategic alignment, unified processes, strong data governance and actionable policies, standards and procedures.

To accomplish this objective, ADOA-ASET plans to continue to provide statewide training opportunities; provide updated policies, standards and procedures as well as proactively assessing strategic technologies and key services that will enhance the value of business services.

EA Projects

Project Name	FY14 Description	Project Budget
Business and Technical EA Training	- Provide statewide Business Analytics, Service and Change Management Training, and Strategic Planning training	$ 100,000
Policy, Standard and Procedure (PSP) Compliance	- Establish statewide PSP working groups - Create and implement tiered approach for updating and reviewing all agency PSPs - Assist agencies in issue mitigation	$ 500,000
Strategic Technology Assessment	- Complete assessment of ADOA-ASET services including assets (hardware and software) and resources - Complete cost analysis of each service and establish new pricing models - Implement IT Financial Management Reporting and Dashboards	$ 400,000
Total EAA		**$ 1,000,000**

EA Projects – Favorable Review Requests – August 20

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Business and Technical EA Training	- Provide statewide Business Analytics, Service and Change Management Training, and Strategic Planning training	$ 100,000	$ 100,000	PIJ Not Required	Approved
Policy, Standard and Procedure (PSP) Compliance	- Establish statewide PSP working groups - Create and implement tiered approach for updating and reviewing all agency PSPs - Assist agencies in issue mitigation	$ 500,000	$ 500,000	PIJ Not Required	Approved
Total EAA			**$ 600,000**		

EA Projects – Favorable Review Request – October 29

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Strategic Technology Assessment	- Complete assessment of ADOA-ASET services including assets (hardware and software) and resources - Complete cost analysis of each service and establish new pricing models - Implement IT Financial Management Reporting and Dashboards	$ 400,000	$ 400,000	PIJ Not Required	Pending
Total EAA			**$ 400,000**		

ADOA-ASET - Statewide Automation & IT Project Management - $2,450,000

Strong project management is the foundation to successful projects. It is critical to have the right project management lifecycle methodology and to empower people with the right resources. ADOA-ASET is dedicated to developing a statewide center of excellence for project management and to increase the oversight capabilities for strategic Automation Projects.

Project Management Projects

Project Name	FY14 Description	Project Budget
Oversight Office Transformation	- Document, streamline and automate statewide IT oversight processes	$ 300,000
Transformation Initiatives Project Managers	- Project management resources to execute ADOA-ASET transformation initiatives	$ 450,000
Automation Projects Fund Strategic Execution Team	- Assist agencies in business case development, project planning, risk mitigation planning, oversight, reporting, communication and financial management - Develop templates, processes and tools *Ongoing for the life of Automation Projects Fund	$ 1,700,000
Total PMO		**$ 2,450,000**

Project Management Projects – Favorable Review Request – August 20

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Automation Projects Fund Strategic Execution Team	- Assist agencies in business case development, project planning, risk mitigation planning, oversight, reporting, communication and financial management - Develop templates, processes and tools *Ongoing for the life of Automation Projects Fund	$ 1,700,000	$ 1,700,000	PIJ Not Required	Approved
Total PMO			**$1,700,000**		

Project Management Projects – Favorable Review Request – October 29

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Transformation Initiatives Project Managers	- Project management resources to execute ADOA-ASET transformation initiatives	$ 450,000	$ 450,000	PIJ Not Required	Pending
Total PMO			**$ 450,000**		

ADOA-ASET - E-government Agency Website Platform - $325,000

E-government is at the heart of the Governor's vision to modernize and transform State Government. In the "The Four Cornerstones of Reform," the Governor defined initiatives to improve licensing timeframes at State agencies. ADOA-ASET currently supports 95 State entities and more than 100 websites. In 2012, the Arizona E-government platform delivered more than 430,000 financial transactions brining in nearly $70 million in revenue to the State.

ADOA-ASET is in the process of developing a statewide platform to host and manage agency websites. This new platform will provide standard templates and color options for agencies to choose from. ADOA-ASET will provide training and resources to help agencies create and maintain content on their own websites.

E-government Projects

Project Name	FY14 Description	Project Budget
Agency Website Transformation and CMS Solution Implementation	- Convert websites to new agency web platform - Consolidate website infrastructure	$ 325,000
Total EGV		**$ 325,000**

E-government Projects – Favorable Review Request – August 20

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Agency Website Transformation and CMS Solution Implementation	- Convert websites to new agency web platform - Consolidate website infrastructure	$ 325,000	$ 325,000	PIJ Approved	Approved
Total EGV			**$ 325,000**		

ADOA-ASET - Web Portal Transition - $1,975,000

In June of 2013, ADOA-ASET awarded a new E-government contract to Business & Decisions, Eagle Creek Software Services, IBM and Unisys. This also means that the State must transition away from the incumbent vendor platform. The State is currently dependent on many components of the incumbent vendor and we must replace core capabilities, such as payment processing, as well as ensure that applications will continue to focus with the new capabilities.

Web Portal Transition Projects

Project Name	FY14 Description	Project Budget
Web Portal Transition	- Transition from current vendor to new E-government model - Transition payment processing engine, legacy applications, infrastructure and support	$ 1,975,000
Total WEB		**$ 1,975,000**

Web Portal Transition Projects – Favorable Review Requests – August 20

There are no Favorable Review requests for Web Portal Transition projects pending at this time.

Web Portal Transition Projects – Favorable Review Request – October 29

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Web Portal Transition	-Transition from current vendor to new e-gov model -Transition payment processing engine, legacy applications, infrastructure and support - Internal operational costs supporting the transition	$1,975,000	$1,530,000	PIJ Approved	Pending
Total WEB			**$1,530,000**		

STATE OF ARIZONA

Joint Legislative Budget Committee

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DATE: October 22, 2013

TO: Representative John Kavanagh, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director RS

FROM: Eric Billings, Principal Fiscal Analyst EB

SUBJECT: ADOA/DOR - Review of DOR Information Technology Projects (Automation Projects Fund)

Request

Pursuant to A.R.S. § 41-714, the Arizona Department of Administration (ADOA) has requested that the Committee review $6.6 million in proposed FY 2014 expenditures from the Automation Projects Fund for Information Technology projects at the Arizona Department of Revenue (DOR).

Recommendation

The Committee has at least the following 2 options:

1. A favorable review.

2. An unfavorable review.

The project has received approval from Arizona Strategic Enterprise Technology (ASET) staff through the Project Investment Justification process. ASET's approval included the following condition:

A. DOR and ADOA-ASET Information Security group agree to work together towards a common goal of updating the Department of Revenue security profile. The ADOA-ASET Information Security group will provide resources to DOR to support their efforts during this project.

As of this writing, Information Technology Authorization Committee (ITAC) approval was pending based on a review that will occur on October 23, 2013. Beyond the ADOA ASET review, there has been no other independent third party review of this project.

(Continued)

The JLBC Staff recommends that the JLBC consider adopting the ITAC/ASET provision as part of its review and that ADOA-ASET report back to JLBC staff regarding their findings relating to the DOR security profile by March 31, 2013.

Analysis

Current Request

ADOA is requesting a favorable review of $6.6 million in proposed FY 2014 expenditures from the Automation Projects Fund, which consists of 2 different projects, as follows:

- Business Reengineering Integrated Tax System (BRITS) $1.7 million
- Data Security and Encryption $4.9 million

BRITS

ADOA's proposal includes $1.7 million in FY 2014 for the second year of a 2-year, $5.1 million project to upgrade DOR's BRITS. BRITS is the state's computer system for collecting and processing tax data and is also utilized for the online submission of tax returns and audit selection. DOR implemented BRITS 10 years ago at a cost of $162.1 million. While relatively new, the system has experienced several issues including overly complex coding that makes implementing changes difficult, the impending expiration of vendor support, and components of the system operating at capacity.

In June 2012, this Committee favorably reviewed $3.4 million for the first year of the 2-year project. To date, DOR has spent $2.8 million of this amount. The current request for $1.7 million in FY 2014 expenditures would consist of 4 components, as follows:

- Taxpayer Accounting System (TAS) Refresh $760,000
- AZTaxes Refresh $571,000
- Disaster Recovery $294,000
- Application Integration Replacement $75,000

The Taxpayer Accounting System (TAS) is the main accounting system in BRITS, and supports data for individual, withholding, corporate and transaction privilege tax collection. DOR is seeking to update the mid-1990's software used by the original vendor. In FY 2013, DOR spent $1.5 million on this project, and plans to spend an additional $760,000 in FY 2014.

AZTaxes is the web-based system that handles the electronic filing of tax returns and all of DOR's bank deposits. DOR reports that electronic filing has increased from 1 million filers in TY 2005 to nearly 1.9 million filers in TY 2011, exceeding the capacity and capability of the current hardware and software. In FY 2013, DOR spent $414,600 on this project, and plans to spend an additional $571,000 in FY 2014.

The Disaster Recovery component is related to relocating the BRITS system to the State Data Center. Previously, BRITS was housed in a data center owned and operated by a private third party. In FY 2013, BRITS relocated to the State Data Centers in Phoenix and Tucson, for a total cost of $557,000, mostly related to purchasing new hardware. In FY 2014, DOR plans to complete the relocation process by providing disaster recovery solutions that were previously provided by the private third party operator. This is estimated to cost a total of $294,000 in FY 2014.

Application Integration Replacement would replace key system software components that are targeted to lose vendor support in the next 15 months. Instead of modifying the custom built software and security systems, DOR plans to purchase commercial off the shelf software. Although the project was budgeted to cost $466,000 in FY 2013, DOR found substantial savings in hardware purchases and only spent $267,200. In FY 2014, DOR estimates that they will spend an additional $75,000 for this project.

(Continued)

The $1.7 million proposal is financed through a General Fund transfer into the Automation Projects Fund that occurred in the FY 2014 General Appropriation Act (Laws 2013, 1st Special Session, Chapter 1). BRITS upgrades received approval from ASET through the Project Investment Justification process, in addition to ITAC approval in November 2011.

Encryption

Encryption is a security technique that uses mathematical algorithms to render data and information unreadable to any unauthorized parties who do not hold the corresponding key to decrypt such information. Both state and federal standards require the encryption of personally identifiable information at DOR. Currently, data within DOR is only encrypted if it is accessed from the same hard drive on which it is loaded. Data that is accessed from other servers is not encrypted.

The Arizona Statewide Information Security and Privacy Office (SISPO), under the direction of ASET, created a state standard to encrypt certain private and confidential information. In addition, the Internal Revenue Service (IRS) often transmits federal taxpayer information to DOR to enforce collections from delinquent Arizona taxpayers. The IRS requires that all federal taxpayer information transmitted to DOR meet specific encryption requirements. The total enforcement revenue benefit of federal taxpayer information to Arizona in FY 2013 was $21.7 million for individual and $7.5 million in corporation collections.

In order to comply with these state and federal security standards, DOR is requesting a review of $4.9 million in FY 2014 expenditures from the Automation Projects Fund. This project would consist of $4.5 million in one-time development costs, and estimated ongoing operational costs of $410,500.

The $4.5 million in one-time development costs would consist of 3 components, as follows:

- Hardware $3.6 million
- Software $518,000
- Professional and Outside Services $428,500

The $410,500 in ongoing costs would consist of 2 components, as follows:

- Software Maintenance $392,500
- Hardware Maintenance $18,000

ASET approved the Encryption proposal on the condition that DOR work with ADOA to update the DOR security profile. The proposal is scheduled to receive ITAC review on October 23.

RS/EB:ts

ADOR - Taxpayer Accounting System Refresh - $1,700,000

To assure the continued business operations of ADOR and to remain a modern and efficient state taxing agency, a technology refresh of the core Taxpayer Accounting System and AZTaxes (electronic filing system) environments was required. This is a continuation of the project from Fiscal Year 2013. On a more reliable and capable foundation, many of our applications challenges can be addressed and operational risk in excess of $12B annually will be mitigated.

This suite of upgrades is comprised of the four following initiatives which mitigate the associated risks:

- Taxpayer Accounting System Application Upgrade (TAS) supporting Individual, Withholding, Corporate and Transaction Privilege Taxes
- AZTaxes Application Upgrade - a web-based system handling electronic filing for multiple tax types
  - These investments replace 10 year old hardware for TAS and AZ Taxes servers thereby mitigating operational risk.
- Disaster Recovery for AZTaxes and TAS at ADOA Tucson
  - ADOR's primary data center, housed at InfoCrossing, is approaching the end of its five-year agreement. Beginning in FY12, ADOR is relocating to the ADOA data centers in Phoenix and Tucson, consistent with State IT Strategy and assuring future cost management. The services of system management and disaster recovery provided by InfoCrossing must be replaced with new capabilities and capacity.
- Application Integration Replacement
  - Key system software components are targeted to lose vendor support within 15 months. The loss of vendor support means termination of software patches, security patches and fixes that are key to sustaining operations and the protection of taxpayer Restricted Personally Identifiable Information (RPII). Therefore, we will replace the custom-built application integration system used to flow transactions and files between systems with a commercially available off the shelf solution.

Taxpayer Accounting System Refresh Projects

Project Name	FY14 Description	Project Budget
Taxpayer Accounting System Refresh	- TAS was one application delivered in the BRITS project. TAS supports Individual, TPT, Withholding, Corporate and Fiduciary & Trust taxes. Upgrade key Oracle software components to current and supported versions.	$ 760,000
AZTaxes Refresh	- AZTaxes was one application delivered in the BRITS project. Upgrade tax application providing taxpayer access and information. Includes: online payment processing, electronic filing, return status, Individual, Transaction Privilege Tax, Licensing, Withholding and Unemployment Insurance. Upgrade application software components to current and supported versions. Improve ability to implement legislated functionality.	$ 571,000
Disaster Recovery	- ADOR 5-year external data center contract expiring in FY13. ADOR BRITS system were moved to State Data Centers (Phoenix and Tucson) completed in FY13. ADOR must provide system management and disaster recovery capabilities previously provided by InfoCrossing. Project is consistent with State Data Center Consolidation Strategy.	$ 75,000
Application Integration Replacement	- Replace customized application integration software deployed for application-to-application transactions for BRITS systems. This project replaces custom code with current release, standard, commercially available software. (Microsoft BizTalk 2013)	$ 75,000
Total ADOR Tax System		**$ 1,700,000**

Taxpayer Accounting System Refresh Projects – Favorable Review Requests – October 29

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Taxpayer Accounting System Refresh	- TAS was one application delivered in the BRITS project. TAS supports Individual, TPT, Withholding, Corporate and Fiduciary & Trust taxes. Upgrade key Oracle software components to current and supported versions.	$ 760,000	$ 760,000	ITAC Approved	Pending
AZTaxes Refresh	- AZTaxes was one application delivered in the BRITS project. Upgrade tax application providing taxpayer access and information. Includes: online payment processing, electronic filing, return status, Individual, Transaction Privilege Tax, Licensing, Withholding and Unemployment Insurance. Upgrade application software components to current and supported versions. Improve ability to implement legislated functionality.	$ 571,000	$ 571,000	ITAC Approved	Pending
Disaster Recovery	- ADOR 5-year external data center contract expiring in FY13. ADOR BRITS system were moved to State Data Centers (Phoenix and Tucson) completed in FY13. ADOR must provide system management and disaster recovery capabilities previously provided by InfoCrossing. Project is consistent with State Data Center Consolidation Strategy.	$ 294,000	$ 294,000	ITAC Approved	Pending
Application Integration Replacement	- Replace customized application integration software deployed for application-to-application transactions for BRITS systems. This project replaces custom code with current release, standard, commercially available software. (Microsoft BizTalk 2013)	$ 75,000	$ 75,000	ITAC Approved	Pending
Total ADE			**$1,700,000**		

ADOR - Data Security and Encryption - $4,900,000

Safeguarding systems and protecting data is never a completed task. Proactive and continual update and replacement of security tools is required in order to ensure data is safeguarded and the network remains resilient and available to support agency-critical applications and a workforce that depends on availability of services and information.

Over the past two years, several states including Utah, South Carolina and Alabama have incurred serious data breaches. The complexity and ferocity of the attacks continue to increase. Basic security "hygiene," day-to-day operational basics, can address a significant portion of risks but not all. The ADOR Security team has developed a comprehensive Security Strategy that improves information protection mechanisms.

Data Security and Encryption Projects

Project Name	FY14 Description	Project Budget
Data Security and Encryption	- Implement Data Encryption Solutions for disk, databases, folders, backups and archive media retention. - Upgrade intrusion detection and intrusion prevention technologies at data center locations.	$ 4,900,000
Total ADOR Security		**$ 4,900,000**

Data Security and Encryption Projects – Favorable Review Request – October 29

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Data Security and Encryption	- Implement Data Encryption Solutions for disk, databases, folders, backups and archive media retention. - Upgrade intrusion detection and intrusion prevention technologies at data center locations.	$4,900,000	$4,900,000	Approved	Pending
Total ADOR Tax System			**$4,900,000**		

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DATE: October 22, 2013

TO: Representative John Kavanagh, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director RS

FROM: Micaela Larkin, Fiscal Analyst ML

SUBJECT: ADOA/DEQ - Review of Department of Environmental Quality Phase 1 (Automation Projects Fund)

Request

Pursuant to A.R.S. § 41-714, the Arizona Department of Administration (ADOA) has requested that the Committee review $5.0 million in proposed FY 2014 expenditures from the Automation Projects Fund for Phase 1 of the development of a web portal for the Department of Environmental Quality (DEQ).

Recommendation

The Committee has at least the following 2 options:

1. A favorable review.

2. An unfavorable review.

The project has received approval from Arizona Strategic Enterprise Technology (ASET) staff through the Project Investment Justification process. ASET's approval included the following condition:

A. DEQ will demonstrate progress to ADOA-ASET within 6 months of the project start date for this project. At that point in time, DEQ and DOA-ASET will determine if the initial strategy is producing the desired and timely results or the initial strategy needs adjustment.

As of this writing, Information Technology Advisory Committee (ITAC) approval was pending based on a review that will occur on October 23, 2013. The JLBC Staff recommends that the JLBC consider adopting the ITAC/ASET provisions as part of its review.

In addition, the JLBC Staff recommends that the Committee consider adopting an additional provision:

(Continued)

B. Additional funding beyond FY 2014 is contingent upon an independent third party review addressing the feasibility of the entire project's design and estimated costs. ADOA and DEQ would collaborate to determine the most appropriate mechanism to conduct the third party review. ADOA shall notify JLBC Staff by November 29, 2013 as to their recommended process for the review. Any third party review findings shall be provided to the JLBC by February 28, 2014.

Analysis

Background
DEQ processes 28,000 transactions annually. They use paper to process permits, reports, and receive fees from 16,000 facilities. DEQ is developing a web portal that will automate most of the permitting and compliance processes, and will allow customers to conduct permitting, billing, payment, and data submissions online. DEQ plans to develop the portal in stages. Phase 1 of this project, known as "myDEQ", supports the addition of the 27 business processes listed in *Table 1*. The proposed spending for FY 2014 builds upon an earlier expenditure of $654,800 from the State Assurance Fund in August 2013 to implement the project infrastructure and develop the first business process action. For FY 2015, DEQ is requesting $6.8 million to add 80 additional business processes to the web portal. After the completion of the proposed FY 2015 work, DEQ would have 95% of the business processes automated.

Procurement
DEQ determined the staffing needs and development timeframe for Phase 1 based on a pilot project that they undertook in August. DEQ plans to develop the Phase 1 transactions with 4 vendor staffed teams. There was no third party review of the design and costs for Phase 1.

Current Proposal
ADOA is requesting a favorable review of $5.0 million in expenditures for the implementation of the 27 business processes listed in *Table 1*. This amount is based upon the hardware, software, and staffing costs. The costs per hour estimates for the staffing are based on standard state contracted rates for the work. The DEQ team determined the hours of work needed for each business process by examining the experiences and time expended during the initial pilot program. The expenditures consist of 3 components:

• Professional & Outside Services	$4,586,592
• Equipment	$ 321,037
• Software	$ 92,371

Project Financing
The FY 2014 General Appropriation Act (Laws 2013, 1st Special Session, Chapter 1) transferred a total of $5.0 million from the Vehicle Emissions Inspection Fund into the Automation Projects Fund to finance this project.

DEQ plans to cover the operational costs of $82,682 per year for licensing and maintenance fees starting in FY 2015 from the Indirect Cost Recovery Fund.

Third Party Review
The JLBC Staff proposes that ADOA and DEQ collaborate to determine an appropriate mechanism to conduct a third party review of the entire project. Additional funding beyond FY 2014 would be contingent upon an independent third party review addressing the feasibility of the project's design and estimated costs.

Recent large scale projects by agencies such as the Arizona Financial Information System (AFIS) project of the Department of Administration, the Arizona Inmate Management System (AIMS) of the Department

(Continued)

of Corrections, and the Student Information Systems (SIS) project of the Department of Education have had third party reviews. The proposed provision calls for results to be available by the end of February, which will allow the information to be used in the FY 2015 budget request process and provide evaluative measurements to DEQ and ADOA.

Table 1

myDEQ Phase 1 Transactions
(Implemented by June 30, 2014)

1. Customer and Place Registration
2. User Registration and CROMERR Compliance
3. Web Portal Main Dashboard (Landing Page)
4. Invoicing and Payments
5. General Permit - Crushing and Screening
6. Compliance Certification - Crushing and Screening
7. General Permit - Aquifer Protection Type
8. Hazardous Waste Annual Report
9. UST Notification
10. Hazardous Waste EPA ID
11. Minor Permit Amendments
12. Hot Mix Asphalt
13. Waste / Used Tires
14. Annual Emissions Inventory
15. Asbestos NESHAP Notification Form
16. ST Suspected Release Report
17. Display of Basic Water Quality Data for Water Systems (Safe Drinking Water Information System (SDWIS) Data
18. Operator Certification
19. SSO Notification
20. 24-Hour, 5-day, and 30-day Exceedences Notification
21. Concrete Batch Plant
22. Soil Vapor Extractor
23. Septage Hauler
24. Industrial Discharge Permits (Pre-treatment)
25. Type 3 (APP and Reuse)
26. Used Oil Marketing Report
27. UST Contractor Certification

RS/ML:ts

E-Licensing System Projects – Favorable Review Requests – October 29

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
DEQ E-Licensing Program	- Implement DEQ online website framework for e-licensing - Streamline and automate seven core business processes	$5,000,000	$5,000,000	PIJ Approved	Pending
Total DEQ			**$5,000,000**		

ADEQ - E-Licensing System - $5,000,000

The Department of Environmental Quality (DEQ) is streamlining and automating services to increase environmental protection and end-user convenience. "Paper transactions and payments between businesses and ADEQ are inefficient, wasteful and burdensome. The Arizona Chamber wholeheartedly supports developing on-line systems that will reduce the transactional costs and ease the regulatory burden on private industry." – Glenn Hamer, Arizona Chamber of Commerce

E-Licensing System Projects

Project Name	FY14 Description	Project Budget
DEQ E-Licensing Program Management / Planning	- Identify Program Management Resources to initiate and facilitate implementation end-to-end - Develop business and technical requirements and roadmap - Develop and maintain risk mitigation plan - Oversee and maintain System Architecture - Provide Technical training to ADEQ's staff	$ 500,000
Online Customer Interfaces	- Design and develop user interface for secure and public access - Identify Profile Management requirements and implement capabilities - Ensure responsive (Mobile) Capabilities	$ 500,000
License, Permit and Reporting Automation	- Prioritize licenses, permits and reports (transactions) to be automated in FY14 - Document and Improve processes (LEAN) - Design and implement technical framework for process automation (forms, templates, wizard capabilities) - Develop, test and deploy online processes	$ 1,800,000
System and Data Integration	-Define system and data integration requirements -DEQ data systems integration -Digital signature integration -Document management Integration and services - Core Arizona Enterprise Services Platform (AESP) capabilities integration (Single sign-on, Payment processing)	$ 900,000
AESP Capabilities Development	- Accelerate core capabilities aligned to DEQ success - Identity management - Messaging platform and protocols - Business rules engine	$ 1,000,000
Reporting and Analytics	- Define organizational performance metrics and reporting - Extend data warehouse capabilities to integrate with the web portal - Implement reports and interfaces	$ 300,000
Total DEQ		**$ 5,000,000**

STATE OF ARIZONA

Joint Legislative Budget Committee

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DATE: October 22, 2013

TO: Representative John Kavanagh, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director RS

FROM: Ben Henderson, Fiscal Analyst BH

SUBJECT: ADOA/ADE - Review of Arizona Education Learning and Accountability System (Automation Projects Fund)

Request

Pursuant to A.R.S § 41-714, the Arizona Department of Administration (ADOA) has requested that the Committee review $3.7 million in proposed FY 2014 expenditures from the Automation Projects Fund for 3 projects related to the development of the Arizona Education Learning and Accountability System (AELAS) at the Arizona Department of Education (ADE).

Recommendation

The Committee has at least the following 2 options:

1. A favorable review.
2. An unfavorable review.

The Arizona Education Data-driven Decision System (AzED^{3}S) received approval from the Information Technology Authorization Committee (ITAC) at its August 2013 meeting. ITAC's approval included the following conditions: (the other 2 projects did not require ITAC approval)

A. ADE must establish a mechanism to ensure that a Project investment Justification (PIJ) is submitted for review, and approved by the Arizona Strategic Enterprise Technology (ASET) office within ADOA, and ITAC as required, prior to any and all expenditures in the amount of $25,000 or more, on IT or telecommunications-related hardware, software, or services, in accordance with A.R.S. 41-3504 and A.R.S. 41-3521.
B. Given the significant investment that has already been made in the technology approach, ADE may continue to build upon the web-based reporting framework and dashboards that have been piloted with 11 Local Education Agencies (LEAs). Prior to deployment beyond the pilot group, further collaboration and approval by ASET will be required to ensure that the web-based initiative will comply with proposed statewide standards.

(Continued)

C. As part of the overall acceptance testing, ADE shall conduct a vulnerability assessment to verify that the proposed web-based components have been configured securely, in compliance with statewide security policies and standards, and in accordance with industry best practices. Based on the results of that assessment, ADE may be required to address identified security and/or privacy flaws prior to statewide deployment, and/or to establish a verifiable remediation plan for less serious issues noted during the security testing/evaluation process.

D. Given the assigned Project Manager is not State of Arizona certified, ADOA will provide additional project oversight to ensure that ASET-specific requirements for ITAC approved projects are met.

ASET approved the Student Information System (SIS) Opt In project with the following conditions:

E. ADE may proceed to issue a Request for Proposal (RFP) for a vendor-hosted commercial off-the-shelf (COTS) Student Information System (SIS). However, ADE may not award a contract or expend funds until a full PIJ is submitted reflecting the results of the solicitation, including any change in proposed costs, technology approach, scope of work, or implementation schedule, and ASET has reviewed and approved the full and final PIJ.

F. An operational funding source must be identified, and review and approval of the full PIJ by ITAC, in Executive Session if applicable, may be required prior to award.

ASET approved the Security Access project with the following condition:

G. ADE may proceed with the design, development and implementation of the proposed solution, however should there be significant differences in the scope of work, costs, implementation schedule, or proposed technology, ADE must amend the PIJ to reflect the changes and submit it to ASET for review and approval prior to further expenditure of funds.

The JLBC Staff recommends that the JLBC consider adopting the ITAC/ASET provisions as part of its review. In addition, JLBC Staff recommends the following provision:

H. ADOA update the status of its recommended ITAC/ASET provisions as parts of its quarterly Automated Project Fund Report.

Analysis

Background

At its August meeting, JLBC reviewed \$3.4 million in FY 2014 expenditures for 3 separate projects related to the Arizona Education and Learning Accountability System (AELAS). See Attachment A for background on this project.

Current Request

ADOA is currently requesting a review of \$3.7 million in FY 2014 expenditures from the Automation Projects Fund, consisting of 3 projects, as follows:

• SLDS – AZ Education Data-driven Decision System (AzED^{3}S)	\$2.8 million
• AELAS – Student Information System (SIS) Opt In	\$450,000
• AELAS – Security Access	\$450,000

SLDS – AZ Education Data-driven Decision System (AzED^{3}S)

The Student Longitudinal Data System (SLDS), also called the Arizona Education Data-driven Decision System (AzED^{3}S), would provide the technology infrastructure that provides education stakeholders with easy access to historical data regarding student and LEA performance. The system would then present this data graphically in dashboards and visualizations to analyze the performance of LEAs and students alike. For example, this may include charts displaying a single student's performance over time and in comparison to their peers, in addition to graphic displays comparing schools and districts' performances over time and in comparison to one another.

(Continued)

The project PIJ indicates that this would cost a total of $6.7 million in FY 2014 and FY 2015, of which $2.8 million in FY 2014 would be funded through the Automation Projects Fund. The remaining $3.9 million will be funded through federal grants, including $1.8 million in FY 2014 and $2.1 million in FY 2015.

The $2.8 million of state funding in FY 2014 would be spent on four components, as follows:

1. Implementing dashboards statewide $1.3 million
In 2012, ADE received a 3-year $5.0 million federal grant to expand its database systems, and provide education stakeholders with longitudinal (historical) data visualizations, graphic displays, and dashboards to support decision-making.

In the 1st year of that grant, ADE developed a web-based reporting system to accomplish these goals, and implemented the system to 11 pilot LEAs. ADOA is currently requesting review of $1.3 million in state funding to expand the use of these dashboards to 200 LEAs for FY 2014, as well as develop and implement training and professional development for teachers and administrators to access and use this data. The additional federal funds will expand the capabilities of these dashboards based on feedback from the 11 pilot LEAs.

2. Data Governance $650,000
Currently there are 280 different data requirements that LEAs must submit to ADE, many of which are redundant. For example, a school must report information on school finance, free and reduced lunch programs, and student achievement in separate reports to ADE, many of which contain duplicate pieces of information, like the student's name and teacher. Currently, no centralized data management policy is in place and data is maintained in multiple locations with little consistency. ADOA is currently requesting review of $650,000 in FY 2014 for data governance, including the implementation of improved processes to ensure clean, consistent data.

3. Identity Management and Security (IMS) $600,000
Currently when accessing historical data under ADE's system (ADE Connect), it is difficult to authenticate who is accessing the data, and whether they are accessing the appropriate data. ADOA is currently requesting review of $600,000 to implement an Identity Management and Security (IMS) system to support the secured access to AzED^{3}S.

4. Hardware $250,000
In addition to these 3 components, ADOA is requesting review of $250,000 to acquire the appropriate hardware to implement this project.

This project received ITAC approval on August 28, 2013, with conditions. The JLBC Staff recommends that the JLBC consider adopting the ITAC and ASET provisions as part of its review.

AELAS - SIS Opt In
LEAs are currently required to maintain their own Student Information Systems (SIS), which track student data. Currently, more than 600 LEAs purchase commercial off-the-shelf (COTS) systems from approximately 15 vendors statewide to operate and maintain these systems. These vendors often charge per student, however, most vendors have a minimum cost. This minimum cost essentially requires many smaller districts to pay a greater amount per student than larger districts. LEAs are then required to upload their student information data to ADE.

ADOA is currently requesting review of $450,000 to issue a request for proposal (RFP) for a vendor-hosted off-the-shelf student information system for use by numerous LEAs across the state. ADE has reported that utilizing economies of scale in this way would result in lower costs for many LEAs and would unify reporting standards to reduce redundancies when data is uploaded to ADE.

(Continued)

The total 5-year cost of the project is estimated to be $21.5 million. The current request would fund estimated licensing costs, hardware, and 3,300 hours of professional and outside services to conduct a pilot of the selected system for 6 LEAs. Over 5 years, $15.3 million would be funded through LEAs opting into the new system and paying a charge to utilize this system. ADE has estimated that LEA costs will be less than what they currently pay. A funding source for the remaining 5-year operational costs of $5.7 million has not yet been determined. ADE has requested additional funds for development of AELAS in their FY 2015 budget request, in part to provide ongoing funding for this specific project.

This project has received ASET approval with conditions. The JLBC Staff recommends that the JLBC consider adopting the ASET provisions as part of its review.

AELAS – Security Access
On August 20, 2013 JLBC reviewed $1.6 million for the AELAS – Education Data Fidelity (Ed-Fi) project. This project is intended to standardize how student data could be exported and imported from LEAs to ADE's systems. However accessing and making modifications to this data is difficult because the current system does not have the capabilities to distinguish between various users and provide these users with the appropriate access to various levels of data. ADOA is currently requesting review of $450,000 for the remainder of the Ed-Fi project, to implement a new Organization Entity Management System. This system will ensure that the appropriate users are accessing the correct data points with the appropriate levels of security clearance.

This project has received ASET approval through the PIJ process, with conditions. The JLBC Staff recommends that the JLBC consider adopting the ASET provisions as part of its review.

Third Party Oversight

On a related note, a contract was awarded to WestEd (a consulting firm) on April 3, 2013 to provide third party review of the AELAS project. The vendor subcontractor for the project (CELT) has interviewed approximately 75 AELAS stakeholders, including ADE staff, key education stakeholders, school superintendents and Chief Technology Officers, and ASET staff in order to gather information for analyzing the project.

The third-party report was released on September 9, 2013. It indicates that ADE and ADOA should continue to pursue current practices regarding the scope and technology approach of the project, which it says reflects best practices and leads most other states. In addition, the report states that AELAS appears to have more external oversight than is typical in other states.

Areas for improvement include enhancing communication to various education stakeholders, including more diverse audiences, and ensuring that bandwidth and infrastructure does not limit small districts and charters from fully utilizing the new system. In addition, the report recommends the creation of a separate non-profit entity designed to engage districts and encourage their participation for any opt in services.

RS:BH/ts

Attachment A

AELAS Background

In 2010, the Legislature passed legislation creating a new statewide educational data system known as the Arizona Education and Learning Accountability System (AELAS). Pursuant to A.R.S. § 15-249, AELAS is required to maintain longitudinal student level data required to meet state and federal reporting requirements, incorporate the Student Accountability Information System (SAIS), and be easily accessible over the internet for data collection, compilation and reporting. Additionally in 2010, the Governor's Office commissioned a third party evaluation of ADE's current IT systems. The report indicated that many aspects were insufficient, including obsolete and unsupported hardware and software, overly complex customization and insufficient resources to provide ongoing support and development.

Since then, ADE has used state and federal monies to stabilize SAIS in order to reduce down time and enable faster processing and reconciliation of data with the existing system until it can be replaced. This has enabled the system to perform better in the short term, but ADE reports that the system "still has a high error rate, is costly to support and maintain, and catastrophic failure is likely without replacement."

In addition to replacing SAIS, AELAS would establish a new statewide Student Information System (SIS) for storing both student data related to funding (currently in SAIS) and student/teacher/course academic data (not currently in SAIS). ADE envisions that districts would opt into the statewide SIS by paying a reduced "group rate" charge for access to the system. ADE believes that the charge would be a savings relative to their current standalone systems, primarily due to economies of scale. AELAS is also intended to create standardized mechanisms for importing and exporting data to/from the SIS in order to reduce data reporting errors ("Education Data Fidelity") and establish a Statewide Longitudinal Data System (SLDS) to provide access to multi-year data for individual students/teachers/courses that is stored in the SIS via data "dashboards."

During the most recent legislative session, ADE requested $34.8 million over 2 years ($23.8 million in FY 2014 and $11.0 million in FY 2015) for AELAS development. This included $23.5 million for SAIS replacement, $4.2 million for the SLDS, $4.1 million for an instructional improvement system, and $4.0 million for integrating, replacing and upgrading ADE's internal information technology systems.

ADE previously used its own funds to administer the project, which included a combination of state General Fund monies ($5 million per year in FY 2012 and FY 2013), mandatory fees of $6 per Full Time Student Equivalent (FTSE) from Arizona universities and community colleges (approximately $1.5 million per year in FY 2012 and FY 2013), and federal monies (approximately $10 million in FY 2012 and FY 2013 combined).

In FY 2014, the Legislature appropriated $7 million to ADOA to oversee the project and work with ADE to implement a portion of the larger project. Of the $7.0 million, $5.4 million is from the state General Fund and $1.6 million is from continued university and community college AELAS fees. On August 20, 2013, JLBC reviewed $3.4 million of this $7.0 million appropriation for 3 separate projects. The remainder of the $7.0 million appropriation, a total of $3.7 million, is included in the current request.

E-Licensing System Projects – Favorable Review Requests – October 29

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
DEQ E-Licensing Program	- Implement DEQ online website framework for e-licensing - Streamline and automate seven core business processes	$5,000,000	$5,000,000	PIJ Approved	Pending
Total DEQ			**$5,000,000**		

ADE – Statewide Longitudinal Data System (SLDS) and the Education Learning and Accountability System (ELAS) - $7,000,000

The Program Support Office (PSO) creates standards for project design, development and implementation as well as financial oversight for ADE's IT contract laborers. The PSO also prepares reports and other materials required for AELAS program oversight. This is a critical quality control function to ensure current and future projects and funds are managed appropriately.

Arizona Education Learning and Accountability System (AELAS) Student Information System (SIS) is replacing the student data portion of the aging Student Accountability and Information System (SAIS). ADE will be creating standardized data stores and preparing a Request for Proposal (RFP) soliciting education software vendors to design a statewide SIS that Local Education Agencies (LEAs) can purchase at a savings. ADE anticipates implementing at least six LEAs in FY14, with further implementations in later years subject to LEA's opt-in participation. Making the optional statewide SIS available to additional LEAs is out of scope for FY14 and will require additional funding in future fiscal years.

Arizona Education Learning and Accountability System (AELAS) Education Data Fidelity (Ed-Fi) is the mechanism to standardize how student data can be imported and exported into the data stores created in the AELAS SIS project. Ed-Fi uploads LEA data from their own student data system in ADE's format and allows for a reduction of the data collection burden placed upon LEAs. This should significantly reduce the student data reporting errors currently created between SAIS and LEA standalone systems. ADE will integrate the four primary student information system vendors, representing more than 95% of LEAs statewide, in FY14.

The AELAS School Finance project will automate a portion of the School Finance functions of SAIS. This work streamlines and automates 13 of the 48 existing, manual financial payments, significantly reducing processing time and time spent by LEAs and ADE fixing errors. Complete School Finance replacement is out of scope for FY14, and SAIS sustainability remains a significant risk as a result.

Statewide Longitudinal Data System (SLDS) – Arizona Education Data Driven Decision System (AzED^{3}S) provides dashboards of the student data collected in the ADE data warehouse using the newly-constructed data stores from the AELAS SIS project. Work will also include concurrent implementation of the new security protocol funded in previous fiscal years. It is estimated that these dashboards, currently displaying only historical data, will be deployed to 200 LEAs in FY14. Complete roll out will be completed by December 2014 and will require additional funding in later fiscal years.

ADE Projects

Project Name	FY14 Description	Project Budget
Program Support Office (PSO)	- Program Support Office (PSO) consisting of Portfolio Director, Phase Gate Management, Vendor Management, Communications, Risk Management, Financial Management and Oversight Management	$ 1,000,000
Arizona Education Learning and Accountability System (AELAS) - Student Information System (SIS)	- Complete SIS RFP and award - Integrate SIS to Student Operational Data Stores - Implement and integrate six LEAs (includes data migration) - Additional LEA integrations out of scope for FY14	$ 450,000
Arizona Education Learning and Accountability System (AELAS) - Education Data Fidelity (Ed-Fi)	- Implement Ed-Fi extractors for the four major SIS Vendors in the State - Additional integration for LEA systems is out of scope for FY14	$ 2,000,000
Arizona Education Learning and Accountability System (AELAS) - School Finance	- Streamline and automate existing manual Class Site Fund (CSF) financial capability - Additional School Finance capabilities are out of scope for FY14	$ 800,000
Statewide Longitudinal Data System (SLDS) – Arizona Education Data Driven Decision System ($AzED^3S$)	- Implement Ed-Fi Dashboards - Roll out to 200 LEAs - Additional data source integration and LEA roll out continued in FY15	$ 2,750,000
Total ADE		**$ 7,000,000**

ADE Projects – Favorable Review Requests – August 20

Project Name	FY14 Description	Total Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Program Support Office (PSO)	- Program Support Office (PSO) consisting of Portfolio Director, Phase Gate Management, Vendor Management, Communications, Risk Management, Financial Management and Oversight Management	$ 1,000,000	$ 1,000,000	PIJ Not Required	Approved
Arizona Education Learning and Accountability System (AELAS) - Education Data Fidelity (Ed-Fi)	- Implement Ed-Fi extractors for the four major SIS Vendors in the State - Additional integration for LEA systems is out of scope for FY14	$ 2,000,000	$ 1,550,000	ITAC Approved	Approved
Arizona Education Learning and Accountability System (AELAS) - School Finance	- Streamline and automate existing manual Class Site Fund (CSF) financial capability - Additional School Finance capabilities are out of scope for FY14	$ 800,000	$ 800,000	PIJ Approved	Approved
Total ADE			**$ 3,350,000**		

ADE Projects – Favorable Review Requests – October 29

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Arizona Education Learning and Accountability System (AELAS) - Student Information System (SIS)	- Complete SIS RFP and award - Integrate SIS to Student Operational Data Stores - Implement and integrate six LEAs (includes data migration) - Additional LEA integrations out of scope for FY14	$ 450,000	$ 450,000	PIJ Approved	Pending

Project Name	FY14 Description	Project Budget	Favorable Review Requested Amount	PIJ/ITAC Status	JLBC Favorable Review Status
Arizona Education Learning and Accountability System (AELAS) - Education Data Fidelity (Ed-Fi)	- Implement Ed-Fi extractors for the four major SIS Vendors in the State - Additional integration for LEA systems is out of scope for FY14	$2,000,000	$ 450,000	PIJ Approved	Pending
Student Longitudinal Data System (SLDS) – Arizona Education Data Driven Decision System (AED3S)	- Implement Ed-Fi Dashboards - Roll out to 200 LEAs - Additional data source integration and LEA roll out continued in FY15	$2,750,000	$2,750,000	PIJ Approved	Pending
Total ADE			**$ 3,650,000**		

STATE OF ARIZONA

Joint Legislative Budget Committee

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DATE: October 22, 2013

TO: Representative John Kavanagh, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director RS

FROM: Amy Upston, Principal Fiscal Analyst AU

SUBJECT: AHCCCS/DHS/DES - Review of Proposed Capitation Rate Changes

Request

Pursuant to footnotes in the FY 2014 General Appropriation Act, the Arizona Health Care Cost Containment System (AHCCCS), the Department of Health Services (DHS), and the Department of Economic Security (DES) must present their plan to the Committee for review prior to implementing any changes in capitation rates. AHCCCS submitted this item for all 3 agencies.

Recommendation

The Committee has at least the following options:

1. A favorable review.

2. An unfavorable review.

The proposal is expected to cost less than the budgeted amounts for rate adjustments.

Analysis

Capitation rates are developed by actuaries based on information provided to them by the agency. Rates are set for the beginning of the contract year – July 1 for the DES program and October 1 for AHCCCS and DHS programs. They must be approved by the Federal Centers for Medicare and Medicaid Services (CMS). Rates for Medicaid programs are composed of adjustments for trends, experience, provider rates, and program changes.

Capitation rates are adjusted annually for medical expense and utilization <u>trends</u>. Utilization refers to the percentage of eligible individuals who use services and the amount of services each member uses. In developing capitation rates, the actuaries also compare prior rate calculations and assumptions to actual

(Continued)

results for medical expenses and utilization. This is referred to as experience adjustments. The CYE 14 capitation rate adjustments also include provider rate increases for select providers. Finally, the capitation rates include a number of program changes which are described below.

Program Changes

The capitation rates include the following program changes:

- *Children's Rehabilitative Services (CRS) Integration.* The CRS program provides services for children with chronic and disabling or potentially disabling conditions. Beginning on October 1, 2013, AHCCCS is integrating care for all services for most Acute Care program children with CRS conditions through one CRS contractor. CRS Children in the Developmentally Disabled (DD) program will have their behavioral health services (BHS) shifted from the DD program to the CRS contractor. CRS Children in the Arizona Long Term Care System (ALTCS) Elderly and Physically Disabled Program (EPD) will receive all of their CRS-related services through the ALTCS EPD program. While AHCCCS expects the integration to be budget neutral, it results in shifting costs between different programs. While the agencies have requested that the cost shift be addressed during the FY 2015 budget process, they intend to address this shift in FY 2014 through interagency transfers.
- *Well Visits.* The FY 2014 Health and Welfare Budget Reconciliation Bill reinstated well visits which had been eliminated since October 1, 2010. AHCCCS estimates this will cost the General Fund approximately $5.4 million across all Medicaid programs.
- *Medicare Coverage of Benzodiazepine and Barbiturate Medications.* Medicare recently approved coverage of benzodiazepines (a class of psychoactive drugs used to treat anxiety, insomnia, and a range of other conditions) used for any condition and barbiturates used for epilepsy treatment. This federal policy change shifts costs from the Medicaid program to Medicare. AHCCCS estimates this will generate approximately $(700,000) in General Fund savings across all Medicaid programs.

In addition to the integration of the CRS program, AHCCCS will be integrating acute care services with behavioral health services for people with a serious mental illness (SMI) in Maricopa County. The integration was planned to begin on October 1, 2013, but due to legal challenges from the current contractor, the integration has been placed on hold. DHS anticipates that the integration will begin approximately 90-120 days after a hearing decision is rendered. The proposed rates do not include the SMI integration.

Adjustments by Program

AHCCCS Acute Care
This population represents members who participate in the Traditional Medicaid, Proposition 204, and KidsCare programs. Overall, the proposed capitation rates for these programs will increase by 0.6%. This change is due to a variety of factors including:

- Increased costs due to medical trends and provider rate increases.
- A change in the reinsurance policy from the current levels of $20,000 and $35,000 to $25,000. Reinsurance represents payments made to health plans for patients with unusually high costs. After the $25,000 deductible has been met, AHCCCS will pay 75%-85% of the cost of service until it reaches $650,000. After this level, AHCCCS pays 100% of the cost. This change is expected to be budget neutral in the long run, but it will increase costs in the current fiscal year.
- Increased costs associated with well exams.
- Competitive bidding for a new 5-year contract which resulted in (3.3)% lower capitation rates.

(Continued)

Additionally, shifting acute care services to CRS contractors will result in an approximate 17,000 fewer member months receiving services in the acute care program.

Although it will not impact the capitation rate, AHCCCS is beginning a payment reform initiative with the intent of improving health outcomes and reducing costs. One percent of the capitation rates will be withheld from contractors and placed into an incentive pool. The incentive pool amount will then be distributed back to contractors after the end of the contract year based on defined quality improvement metrics. Some contractors may receive more or less than the 1% payment depending on these measures.

AHCCCS Long-Term Care (ALTCS) for the Elderly and Physically Disabled
ALTCS services are provided to the elderly and physically disabled in need of long-term care either in nursing care facilities or in home and community-based settings. The state, counties, and federal government share in the cost of ALTCS services. The proposed capitation rates are 3.4% above last year's rates. This increase is the result of increases in utilization and medical expenses due to experience and trends, an increase in provider rates, and a shift of CRS-specific services from the CRS program.

Children's Rehabilitative Services (CRS)
The CRS program is administered by AHCCCS and provides services for children with chronic and disabling or potentially disabling conditions. Rates will go up 78.4% from last year, primarily the result of shifting acute care and behavioral health services for these children to the CRS contractor.

Long-Term Care for the Developmentally Disabled (DD)
DES administers the DD program, providing services for individuals with cognitive disabilities, cerebral palsy, autism, or epilepsy. The proposed rate is an increase of 1.8% over last year's rate. The increase is primarily driven by a 3% rate increase for institutional and home and community service providers as authorized in the FY 2014 budget. The increase is partially offset by shifting behavioral health services to the CRS program and reductions in utilization and medical trends.

Behavioral Health Services (BHS)
DHS oversees most behavioral health and substance abuse services. The proposed rate is an increase of 2.3%. The majority of the increase results from a 3% provider rate increase for most community-based and residential services as authorized in the FY 2014 budget. Additionally, the shifting of behavioral health services to CRS contractors will result in an approximate 17,000 fewer members per month receiving services in the acute care program.

Monthly Capitation Rates
The table below compares the proposed rates to the current rates for the 5 populations.

Table 1

Monthly Regular Capitation Rates

Populations	**Previous Rates**	**New Rates**	**% Change**
AHCCCS Acute	$ 236.18	$ 237.62	0.6%
AHCCCS Elderly & Physically Disabled	3,022.21	3,123.56	3.4
Children's Rehabilitative Services	369.61	659.41	78.4 1/
DES Developmentally Disabled	3,125.69	3,181.77	1.8
DHS Behavioral Health Services	85.61	87.58	2.3

1/ New rate includes acute and behavioral health services.

RS/AU:ts

Janice K. Brewer, Governor
Thomas J. Betlach, Director

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AHCCCS

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October 8, 2013

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JOINT BUDGET COMMITTEE

The Honorable John Kavanagh
Arizona House of Representatives
1700 West Washington
Phoenix, Arizona 85007

Dear Representative Kavanagh:

The Arizona Health Care Cost Containment System (AHCCCS) is Arizona's single state Medicaid agency. However, the Arizona Medicaid system includes state agency subcontractors represented by the Arizona Department of Economic Security (DES) for both the Arizona Long Term Care System (ALTCS) Division of Developmental Disabilities (DDD) and the Comprehensive Medical and Dental Program (CMDP); and the Arizona Department of Health Services (ADHS) for Behavioral Health Services (BHS). AHCCCS, DES and ADHS respectfully request to be placed on the agenda of the next Joint Legislative Budget Committee (JLBC) meeting to review the capitation rates for Contract Year Ending (CYE) 2014 (October 1, 2013 through September 30, 2014, unless otherwise noted) for the following programs:

- Acute Care
- ALTCS Elderly and Physically Disabled (EPD)
- Children's Rehabilitative Services (CRS)
- DES/CMDP (update for October 1, 2013 through December 31, 2013 only)
- ALTCS DES/DDD (July 1, 2013 through June 30, 2014)
- ADHS/BHS

Background and Summary

As required by the Federal Balanced Budget Act of 1997, Title XIX Managed Care Programs must have actuarially sound capitation rates. The proposed rate adjustments have been approved by the Centers for Medicare and Medicaid Services (CMS) for an October 1, 2013 implementation.

Effective October 1, 2013, AHCCCS is implementing several integration efforts in order to improve member care. Today, AHCCCS members with complex care needs must navigate through multiple AHCCCS programs to meet all their medical service needs. Care is fragmented between different Contractors and different providers. With the AHCCCS integration initiatives, the complete needs of the whole person will be covered by one Contractor, whenever possible, for children with special health care needs (CRS members), and members with Serious Mental Illness (SMI) in Maricopa County. (At this time, due to legal challenges, the integration in Maricopa County for members with SMI is on hold. BHS anticipates implementing the integrated Regional Behavioral Health Authority (RBHA) approximately 90-120 days after a hearing decision is rendered.)

The integration efforts result in shifting expenditures from one or more programs to another, in some cases causing significant distortion to the rate changes by program; however, despite these individual program rate changes, the shifts are budget neutral across the system. The overall change to the total Medicaid program for CYE 14, over the most recently approved rates, is 2.76%, and AHCCCS estimates that, based on current estimated enrollment, there is sufficient funding in the SFY 2014 budget. Table 1 below displays the CYE 2014 rate changes by program, which includes the shifting funds for the CRS integration. These rates do not reflect the shift in funds from the Acute program to BHS that will need to occur for the integrated RBHA implementation. When that initiative is ready to begin, capitation rate changes will be necessary and AHCCCS will notify JLBC for review.

Table 1

Program	Rate Change (over most recently approved rates)
AHCCCS	
Acute	0.82%
ALTCS EPD	3.49%
CRS	78.41%
CMDP*	0.75%
DES	
DDD	1.69%
ADHS	
BHS	2.16%
Total	**2.76%**

* The CMDP rate change represents one quarter from October 1 - December 30, 2013. CMDP rates will be amended January 1, 2014 for CYE 14

The five year average capitation rate adjustment across the programs displayed above is (1.99)%.

Acute Care Capitation Rates
The overall rate adjustment for the Acute program for CYE 2014 is an increase of 0.82%.

CYE 2014 is the first year of a new contracting cycle for the Acute program. A competitive bidding process via a Request for Proposals (RFP) was utilized with the RFP released in early-2013 and contracts awarded in the spring. Offerors submitted capitation bids based on actuarially-sound rate ranges developed by AHCCCS' actuaries for the majority of the Acute program membership. Awarded rates were then adjusted by AHCCCS to account for issues impacting cap rates decided after the rates were awarded, such as the reinstatement of well visits for adults passed by the Legislature.

The three largest factors impacting the Acute rates are competitive bidding resulting in a (3.30)% decrease; a change to the reinsurance offsets bringing all Managed Care Organizations (MCOs) to the same annual deductible level, accounting for a 2.00% increase; and inflationary cost trends and provider rate adjustments increasing the rates by 2.08%.

Elderly and Physically Disabled Long Term Care Capitation Rates
The overall rate adjustment for the ALTCS EPD program for CYE 2014 is an increase of 3.49%.

The three largest factors impacting the ALTCS EPD rates are utilization and inflationary trends on long-term care services due to change in mix of services, accounting for a 1.40% increase; a provider rate adjustment for Home and Community Based Services (HCBS) and Nursing Facility services to maintain appropriate access, resulting in a 1.30% increase; and a shift in funding for CRS services for EPD members, accounting for a 0.50% increase. Because the EPD MCOs are already responsible for the provision of long-term, acute, and behavioral health services for EPD members with CRS conditions, AHCCCS elected to fully-integrate care for these members by moving CRS service responsibility to the EPD MCOs as well. All physical and behavioral health needs for EPD members with CRS conditions will be met by the EPD MCO, improving the odds for better health outcomes and care coordination for these members.

Children's Rehabilitative Services Capitation Rates
The overall rate adjustment for the CRS program for CYE 2014 is an increase of 78.41%.

This rate change is attributable to the integration changes mentioned above that aligned the medical service package offered by the CRS Contractor. AHCCCS shifted funding for acute care and behavioral health services from the Acute and BHS programs to the CRS program due to integration. As noted above, the integration is budget neutral across the system and there is a corresponding acuity change built into the Acute and BHS rates to account for the shift. If the impact of integration is set-aside, the medical service expense is flat over CYE 2013.

Comprehensive Medical and Dental Program (CMDP)
The overall rate adjustment for CMDP for the last calendar quarter of 2013 is an increase of 0.75%.

CMDP has a contract year that spans the calendar year, from January 1 through December 31. For this reason, the CYE 2014 CMDP rates won't be implemented until January 1, 2014. However, CMDP has a state legislative mandate to pay providers at the AHCCCS fee schedule rates. Since AHCCCS is adjusting its fee schedules effective October 1, 2013, to conform with Medicare and to maintain appropriate access, it is necessary to make corresponding adjustments to the CMDP cap rates effective October 1 through December 31, 2013. These are the only adjustments reflected in the rates.

Developmental Disabilities Long Term Care Capitation Rates
The overall rate adjustment for the ALTCS DDD program for CYE 2014 is an increase of 1.69%.

The primary factor impacting the rate is an increase to the developmental disabilities service provider rates of 3% as mandated by the Legislature, effective July 1, 2013 which resulted in a 2.14% increase. A secondary factor accounting for a (0.53)% impact to the rate is the trend observed in utilization and unit costs.

Behavioral Health Services Capitation Rates
The overall rate adjustment for the BHS program for CYE 2014 is an increase of 2.16%.

The majority of the rate change can be explained by the 3% provider rate increase mandated by the Legislature effective October 1, 2013, resulting in a 1.86% overall impact on the capitation rates. Miscellaneous other adjustments combine to increase the rate by an additional 0.30%

Overall Budget Impact

Table 2 below displays the budget impact of the rate changes. This data is displayed on a state fiscal year (SFY) basis due to budgetary timeframes. Likewise, the 2014 population below is on a SFY basis. For these reasons, the impacts on this table will not tie exactly to impacts stated elsewhere in this letter or attached documents.

Table 2

	Statewide Rates SFY13	Statewide Rates SFY14	FY14 Population	SFY13 Rate with FY14 Pop.	SFY14 Rate with FY14 Pop.	Change Inc. (Dec.)	Percent Impact
AHCCCS Acute	$ 237.95	$ 239.97	14,976,933	3,563,788,500	3,594,044,100	30,255,600	0.85%
AHCCCS EPD	$ 2,945.03	$ 3,047.69	326,320	961,021,900	994,523,700	33,501,800	3.49%
CMDP	$ 225.47	$ 227.17	172,642	38,925,200	39,218,800	293,600	0.75%
CRS	$ 369.61	$ 659 41	305,105	112,770,500	201,190,200	88,419,700	78.41%
BHS Title XIX/XXI	$ 87.28	$ 89.17	15,529,211	1,355,365,200	1,384,687,600	29,322,400	2.16%
LTC - DD/DES	$ 3,265.92	$ 3,321.15	313,507	1,023,889,200	1,041,204,400	17,315,200	1.69%
Total Budget Impact	$ 438.40	$ 450.77	16,094,508	7,055,760,500	7,254,868,800	199,108,300	2.82%
					AHCCCS Total Fund Impact	152,470,700	76.6%
					Pass-through Total Fund Impact	46,637,600	23.4%
					AHCCCS State Impact	49,665,700	77.3%
					Pass-through State Impact	14,573,600	22.7%
					Total State Impact	64,239,300	
					AHCCCS Federal Impact	102,805,000	76.2%
					Pass-through Federal Impact	32,064,000	23.8%
					Total Federal Impact	134,869,000	

AHCCCS is currently projecting that, based on these capitation rates and projected enrollment, the agency has sufficient funding available for the SFY 2014 budget.

Policy Changes

Per the legislative mandates in ARS 36-2901.06 and 36-2941, AHCCCS has not included any changes beyond those already approved by the Legislature.

The actuarial certifications for the rates are attached. Should you have any questions on any of these issues, please feel free to contact Shelli Silver, Assistant Director, at (602) 417-4647.

Sincerely,

Thomas J. Betlach
Director

cc: The Honorable Don Shooter, Arizona State Senate
John Arnold, Office of Strategic Planning & Budgeting
Richard Stavneak, Joint Legislative Budget Committee
Don Hughes, Office of the Governor

Acute Care Actuarial Memorandum

I. Purpose

The purpose of this actuarial memorandum is to demonstrate that the Acute Care capitation rates were developed in compliance with 42 CFR 438.6(c). It is not intended for any other purpose.

Arizona Health Cost Containment System (AHCCCS) intends to update these capitation rates for January 1, 2013 to include changes in cost sharing and benefits resulting from mandated Affordable Care Act (ACA) requirements and any other necessary changes.

AHCCCS will be applying risk adjustment factors with an anticipated implementation date of April 1, 2015 retroactive to October 1, 2013. This adjustment will be budget neutral to AHCCCS.

ACA places an annual fee on the health insurance industry nationwide including most Medicaid health plans effective January 1, 2014. The fee will be allocated to health insurers based on their respective market share of premium revenue in the previous year. Due to the uncertainty of the actual fees and other unknowns, AHCCCS will not be adjusting the capitation rates for this fee at this time, but intends to make a revision once the impacts are known.

II. Overview of Bid and Rate Setting Methodology

Contract year ending 2014 (CYE 14) is the first year of a new cycle for the Acute contract. Therefore, the CYE 14 rates were developed using one of the following methods:

- For the risk groups that were bid: the medical and administrative rates were awarded as part of the competitive bid process for the CYE 14 Request for Proposal (RFP). The awarded medical rates were then updated for any programmatic and/or AHCCCS Fee-For-Service (FFS) provider rate changes that were not known at the time of the bid process. Other adjustments to the rates included a reinsurance offset (developed by AHCCCS actuaries), risk contingency, premium tax and payment withhold.
- For the non-bid risk groups: AHCCCS' actuaries developed actuarially sound capitation rates.

These rates represent the twelve month contract period October 1, 2013 through September 30, 2014.

For the bid process, prospective Offerors were required to submit two separate rate components for each risk group and Geographical Service Area (GSA) bid: one for medical and one for administrative.

- For the medical component, AHCCCS' actuaries developed actuarially sound rate ranges for the CYE 14 contract year to be used in the evaluation of the bids submitted. The rate ranges were published for use by the prospective

Offerors and represented the lower half, or midpoint to minimum, of the actuarially sound rate range. AHCCCS' actuaries set the ranges based on average expenditures. The medical rate ranges excluded reinsurance offsets and did not reflect any withheld amounts for payment reform initiatives.

- An 8% maximum limit was imposed for the administrative component bid.
- For those risk groups for which the Offerors were not required to bid (Prior Period Coverage (PPC), SOBRA Family Planning Extension Program (SFPEP), Newly Eligible Adults and State Only Transplants), AHCCCS' actuaries developed actuarially sound capitation rates.

Because CYE 14 is classified as a rate development year rather than a rate update to the previously approved CYE 13 capitation rates, AHCCCS' actuaries developed a new base time period to compute CYE 14 rates and ranges. Historical Medicaid managed care encounter data was used as the primary data source in development of the base time period. This encounter data was made available to AHCCCS' actuaries and Offerors via an extract that provides utilization and cost data, referred to as the "databook". The databook also includes member month information.

Due to integration efforts at AHCCCS, the databook excludes both encounter and member month data associated with those members who would be enrolled with an integrated Contractor effective October 1, 2013. This includes members eligible for the Children's Rehabilitative Services (CRS) program as well as adult members in Maricopa County with Serious Mental Illness (SMI). The capitation rate ranges and the Offerors' bids were built upon these assumptions. However, due to a challenge received by the Arizona Department of Health Services (ADHS) related to their award of the Maricopa County integrated Contractor, the move to integrate services for members with SMI residing in Maricopa County will be delayed. The capitation rates were appropriately adjusted to reflect this change.

The contract between AHCCCS and the Contractors specifies that the Contractors may cover additional services not covered by Medicaid. Non-covered services were removed from the databook and excluded from rate development.

Other data sources used in setting the actuarially sound rates and ranges include Contractors' financial statements, programmatic changes, AHCCCS FFS provider rate changes, anticipated ADHS transportation rate changes, Center for Medicare and Medicaid Services (CMS) National Health Expenditure (NHE) Report estimates and Global Insight Prospective Hospital Market Basket Inflation Index (GI) information.

AHCCCS posted the encounter databook, other supplemental resources noted above, and enrollment information to its website in order to provide all prospective Offerors with the data necessary to submit appropriate bids for CYE 14.

Trend rates were calculated from the databook and other sources on a unit cost and/or utilization basis by category of service (COS) and a cap was applied to limit the negative and positive trends to a reasonable level. Unit cost trends were further refined by actual changes in AHCCCS FFS provider rates. These adjustments also include state mandates, court ordered programs and other programmatic changes, if necessary. Additional analysis was performed on all prospective populations due to shifts in the economy and policy impacts that have caused deviations from the historical encounter data costs and trends. These historical trends were then applied to the base data. Additional trends were applied for anticipated changes in AHCCCS FFS rates and programmatic changes. For more information on trends see Section IV Projected Trend Adjustments.

The Acute Care program has a large membership base, which allows for the experience data to be analyzed by different rate cells. These rate cells are comprised of members with similar risk characteristics. The rate cells were analyzed by major categories of aid (COA), i.e. risk groups, and COS. In addition, AHCCCS develops rates by GSA.

The experience data includes only Acute Care Medicaid eligible expenses for Acute Care Medicaid eligible individuals, as well as reinsurance amounts. The PPC rates are reconciled to a maximum 2% profit or loss. The prospective risk groups are reconciled based on a tiered methodology (see Section XIX CMS Rate Setting Checklist for additional information). Additional payments are made for members giving birth via a Delivery Supplemental Payment.

The general process in developing the prospective rates and rate ranges involves trending the base data, adjusted for programmatic and AHCCCS FFS provider rate changes, to the midpoint of the effective period, which is April 1, 2014. The next step involves the deduction of the reinsurance offsets. Following this calculation, the projected administrative expenses, risk/contingency margin and premium tax are added to the projected claim PMPMs to obtain the capitation rates. New for this contract year, AHCCCS will be implementing a payment reform initiative (PRI) which involves withholding 1% of the Contractors' capitation rate. Each step is described in the sections below.

In addition there are sections dedicated to the development of other rates including, but not limited to, the SFPEP, Newly Eligible Adults and PPC rates.

III. Base Period Experience

AHCCCS used historical yearly encounter data for the time period from October 1, 2008 through March 31, 2012. The data was reviewed for accuracy, timeliness and completeness through encounter validation studies as well as studies comparing the encounter data to the Contractors' financial statements. One adjustment to the base data was the removal of the encounters associated with a birth event since these costs are paid for in the Delivery Supplemental rate. The encounters that were removed from the base data were used to develop this Supplemental rate. Other adjustments to the base data included, but were not limited to the following: completion factors, seasonality factors, historical programmatic changes and historical AHCCCS FFS provider rate changes. The final result was the adjusted base data for CYE 09 (10/01/08 – 09/30/10), CYE 10 (10/01/09 – 09/30/10), CYE 11 (10/01/10 – 09/30/11) and CYE 12 (10/01/11 – 03/31/12). The base data was computed by averaging all four time periods.

IV. Projected Trend Adjustments

Historical trend rates were developed from the adjusted base data. These trends were developed by major COA and COS, with a cap on the percentage increase and decrease to smooth out exceptional trends. Once these trends were developed they were analyzed by comparing the results to Contractor financial statements and data and trends in the marketplace such as NHEs.

Effective October 1, 2013, AHCCCS is increasing FFS provider rates for certain providers based either on access to care needs, Medicare or ADHS fee schedule rates, legislative mandates, or cost of living adjustments. The unit cost (inflation) trends were adjusted appropriately for these changes. The estimated statewide impact is an increase of approximately $12.6 million.

The utilization and unit cost trend rates (which reflect the AHCCCS FFS provider rate changes) used in projecting the claim costs are summarized in Appendix I. The prospective PMPM trends are shown below in Table I. These trends do not reflect the impact of any programmatic changes.

Table I: Prospective Average Annual PMPM Trends

	PMPM Trends			
Categories of Service	TANF & KidsCare Combined	SSI With Medicare	SSI without Medicare	AHCCCS Care
Hospital Inpatient	1.4%	3.5%	1.0%	0.4%
Outpatient Facility	4.5%	2.2%	2.9%	4.4%
Emergency Room	4.3%	1.1%	5.7%	0.5%
Physician	3.9%	0.2%	4.1%	0.7%
Other Professional	6.3%	3.7%	6.5%	1.8%
Pharmacy	4.6%	2.3%	4.2%	3.4%
Other	0.7%	1.0%	2.0%	-1.0%

V. State Mandates, Court Ordered Programs, Programmatic Changes and Other Changes

The changes in this section describe other changes that were not included in the adjusted base data.

Medicare Coverage of Benzodiazepine and Barbiturate Medications
Effective January 1, 2013 for dual eligible members, Medicare will cover benzodiazepines for any condition and barbiturates used for the treatment of epilepsy, cancer or chronic mental health conditions. Therefore, Contractors will no longer be permitted to reimburse prescription claims for these services. The Offerors' bid rates and rate ranges do not reflect this change thus they need to be adjusted. The estimated statewide impact to the Acute program is a decrease of approximately $1.4 million.

Medical Management Changes
The State of Arizona's 2013 Health and Welfare Budget Reconciliation Bill (BRB) reinstated well visits, which were previously eliminated October 1, 2010, as a covered service for enrolled adults for federal fiscal year 2014. The estimated statewide impact is an increase of approximately $16.1 million.

CRS Integration
In order to facilitate efficient coordination of care and improve member outcomes, AHCCCS has integrated the services for children with special health care needs effective October 1, 2013. Members with diagnoses who qualify for Children's Rehabilitative Services will now receive care related to their CRS services, unrelated physical health services, and behavioral health care through a single CRS Contractor. All physical health costs for these members have been removed from the base data as well as the associated member months. This resulted in a shift of approximately $61.9 million.

Primary Care Provider (PCP) Payment Increase
Section 1902(a)(13)(C) of the Social Security Act, as amended by the Affordable Care Act, requires minimum levels of Medicaid payment for certain primary care services, provided by certain physicians. The AHCCCS managed care model, with strict requirements regarding actuarially-sound capitation rates, necessitates that Contractors be funded for expected cost increases due to primary care rate parity. AHCCCS proposes to provide Contractors the necessary funds to increase primary care payments by using Model 3: Non-risk Reconciled Payments for Enhanced Rates as referenced in the *Medicaid Managed Care Payment for PCP Services in 2013 and 2014, Technical Guidance and Rate Setting Practices* (Technical Guidance) document released by CMS.

In summary, under Model 3, prospective capitation rates would not be adjusted for the enhanced primary care payments. Rather, AHCCCS would query actual encounter data on a quarterly basis to calculate the total payments that eligible providers were paid for eligible services in order to reach the mandated enhanced payment rates. Once the data on this report is verified, AHCCCS would pay the Contractors the calculated additional payment amounts. A more detail explanation of the process and methodology can be found in the Actuarial Certification submitted to CMS for approval of AHCCCS methodology. There is no impact to the CYE 14 capitation rates.

In-Lieu of Services
Included in the base rates is funding for "in lieu of" services, substituting cost-effective alternative inpatient settings in place of more costly inpatient non-specialty hospital placements. State approved FFS rates at inpatient non-specialty hospitals are approximately 93.5% more expensive than those provided in alternative inpatient settings. The proposed capitation rates allow for the provision of services in alternative inpatient settings that are licensed by ADHS/Arizona Licensing Services/Office of Behavioral Health License, in lieu of services in an inpatient non-specialty hospital, thus no increase to cap rates is included.

VI. Prospective Projected Net Claim PMPM

The base utilization, unit costs and net claims PMPMs are trended forward and adjusted for state mandates, court ordered programs and programmatic changes to arrive at the CYE 14 utilization, unit costs and net claims PMPMs for each COS and COA.

VII. Prospective Reinsurance Offsets

The reinsurance offsets were reviewed by AHCCCS for appropriateness and reasonableness using reinsurance encounter and payment information. As a result of this review, AHCCCS rebased the reinsurance offsets using data from October 2010 through September 2012. The data was adjusted to account for:

- the shift of members with CRS conditions to the CRS Integrated Contractor
- a change in deductible levels from the current levels of $20,000 and $35,000 to one deductible level for all Contractors of $25,000, effective October 1, 2013

Completion factors and programmatic changes were added to the data and these results were trended forward. These changes to the reinsurance offsets impact the overall capitation rates by 2%.

VIII. Coordination of Benefits

Inherent in the encounter and financial data are unit cost trends which incorporate Contractors' Coordination of Benefits (COB) activities. AHCCCS provides Contractors with verified commercial and Medicare coverage information for their members which Contractors utilize to ensure payments are not made for medical services that are covered by the other carriers. When Contractors make a payment to cover members' coinsurance, deductibles, or Medicaid-covered services that are not covered by the other carriers, they submit encounters containing these reduced amounts. From state fiscal year (SFY) 2008 to SFY 2013, encounter-reported COB cost avoidance grew by greater than 51%, from $391 million to $590 million. Additionally, in CYE 2013 Acute Contractors cost-avoided $159 million in additional claims in the nine months ending March 31, 2013 for which the Contractor had no financial obligation after the private insurance or Medicare payment was made. Consequently no encounters were submitted to AHCCCS and therefore those services are excluded completely from capitation expenditure projections. AHCCCS continues to emphasize the importance of COB activities with the Acute Contractors.

IX. Prospective Administrative Expenses and Risk Contingency

The administrative expense represents those rates awarded as part of the CYE 14 RFP process, which resulted in a reduction of administrative expense by approximately 1%. The risk contingency load remains the same for all risk groups at 1%.

X. Payment Reform Initiative

AHCCCS has mandated a payment reform initiative that all Contractors must implement effective October 1, 2013. The purpose of this initiative is to improve members' health outcomes while reducing costs. One percent (1%) of the actuarially sound prospective capitation rates will be withheld from payment to Contractors and used to fund a quality improvement withhold pool exclusive of Delivery Supplement, SFPEP, KidsCare and State Only Transplant payments. Quality improvement metrics have been established and Contractors' performance will be measured against these measures. The entire incentive pool amount will be distributed back to the Contractors based on the results of this measurement. Some Contractors may receive greater than a 1% payment and some may receive less than a 1% payment. Results will be analyzed after completion of the contract year to ensure the use of complete encounter data.

XI. Prospective Proposed Capitation Rates and Their Impacts

The proposed capitation rates equal the sum of the projected net claim PMPM (in Section VI) less the reinsurance offsets (in Section VII) and the projected administrative expenses and risk contingency PMPM (in Section IX), divided by 1 minus the 2% premium tax. For those risk groups involved in the PRI an additional 1% is removed to fund the quality improvement withhold pool. Appendix II contains the proposed capitation rates and the budget impact for all capitation rates using projected CYE 14 member months and actual Contractor reinsurance deductible levels.

XII. Risk Adjustment Factor

AHCCCS implemented the current risk adjustment methodology effective October 1, 2008. It is AHCCCS' intent to use a similar risk adjustment process for CYE 14 with a few changes as discussed below.

Due to the transition of members resulting from unsuccessful Contractors leaving particular GSAs as a result of the RFP, enhanced auto-assignment activity dictated by the RFP, and anticipated membership changes expected to occur due to restoration of the childless adult population and Medicaid expansion, enrollment by Contractor may be volatile in CYE 14. As such, risk adjustment should not be performed until such time that membership changes have stabilized. AHCCCS anticipates applying risk adjustment risk factors for CYE 14 as follows, subject to changes at AHCCCS' discretion: encounter data with dates of service from October 1, 2013 to September 30, 2014 will be processed in January 2015 using retrospective weighting with the resulting risk factors applied by April 2015, retroactive to October 1, 2013.

XIII. Delivery Supplemental Payment

The methodology followed in developing the Delivery Supplemental Payment is similar to the methodology used in the development of the prospective capitation rates where the Offerors bid the rate based on rate ranges that were developed by AHCCCS using the same methodology discussed above. When developing this PMPM, the number of Delivery Supplement payments becomes the denominator rather than total member months. No reinsurance offset applies to this rate, nor does the PRI withhold. The impact is a 2.6% decrease over the CYE 13 Delivery Supplemental Payment.

XIV. SOBRA Family Planning Extension Program (SFPEP)

The methodology followed in developing the SFPEP rate is similar to the methodology used in the development of the prospective capitation rates. This methodology involves rebasing the rates using the same base period discussed in Section III, applying similar trends as discussed in Section IV and programmatic changes (if appropriate) as discussed in Section V. This rate was not bid, and the administrative expense was set at the same percent as the CYE 13 rates which was 8% of medical expense. Risk contingency also remains unchanged at 1%. The SFPEP rates do not qualify for reinsurance and thus will not have a reinsurance offset. They also do not qualify for the PRI so they do not have a withhold amount applied. The impact is an 8.1% decrease over the CYE 13 capitation rate.

XV. KidsCare Rates

Continuing with the methodology of previous years, Contractors will be paid one blended capitation rate that includes experience from both the traditional TANF Medicaid population and the Title XXI SCHIP population. For CYE 14, the Title XXI population includes those children enrolled in KidsCare II as well as those members in the traditional KidsCare program. Traditional KidsCare provides coverage to children who have income levels between 100-200% of the FPL. This program was frozen on January 1, 2010. At that time, all KidsCare applicants were placed on a waiting list in the event that enrollment could be re-opened. On April 6, 2012, CMS approved a new 2012 Waiver Amendment, which included funding for KidsCare II. Enrollment was reopened on May 1, 2012 through the funding made available by the Waiver Amendment. KidsCare II provides coverage to children who have income levels up to 175% of the federal poverty level (FPL) and meet other eligibility requirements. KidsCare II is temporary and will end December 31, 2013.

The rate cohorts whose experience is blended together are detailed as follows (more information on Child Expansion can be found in Section XVI):

- TANF < 1 and KidsCare < 1
- TANF 1– 13 M&F, KidsCare 1 – 13 M&F, and Child Expansion 6-13 M&F
- TANF 14 – 44 F, KidsCare 14 – 18 F, and Child Expansion 14-18 F
- TANF 14 – 44 M, KidsCare 14 – 18 M, and Child Expansion 14-18 M

Because quality measures for KidsCare members are excluded from the PRI, capitation rates for these members will not include the PRI withhold and thus will differ by 1% from the TANF capitation rates.

The related member month, capitation rate and dollar information is as follows:

KidsCare Info	CYE 14 Projected Member Months	CYE 14 Proj Cap Rate	Total Annual Dollars CYE 14 (before withhold) based on CYE 14 Proj MMs
KC <1	1,634	$ 461.25	$ 753,533
KC 1-13	125,921	$ 99.07	$ 12,474,421
KC 14-44F	23,806	$ 233.46	$ 5,557,775
KC 14-44M	24,575	$ 146.75	$ 3,606,462

XVI. Expansion Rates (Child and Newly Eligible Adults)

The Supreme Court ruling on the ACA provides states multiple and complex opportunities with respect to the future of their Medicaid programs. With these opportunities in mind, Governor Brewer signed into law the Medicaid Restoration Plan which restores coverage to thousands of Childless Adults (i.e. AHCCCS Care) and provides coverage for Newly Eligible Adults between 100-133% of the Federal Poverty Level (FPL), beginning January 1, 2014. In addition, ACA mandates the expansion of the child population. AHCCCS anticipates approximately 45% of the KidsCare II population will move to child expansion beginning January 1, 2014.

It is AHCCCS' expectation that the child expansion population will utilize services in the same manner as the KidsCare and TANF populations, thus no separate capitation rates were developed for this population and their capitation rate will be the respective TANF capitation rates.

AHCCCS anticipates the utilization of the Newly Eligible Adult population to differ from the current risk groups, thus AHCCCS established a new risk group and capitation rate for this population. This population includes adults aged 19-64, without Medicare and between 100-133% of the FPL. The methodology followed in developing this capitation rate is similar to the methodology used in the development of the prospective capitation rates. However, since this population does not have actual historical experience, AHCCCS used the projected FFY 14 medical midpoint of the published ranges for the AHCCCS Care, TANF 14-44 F, TANF 14-44 M and TANF 45+ populations. AHCCCS then adjusted the data to appropriately reflect the makeup of this population, i.e. adults aged 19-64 without Medicare. This rate was not bid under the RFP and the administrative expense was set at the same percentage as the other non-bid rates which was 8% of medical expense. Risk contingency is at 1%. This risk group qualifies for reinsurance and the reinsurance offset was set using a similar methodology as described above. This risk group also qualifies for the PRI so they do have a withhold amount.

XVII. Prior Period Coverage Rates (PPC)

PPC rates cover the period of time from the effective date of eligibility to the day a member is enrolled with the Contractor. PPC rates are established using a similar methodology that was followed in developing the prospective capitation rates. This methodology involves rebasing the rates using the same base period discussed in Section III, applying similar trends as discussed in Section IV and programmatic changes (if appropriate) as discussed in Section V. This rate was not bid under the RFP and the administrative expense was set at the same percent as the CYE 13 rates which was 8% of medical expense. Risk contingency also remains unchanged at 1%. The PPC rates do not qualify for reinsurance and thus will not have a reinsurance offset. They also do not qualify for the PRI so they do not have a withhold amount. The overall statewide impact is an increase of 2.4%. The PPC rates are reconciled to a maximum 2.0% profit or loss in CYE 14.

XVIII. Final Capitation Rates and Their Impact

Table II below summarizes overall statewide changes from the CYE 13 rates. Since this was a bid year and the mix of Contractors by GSA has changed, the CYE 13 rates by Contractor do not provide an appropriate comparison. Likewise, AHCCCS cannot provide a range describing the capitation impacts by Contractor. However the GSA impact does provide an appropriate comparison, and ranges from -2.5% to 3.3%. Individual Contractor capitation rates are provided in Section B of each contract.

Table II: Changes from the CYE 13 Rates

AHCCCS Medicaid Managed Care Summary			
	Prospective	PPC	Weighted Average
Trend:			
1. Utilization	0.48%	1.41%	0.52%
2. Inflation	2.05%	2.68%	2.08%
Other Base Adjustments			
1. Rebase	-3.33%	-1.78%	-3.27%
2. SMI Acuity Adjustments	0.04%	-0.09%	0.04%
Program Changes			
1. Part D Adjustments	-0.04%	0.00%	-0.04%
2. Medical Management Adjustments	0.44%	0.00%	0.43%
Misc			
1. Reinsurance Offset Change	2.07%	0.00%	2.00%
2. Other Changes (ie Admin, Risk, Prem Tax)	-0.98%	0.24%	-0.93%
Total Percentage Change Before Withhold	0.75%	2.45%	0.82%
Withhold Impact	-0.94%	0.00%	-0.91%
Total Percentage Change Post Withhold	-0.19%	2.45%	-0.09%

XIX. CMS Rate Setting Checklist

1. Overview of rate setting methodology

A.A.1.0: Overview of rate setting methodology

AHCCCS is performing a rebase from the previously approved contract year ending 2013 (CYE 13) rates under 42 CFR 438.6(c). Please refer to Section II.

AA.1.1: Actuarial certification

Please refer to Section XX.

AA.1.2: Projection of expenditure

Please refer to Appendix II.

AA.1.3: Procurement, prior approval and rate setting

AHCCCS is operating under the Competitive Procurement contracting method.

AA.1.5: Risk contract

AHCCCS limits risk for the PPC risk groups to 2% profit or loss. All of the prospective risk groups are reconciled as follows:

Profit	MCO Share	State Share	Maximum Contractor Profit
<=3%	100%	0%	3.0%
>3% and <=6%	50%	50%	1.5%
>6%	0%	100%	0%
Total			4.5%

Loss	MCO Share	State Share	Maximum Contractor Loss
<=3%	100%	0%	3.0%
>3%	0%	100%	0%
Total			3.0%

AA.1.6: Limit on payment to other providers

AHCCCS makes no additional payment to providers, except for Disproportionate Share Hospital (DSH), Graduate Medical Education (GME) and Critical Access Hospitals. GME is paid in accordance with state plan. DSH and Critical Access Hospital payments are paid in accordance with the Waiver Special Terms and Conditions. None of the additional payments to providers were included in the capitation calculation.

AA.1.7: Rate modification

Please refer to Sections II through V, VII through X, and XII through XVII.

2. Base Year Utilization and Cost Data

AA.2.0: Base year utilization and cost data

Please refer to Sections III and IV.

AA.2.1: Medicaid eligibles under the contract

The data includes only those members eligible for managed care.

AA.2.2: Dual Eligibles (DE)

There are dual eligibles.

AA.2.3: Spenddown

Not applicable, not covered under this contract.

AA.2.4: State plan services only

The contract between AHCCCS and its Contractors specifies that the Contractors may cover additional services. Non-covered services were removed from the encounter data used to set the rates.

AA.2.5: Services that can be covered by a capitated entity out of contract savings.

Same as AA.2.4

3. Adjustments to the Base Year Data

AA.3.0 Adjustments to base year data

Please refer to Sections III, IV, V and VII.

AA.3.1 Benefit differences

Please refer to Section V for benefit changes to reinstate well visits for all adult members.

AA.3.2 Administrative cost allowance calculation

Please refer to Section IX.

AA.3.3 Special populations' adjustment

Please refer to Section XVI.

AA.3.4 Eligibility Adjustments

Besides CRS members shifting to the CRS Integrated Contractor, which was handled by adjusting the encounter and member month data as detailed in Section II and V, it is anticipated that the risk characteristics of this population will not change materially from the base period to the effective period of the capitation rates. Therefore, no adjustment was made.

AA.3.5 DSH Payments

No DSH payment was included in the capitation development.

AA.3.6 Third party Liability (TPL)

This is a contractual arrangement between AHCCCS and its Contractors.

AA.3.7 Copayments, coinsurance and deductible in the capitated rates

In general, most Acute members do not pay any copays, coinsurance or deductibles, though there are some copays that apply. The encounter data is net of copays. Further adjustments may be necessary due to the recent publication of Federal regulations related to the cost sharing requirements in the ACA.

AA.3.8 Graduate Medical Education (GME)

The experience excludes any payment for GME.

AA.3.9 FQHC and RHC reimbursement

The experience excludes any additional payments that FQHCs may receive from the state.

AA.3.10 Medical cost/ trend inflation

Please refer to Section IV.

AA.3.11 Utilization adjustment

Other than trend, no specific adjustment was made to utilization.

AA.3.12 Utilization and cost assumptions

Not applicable since actual experience was used.

AA.3.13 Post-eligibility treatment of income (PETI)

Not applicable, not required to consider PETI.

AA.3.14 Incomplete data adjustment.

The encounter data was not fully complete. AHCCCS applied completion factors by form type, geographical area and contract year to the encounter data.

4. Establish Rate Category Groupings

AA.4.0: Establish rate category groupings

Please refer to Section II.

AA.4.1: Age

Please refer to Section II.

AA.4.2: Gender

Please refer to Section II.

AA.4.2: Locality/region

Please refer to Section II.

AA.4.2: Eligibility category

Please refer to Section II.

5. Data Smoothing, Special Populations and Catastrophic Claims

AA.5.0: Data smoothing

Please refer to Sections II, III, IV and V.

AA.5.1: Special populations and assessment of the data for distortions

Data was not adjusted for special populations.

AA.5.2: Cost-neutral data smoothing adjustments

AHCCCS has a reinsurance program; please refer to Section VII. AHCCCS also has a delivery supplemental payment program; please refer to Section XIII.

AA.5.3: Risk-adjustment

Please refer to Section XII.

6. Stop Loss, Reinsurance, or Risk-Sharing arrangements

AA.6.1: Commercial reinsurance

There is no commercial reinsurance.

AA.6.2: Simple stop loss program

Please refer to Section VII.

AA.6.3: Risk corridor program

There is the stop loss program (i.e. Reinsurance), and PPC and prospective reconciliations.

7. Incentive Arrangements

A quality improvement incentive withhold pool equal to 1% of actuarially sound capitation rates will be established and paid to Contractors at the time of reconciliation. Please refer to Section X.

XX. Actuarial Certification of the Capitation Rates

I, Windy J. Marks, am an employee of Arizona Health Care Cost Containment System (AHCCCS). I am a Member of the American Academy of Actuaries and a Fellow of the Society of Actuaries. I meet the qualification standards established by the American Academy of Actuaries and have followed the practice standards established from time to time by the Actuarial Standards Board.

The rates were developed using generally accepted actuarial principles and practices and are considered to be actuarially sound. The rates were developed to demonstrate compliance with the CMS requirements under 42 CFR 438.6(c) and are in accordance with applicable laws and regulations. The rates are appropriate for the Medicaid populations covered and Medicaid services to be furnished under the contract. The rates may not be appropriate for any other purpose. The documentation has been included with this certification. The actuarially sound capitation rates that are associated with this certification are effective for the twelve-month period beginning October 1, 2013.

The actuarially sound capitation rates are a projection of future events. It may be expected that actual experience will vary from the values in the rates.

In developing the actuarially sound capitation rates, I have relied upon data and information provided by the Contractors and the AHCCCS internal databases. I have accepted the data without audit and have relied upon the Contractor's auditors and other AHCCCS employees for the accuracy of the data.

1% of the actuarially sound capitation rates will be withheld from monthly capitation payments to Contractors to fund a quality improvement incentive withhold pool. All of the withhold pool amounts will be distributed to Contractors at the time of reconciliation.

This actuarial certification has been based on the actuarial methods, considerations, and analyses promulgated from time to time through the Actuarial Standards of Practice by the Actuarial Standards Board.

This certification letter assumes the reader is familiar with the Acute program, Medicaid eligibility rules and actuarial rating techniques. It is intended for AHCCCS and CMS and should not be relied upon by third parties. Other readers should seek the advice of actuaries or other qualified professionals competent in the area of actuarial rate projections to understand the technical nature of these results.

Windy J. Marks — 08/23/13

Windy J. Marks — Date

Fellow of the Society of Actuaries
Member, American Academy of Actuaries

Appendix I

Prospective Trends

Utilization per 1,000 trends				
Categories of Service	TANF & KidsCare Combined	SSI With Medicare	SSI without Medicare	AHCCCS Care
Hospital Inpatient	0.2%	0.0%	0.0%	0.0%
Outpatient Facility	0.3%	-1.5%	0.7%	-0.9%
Emergency Room	0.8%	-1.3%	3.2%	-1.5%
Physician	0.6%	-1.5%	1.4%	-1.5%
Other Professional	3.8%	2.6%	3.3%	-1.3%
Pharmacy	2.4%	-0.1%	1.5%	-1.5%
Other	n/a	n/a	n/a	n/a

Unit Cost Trends				
Categories of Service	TANF & KidsCare Combined	SSI With Medicare	SSI without Medicare	AHCCCS Care
Hospital Inpatient	1.2%	3.5%	1.0%	0.4%
Outpatient Facility	4.2%	3.7%	2.2%	5.3%
Emergency Room	3.4%	2.4%	2.3%	2.0%
Physician	3.2%	1.7%	2.7%	2.2%
Other Professional	2.4%	1.1%	3.2%	3.1%
Pharmacy	2.2%	2.4%	2.7%	5.0%
Other	n/a	n/a	n/a	n/a

PMPM Trends				
Categories of Service	TANF & KidsCare Combined	SSI With Medicare	SSI without Medicare	AHCCCS Care
Hospital Inpatient	1.4%	3.5%	1.0%	0.4%
Outpatient Facility	4.5%	2.2%	2.9%	4.4%
Emergency Room	4.3%	1.1%	5.7%	0.5%
Physician	3.9%	0.2%	4.1%	0.7%
Other Professional	6.3%	3.7%	6.5%	1.8%
Pharmacy	4.6%	2.3%	4.2%	3.4%
Other	0.7%	1.0%	2.0%	-1.0%

APPENDIX II

Acute Capitation Rate Analysis (Renewal Rates - pending approval)

Point in Time Comparison - no member growth factor

CYE 14

		CYE 14 Projected Member Months [1]	CYE 13 Cap Rate based on CYE 14 Proj Member Months [2]	Total Annual Dollars CYE 13 based on CYE 14 Proj MMs	CYE 14 Gross Cap Rate (before withhold) based on CYE 14 Proj Member Months [2]	Total Annual Dollars CYE 14 (before withhold) based on CYE 14 Proj MMs	Difference CYE 14 Dollars (before withhold) and CYE 13 Dollars	% Increase CYE 14 (before withhold) over CYE 13	CYE 14 Net Cap Rate (after withhold) based on CYE 14 Proj Member Months [2]	Total Annual Dollars CYE 14 (after withhold) based on CYE 14 Proj MMs	Difference CYE 14 Dollars (after withhold) and CYE 13 Dollars	% Increase CYE 14 (after withhold) over CYE 13
TXIX												
	Prospective											
	TANF < 1 [3]	634,720	$ 481.98	$ 305,923,689	$ 461.25	$ 292,767,136	$ (13,156,553)	-4.3%	$ 456.64	$ 289,839,464	$ (16,084,224)	-5.3%
	TANF 1-13 [3]	5,798,573	$ 103.07	$ 597,680,397	$ 99.07	$ 574,438,758	$ (23,241,638)	-3.9%	$ 98.07	$ 568,694,371	$ (28,986,026)	-4.8%
	TANF 14-44F [3]	2,962,319	$ 224.63	$ 665,422,569	$ 233.46	$ 691,586,908	$ 26,164,339	3.9%	$ 231.13	$ 684,671,039	$ 19,248,470	2.9%
	TANF 14-44M [3]	1,426,603	$ 142.85	$ 203,791,759	$ 146.75	$ 209,357,816	$ 5,566,057	2.7%	$ 145.29	$ 207,264,237	$ 3,472,479	1.7%
	TANF 45+ [3]	507,976	$ 375.29	$ 190,640,272	$ 394.94	$ 200,621,102	$ 9,980,831	5.2%	$ 390.99	$ 198,614,891	$ 7,974,620	4.2%
	SSI w/ Medicare	1,030,869	$ 140.32	$ 144,647,836	$ 142.76	$ 147,170,406	$ 2,522,570	1.7%	$ 141.34	$ 145,698,702	$ 1,050,866	0.7%
	SSI w/o Medicare	826,961	$ 731.88	$ 605,239,722	$ 767.04	$ 634,308,061	$ 29,068,340	4.8%	$ 759.36	$ 627,964,981	$ 22,725,259	3.8%
	AHCCCS Care	1,456,766	$ 401.01	$ 584,173,036	$ 398.55	$ 580,597,910	$ (3,575,126)	-0.6%	$ 394.57	$ 574,791,930	$ (9,381,106)	-1.6%
	Newly Eligible Adults [4]	266,959	$ 294.06	$ 78,503,075	$ 294.06	$ 78,503,075	$ -	0.0%	$ 291.12	$ 77,718,044	$ (785,031)	-1.0%
	SFPEP	25,025	$ 14.15	$ 354,082	$ 13.01	$ 325,469	$ (28,614)	-8.1%	$ 13.01	$ 325,469	$ (28,614)	-8.1%
	Delivery Supplemental Payment	35,971	$ 6,086.08	$ 218,925,553	$ 5,925.72	$ 213,157,064	$ (5,768,490)	-2.6%	$ 5,925.72	$ 213,157,064	$ (5,768,490)	-2.6%
	Total Prospective TXIX	14,972,742		$ 3,595,301,988		$ 3,622,833,703	$ 27,531,715	0.8%		$ 3,588,740,192	$ (6,561,797)	-0.2%
	PPC											
	TANF < 1 [3]	13,573	$ 955.32	$ 12,966,614	$ 1,059.33	$ 14,378,343	$ 1,411,730	10.9%	$ 1,059.33	$ 14,378,343	$ 1,411,730	10.9%
	TANF 1-13 [3]	212,778	$ 56.40	$ 12,000,138	$ 56.17	$ 11,950,901	$ (49,237)	-0.4%	$ 56.17	$ 11,950,901	$ (49,237)	-0.4%
	TANF 14-44F [3]	141,969	$ 187.22	$ 26,579,180	$ 194.65	$ 27,634,660	$ 1,055,480	4.0%	$ 194.65	$ 27,634,660	$ 1,055,480	4.0%
	TANF 14-44M [3]	62,200	$ 155.38	$ 9,664,337	$ 165.65	$ 10,303,504	$ 639,166	6.6%	$ 165.65	$ 10,303,504	$ 639,166	6.6%
	TANF 45+ [3]	18,495	$ 305.57	$ 5,651,276	$ 405.86	$ 7,506,119	$ 1,854,842	32.8%	$ 405.86	$ 7,506,119	$ 1,854,842	32.8%
	SSI w/ Medicare	17,331	$ 118.81	$ 2,059,089	$ 93.34	$ 1,617,716	$ (441,374)	-21.4%	$ 93.34	$ 1,617,716	$ (441,374)	-21.4%
	SSI w/o Medicare	33,043	$ 365.79	$ 12,087,003	$ 471.79	$ 15,589,541	$ 3,502,539	29.0%	$ 471.79	$ 15,589,541	$ 3,502,539	29.0%
	AHCCCS Care	69,902	$ 730.72	$ 51,079,334	$ 664.44	$ 46,445,832	$ (4,633,501)	-9.1%	$ 664.44	$ 46,445,832	$ (4,633,501)	-9.1%
	Newly Eligible Adults [4]	12,810	$ 330.04	$ 4,227,761	$ 330.04	$ 4,227,761	$ -	0.0%	$ 330.04	$ 4,227,761	$ -	0.0%
	Total PPC TXIX	582,102		$ 136,314,731		$ 139,654,376	$ 3,339,645	2.4%		$ 139,654,376	$ 3,339,645	2.4%
	Total Title XIX	15,554,844		$ 3,731,616,719		$ 3,762,488,080	$ 30,871,360	0.8%		$ 3,728,394,568	$ (3,222,151)	-0.1%
TXXI												
	KidsCare <1	1,634	$ 481.98	$ 787,396	$ 461.25	$ 753,533	$ (33,863)	-4.3%	$ 461.25	$ 753,533	$ (33,863)	-4.3%
	KidsCare 1-13	125,921	$ 103.07	$ 12,979,133	$ 99.07	$ 12,474,421	$ (504,712)	-3.9%	$ 99.07	$ 12,474,421	$ (504,712)	-3.9%
	KidsCare 14-18 F	23,806	$ 224.63	$ 5,347,512	$ 233.46	$ 5,557,775	$ 210,264	3.9%	$ 233.46	$ 5,557,775	$ 210,264	3.9%
	KidsCare 14-18 M	24,575	$ 142.85	$ 3,510,580	$ 146.75	$ 3,606,462	$ 95,883	2.7%	$ 146.75	$ 3,606,462	$ 95,883	2.7%
	Total TXXI	175,936	$ 952.54	$ 22,624,620	$ 940.53	$ 22,392,191	$ (232,428)	-1.0%	$ 940.53	$ 22,392,191	$ (232,428)	-1.0%
State Only												
	Transplants	48	$ 16.50	$ 792	$ 16.50	$ 792	$ -	0.0%	$ 16.50	$ 792	$ -	0.0%
Grand Total Capitation				$ 3,754,242,131		$ 3,784,881,063	$ 30,638,932	0.8%		$ 3,750,787,551	$ (3,454,580)	-0.1%

Notes

[1] Population estimates for CYE 14 are taken from DBF projections.

[2] Reinsurance levels for CYE 13 include two plans at the $35,000 deductible level and the rest at $20,000. For CYE 14 all plans are at a $25,000 deductible level.

[3] TANF rate cells include SOBRA and Child Expansion groups. Child Expansion are only for those children ages 6-18.

[4] Newly Eligible Adults is a new risk group effective 1/1/2014 thus there was no official rate for that group in CYE 13 and for budget purposes we assume a CYE 13 rate equal to CYE 14 rate.

Arizona Long Term Care System (ALTCS), Elderly and Physically Disabled (EPD) Actuarial Memorandum

I. Purpose

The purpose of this actuarial memorandum is to demonstrate that the Arizona Long Term Care System (ALTCS) Elderly and Physically Disabled (EPD) capitation rates were developed in compliance with 42 CFR 438.6(c). It is not intended for any other purpose.

Arizona Health Care Cost Containment System (AHCCCS) intends to update these capitation rates quarterly on a retroactive basis to reflect enhanced payments to nursing facilities.

The Affordable Care Act (ACA) places an annual fee on the health insurance industry nationwide including most Medicaid health plans effective January 1, 2014. The fee will be allocated to health insurers based on their respective market share of premium revenue in the previous year. Due to the uncertainty of the actual fees and other unknowns, AHCCCS will not be adjusting the capitation rates for this fee at this time, but intends to make a revision once the impacts are known.

II. Overview of Rate Setting Methodology

The contract year ending 2014 (CYE 14) rates were developed as a rate update from the CYE 13 rates as adjusted January 1, 2013 and approved by CMS. These rates represent the twelve month contract period October 1, 2013, through September 30, 2014.

The assumed trend rates were developed from EPD encounter data for CYE 10, CYE 11 and CYE 12. This encounter data was made available to AHCCCS' actuaries via an extract that provides utilization and cost data, referred to as the "databook". Claims' costs observed for all categories of service were then adjusted to reflect program changes and reimbursement reductions that were effective subsequent to the experience periods used, and the May 2012 termination of the EPD contract with the Senior Care Action Network (SCAN) health plan in Maricopa County. Prospective capitation rates for CYE 14 are built up separately for members dually eligible for Medicare and Medicaid ("duals") and members not eligible for Medicare ("non-duals"). The databook contained the information necessary to distinguish duals from non-duals. The dual and non-dual prospective capitation rates are actuarially sound, as are the rates for the Prior Period Coverage (PPC) and Acute Care Only rate cohorts. Those cohorts are not split out into dual and non-dual rates.

Other data sources used in setting the actuarially sound rates and ranges include health plan financial statements, projected changes in the home and community based services (HCBS) placement, and cost of living adjustment (COLA) figures from the Social Security Administration for use in updating the share of cost (SOC) projection for members placed in nursing facilities.

Trend rates were calculated from the databook and other sources on a unit cost and/or utilization basis by category of service (COS). For more information on trends see Section IV Projected Trend Rates.

Ideally, the experience data should be analyzed by different rate cells which are comprised of members with similar risk characteristics. However, segregating the ALTCS population into different rate cells would lead to a statistical credibility problem due to the statewide dispersion of the relatively small membership base. The ALTCS program has four rate cells: a prospective dual rate, a prospective non-dual rate, a prior period coverage (PPC) rate and an Acute Care Only rate. Capitation rates for the ALTCS population do not differ by gender and/or age, but do differ by Geographical Service Area (GSA).

The experience data includes only ALTCS Medicaid eligible expenses for ALTCS Medicaid eligible individuals, as well as reinsurance amounts. The Prior Period Coverage (PPC) rates are reconciled to a maximum 5% profit or loss.

The general process in developing the prospective rates involves:

- trending the CYE 13 projected capitation gross costs PMPM for nursing facility (NF) and HCBS components to the midpoint of the effective period, which is April 1, 2014, and applying the projected mix percentage;
- projecting the CYE 14 gross costs PMPM for acute care;
- making adjustments for share of cost offsets, provider reimbursement changes and program changes;
- applying a deduction of the reinsurance offsets;
- adding the projected case management, administrative expenses, risk/contingency and premium tax to the projected claim PMPMs to obtain the capitation rates.

Each step is described in the sections below. There are also separate sections describing the PPC population and the Acute Care Only population.

III. Gross Costs PMPM by Category of Service

For NF and HCBS components AHCCCS used the gross costs PMPM from the CYE 13 capitation rates and trended those components forward one year to develop the CYE 14 projected gross costs. For the acute component AHCCCS used actual CYE 12 encounter data, with completion factors, and trended that component forward two years to develop the CYE 14 projected acute component gross cost. The encounter data was reviewed and audited for accuracy, timeliness and completeness through encounter validation studies as well as studies comparing the encounter data to the Contractors' financial statements.

IV. Projected Trend Rates

The trend calculation is based on the time period from October 1, 2009 through September 30, 2012. The claim PMPMs were computed on a yearly basis and a trend factor was calculated. Trend factors are built up separately for dual, non-dual, and

PPC. Trend factors also vary by COS. The trend rates developed were used to bring the base encounter data and gross cost projections from previous periods to the effective midpoint of the contract year.

The trend rates used in projecting the claim costs by rate cell and category of service are identified in Table I. The trend rates shown below in Table I do not include AHCCCS FFS provider rate changes.

Table I: Average Annual Trend Rate before Mix and SOC

	NF	HCBS	Acute
Prospective Dual	1.7%	0.6%	-1.4%
Prospective Non-Dual	2.9%	2.0%	-3.9%
PPC	-1.4%	-5.7%	39.0%

V. Projected Gross Claim PMPM

The contract period for CYE 14 rates is October 1, 2013, through September 30, 2014, so the midpoint is April 1, 2014. The claims' PMPMs from the base data were trended to the midpoint of the CYE 14 rate period.

VI. Mix Percentage

The CYE 14 dual and non-dual mix percentages are set using a combination of current placement percentages, program growth/saturation and the number of ALTCS members. These sources were reviewed by Contractor and by county. The HCBS mix percentages can be found in Table II.

Table II: HCBS Mix Percentages (Dual and Non-Dual)

			CYE13 HCBS Mix		CYE14 HCBS Mix	
GSA	County	Plan	Dual	Non-Dual	Dual	Non-Dual
40	Pinal/Gila	Bridgeway	74.10%	85.24%	74.23%	82.30%
42	LaPaz/Yuma	UHC LTC	61.63%	74.38%	61.79%	74.95%
44	Apache/Coconino/Mohave/Navajo	UHC LTC	68.31%	80.31%	67.77%	76.62%
46	Cochise/Graham/Greenlee	Bridgeway	60.54%	76.45%	59.28%	73.50%
48	Yavapai	UHC LTC	61.62%	78.17%	62.12%	79.11%
50	Pima/Santa Cruz	UHC LTC	72.42%	82.59%	74.72%	83.53%
50	Pima	Mercy Care	65.60%	71.64%	66.00%	71.16%
52	Maricopa	Bridgeway	78.82%	77.85%	77.49%	75.65%
52	Maricopa	UHC LTC	69.58%	79.16%	69.98%	78.48%
52	Maricopa	Mercy Care	74.17%	80.55%	74.12%	81.41%
Statewide Total			71.96%	79.44%	71.94%	79.11%

VII. State Mandates, Court Ordered Programs, Program Changes and Other Changes

Children's Rehabilitative Services (CRS) Costs Moving to EPD

Some EPD members with special health care needs receive services related to specific conditions through the Children's Rehabilitative Services (CRS) program at that same time they are enrolled with an EPD Contractor for unrelated physical health services, and long-term care and behavioral health services. Effective October 1, 2013, the CRS-specific services for those members will be delivered through the members' EPD Contractors in order to integrate total member service delivery through a single Contractor. This results in a shift of approximately $5.5 million to EPD Contractors for CYE 14. The anticipated impact varies by Contractor and GSA.

Provider Rate Changes

Effective October 1, 2013, AHCCCS is increasing FFS provider rates for certain providers based either on access to care needs, Medicare or ADHS fee schedule rates, legislative mandates, or cost of living adjustments. The unit cost (inflation) trends were adjusted appropriately for these changes. The estimated statewide impact is an increase of approximately $13.1 million.

Medical Management Changes

The State of Arizona's 2013 Health and Welfare Budget Reconciliation Bill (BRB) reinstated well visits, which were previously eliminated October 1, 2010, as a covered service for enrolled adults for federal fiscal year 2014. The estimated statewide impact is an increase of approximately $84,000.

Primary Care Provider (PCP) Payment Increase

Section 1902(a)(13)(C) of the Social Security Act, as amended by the Affordable Care Act, requires minimum levels of Medicaid payment for certain primary care services, provided by certain physicians. The AHCCCS managed care model, with strict requirements regarding actuarially-sound capitation rates, necessitates that Contractors be funded for expected cost increases due to primary care rate parity. AHCCCS proposes to provide Contractors the necessary funds to increase primary care payments by using Model 3: Non-risk Reconciled Payments for Enhanced Rates as referenced in the *Medicaid Managed Care Payment for PCP Services in 2013 and 2014, Technical Guidance and Rate Setting Practices* (Technical Guidance) document released by CMS.

In summary, under Model 3, prospective capitation rates would not be adjusted for the enhanced primary care payments. Rather, AHCCCS would query actual encounter data on a quarterly basis to calculate the total payments that eligible providers were paid for eligible services in order to reach the mandated enhanced payment rates. Once the data on this report is verified, AHCCCS would pay the Contractors the calculated additional payment amounts. A more detail explanation of the process and methodology can be found in the Actuarial Certification submitted to CMS for approval of AHCCCS methodology. There is no impact to the CYE 14 capitation rates.

In-Lieu of Services

Included in the base rates is funding for "in lieu of" services, substituting cost-effective alternative inpatient settings in place of more costly inpatient non-specialty hospital placements. State approved FFS rates at inpatient non-specialty hospitals are approximately 93.5% more expensive than those provided in alternative inpatient settings. The proposed capitation rates allow for the provision of services in alternative inpatient settings that are licensed by Arizona Department of Health Services/Arizona Licensing Services/Office of Behavioral Health License, in lieu of services in an inpatient non-specialty hospital, thus no increase to cap rates is included.

VIII. Projected Net Claim PMPM

The NF and HCBS projected gross claim PMPMs were adjusted for the mix percentages. The projected gross claims PMPMs were then discounted for the recipients' Share of Cost (SOC). The SOC component is fully reconciled with each Contractor. To develop the reinsurance offset PMPM AHCCCS used actual CYE 12 reinsurance payment data and trended forward two years using the trend assumption from the acute component of the capitation rates. The calculation of the reinsurance offset PMPM was performed separately for dual and non-dual members.

IX. Coordination of Benefits

Inherent in the encounter and financial data are unit cost trends which incorporate Contractors' Coordination of Benefits (COB) activities. AHCCCS provides Contractors with verified commercial and Medicare coverage information for their members which Contractors utilize to ensure payments are not made for medical services that are covered by the other carriers. When Contractors make a payment to cover members' coinsurance, deductibles, or Medicaid-covered services that are not covered by the other carriers, they submit encounters containing these reduced amounts. From state fiscal year (SFY) 2008 to SFY 2013, encounter-reported COB cost avoidance grew by greater than 128%, from $130 million to $297 million. Additionally, in CYE 2013 ALTCS EPD Contractors cost-avoided $61 million in the nine months ending March 31, 2013, in additional claims for which the Contractor had no financial obligation after the private insurance or Medicare payment was made. Consequently no encounters were submitted to AHCCCS and thus those services are excluded from capitation expenditure projections completely. AHCCCS continues to emphasize the importance of COB activities.

X. Case Management, Administrative Expenses and Risk Contingency

The Case Management rates represent those rates awarded as part of the CYE 12 RFP process, adjusted for expected growth in the HCBS mix, which would increase case management expenses. The administrative expenses also represent rates awarded as part of the RFP process. The risk contingency percentage remains the same as CYE 13 at 1%.

XI. Proposed Capitation Rates and Their Impacts

The proposed capitation rates for the EPD population equal the sum of the projected net claim PMPM (in Section VIII) and the projected case management, administrative expenses and risk contingency PMPM (in section X) divided by one minus the two percent premium tax. Tables IIIa and IIIb show the proposed dual and non-dual capitation rates for the EPD population statewide.

Table IIIa: Statewide Projected Net Capitation PMPM EPD - Dual

Service Category	Gross CYE13 Rate	Mix	Net CYE13 Rate	Pct Gross Change	Pct Net Change	Gross CYE14 Rate	Mix	Net CYE14 Rate
Nursing Facility (NF)	$5,538.45	28.04%	$1,553.26	3.2%	3.3%	$5,717.71	28.06%	$1,604.59
Share of Cost			($268.16)		-6.3%			($251.31)
Net Nursing Facility			$1,285.09		5.3%			$1,353.28
Home/Community (HCBS)	$1,397.40	71.96%	$1,005.50	2.3%	2.2%	$1,428.87	71.94%	$1,027.88
Case Management			$113.55		0.2%			$113.74
Acute Care			$137.77		-5.2%			$130.61
Administration			$166.84		-0.4%			$166.24
Risk Contingency			$27.90		2.6%			$28.64
Premium Tax			$55.85		3.1%			$57.56
Net Capitation PMPM			$2,792.50		3.1%			$2,877.94

Table IIIb: Statewide Projected Net Capitation PMPM EPD - Non-Dual

Service Category	Gross CYE13 Rate	Mix	Net CYE13 Rate	Pct Gross Change	Pct Net Change	Gross CYE14 Rate	Mix	Net CYE14 Rate
Nursing Facility (NF)	$6,784.50	20.56%	$1,395.22	4.1%	5.7%	$7,060.54	20.89%	$1,474.94
Share of Cost			($32.19)		0.7%			($32.41)
Net Nursing Facility			$1,363.03		5.8%			$1,442.53
Home/Community (HCBS)	$1,719.72	79.44%	$1,366.06	3.6%	3.2%	$1,781.70	79.11%	$1,409.50
Case Management			$114.26		0.1%			$114.34
Acute Care			$1,311.29		6.7%			$1,398.82
Administration			$162.72		0.2%			$163.08
Risk Contingency			$50.01		0.0%			$50.01
Premium Tax			$89.13		4.8%			$93.43
Net Capitation PMPM			$4,456.50		4.8%			$4,671.72

Note: The product of the gross NF or HCBS rate and mix percentages as shown may not equal the net rate due to rounding.

XII. Acute Care Only Members

As in prior years, for members who are only eligible for acute care services in the ALTCS program, Contractors will be paid the combined acute care component plus the case management and administrative components. Since the reinsurance policy is the same for these members as for the other ALTCS members, the same reinsurance offset is appropriate.

XIII. Prior Period Coverage (PPC) Rates

PPC rates cover the period of time from the effective date of eligibility to the day a member is enrolled with the Contractor. AHCCCS developed the CYE 14 PPC rates by applying a trend factor to the CYE 13 rates. The trend calculation is based on the time period from October 1, 2009 through September 30, 2012. Due to the relatively short PPC enrollment period and low member month counts, AHCCCS' actuaries combined geographic regions in order to enhance statistical credibility when needed. Since PPC costs are highly volatile and unable to be managed by the Contractors, AHCCCS limits the magnitude of the rate change for each geographic area. PPC rates are reconciled to a five percent profit/loss corridor.

XIV. Proposed Capitation Rates and Budget Impact

Table IV includes the net capitation rates on a statewide basis for all rate cells as well as the estimated budget impact based off of CYE 14 projected member months. The adjustments impact Contractors ranging from +3.0% to +5.0%. Appendix I shows EPD rates by geographical service area and Contractor.

Table IV: Proposed Capitation Rates and Budget Impact

Rate Cell	EPD Prospective - Dual	EPD Prospective - Non-Dual	PPC	Acute Only	Total
CYE 14 Projected MMs	258,191	48,965	11,186	4,744	
CYE 13 Rate (1/1/13)	$2,792.50	$4,456.50	$855.56	$497.57	
CYE 14 Rate	$2,877.94	$4,671.72	$899.76	$511.80	
Estimated CYE 13 Capitation	$720,998,611	$218,211,329	$9,570,627	$2,360,400	$951,140,967
Estimated CYE 14 Capitation	$743,058,157	$228,749,601	$10,065,065	$2,427,905	$984,300,728
Dollar Impact	$22,059,546	$10,538,272	$494,438	$67,505	$33,159,762
Percentage Impact	3.1%	4.8%	5.2%	2.9%	3.5%

XV. CMS Rate Setting Checklist

1. Overview of rate setting methodology

A.A.1.0: Overview of rate setting methodology

AHCCCS is performing a rate update from the previously approved contract year ending 2013 (CYE 13) rates under 42 CFR 438.6(c). Please refer to Section II.

AA.1.1: Actuarial certification

Please refer to Section XVI.

AA.1.2: Projection of expenditure

Please refer to Section XIV.

AA.1.3: Procurement, prior approval and rate setting

AHCCCS is operating under the Competitive Procurement contracting method.

AA.1.5: Risk contract

The contract is an at risk contract.

AA.1.6: Limit on payment to other providers

AHCCCS makes no additional payment to the providers, except for Disproportionate Share Hospital (DSH), Graduate Medical Education (GME) and Critical Access Hospitals. GME is paid in accordance with state plan. DSH and Critical Access Hospital payments are paid in accordance with Waiver Special Terms and Conditions. None of the additional payments to the providers were included in the capitation calculation.

AA.1.7: Rate modification

Please refer to Sections III, IV, VI, VII, VIII, XII, and XIII.

XVI. Actuarial Certification of the Capitation Rates

I, Matthew C. Varitek, am an employee of Arizona Health Care Cost Containment System (AHCCCS). I am a Member of the American Academy of Actuaries and a Fellow of the Society of Actuaries. I meet the qualification standards established by the American Academy of Actuaries and have followed the practice standards established from time-to-time by the Actuarial Standards Board.

The rates were developed using generally accepted actuarial principles and practices and are considered to be actuarially sound. The rates were developed to demonstrate compliance with the CMS requirements under 42 CFR 438.6(c) and are in accordance with applicable laws and regulations. The rates are appropriate for the Medicaid populations covered and Medicaid services to be furnished under the contract. The rates may not be appropriate for any other purpose. The documentation has been included with this certification. The actuarially sound capitation rates that are associated with this certification are effective for the twelve-month period beginning October 1, 2013.

The actuarially sound capitation rates are a projection of future events. It may be expected that actual experience will vary from the values in the rates.

In developing the actuarially sound capitation rates, I have relied upon data and information provided by the Program Contractors and the AHCCCS internal databases. I have accepted the data without audit and have relied upon the Program Contractors auditors and other AHCCCS employees for the accuracy of the data.

This actuarial certification has been based on the actuarial methods, considerations, and analyses promulgated from time to time through the Actuarial Standards of Practice by the Actuarial Standards Board.

This certification letter assumes the reader is familiar with the EPD program, Medicare and Medicaid eligibility rules and actuarial rating techniques. It is intended for AHCCCS and CMS and should not be relied upon by third parties. Other readers should seek the advice of actuaries or other qualified professionals competent in the area of actuarial rate projections to understand the technical nature of these results.

Matthew C. Varitek 08.28.2013

Matthew C. Varitek Date

Fellow of the Society of Actuaries
Member, American Academy of Actuaries

Appendix I

GSA	County	Contractor	EPD Dual	EPD Non-Dual	Acute Only	PPC
40	Pinal/Gila	Bridgeway	$3,031.61	$4,341.89	$475.58	$985.24
42	LaPaz/Yuma	UHC LTC	$2,954.83	$4,089.22	$464.85	$985.24
44	Apache/Coconino/Mohave/Navajo	UHC LTC	$2,486.88	$4,454.40	$442.81	$985.24
46	Cochise/Graham/Greenlee	Bridgeway	$2,936.61	$4,306.48	$441.19	$985.24
48	Yavapai	UHC LTC	$3,119.45	$4,386.19	$375.43	$985.24
50	Pima/Santa Cruz	UHC LTC	$2,821.21	$4,245.36	$378.66	$733.38
50	Pima	Mercy Care	$3,082.38	$4,980.13	$496.09	$733.38
52	Maricopa	Bridgeway	$2,616.67	$5,136.17	$496.08	$899.90
52	Maricopa	UHC LTC	$2,871.00	$4,816.84	$353.47	$899.90
52	Maricopa	Mercy Care	$2,962.57	$4,686.70	$576.01	$899.90

Children's Rehabilitative Services (CRS)
Actuarial Memorandum for CYE 2014

I. Purpose

The purpose of this actuarial memorandum is to demonstrate that the Children's Rehabilitative Services (CRS) capitation rates were developed in compliance with 42 CFR 438.6(c). It is not intended for any other purpose.

The Affordable Care Act (ACA) places an annual fee on the health insurance industry nationwide including most Medicaid health plans effective January 1, 2014. The fee will be allocated to health insurers based on their respective market share of premium revenue in the previous year. Due to the uncertainty of the actual fees and other unknowns, AHCCCS will not be adjusting the capitation rates for this fee at this time, but intends to make a revision once the impacts are known.

The historical CRS carve-out program provides specialty services to children with special health care needs. Children qualify for CRS based on particular diagnoses, and currently a CRS member receives services specific to the health condition that qualifies him/her for CRS through the sole CRS Contractor. However, that same member may currently receive other acute care services through a different Contractor or through the American Indian Health Plan (AIHP), they may receive long-term care services through a different Contractor or the American Indian Fee-for-Service environment, and they may receive behavioral health services through a Regional Behavioral Health Authority (RBHA) or a Tribal Regional Behavioral Health Authority (TRBHA).

Beginning October 1, 2013, AHCCCS is integrating all services for most Acute Care Program children with CRS conditions through one CRS Contractor with the goals of improved member outcomes, reduced member confusion, improved care coordination, and streamlined administration. At the same time, children with CRS conditions who are enrolled in the long term care program, and who today have integrated acute and long term care services, will begin to receive their CRS related services through the Arizona Long Term Care System (ALTCS) Contractors.

II. Overview of Bid, Rate Setting Methodology and Base Period Experience

Contract year ending 2014 (CYE 14) is the first year of a new cycle for the CRS contract. The medical component of the contract year ending 2014 (CYE 14) rates were developed as a rate rebase in order to include experience data for acute care and behavioral health services received by CRS members. The administrative component of the CYE 14 rates are the rates awarded as part of the competitive bid process for the CYE 14 Request for Proposal (RFP). The CYE 14 rates cover the twelve month contract period of October 1, 2013 through September 30, 2014.

There are four permutations of the program enrollment, hereafter called "coverage types" and described as follows:

- A Fully Integrated member will receive acute care, behavioral health, and specialty care for CRS conditions through the sole CRS contractor.

- A Partially Integrated-BH member will receive behavioral health and specialty care through the sole CRS contractor. These members are typically enrolled with the Developmentally Disabled (DD) or the Comprehensive Medical and Dental Program (CMDP) for their acute care services.

- A Partially Integrated-Acute member will receive acute care and specialty care through the sole CRS contractor. These members are typically Native Americans receiving behavioral health services through a TRBHA.

- A CRS Only member will only receive specialty care through the sole CRS contractor. These members are typically enrolled in the American Indian Health Plan (AIHP), receiving acute care in a fee-for-service environment, and receiving behavioral health services through a TRBHA.

Since CRS has a relatively small membership base, multiple years and sources of data were used to increase the statistical credibility. For CYE 14 rate development, CRS' encounter data was found to be appropriate for all service categories, except clinic fees. For all categories other than clinic fees the base year experience includes encounters with dates of service between October 1, 2009 and March 31, 2012. Completion and credibility factors were added to the encounter data. CRS did not begin encountering clinic fees until January 2011 thus limited encounter data is available for these expenses. Consequently, financial statement data for CYE 09 through CYE 12 was used to estimate the CYE 14 clinic expenses. That forecast also incorporates anticipated changes to clinic reimbursement due to a location and administrative change for the Maricopa County clinic. The per member per month (PMPM) claim costs observed for all categories of service were then adjusted to reflect program changes and reimbursement reductions that were effective subsequent to the experience periods used.

The assumed trend rates were developed from an internal data extract ("databook") that tracks historical enrollment, as well as utilization counts and unit costs for encounters adjudicated by AHCCCS. Other data sources include Contractor financial statements, AHCCCS Fee-For-Service rate changes, anticipated Arizona Department of Health Services (ADHS) transportation increases, programmatic changes, and CMS statistics on national health expenditures (NHEs).

Because of the relatively small membership base and statewide disbursement of members, segregating the CRS population into different rate cells with similar risk characteristics would lead to a statistical credibility problem. Therefore, AHCCCS believes that a single CRS capitation rate for each coverage type leads to a more actuarially sound rate than creating additional rate cells.

The experience includes all Medicaid eligible expenses for CRS Medicaid eligible individuals. In addition, the experience includes reinsurance amounts. For CYE 14 the CRS capitation rates will be reconciled using a tiered reconciliation methodology. See Section XI for additional information. There are no other incentives or risk sharing arrangements.

The base period claim PMPMs for each of the acute, behavioral, and specialty components are built up from utilization and unit cost data for the experience period, adjusted for completion estimates, adjusted for programmatic and AHCCCS Fee-For-Service (FFS) provider rate changes, and trended to the midpoint of the effective period, April 1, 2014. The trended PMPMs for each component are added together as appropriate for each of the four coverage types described in this Section. The administrative expense from the successful Offeror, risk/contingency, reinsurance offset and premium tax are then added to the projected claim PMPMs to obtain the capitation rates. Each step is described in the sections below.

III. Projected Trend Assumptions

PMPM trend rates were calculated from the encounter data experience for CYE 09, CYE 10, CYE 11 and CYE 12 dates of service. Financial statements for the same time periods were used to validate the encounter data and trends. The trend rates shown below in Table I do not include AHCCCS FFS provider rate changes.

The trend rates used in projecting the claim costs are as follows:

Table I: Annual Trend Rates by Program Component and Service Category

Program Component	Service Category	PMPM Trend
Acute Care	Inpatient	1.5%
Acute Care	Outpatient	6.5%
Acute Care	Professional	4.9%
Acute Care	Pharmacy	0.1%
Acute Care	Long-Term Care	-4.7%
Acute Care	Dental	2.7%
Behavioral Health	Inpatient	-2.2%
Behavioral Health	Professional	4.8%
Behavioral Health	Pharmacy	2.4%
Specialty Care	Inpatient	-2.2%
Specialty Care	Outpatient	1.6%
Specialty Care	Professional	3.5%
Specialty Care	Pharmacy	-3.2%
Specialty Care	Long-Term Care	0.3%
Specialty Care	Dental	-2.2%

IV. Projected Gross Claim PMPM

The claims PMPMs for each contract year in the experience period were trended from the midpoint of the contract year to the midpoint of the rating period. The midpoint of the rating period is April 1, 2014.

V. State Mandates, Court Ordered Programs, Program Changes and Other Changes

Provider Rate Changes

Effective October 1, 2013, AHCCCS is increasing FFS provider rates for certain providers based either on access to care needs, Medicare or ADHS fee schedule rates, legislative mandates, or cost of living adjustments. The unit cost (inflation) trends were adjusted appropriately for these changes. The estimated statewide impact is an increase of approximately $1.9 million.

Primary Care Provider (PCP) Payment Increase

Section 1902(a)(13)(C) of the Social Security Act, as amended by the Affordable Care Act, requires minimum levels of Medicaid payment for certain primary care services, provided by certain physicians. The AHCCCS managed care model, with strict requirements regarding actuarially-sound capitation rates, necessitates that Contractors be funded for expected cost increases due to primary care rate parity. AHCCCS proposes to provide Contractors the necessary funds to increase primary care payments by using Model 3: Non-risk Reconciled Payments for Enhanced Rates as referenced in the *Medicaid Managed Care Payment for PCP Services in 2013 and 2014, Technical Guidance and Rate Setting Practices* (Technical Guidance) document released by CMS.

In summary, under Model 3, prospective capitation rates would not be adjusted for the enhanced primary care payments. Rather, AHCCCS would query actual encounter data on a quarterly basis to calculate the total payments that eligible providers were paid for eligible services in order to reach the mandated enhanced payment rates. Once the data on this report is verified, AHCCCS would pay the Contractors the calculated additional payment amounts. A more detail explanation of the process and methodology can be found in the Actuarial Certification submitted to CMS for approval of AHCCCS methodology. There is no impact to the CYE 14 capitation rates.

In-Lieu of Services

Included in the base rates is funding for "in lieu of" services, substituting cost-effective alternative inpatient settings in place of more costly inpatient non-specialty hospital placements. State approved FFS rates at inpatient non-specialty hospitals are approximately 93.5% more expensive than those provided in alternative inpatient settings. The proposed capitation rates allow for the provision of services in alternative inpatient settings that are licensed by ADHS/Arizona Licensing Services/Office of Behavioral Health License, in lieu of services in an inpatient non-specialty hospital, thus no increase to cap rates is included.

VI. Projected Net Claim PMPM

The base period utilization, unit costs, and net claims' PMPMs are trended forward and adjusted for AHCCCS fee schedule changes, state mandates, court ordered programs and program changes to arrive at the CYE 14 utilization, unit costs and net claims' PMPMs.

VII. Projected Reinsurance Offsets

The projected CYE 14 reinsurance offsets were developed using CYE12 encounter data and reinsurance payment information. The projected CYE 14 reinsurance offsets take into consideration that a single threshold for reinsurance will apply to the total encounters incurred under all of the program components for which each member is enrolled.

VIII. Coordination of Benefits

Inherent in the encounter and financial data are unit cost trends which incorporate Contractors' Coordination of Benefits (COB) activities. AHCCCS provides Contractors with verified commercial and Medicare coverage information for their members which Contractors utilize to ensure payments are not made for medical services that are covered by the other carriers. When Contractors make a payment to cover members' coinsurance, deductibles, or Medicaid-covered services that are not covered by the other carriers, they submit encounters containing these reduced amounts. From state fiscal year (SFY) 2008 to SFY 2013, encounter-reported COB cost avoidance grew from $34,000 to $7.7 million. Additionally, in CYE 13 the CRS Contractor cost-avoided $667,000 in the nine months ending March 31, 2013, in claims for which the Contractor had no financial obligation after the private insurance or Medicare payment was made. Consequently no encounters were submitted to AHCCCS and thus those services are excluded from capitation expenditure projections completely. AHCCCS continues to emphasize the importance of COB activities.

IX. Administrative Expenses and Risk Contingency

The administrative expense PMPM bid by the successful Offeror was adjusted by AHCCCS to cover additional administrative responsibility and is built into the rates. The risk contingency load is set at 1%.

X. Proposed Capitation Rates and Their Impact

The proposed capitation rates equal the sum of the projected net claim PMPM (in Section VI) less the reinsurance offsets (in section VII), the awarded administrative expenses, and the risk contingency PMPM (in section IX), divided by one minus two percent for premium tax. Table II below summarizes the projected member months, proposed capitation rates, and estimated total capitation by coverage type and in total on a statewide basis.

Table II: Proposed Capitation Rates by Coverage Type

	Projected Member Months October 1, 2013 - September 30, 2014	CYE 14 Proposed Rate	Estimated CYE 14 Capitation
Fully Integrated	213,069	$741.22	$157,930,542
Partially Integrated/BHS	75,943	$478.75	$36,357,592
Partially Integrated/Acute	1,895	$656.43	$1,243,769
CRS Only	13,955	$393.96	$5,497,521
Statewide Total	304,861		$201,029,424

XI. CMS Rate Setting Checklist

1. Overview of rate setting methodology

AA.1.1: Actuarial certification

Please refer to Section XII.

AA.1.2: Projection of expenditure

Please refer to Section X.

AA.1.3: Procurement, prior approval and rate setting

AHCCCS is operating under the Competitive Procurement contracting method.

AA.1.5: Risk contract

The contract is an at risk contract, however there are some provisions for reconciliations and reinsurance. The reconciliation is as follows:

Profit	MCO Share	State Share	Maximum Contractor Profit
<=3%	100%	0%	3.0%
>3% and <=6%	50%	50%	1.5%
>6%	0%	100%	0%
Total			4.5%

Loss	MCO Share	State Share	Maximum Contractor Loss
<=3%	100%	0%	3.0%
>3%	0%	100%	0%
Total			3.0%

AA.1.6: Limit on payment to other providers

AHCCCS makes no additional payment to providers, except for DSH, GME, and Critical Access Hospitals. GME is paid in accordance with state plan. DSH and Critical Access Hospital payments are paid in accordance with the Waiver Special Terms and Conditions. None of the additional payments to providers were included in the capitation calculation.

AA.1.7: Rate modification

Please refer to Sections II, III, V, VII and IX.

2. Base Year Utilization and Cost Data

AA.2.0: Base year utilization and cost data

Please refer to Section II.

AA.2.1: Medicaid eligibles under the contract

The data includes only those members eligible for managed care.

AA.2.2: Spenddown

Not applicable, not covered under this contract.

AA.2.3: State plan services only

The contract between AHCCCS and the Contractor specifies that the Contractor may cover additional services. Non-covered services were not included in the encounter data used to set the rates.

AA.2.4: Services that can be covered by a capitated entity out of contract savings.

Same as AA.2.3

3. Adjustments to the Base Year Data

AA.3.0 Adjustments to base year data

Please refer to Section II, III, V and VII.

AA.3.1 Benefit differences

Please refer to Sections I and II for descriptions of the benefits provided under the integrated contract and the four coverage types.

AA.3.2 Administrative cost allowance calculation

Please refer to Section IX.

AA.3.3 Special populations' adjustment

It is anticipated that the risk characteristics of this population will not change materially from the base period to the effective period of the capitation rates. Therefore, no adjustment was made.

AA.3.4 Eligibility Adjustments

No adjustment was made.

AA.3.5 DSH Payments

No DSH payments were included in the capitation development

AA.3.6 Third party Liability (TPL)

This is a contractual arrangement between AHCCCS and the Contractors.

AA.3.7 Copayments, coinsurance and deductible in the capitated rates

Not applicable, member cost sharing is not required.

AA.3.8 Graduate Medical Education (GME)

The experience excludes any payments for GME.

AA.3.9 FQHC and RHC reimbursement

The experience excludes any additional payments that FQHCs may receive from the State.

AA.3.10 Medical cost/ trend inflation

Please refer to Section III.

AA.3.11 Utilization adjustment

Other than trend, no specific adjustment was made to utilization.

AA.3.12 Utilization and cost assumptions

Not applicable, since actual experience was used.

AA.3.13 Post-eligibility treatment of income (PETI)

Not applicable, not required to consider PETI.

AA.3.14 Incomplete data adjustment.

The encounter data was not fully complete. AHCCCS applied completion factors by form type and contract year to the encounter data.

4. Establish Rate Category Groupings

AA.4.0: Establish rate category groupings

Please refer to Section II.

AA.4.1: Age

Please refer to Section II.

AA.4.2: Gender

Please refer to Section II.

AA.4.2: Locality/region

Please refer to Section II.

AA.4.2: Eligibility category

Please refer to Section II.

5. Data Smoothing, Special Populations and Catastrophic Claims

AA.5.0: Data smoothing

Please refer to Section II.

AA.5.1: Special populations and assessment of the data for distortions

Data was not adjusted for special populations.

AA.5.2: Cost-neutral data smoothing adjustments

There was no cost-neutral data smoothing adjustments

AA.5.3: Risk-adjustment

There is no other risk adjustment, except for reconciliation and reinsurance.

6. Stop Loss, Reinsurance, or Risk-Sharing arrangements

AA.6.1: Commercial reinsurance

There is no commercial reinsurance.

AA.6.2: Simple stop loss program

AHCCCS has a reinsurance program. Please refer to Section VII.

AA.6.3: Risk corridor program

There is the stop loss program (i.e. Reinsurance) and a reconciliation for the CRS population.

7. Incentive Arrangements

At this time there are no incentive arrangements.

XII. Actuarial Certification of the Capitation Rates

I, Matt Varitek, am an employee of Arizona Health Care Cost Containment System (AHCCCS). I am a Member of the American Academy of Actuaries and a Fellow of the Society of Actuaries. I meet the qualification standards established by the American Academy of Actuaries and have followed the practice standards established from time-to-time by the Actuarial Standards Board.

The rates were developed using generally accepted actuarial principles and practices and are considered to be actuarially sound. The rates were developed to demonstrate compliance with the CMS requirements under 42 CFR 438.6(c) and are in accordance with applicable laws and regulations. The rates are appropriate for the Medicaid populations covered and Medicaid services to be furnished under the contract. The rates may not be appropriate for any other purpose. The documentation has been included with this certification. The actuarially sound capitation rates that are associated with this certification are effective for the twelve month period beginning October 1, 2013.

The actuarially sound capitation rates are a projection of future events. It may be expected that actual experience will vary from the values in the rates.

In developing the actuarially sound capitation rates, I have relied upon data and information provided by the health plan and the AHCCCS internal databases. I have accepted the data without audit and have relied upon the health plan auditors and other AHCCCS employees for the accuracy of the data.

This actuarial certification has been based on the actuarial methods, considerations and analyses promulgated from time-to-time through the Actuarial Standards of Practice by the Actuarial Standards Board.

This certification letter assumes the reader is familiar with the CRS program, Medicaid eligibility rules and actuarial rating techniques. It is intended for AHCCCS and CMS and should not be relied upon by third parties. Other readers should seek the advice of actuaries or other qualified professionals competent in the area of actuarial rate projections to understand the technical nature of these results.

Matthew C. Varitek 08.23.2013

Matthew C. Varitek Date

Fellow of the Society of Actuaries
Member, American Academy of Actuaries

Comprehensive Medical and Dental Program (CMDP)
Updated Actuarial Memorandum for CYE 2013

I. Purpose

This memorandum presents a discussion of the revision to the capitation rates for the Comprehensive Medical and Dental Program (CMDP) program, for the period October 1, 2013 to December 31, 2013. This update to the rates is required due to changes to the AHCCCS Fee-for-Service (FFS) provider rate schedule effective October 1, 2013. The purpose of this actuarial memorandum is to demonstrate that the updated capitation rates were developed in compliance with 42 CFR 438.6(c). It is not intended for any other purpose.

Effective October 1, 2013, AHCCCS is increasing FFS provider rates for certain providers based either on access to care needs, Medicare or ADHS fee schedule rates, legislative mandates, or cost of living adjustments. The unit cost (inflation) trends were adjusted appropriately for these changes. The estimated three month statewide impact is an increase of approximately $72,600.

II. Proposed Revised Capitation Rates and Their Impact

Table I below summarizes the changes from the current approved CYE 13 capitation rates and the estimated budget impact, effective for the period October 1, 2013 through December 31, 2013 on a statewide basis.

Table I: Proposed Statewide Capitation Rates and Budget Impact

Rate Cell	Projected Oct-Dec 2013 Member Months	CYE 13 Rate (1/1/13)	CYE 13 Rate (10/1/13)	Estimated Oct-Dec 2013 Capitation (1/1 Rates)	Estimated Oct-Dec 2013 Capitation (10/1 Rates)	Dollar Impact	Percentage Impact
Prospective	41,726	$222.08	$223.79	$9,266,525	$9,337,877	$71,352	0.8%
PPC	977	$368.88	$370.18	$360,266	$361,536	$1,270	0.4%
Total				$9,626,791	$9,699,413	$72,622	0.8%

III. Actuarial Certification of the Capitation Rates

I, Matthew C. Varitek, am an employee of Arizona Health Care Cost Containment System (AHCCCS). I am a Member of the American Academy of Actuaries and a Fellow of the Society of Actuaries. I meet the qualification standards established by the American Academy of Actuaries and have followed the practice standards established from time-to-time by the Actuarial Standards Board.

The rates were developed using generally accepted actuarial principles and practices and are considered to be actuarially sound. The rates were developed to demonstrate compliance with the CMS requirements under 42 CFR 438.6(c) and are in accordance with applicable laws and regulations. The rates are appropriate for the Medicaid populations covered and Medicaid services to be furnished under the contract. The rates may not be appropriate for any other purpose. The documentation has been included with this certification. The actuarially sound capitation rates that are associated with this certification are effective for the three month period beginning October 1, 2013.

The actuarially sound capitation rates are a projection of future events. It may be expected that actual experience will vary from the values in the rates.

In developing the actuarially sound capitation rates, I have relied upon data and information provided by CMDP and AHCCCS internal database. I have accepted the data without audit and have relied upon the CMDP auditors and other AHCCCS employees for the accuracy of the data.

This actuarial certification has been based on the actuarial methods, considerations and analyses promulgated from time-to-time through the Actuarial Standards of Practice by the Actuarial Standards Board.

This certification letter assumes the reader is familiar with the CMDP program, Medicaid eligibility rules and actuarial rating techniques. It is intended for AHCCCS and CMS and should not be relied upon by third parties. Other readers should seek the advice of actuaries or other qualified professionals competent in the area of actuarial rate projections to understand the technical nature of these results.

Matthew C. Varitek 08.23.2013

Matthew C. Varitek Date

Fellow of the Society of Actuaries
Member, American Academy of Actuaries

Arizona Long Term Care System (ALTCS), Department of Economic Security/Division of Developmental Disabilities (DES/DDD) Actuarial Memorandum

I. Purpose

This memorandum presents a discussion of revisions to the already approved Contract Year Ending 2014 (CYE 14) capitation rates for the ALTCS/DDD program, for the period July 1, 2013 to June 30, 2014.

The purpose of this actuarial memorandum is to demonstrate that the updated capitation rates were developed in compliance with 42 CFR 438.6(c). It is not intended for any other purpose.

Arizona Health Care Cost Containment System (AHCCCS) has computed a capitation rate change due to changes in provider fee schedules, a rebase of the behavioral health (BH) and acute components, as well as programmatic changes that have occurred since these rates were initially developed.

Due to provider rate changes mandated with an effective date of July 1, 2013, versus other changes impacting the rates with an effective date of October 1, 2013, AHCCCS has computed one capitation rate retroactively effective from July 1, 2013 through September 30, 2013, and a revised capitation rate effective October 1, 2013 through June 30, 2014.

II. Overview of Changes

Institutional and HCBS Provider Fee Schedule Changes
A 3% rate increase for developmental disabilities service providers was included in the DDD appropriation with an effective date of July 1, 2013. DDD completed an analysis of their published rates subsequent to this date and provided a recommendation to increase HCBS published rates and private Intermediate Care facility (institutional) rates. The capitation rates were adjusted to reflect this recommendation. The estimated twelve month statewide impact is an increase of approximately $21.9 million.

Behavioral Health Provider Fee Schedule Changes
A 3% rate increase for behavioral health service providers was included in the Arizona Department of Health Services/Division of Behavioral Health Services (ADHS/DBHS) appropriation with an effective date of October 1, 2013.

ADHS/DBHS completed an analysis of encounter and financial expenditures for certain behavioral health (BH) categories of services and provided AHCCCS with a recommendation to increase multiple community-based and residential providers, but excluding inpatient, subacute facility, transportation, laboratory and radiology, pharmacy and electro-convulsive.. The DDD BH capitation rates were adjusted to reflect this recommendation. The estimated nine month statewide impact is an increase of approximately $644,000.

AHCCCS Fee Schedule Changes

Effective October 1, 2013, AHCCCS is increasing FFS provider rates for certain providers based either on access to care needs, Medicare or ADHS fee schedule rates, legislative mandates, or cost of living adjustments. The unit cost (inflation) trends were adjusted appropriately for these changes. The estimated nine month statewide impact is an increase of approximately $522,000.

Medical Management Changes

The State of Arizona's 2013 Health and Welfare Budget Reconciliation Bill (BRB) reinstated well visits, which were previously eliminated effective October 1, 2010, as a covered service for enrolled adults for federal fiscal year 2014. The estimated nine month statewide impact is an increase of approximately $170,000.

Shift of BH Services for DDD members who are eligible for CRS

In order to facilitate efficient coordination of care and improve member outcomes, AHCCCS has integrated the services for children with special health care needs effective October 1, 2013. DDD members with diagnoses who qualify for Children's Rehabilitative Services (CRS) will now receive care related not only to their CRS services, but also their behavioral health care through a single CRS Contractor. These DDD members will continue to receive their unrelated physical health services and long term care services through DDD. All behavioral health costs for these members have been removed from the base data. This resulted in a shift of approximately $4.5 million to the CRS Contractor over nine months.

Behavioral Health Component Rate Rebase

The BH component was rebased to follow the same method used in setting the non-DDD BHS capitation rates. The base period data consisted of the state fiscal year 12 (July 1, 2011 to June 30, 2012) Regional Behavioral Health Authority (RBHA) audited financial statements and SFY 12 member months provided by ADHS/DBHS. This base data was adjusted for historical programmatic changes, provider fee schedule changes and encounter data completeness. The base data was then trended forward and adjusted by any new programmatic and provider fee schedule changes and integration of DDD members eligible for CRS (as discussed above). Finally administration and risk contingency were applied to this rate to establish the final BH component rate. The estimated nine month statewide impact of all the changes is a decrease of approximately $634,000 from the currently approved CYE 14 capitation rates.

Acute Care Component Rate Rebase including Reinsurance Offset Rebase

DDD contracts with Managed Care Organization (MCO) subcontractors to provide acute care services for their members. DDD's reinsurance deductible level with their MCOs is at $20,000. However, DDD's reinsurance deductible level with AHCCCS is at $100,000. In order to better align the two, DDD's reinsurance deductible level with AHCCCS will be adjusted from $100,000 to $50,000 effective October 1, 2013.

The reinsurance offset was rebased to account for this change using actual reinsurance paid information for federal fiscal years ending 11 and 12 and adjusted when necessary for completion, historical programmatic and provider fee schedule changes. The estimated nine month statewide impact due to the change in the deductible level was a decrease in capitation paid of approximately $937,000.

The Acute gross medical component was rebased due to the reinsurance offset adjustment. The acute medical base period data consisted of three and a half years of encounter data for dates of service October 1, 2009 through March 31, 2013 and enrolled member month data for the same time frame. The base data was viewed on a federal fiscal year basis and adjusted, when necessary, by completion factors, seasonality factors, historical programmatic changes and provider fee schedule changes. The final base data consisted of an average of all the years which was then trended forward and adjusted by new programmatic and provider fee schedule changes (as discussed above) to establish the final gross medical rate for the acute component. The reinsurance offset was deducted from this rate to arrive at the final net medical rate for the acute component.

The estimated nine month statewide impact for all Acute component changes, including the rebase, is a decrease of approximately $477,000 from the currently approved CYE 14 capitation rates.

III. Proposed Capitation Rates and Their Impacts

Table I below summarizes the changes per rate cell with the estimated budget impact. Since the already approved CYE 14 capitation rates are being replaced in full, the table summarizes the impact from the CYE 13 (April 1, 2013) approved capitation rates to the proposed, revised CYE 14 capitation rates, effective for the period July 1, 2013 through June 30, 2014 on a statewide basis. Because one rate will be in place for the period retroactive to July 1, 2013 through September 30, 2013, with an updated rate beginning October 1, 2013, both rates are identified in the table below.

Table I: Proposed Capitation Rates and Budget Impact

Rates Effective: July 1, 2013 - September 30, 2013	Based on Projected Member Months July 1, 2013 - Sept 30, 2013			Based on Projected Member Months July 1, 2013 - Sept 30, 2013			
Rate Cell		CYE 13 (4/1/13-6/30/13) Rate	CYE 14 Revised Rate [1]	Estimated CYE 13 (4/1/13 - 6/30/13) Capitation	Estimated CYE 14 Revised Capitation	Dollar Impact	Percentage Impact
DDD	77,275	$ 3,125.69	$ 3,184.04	$ 241,538,136	$ 246,047,141	$ 4,509,004	1.87%
Behavioral Health [2]	77,275	$ 120.67	$ 120.82	$ 9,324,791	$ 9,336,383	$ 11,591	0.12%
Targeted Case Management	13,544	$ 113.18	$ 115.86	$ 1,532,911	$ 1,569,209	$ 36,298	2.37%
Total				$ 252,395,839	$ 256,952,733	$ 4,556,894	1.81%

Rates Effective: October 1, 2013 - June 30, 2014	Based on Projected Member Months October 1, 2013 - June 30, 2014			Based on Projected Member Months October 1, 2013 - June 30, 2014			
Rate Cell		CYE 13 (4/1/13-6/30/13) Rate	CYE 14 Updated Rate	Estimated CYE 13 (4/1/13 - 6/30/13) Capitation	Estimated CYE 14 Updated Capitation	Dollar Impact	Percentage Impact
DDD	236,232	$ 3,125.69	$ 3,181.77	$ 738,387,659	$ 751,635,543	$ 13,247,884	1.79%
Behavioral Health [2]	236,232	$ 120.67	$ 118.14	$ 28,506,102	$ 27,908,436	$ (597,667)	-2.10%
Targeted Case Management	40,632	$ 113.18	$ 115.86	$ 4,598,733	$ 4,707,627	$ 108,894	2.37%
Total				$ 771,492,494	$ 784,251,606	$ 12,759,112	1.65%

Total Budget Impact (July 1, 2013 - June 30, 3014)	$ 1,023,888,333	$ 1,041,204,338	$ 17,316,005	1.69%

1) For Behavioral Health and Targeted Case Management rate cell the CYE 14 rates are the rates already approved by CMS form the prior actuarial cert
2) Behavioral Health rate does not reflect premium tax

IV. Actuarial Certification of the Capitation Rates

I, Windy J. Marks, am an employee of Arizona Health Care Cost Containment System (AHCCCS). I am a Member of the American Academy of Actuaries. I meet the qualification standards established by the American Academy of Actuaries and have followed the practice standards established from time to time by the Actuarial Standards Board.

The rates were developed using generally accepted actuarial principles and practices and are considered to be actuarially sound. The rates were developed to demonstrate compliance with the CMS requirements under 42 CFR 438.6(c) and are in accordance with applicable laws and regulations. The rates are appropriate for the Medicaid populations covered and Medicaid services to be furnished under the contract. The rates may not be appropriate for any other purpose. The documentation has been included with this certification. The actuarially sound capitation rates that are associated with this certification are effective for the twelve-month period beginning July 1, 2013.

The actuarially sound capitation rates are a projection of future events. It may be expected that actual experience will vary from the values in the rates.

In developing the actuarially sound capitation rates, I have relied upon data and information provided by DES/DDD, ADHS/DBHS and the AHCCCS internal databases. I have accepted the data without audit and have relied upon the DES/DDD employees, ADHS/DBHS employees and other AHCCCS employees for the accuracy of the data.

This actuarial certification has been based on the actuarial methods, considerations, and analyses promulgated from time to time through the Actuarial Standards of Practice by the Actuarial Standards Board.

This certification letter assumes the reader is familiar with the DDD program, Medicaid eligibility rules and actuarial rating techniques. It is intended for AHCCCS, DES/DDD and CMS and should not be relied upon by third parties. Other readers should seek the advice of actuaries or other qualified professionals competent in the area of actuarial rate projections to understand the technical nature of these results.

Windy J. Marks   09-30-13

Windy J. Marks   Date

Fellow of the Society of Actuaries
Member, American Academy of Actuaries

Arizona Department of Health Services
Division of Behavioral Health Services
Actuarial Memorandum

I. Purpose

The purpose of this actuarial memorandum is to demonstrate that the capitation rates for the Arizona Department of Health Services (ADHS), Division of Behavioral Health Services (BHS) for the period of October 1, 2013 through September 30, 2014 were developed in compliance with 42 CFR 438.6(c). It is not intended for any other purpose.

The Affordable Care Act (ACA) places an annual fee on the health insurance industry nationwide including most Medicaid health plans effective January 1, 2014. The fee will be allocated to health insurers based on their respective market share of premium revenue in the previous year. Due to the uncertainty of the actual fees and other unknowns, AHCCCS will not be adjusting the capitation rates for this fee at this time, but intends to make a revision once the impacts are known.

II. Overview of Rate Setting Methodology

The contract year ending 2014 (CYE 14) rates cover the twelve month contract period of October 1, 2013 through September 30, 2014.

Actuarially sound capitation rates were developed utilizing the steps outlined as follows:

1. Develop base period data

    a) State fiscal year 2012 (SFY 12) Regional Behavioral Health Authority (RBHA) audited financial statements and member month data provided by ADHS/BHS were used as the primary basis for developing capitation rates for each rate category.

    b) Adjust base data for programmatic, ADHS/BHS provider fee schedule changes, encounter data completeness, and revenue neutral service expense reallocation.

2. Develop CYE 14 actuarially sound rates

    a) Apply a trend factor to bring SFY 12 claim costs forward to CYE 14.

    b) Adjust base CYE 14 claims costs for programmatic and ADHS provider fee schedule changes occurring between the base period and CYE 14.

    c) Make an adjustment for the change in expected claims costs due to the shift of costs associated with Children's Rehabilitative Services (CRS) recipients to the integrated CRS program in CYE 14.

d) Add provision for administration and risk contingency.

III. Base Period Experience

The base data consisted of audited financial statements and member month data for all RBHAs for the July 1, 2011 through June 30, 2012 (SFY 12) time period. BHS has periodically performed reviews of the RBHA financial statements and has determined that the data does not include any non-covered services.

Adjustments were made to the base data for fee schedule and programmatic changes and encounter data completeness, described as follows:

a) 10/1/2011 Provider Fee Schedule (Rate) Reduction – BHS implemented a 5% provider rate decrease effective October 1, 2011 for all provider types, excluding pharmacy.

   The estimated statewide impact due to this adjustment is a decrease of approximately $10.6 million to the base period costs.

b) Respite Hour Reduction – effective October 1, 2011, the number of respite hours for adults and children receiving BHS services was reduced from 720 to 600 hours per twelve month period, October 1 through September 30 each year.

   The estimated statewide impact due to this adjustment is a decrease of approximately $66,000 to the base period costs.

c) Best for Babies Initiative – This change was introduced in Maricopa County on July 1, 2011. However, the program did not fully affect claims costs in SFY 12, so an adjustment was made to reflect an expected full year's cost. The Best for Babies/Court Team Project is a national initiative sponsored by Zero to Three, targeting children from birth to three years of age involved with dependency court. This project is based on best practices in infant mental health to improve outcomes for young dependent children exposed to trauma and separation through greater judicial oversight of their services and time to permanency. Timely assessment and services for both children and parents, emotional care of infants in foster care, addressing health issues and developmental delays, frequent visitation which supports security and skill building for parents and improving child-centered court procedures are all emphasized in the national initiative. This initiative only affects CMDP capitation rates for GSA 6.

   The estimated statewide impact due to this adjustment is an increase of approximately $900,000 to the base period costs.

d) 340B Pricing – Effective April 2012, the RBHAs began reimbursing claims for 340B drugs consistent with the requirements of AHCCCS Rule A.A.C. R9-22-

710 C. In general, this provision requires that claims for drugs identified on the 340B pricing file dispensed by federally qualified health centers (FQHCs) and FQHC Look Alike pharmacies be reimbursed at the lesser of the actual acquisition cost or the 340B ceiling price, plus a dispensing fee listed in the AHCCCS capped FFS schedule.

The estimated statewide impact due to this adjustment is a decrease of approximately $233,000 to the base period costs.

e) Encounter Data Adjustment – ADHS/BHS has for several years stressed the importance of timely and accurate encounter data submission by the RBHAs for capitation rate setting (among other valuable uses). An adjustment factor was applied to the base data which incorporated the relative level of completeness of the encounter data submitted by the RBHAs.

The total statewide dollar impact of the adjustment was a decrease of $6.4 million to the base period costs.

f) Revenue Neutral Service Expense Reallocation – In GSA 6, a CYE 14 revenue neutral adjustment was made to the base period service costs to reallocate expense between the TXIX/TXXI non-CMDP and CMDP rate categories. ADHS reviewed the service expense reporting relationship between these two rate categories for SFY 12 and SFY 13. The adjustment was made to realign the service expense allocation based on the SFY 13 relationship, which was deemed to be appropriate by ADHS.

Primary Care Provider (PCP) Payment Increase

Section 1902(a)(13)(C) of the Social Security Act, as amended by the Affordable Care Act, requires minimum levels of Medicaid payment for certain primary care services, provided by certain physicians. The AHCCCS managed care model, with strict requirements regarding actuarially-sound capitation rates, necessitates that Contractors be funded for expected cost increases due to primary care rate parity. AHCCCS proposes to provide Contractors the necessary funds to increase primary care payments by using Model 3: Non-risk Reconciled Payments for Enhanced Rates as referenced in the *Medicaid Managed Care Payment for PCP Services in 2013 and 2014, Technical Guidance and Rate Setting Practices* (Technical Guidance) document released by CMS.

In summary, under Model 3, prospective capitation rates would not be adjusted for the enhanced primary care payments. Rather, AHCCCS would query actual encounter data on a quarterly basis to calculate the total payments that eligible providers were paid for eligible services in order to reach the mandated enhanced payment rates. Once the data on this report is verified, AHCCCS would pay the Contractors the calculated additional payment amounts. A more detail explanation of the process and methodology can be found in the Actuarial Certification submitted to CMS for approval of AHCCCS methodology. There is no impact to the CYE 14 capitation rates.

"In Lieu of" Services

Included in the base rates is funding for "in lieu of" services, substituting cost-effective alternative inpatient settings in place of more costly inpatient non-specialty hospital placements. State-approved fee-for-service (FFS) rates at inpatient non-specialty hospitals are approximately 93.5% more expensive than those provided in alternative inpatient settings. The proposed capitation rates allow for the provision of services in alternative inpatient settings that are licensed by Arizona Department of Health Services/Division of Licensing Services/Office of Behavioral Health Licensing, in lieu of services in an inpatient non-specialty hospital, with unit cost savings of approximately 48.3% and total yearly cost savings of approximately $1.8 million. These savings are already reflected in the base data.

Coordination of Benefits (COB)

Inherent in the encounter and financial data are unit cost trends which incorporate Contractors' Coordination of Benefits (COB) activities. AHCCCS provides Contractors with verified commercial and Medicare coverage information for their members which Contractors utilize to ensure payments are not made for medical services that are covered by the other carriers. When Contractors make a payment to cover members' coinsurance, deductibles, or Medicaid-covered services that are not covered by the other carriers, they submit encounters containing these reduced amounts. From SFY 2008 to SFY 2013, encounter-reported COB cost avoidance grew by greater than 171%, from $7.7 million to $20.9 million. Additionally, in CYE 13, BHS subcontractors cost-avoided $9.0 million in the nine months ending March 31, 2013, in additional claims for which the Contractor had no financial obligation after the private insurance or Medicare payment was made. Consequently no encounters were submitted to AHCCCS and therefore those services are excluded completely from capitation expenditure projections. AHCCCS continues to emphasize the importance of COB activities with Contractors.

IV. Projected Trend Rates

A trend analysis was performed using services expenses from RBHA audited financial statements for July, 2009 through June, 2012 (SFY 10-SFY 12). In addition, standard sources of health care cost trends were examined, including the 2012 Actuarial Report on the Financial Outlook for Medicaid and the National Health Expenditure (NHE) Report published by CMS.

The RBHA service expense trend analysis was adjusted for fee schedule and programmatic changes made during the respective periods. Service expenses for the behavioral health category for members with Serious Mental Illness (SMI) were also adjusted for the effect of population changes during the period of the study. The resulting overall average "residual" trend rate of 3.6% for the SFY 10-SFY 12 period for all

RBHAs and behavioral health categories was deemed to be a reasonable estimate of future trend since it was specific to the behavioral health population base and represented a large enough volume of experience to provide a reliable statistic.

For all RBHAs excluding GSA 6, claims PMPMs were trended 27 months from the midpoint of the base claims period to the midpoint of the projected claims period. The midpoint of the projected claims period is April 1, 2014. The midpoint of the base claims period is January 1, 2012.

For the GSA 6 RBHA, a subcontractor change is expected to transpire on or around January 1, 2014. Simultaneously the AHCCCS membership is expected to materially increase due to the restoration of a previously frozen eligibility group and Medicaid expansion. Consequently, it was desired to split the CYE 14 rates into two periods – October 1, 2013 to December 31, 2013 (Period 1) and January 1, 2014 to September 30, 2014 (Period 2). Accordingly, the claims PMPMs were trended 22.50 months from the midpoint of the base claims period to the midpoint of Period 1 and 28.50 months to the midpoint of Period 2. This action helps ensure that rates which are developed to be actuarially sound over the course of a potentially volatile 12 month period are also actuarially sound over the two periods of membership change that might cross over two subcontractors.

V. Programmatic and Fee Schedule Changes – Prospective Adjustments

The following adjustments have taken place after the SFY12 base period.

a) 4/1/2013 Provider Fee Schedule (Rate) Increase – BHS implemented a provider rate increase effective April 1, 2013 for multiple community-based services, but excluding inpatient, residential, subacute facility, transportation, laboratory and radiology, pharmacy, and electro-convulsive therapy services.

   The estimated statewide impact due to this adjustment is an increase of approximately $18.1 million to CYE 14 costs.

b) 10/1/2013 Provider Fee Schedule (Rate) Increase – BHS implemented a provider rate increase effective October 1, 2013 for multiple community-based and residential services, but excluding inpatient, subacute facility, transportation, laboratory and radiology, pharmacy, and electro-convulsive therapy services.

   The estimated statewide impact due to this adjustment is an increase of approximately $25.2 million to CYE 14 costs.

c) Psych Consults – Effective since the start of the 2013 contract period, the RBHAs are responsible for payment of medically necessary psychiatric consultations and evaluations provided to acute care members in inpatient facilities in medical/surgical beds, regardless of the bed or floor where the member is placed, including emergency departments, even if the member is being treated for other co-morbid physical conditions. Historically, the AHCCCS Acute Care

Contractors were financially responsible for these psychiatric consultations/evaluations. This adjustment represents a shift of dollars from the AHCCCS Acute Care Contractors to the RBHAs.

The estimated statewide impact due to this adjustment is an increase of approximately $363,000 to CYE 14 costs.

d) ER Transportation – Effective July 1, 2012, the AHCCCS Acute Care Contractors pay for all emergency transportation for a behavioral health member, unless the emergency transport is to a behavioral health facility. Historically, the RBHAs were financially responsible for emergency transportation for a behavioral health member. This adjustment represents a shift of dollars out of the RBHAs and into the AHCCCS Acute Care Contractors.

The estimated statewide impact due to this adjustment is a decrease of approximately $520,000 to CYE 14 costs.

e) Benzodiazepines and Barbiturates – Effective January 1, 2013, for dual eligible members, Medicare pays for benzodiazepines for any condition and barbiturates used for the treatment of epilepsy, cancer or chronic mental health conditions. Therefore, the RBHAs will no longer be required to reimburse prescription claims for these services as they relate to mental health conditions.

The estimated statewide impact due to this adjustment is a decrease of approximately $852,000 to CYE 14 costs.

f) CRS Integration – In order to facilitate efficient coordination of care and improve member outcomes, AHCCCS has integrated the services for children with special health care needs effective October 1, 2013. Members with diagnoses who qualify for Children's Rehabilitative Services will now receive care related to their CRS services, unrelated physical health services, and behavioral health care through a single CRS Contractor. All behavioral health costs for these members have been removed as well as the associated member months and shifted to the CRS Contractor. After the CRS members were removed an acuity difference was observed in the non-CMDP children category only. The resulting PMPM rate for the non-CMDP children category is reduced by 2%.

g) Behavioral Health Penetration Adjustment – Previous capitation developments included an adjustment for projected increases or decreases in the rate of members utilizing BHS services compared to the entire AHCCCS population. This "penetration rate" incorporated two effects: Effect 1, a change due to the premise that the rate of change in BHS-utilizing members is different than the rate of change in the eligible population, and Effect 2, the general trend in the rate of BHS-utilizing members compared to the eligible population. It was surmised that Effect 1 would be realized in the SMI population due to a significant rise and then decline in the eligible population of the AHCCCS Medical Expense Deduction (MED) and Childless Adult populations due to an elimination and enrollment freeze, respectively, associated with these programs, coupled with a corresponding effort to maintain enrollment for SMI members via another risk group.

A statistical analysis was done to test Effect 1 which suggested that the penetration rate for SMI members was affected by changes in the eligible population. An adjustment was made in the historical SMI PMPMs of the trend analysis to reflect this effect. This analysis was also performed on the other behavioral health categories, but Effect 1 was not conclusively observed in those populations.

For the RBHAs excluding GSA 6, no adjustment for Effect 1 was made in CYE 14 capitation rates due to the high degree of the uncertainty inherent in the amount and timing of the 2014 Medicaid enrollment expansion which was not conducive to the development of a reliable rating factor.

For the GSA 6 RBHA, the SMI enrollment for Period 1 is expected to be considerably lower than the enrollment for Period 2 and the effect was significant enough to warrant the use of a penetration adjustment for Effect 1 which was subsequently applied to the rates for GSA 6 in the respective periods.

No adjustment was included in this rate development for Effect 2 since the historical aggregate penetration rate increase is included in the residual trend rate noted above. The penetration rate data was not considered to be of sufficient quality to warrant any further use in the rate development.

VI. Administration and Risk Contingency

The CYE 14 capitation rates include a provision for RBHA administration, RBHA interpretive services administration, and RBHA risk contingency. The component for administration and risk contingency is calculated as a percentage of the final capitation rate. A 9% load was added across all populations, which is the same as was applied to the CYE 13 capitation rates. The component for interpretive services administration was determined by ADHS/BHS. For GSA 6 capitation rates effective January 1, 2014, an adjustment to administration was made to account for the shift of certain administrative responsibilities from the RBHA to ADHS. This resulted in shift of approximately $1.1 million for the nine month period through September 30, 2014.

VII. Risk Corridors and Performance Incentive

BHS has in place a risk corridor arrangement with the RBHAs that provides motivation for the RBHAs to appropriately manage expenses, yet provides financial protection against unmanageable losses. The risk corridor provides impetus for the RBHAs to operate efficiently and generate net income, but also provides for the return of any excessive profit to the State.

The proposed CYE 14 BHS risk corridor approach provides for gain/loss risk sharing symmetry around the service revenue portion of the capitation rates. This risk corridor model is designed to be cost neutral, with no net aggregate assumed impact across all payments. Also, as in prior years, the RBHAs' contracts provide for a potential 1% performance incentive.

VIII. Tribal FFS Claims Estimate

Tribal claims data was reviewed and an amount of $73.1 million was projected for CYE 14.

IX. BHS Administration and Premium Tax

AHCCCS has placed BHS Administration at financial risk for the provision of BHS covered services for CYE 14. Accordingly, the capitation rates were developed to include compensation to BHS for the cost of ensuring the delivery of all BHS covered services. The capitation rates paid to BHS include an administrative load, which was negotiated between AHCCCS and BHS administration. The load represents a 2% premium tax, a 1.356% administrative load for the twelve month period of October 1, 2013 through September 30, 2014, and a 0.239% administrative load for the nine month period of January 1, 2014 through September 30, 2014. The BHS administrative costs ensure the efficient delivery of services in a managed care environment.

X. Title XXI Capitation Rates

For CYE 14, the Title XXI population includes those children enrolled in KidsCare II as well as those members in the traditional KidsCare program. On April 6, 2012, CMS approved a new 2012 Waiver Amendment, which included funding for KidsCare II. KidsCare II provides coverage to children who have income levels up to 175% of the federal poverty level (FPL) and meet other eligibility requirements.

Due to the small amount of experience data for the Title XXI population, the RBHAs will be paid one blended capitation rate that includes experience from both the traditional Medicaid population and the Title XXI SCHIP population.

The service expense and member month data for the Title XXI members that are under the age of 18 are included in the non-CMDP Child capitation rate development and the service expense and member month data for the Title XXI members that are age 18 and older are included in the GMH/SA capitation rate development. As a result, the CYE 14 capitation rates for these populations are the same as for the Title XIX members.

XI. Development of Statewide Capitation Rates and Their Budget Impact

Statewide capitation rates were developed by blending the CYE 14 capitation rates for each RBHA and rate category using projected CYE 14 member months, the estimated dollar amount of CYE 14 tribal claims and the administrative percentage add-on component for BHS.

Table I shows the current and proposed capitation rates on a statewide basis for all BHS risk groups as well as their estimated budget impact off of CYE 14 projected member months for the October 1, 2013 through December 31, 2013 and January 1, 2014 through September 30, 2014 rating periods.

Table I: Proposed Capitation Rates and Budget Impact

Note: This section uses CYE 14 Projected Member Months applied to both CYE 13 and CYE 14 Rates

10/1/13 - 12/31/13 Statewide Capitation Rates

	Statewide Rates		10/1/13-12/31/13	Projected Expenditures		
Rate Category	4/1/13 Rates	10/1/13-12/31/13	Projected MMs	4/1/2013	10/1/13-12/31/13	Change
Children	60.55	60.89	1,917,190	116,083,034	116,737,356	0.6%
SMI	77.62	81.99	1,565,654	121,526,049	128,365,409	5.6%
GMH/SA and TXXI Adult	44.03	44.48	1,570,860	69,157,528	69,878,107	1.0%
Total	60.70	62.33	5,053,704	306,766,610	314,980,872	2.7%

	Statewide Rates		10/1/13-12/31/13	Projected Expenditures		
Rate Category	4/1/13 Rates	10/1/13-12/31/13	Projected MMs	4/1/2013	10/1/13-12/31/13	Change
TXIX and TXXI non-CMDP Children	38.88	36.60	1,873,799	72,848,575	68,573,197	-5.9%
CMDP Children	996.38	1,109.99	43,392	43,234,459	48,164,159	11.4%
Total Children	60.55	60.89	1,917,190	116,083,034	116,737,356	0.6%

1/1/14 - 9/30/14 Statewide Capitation Rates

	Statewide Rates		1/1/14-9/30/14	Projected Expenditures		
Rate Category	4/1/13 Rates	1/1/14-9/30/14	Projected MMs	4/1/2013	1/1/14-9/30/14	Change
Children	57.04	57.65	6,451,821	368,015,031	371,918,851	1.1%
SMI	77.62	79.73	5,594,545	434,248,622	446,073,507	2.7%
GMH/SA and TXXI Adult	44.03	44.99	5,595,307	246,334,908	251,714,362	2.2%
Total	59.44	60.64	17,641,674	1,048,598,561	1,069,706,720	2.0%

	Statewide Rates		1/1/14-9/30/14	Projected Expenditures		
Rate Category	4/1/13 Rates	1/1/14-9/30/14	Projected MMs	4/1/2013	1/1/14-9/30/14	Change
TXIX and TXXI non-CMDP Children	38.88	36.98	6,329,435	246,072,479	234,056,469	-4.9%
CMDP Children	996.38	1,126.46	122,386	121,942,552	137,862,382	13.1%
Total Children	57.04	57.65	6,451,821	368,015,031	371,918,851	1.1%

XII. CMS Rate Setting Checklist

1. Overview of rate setting methodology

A.A.1.0: Overview of rate setting methodology

AHCCCS is performing a rebase from the previously approved contract year ending 2013 (CYE 13) rates under 42 CFR 438.6(c). Please refer to Sections I-II.

AA.1.1: Actuarial certification

Please refer to Section XIII.

AA.1.2: Projection of expenditure

Please refer to Section XI.

AA.1.3: Procurement, prior approval and rate setting

This is a sole source contracting method, between AHCCCS and ADHS.

AA.1.5: Risk contract

The contract is an at risk contract, however there is a provision for a risk corridor reconciliation. Please refer to Section VII.

AA.1.6: Limit on payment to other providers

AHCCCS makes no additional payment to providers, except for Disproportionate Share Hospital (DSH), Graduate Medical Education (GME) and Critical Access Hospitals. GME is paid in accordance with state plan. DSH and Critical Access Hospital payments are paid in accordance with the Waiver Special Terms and Conditions. None of the additional payments to providers were included in the capitation calculation.

AA.1.7: Rate modification

Please refer to Sections III through V.

2. Base Year Utilization and Cost Data

AA.2.0: Base year utilization and cost data

Please refer to Section III.

AA.2.1: Medicaid eligibles under the contract

The data includes only those members eligible for managed care.

AA.2.2: Dual Eligibles (DE)

There are dual eligibles.

AA.2.3: Spenddown

Not applicable, not covered under this contract.

AA.2.4: State plan services only

Please refer to Section III.

AA.2.5: Services that can be covered by a capitated entity out of contract savings.

Same as AA.2.4.

3. Adjustments to the Base Year Data

AA.3.0 Adjustments to base year data

Please refer to Sections III through IX.

AA.3.1 Benefit differences

Not applicable.

AA.3.2 Administrative cost allowance calculation

Please refer to Sections VI and IX.

AA.3.3 Special populations' adjustment

Please refer to Sections II, V and VIII.

AA.3.4 Eligibility Adjustments

No adjustment was made.

AA.3.5 DSH Payments

No DSH payment was included in the capitation development.

AA.3.6 Third party Liability (TPL)

This is a contractual arrangement between AHCCCS and its Contractors.

AA.3.7 Copayments, coinsurance and deductible in the capitated rates

In general, members utilizing behavioral health services do not pay any copays, coinsurance or deductibles, but there are a few that pay copays. The data is net of copays. Further adjustments might be necessary due to Health Care Reform and if so the capitation rates will appropriately be adjusted at that time with an amendment.

AA.3.8 Graduate Medical Education

The experience excludes any payment for GME.

AA.3.9 FQHC and RHC reimbursement

The experience excludes any additional payments that FQHCs may receive from the state.

AA.3.10 Medical cost/trend inflation

Please refer to Section IV.

AA.3.11 Utilization adjustment

Please refer to Section V.

AA.3.12 Utilization and cost assumptions

Not applicable since actual experience was used.

AA.3.13 Post-eligibility treatment of income (PETI)

Not applicable, not required to consider PETI.

AA.3.14 Incomplete data adjustment

Please refer to Section III.

4. Establish Rate Category Groupings

AA.4.0: Establish rate category groupings

Please refer to XI.

AA.4.1: Age

Please refer to XI.

AA.4.2: Gender

Not applicable.

AA.4.3: Locality/region

Not applicable.

AA.4.4: Eligibility category

Please refer to XI.

5. Data Smoothing, Special Populations and Catastrophic Claims

AA.5.0: Data smoothing

Please refer to Sections II, III and X.

AA.5.1: Special populations and assessment of the data for distortions

Data was not adjusted for special populations.

AA.5.2: Cost-neutral data smoothing adjustments

Please refer to Section III.

AA.5.3: Risk-adjustment

Not applicable.

6. Stop Loss, Reinsurance, or Risk-Sharing arrangements

AA.6.1: Commercial reinsurance

There is no commercial reinsurance.

AA.6.2: Simple stop loss program

Not applicable.

AA.6.3: Risk corridor program

Please refer to Section VII.

7. Incentive Arrangements

Please refer to Section VII.

XIII. Actuarial Certification of the Capitation Rates

I, Anthony Wittmann, am an employee of Arizona Health Care Cost Containment System (AHCCCS). I am a Member of the American Academy of Actuaries and a Fellow of the Society of Actuaries. I meet the qualification standards established by the American Academy of Actuaries and have followed the practice standards established from time to time by the Actuarial Standards Board.

The attached capitation rates were developed using generally accepted actuarial principles and practices and are considered to be actuarially sound. The rates were developed to demonstrate compliance with the CMS requirements under 42 CFR 438.6(c) and are in accordance with applicable laws and regulations. The rates are appropriate for the Medicaid populations covered and Medicaid services to be furnished under the contract. The rates may not be appropriate for any other purpose. The documentation has been included with this certification. The actuarially sound capitation rates that are associated with this certification are effective for the twelve month period beginning October 1, 2013.

The actuarially sound capitation rates are a projection of future events. It may be expected that actual experience will vary from the values in the rates.

In developing the actuarially sound capitation rates, I have relied upon data and information provided by BHS and the AHCCCS internal database. I have accepted the data without audit and have relied upon the ADHS auditors and other AHCCCS employees for the accuracy of the data.

This actuarial certification has been based on the actuarial methods, considerations, and analyses promulgated from time to time through the Actuarial Standards of Practice by the Actuarial Standards Board.

RBHAs are advised that the use of these rates may not be appropriate for their particular circumstance. RBHAs considering contracting with BHS should analyze their own projected medical expense, administrative expense and other premium needs for comparison to these rates before deciding whether to contract with BHS.

This certification letter assumes the reader is familiar with the BHS program, Medicaid eligibility rules and actuarial rating techniques. It is intended for BHS and CMS and should not be relied upon by third parties. Other readers should seek the advice of actuaries or other qualified professionals competent in the area of actuarial rate projections to understand the technical nature of these results.

Anthony Wittmann 9/27/13

Anthony Wittmann — Date

Fellow of the Society of Actuaries
Member, American Academy of Actuaries

STATE OF ARIZONA

Joint Legislative Budget Committee

1716 WEST ADAMS
PHOENIX, ARIZONA 85007

PHONE (602) 926-5491

FAX (602) 926-5416

http://www.azleg.gov/jlbc.htm

DATE: October 22, 2013

TO: Representative John Kavanagh, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director RS

FROM: Eric Billings, Principal Fiscal Analyst EB

SUBJECT: Automobile Theft Authority (ATA) - Review of the Proposed Expenditures from the Reimbursable Programs Special Line Item (SLI)

Request

Pursuant to a FY 2014 General Appropriation Act (Laws 2013, 1st Special Session, Chapter 1) footnote, the ATA is required to submit for review a report outlining any proposed expenditures from the Reimbursable Programs SLI.

ATA has submitted for review a proposal to expend $10,000, donated by the National Insurance Crime Bureau (NCIB), in FY 2014 to support the Arizona Vehicle Theft Task Force in an ongoing investigation. The monies would be used for salary, equipment, and other operational expenses.

Recommendation

The Committee has at least the following options:

1. A favorable review.

2. An unfavorable review of the request.

Analysis

The Reimbursable Programs SLI was created in FY 2006 to fund programs such as training seminars, the cost of sending staff to training seminars, and bait car system projects throughout the state. The SLI's only revenue source is donations, grants, and fee collections given to ATA by the private sector. If approved this would represent the first expenditures from the SLI since its creation.

ATA reports that the NCIB made the donation for the purpose of funding a portion of the costs of the Arizona Vehicle Theft Task Force for a specific ongoing investigation. The Arizona Vehicle Theft Task

(Continued)

Force is comprised of 14 individuals housed within DPS that are solely dedicated to the investigation of auto-theft crimes. In FY 2013, the total cost of the Arizona Vehicle Task Force was $3,371,797.

The investigation is an undercover operation involving multiple jurisdictions that has been ongoing for the past 18 months.

RS/EB:ts

ARIZONA AUTOMOBILE THEFT AUTHORITY

1400 W. WASHINGTON STREET, SUITE 270 PHOENIX, ARIZONA 85007
TEL (602) 364-2886 FAX (602) 364-2897 www.azwatchyourcar.com

RECEIVED
OCT 04 2013
JOINT BUDGET COMMITTEE

October 4, 2013

The Honorable John Kavanagh, Chairman
Joint Legislative Budget Committee
1700 West Washington Street
Phoenix, Arizona 85007

The Honorable Don Shooter, Vice-Chairman
Joint Legislative Budget Committee
1700 West Washington Street
Phoenix, Arizona 85007

Re: AATA Reimbursable Program

Dear Representative Kavanagh and Senator Shooter:

The Arizona Automobile Theft Authority (AATA) received a donation in the amount of $10,000.00 from the National Insurance Crime Bureau (NICB), which is presently deposited in our Reimbursable Programs Account. The specific purpose of the donation is to support the efforts of the Arizona Vehicle Theft Task Force (Task Force) and to defray expenses involved in a specific organized crime investigation involving the Task Force.

The AATA requests that this matter be placed on the October agenda for consideration by the Joint Legislative Budget Committee. The Reimbursable Programs line item was created by the legislature as a fund to receive grants, gifts, and donations to the agency. The AATA is required to "submit a report to the joint legislative budget committee before expending any monies for the reimbursable programs line item. The agency shall show sufficient funds collected to cover the expenses indicated in the report." H.B. 2001, Section 13 (2013).

The attached supporting memorandum/report contains a brief explanation of the investigation and the intended use of the funds. I am available to meet with your staff and provide further explanation as appropriate.

Very truly yours,

Brian R. Salata
Executive Director

ARIZONA AUTOMOBILE THEFT AUTHORITY
1400 W. WASHINGTON STREET, SUITE 270 PHOENIX, AZ 85007
TEL (602) 364-2886 FAX (602) 364-2897 www.azwatchyourcar.com

Date: October 4, 2013
To: JLBC
From: Brian R. Salata, Executive Director
Re: Report on AATA Reimbursable Program

The Arizona Vehicle Theft Task Force (Task Force) has been engaged in a long term undercover investigation. The AATA funds the multi-jurisdictional Task Force. The specific Task Force investigation the subject of this report involves multiple agencies and jurisdictions, and has burdened significant resources of the Task Force.

The National Insurance Crime Bureau (NICB) is a non-profit membership organization that was created by the insurance industry to address insurance related crime. NICB convenes collective industry resources involving vehicle theft, maintains extensive data bases, and provides analytical and investigative support to law enforcement. Several Special Agents of the NICB Field Operations Department are assigned to and work with the Task Force.

NICB has made a donation to the AATA in the amount of $10,000.00. Those funds have been deposited in the AATA Reimbursable Program account and are the only funds presently in the account. The purpose of NICB making the contribution to the AATA was specifically for the purpose of supporting the aforementioned undercover operation.

The specific Task Force operation/investigation that prompted the NICB donation has been ongoing for approximately 18 months. It involves a major crime syndicate that has operated within Arizona for many years. The Task Force has led the investigation and its detectives have been involved in wide-ranging undercover operations that have depleted significant Task Force resources. Even after the present operations are complete, it is expected that there will be significant follow-up investigation, as well as derivative cases that will continue to deplete Task Force resources.

The AATA requests that JLBC approve the expenditure of the $10,000.00 in the form of a single grant to the Arizona Vehicle Theft Task Force to be used for operational expenses, equipment, officer salary and overtime as it relates to the aforementioned organized crime investigation.

The identities of the individuals involved and specific details of the investigation will be made available to JLBC. Officer safety issues and the integrity of the investigation prevent disclosure as of the date of this report.

STATE OF ARIZONA

Joint Legislative Budget Committee

1716 WEST ADAMS
PHOENIX, ARIZONA 85007

PHONE (602) 926-5491

FAX (602) 926-5416

http://www.azleg.gov/jlbc.htm

DATE: October 22, 2013

TO: Representative John Kavanagh, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director RS

FROM: Eric Billings, Principal Fiscal Analyst EB

SUBJECT: Department of Public Safety - Review of the Expenditure Plan for the Gang and Immigration Intelligence Team Enforcement Mission (GIITEM) Fund Border Security and Law Enforcement Subaccount

Request

Pursuant to Laws 2013, 1st Special Session, Chapter 5, the Department of Public Safety (DPS) is required to submit for review the entire FY 2014 expenditure plan for the GIITEM Fund Border Security and Law Enforcement Subaccount prior to expending any monies.

DPS has submitted for review a proposal to distribute the $2,390,000 FY 2014 appropriation from the Subaccount amongst Border Security and Law Enforcement Grants, Pima County's Border Crimes Unit, Detention Liaison Officers, and Border County Officers. All 15 county sheriffs, 4 municipalities, and the Arizona Department of Corrections would receive some money under the proposed plan. Funds could be used for law enforcement purposes related to border security, including border personnel and safety equipment that is worn or used by a peace officer who is employed by a county sheriff.

Recommendation

The Committee has at least the following options:

1. A favorable review.

2. An unfavorable review of the request.

Analysis

Pursuant to A.R.S. § 12-116.04, the GIITEM Fund Border Security and Law Enforcement Subaccount receives revenues from a $4 criminal fee assessed on fines, violations, forfeitures and penalties imposed by the courts for criminal offenses and civil motor vehicle statute violations. These monies are distributed by DPS to county sheriffs and other local law enforcement agencies to fund border security

(Continued)

programs, personnel, and safety equipment. The proposed DPS expenditure plan would allocate the entire FY 2014 GIITEM Border Security and Law Enforcement Subaccount appropriation to 4 programs which are as follows:

- Detention Liaison Officers Program - $619,600 to hire detention and correctional officers that serve within jails and prisons to gather intelligence from inmates about illegal activities along the border.
- Border County Officers Program - $370,400 to hire county sheriff deputies and municipal police officers that work as part of the GIITEM Task Force's Border District investigating border-related crimes such as drug trafficking and human smuggling.
- Pima County Border Crimes Unit - $350,000 to fund a portion of the costs of hiring 10 Pima County Sheriff's deputies that focus exclusively on border related crimes.
- Border Security and Law Enforcement Grants - $1,050,000 that DPS will distribute to all 15 county sheriffs' offices for border security.

Table 1 displays the grant recipients in FY 2013 and FY 2014.

Table 1

DPS Expenditure Plan – GIITEM Subaccount

Proposed Recipient	FY 2013 Allocation	FY 2014 Proposed Allocation [1/]
Police Departments/Marshall's Offices		
Benson Police Department	$63,000	$63,035
Coolidge Police Department	62,900	62,820
Douglas Police Department	124,800	124,765
Oro Valley Police Department	54,800	54,787
Subtotal	**$305,500**	**$305,407**
County Sheriffs		
Apache County Sheriff's Office	0	11,600
Cochise County Sheriff's Office	39,800	60,550
Coconino County Sheriff's Office	0	21,500
Gila County Sheriff's Office	0	8,400
Graham County Sheriff's Office	31,200	36,514
Greenlee County Sheriff's Office	0	1,400
La Paz County Sheriff's Office	0	3,200
Maricopa County Sheriff's Office	0	622,100
Mohave County Sheriff's Office	0	32,100
Navajo County Sheriff's Office	0	16,900
Pima County Sheriff's Department	544,500	551,055
Pinal County Sheriff's Office	104,400	164,568
Santa Cruz County Sheriff's Office	0	47,500
Yavapai County Sheriff's Office	0	33,600
Yuma County Sheriff's Office	42,400	89,701
Subtotal	**$762,300**	**$1,700,688**
Arizona Department of Corrections	**$180,400**	**$366,958**
Unallocated	**$1,141,800**	**$16,947**
Total	**$2,390,000**	**$2,390,000**

1/ Represents new proposed allocation from the subaccount.

In determining allocations, DPS gave preference to 3 pre-existing programs (Detention Liaison Officers, Border County Officers, and the Pima County Border Crimes Unit) that received a favorable review from the JLBC at the August 2007 meeting when they were funded from General Fund monies allocated to the GIITEM SLI.

Also, DPS is proposing allocating funds to the new Border Security and Law Enforcement Grants program which will provide funds to county sheriffs based on the following assumptions: 1) all Arizona communities are impacted by border crime; 2) Subaccount funding is not sufficient to provide meaningful

(Continued)

assistance to all law enforcement agencies in the state; 3) smuggling corridors lead into the State's interior and are significant contributors to crime; 4) sheriff's offices are typically more heavily involved in interdicting smugglers than municipal police departments; 5) crime statistics are not detailed enough to distinguish between border related crime and crime unrelated to the border; and 6) a per capita distribution method is the fairest distribution system. The size of the allocation is determined by the relative size of each county's population and whether or not the recipient is a sheriff's office. As required by law, all recipients of GIITEM Fund Border Security and Law Enforcement Subaccount monies except Maricopa and Pinal Counties are required provide at least 25% of the personnel costs of any agreement or contract with DPS as a match. DPS may opt to fund all associated capital costs.

As previously noted, DPS has access to additional immigration enforcement and border security resources beyond the GIITEM Border Security and Law Enforcement Subaccount. DPS' GIITEM Fund is appropriated $2.6 million in General Fund monies annually for local immigration enforcement grants. Additionally, a series of footnotes that were codified in Laws 2011, Chapter 33 require DPS to allocate $1,600,000 to the Maricopa County Sheriff's Office and $500,000 to the Pinal County Sheriff's Office leaving $503,400 in GIITEM Fund monies at DPS' discretion.

In addition to the DPS immigration enforcement and border security resources, the Arizona Department of Administration receives $1.2 million in General Fund monies annually for grants to county attorneys and sheriff's offices to enforce employer sanctions statutes.

RS/EB:ts

ARIZONA DEPARTMENT OF PUBLIC SAFETY

2102 WEST ENCANTO BLVD. P.O. BOX 6638 PHOENIX, ARIZONA 85005-6638 (602) 223-2000

"Courteous Vigilance"

JANICE K. BREWER Governor ROBERT C. HALLIDAY Director

RECEIVED JUL 18 2013 JOINT BUDGET COMMITTEE

July 18, 2013

Representative John Kavanagh, Chairman
Joint Legislative Budget Committee
1716 West Adams
Phoenix, AZ 85007

Dear Chairman Kavanagh:

Pursuant to Laws 2013, 1st Special Session, Chapter 5, Section 13, the Department of Public Safety is submitting its entire FY 2014 expenditure plan for the Border Security and Law Enforcement Subaccount ("Subaccount") to the Joint Legislative Budget Committee for review.

The FY 2014 General Appropriations Act appropriates $2,390,000 from the Subaccount to DPS. Pursuant to A.R.S. § 41-1724, "...monies in the subaccount shall be used for law enforcement purposes related to border security, including border personnel". Laws 2013, 1st Special Session, Chapter 5, Section 8 also added language to clarify that the monies may be used for "...safety equipment that is worn or used by a peace officer who is employed by a county sheriff."

DPS intends to continue funding three existing programs that have been previously given a favorable review by the JLBC and seeks to distribute additional monies in the form of grants to assist law enforcement agencies with combating border crime. The overall expenditure plan is as follows:

Detention Liaison Officer Program	$619,600
Border County Officers	370,400
Border Crimes Unit	350,000
Border Security and Law Enforcement Grants	1,050,000
TOTAL	**$2,390,000**

Detention Liaison Officers Program

The Detention Liaison Officer (DLO) Program provides funding for detention and correctional officers in southern Arizona jails and prisons. The concept of the program is to utilize these specially trained officers to glean as much intelligence as possible from detainees and inmates about activities related to border crimes. Information gathered by these officers is fed into DPS-managed databases (e.g., GangNet) and shared among law enforcement agencies throughout the State.

The program currently funds one detention officer in each of Cochise, Graham, Pima, Pinal, Santa Cruz and Yuma Counties, and four correctional officers and two data entry positions in southern Arizona prisons operated by the Department of Corrections. At any given time, the agencies participating in the program may shift based on jurisdictions' ability and willingness to participate and on program budget constraints. DPS has allocated $619,600 for the program in FY 2014. Local agencies pay 25% of the payroll costs of their positions. The DLO Program was first reviewed by JLBC in August 2007.

Border County Officers

The Border County Officers Program provides funding for county sheriff deputies and municipal police officers who work as part of the GIITEM Task Force's Border District. The district investigates border crimes and disrupts criminal organizations involved in drug trafficking, human smuggling, and other border-related crimes.

The program currently funds officers and deputies with the Benson, Coolidge, Douglas (2), and Oro Valley Police Departments, and with the Pinal County Sheriff's Office. At any given time, the agencies participating in the program may shift based on jurisdictions' ability and willingness to participate and on program budget constraints. DPS has allocated $370,400 for the program in FY 2014. Local agencies pay 25% of the payroll costs of their positions. The Border County Officers Program was first reviewed by JLBC in August 2007.

Border Crimes Unit

Subaccount monies fund a portion of the costs of 10 deputies from the Pima County Sheriff's Department who operate as part of the Border Crimes Unit. The BCU works in close cooperation with GIITEM and conducts interdiction efforts in remote areas of Pima County. Over the first three quarters of FY 2013, BCU has made 59 arrests, seized over 3,300 pounds of illegal drugs, and apprehended or released to the Border Patrol 301 undocumented persons.

DPS has allocated $350,000 for the project in FY 2014. Pima County pays for all costs above the $350,000 level. The BCU was first reviewed by JLBC in August 2007.

Border Security and Law Enforcement Grants

DPS intends to distribute the remaining $1,050,000 to the 15 county sheriffs' offices, based on county population. In arriving at this distribution plan, DPS followed a number of assumptions, including:

- All Arizona communities are impacted by border crime
- Subaccount funding is not sufficient to provide meaningful assistance to all law enforcement agencies in the State
- Smuggling corridors lead into the State's interior and are significant contributors to crime
- Sheriffs' offices are typically more heavily involved in interdicting smugglers than municipal police departments
- Crime statistics are not detailed enough to distinguish between border related crime and crime unrelated to the border
- A per capita distribution method is the fairest distribution system

Based on the above criteria, the Border Security and Law Enforcement Grant distribution plan is as follows:

Agency	County Population	Grant Amount	% of Total
Apache County Sheriff's Office	73,195	$11,600	1.1%
Cochise County Sheriff's Office	132,088	20,800	2.0%
Coconino Sheriff's Office	136,011	21,500	2.0%
Gila County Sheriff's Office	53,144	8,400	0.8%
Graham County Sheriff's Office	37,416	5,900	0.6%
Greenlee County Sheriff's Office	8,802	1,400	0.1%
La Paz County Sheriff's Office	20,281	3,200	0.3%
Maricopa County Sheriff's Office	3,942,169	622,100	59.3%
Mohave County Sheriff's Office	203,334	32,100	3.1%
Navajo County Sheriff's Office	107,094	16,900	1.6%
Pima County Sheriff's Department	992,394	156,600	14.9%
Pinal County Sheriff's Office	387,365	61,100	5.8%
Santa Cruz County Sheriff's Office	47,303	7,500	0.7%
Yavapai County Sheriff's Office	212,637	33,600	3.2%
Yuma County Sheriff's Office	300,022	47,300	4.5%
TOTAL	**6,653,255**	**$1,050,000**	**100.0%**

DPS believes this grants distribution plan provides a fair and meaningful approach to allocating scarce resources. While some sheriffs' offices would receive very small awards, it is likely that the allocations will become annual amounts that would provide concrete support over time. Recipient agencies may use the funding for any purpose consistent with statute. As required by statute, in order to receive the funding, recipient agencies must certify each fiscal year to the DPS Director that the agency is complying with A.R.S. §11-1051 to the fullest extent of the law.

If you have any questions, please contact Phil Case, DPS Budget Director, at 602-223-2463 or pcase@azdps.gov.

Sincerely,

Robert C. Halliday, Colonel
Director

STATE OF ARIZONA

Joint Legislative Budget Committee

STATE
SENATE

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DATE: October 22, 2013

TO: Representative John Kavanagh, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director RS

FROM: Matt Gress, Fiscal Analyst MG

SUBJECT: JLBC Staff - Review of Agency Legal Services Charges

Request

Pursuant to A.R.S. § 41-191.09, agencies are required to submit for Committee review funding sources for the Attorney General (AG) legal services charges for general agency counsel.

To reimburse the Attorney General for services, non-General Fund accounts are levied with a flat dollar amount charge. The FY 2014 General Appropriation Act specified a total flat charge amount for the relevant agencies, but did not delineate the specific funds. Agencies are required to pay this charge from non-General Fund sources and cannot include Federal Funds or other funds that are legally restricted from making the legal services payment.

Recommendation

The JLBC Staff recommends that the Committee give a favorable review of the fund source reports for the AG legal services charges as appears in the attachment.

RS/MG:kp
Attachment

FY 2014 Legal Services Charges

Agencies and Fund Sources	Legal Services Charge
Arizona Department of Administration	
Capital Outlay Stabilization Fund	$26,000
Corrections Fund	1,100
Special Employee Health Insurance Trust Fund	12,200
Personnel Division Fund	25,800
Automation Operations Fund	32,700
Telecommunications Fund	2,900
Information Technology Fund	6,200
Special Services Revolving Fund	1,100
State Surplus Materials Revolving Fund	3,500
Motor Vehicle Pool Revolving Fund	4,500
State Employee Travel Reduction Fund	1,000
IGA and ISA Fund	2,600
Administration - AFIS II Collections Fund	1,600
Co-Op State Purchasing Agreement Fund	3,900
Emergency Telecommunication Services Revolving Fund	1,500
Construction Insurance Fund	1,100
Subtotal	$127,700
Arizona Department Administrative Hearings	
IGA and ISA Fund	$3,000
Subtotal	$3,000
Arizona Commission on the Arts	
Arts Special Revenues Fund	$3,100
Subtotal	$3,100
Automobile Theft Authority	
Automobile Theft Authority Fund	$1,400
Subtotal	$1,400
Citizens Clean Elections Commission	
Citizens Clean Elections Fund	$2,700
Subtotal	$2,700
State Department of Corrections	
Inmate Store Proceeds Fund	$2,000
Subtotal	$2,000
Arizona Criminal Justice Commission	
Criminal Justice Enhancement Fund (Appropriated)	$4,350
Criminal Justice Enhancement Fund (Non-Appropriated)	4,350
Subtotal	$8,700
Arizona State Schools for the Deaf and Blind	
Schools for the Deaf and Blind Fund	$100,200
Subtotal	$100,200
Commission for the Deaf and the Hard of Hearing	
Telecommunication Fund for the Deaf	$4,100
Subtotal	$4,100
Arizona Early Childhood Development & Health Board	
Early Childhood Development & Development & Health Fund	$47,100
Subtotal	$47,100

FY 2014 Legal Services Charges

Agencies and Fund Sources	Legal Services Charge
Department of Education	
Indirect Cost Recovery Fund	$132,000
Subtotal	$132,000
Department of Emergency and Military Affairs	
Camp Navajo Fund	$25,900
Indirect Cost Recovery Fund	3,000
Nuclear Emergency Management Fund	1,100
Subtotal	$30,000
Department of Environmental Quality	
Underground Storage Tank Revolving Fund	$135,600
Subtotal	$135,600
Arizona Exposition and State Fair Board	
Arizona Exposition and State Fair Fund	$20,900
Subtotal	$20,900
Department of Financial Institutions	
Financial Services Fund	$1,706
IGA and ISA Fund	194
Subtotal	$1,900
Department of Fire, Building and Life Safety	
Mobile Home Relocation Fund	$2,500
Subtotal	$2,500
State Forester	
Cooperative Forestry Fund	$12,100
Subtotal	$12,100
Department of Gaming	
Arizona Benefits Fund	$35,000
Subtotal	$35,000
Arizona Geological Survey	
Geological Survey Fund	$6,800
Subtotal	$6,800
Department of Health Services	
Tobacco Tax and Healthcare Fund-Health Education Account	$400
Health Services Licensing Fund	2,000
Disease Control Research Fund	100
Emergency Medical Services Operating Fund	800
Newborn Screening Program Fund	500
IGA and ISA Fund	200
Smoke Free Arizona Fund	4,800
Medical Marijuana Fund	159,000
Environmental Laboratory Licensure Revolving Fund	200
Vital Records Electronic Systems Fund	500
Arizona State Hospital Fund	600
Indirect Cost Fund	900
Subtotal	$170,000
Arizona Historical Society	
Permanent Arizona Historical Society Revolving Fund	$700
Subtotal	$700
Arizona Department of Housing	
Housing Program Fund	$18,100
Subtotal	$18,100

FY 2014 Legal Services Charges

Agencies and Fund Sources	Legal Services Charge
Department of Insurance	
Insurance Examiners' Revolving Fund	$6,645
Assessment Fund for Voluntary Plans	946
Captive Insurance Regulatory and Supervision Fund	946
Health Care Appeals Fund	473
Financial Surveillance Fund	1,182
Receivership Liquidation Fund	308
Subtotal	$10,500
Department of Juvenile Corrections	
Juvenile Corrections Fund	$9,400
Subtotal	$9,400
State Land Department	
Trust Land Management Fund	$2,100
Subtotal	$2,100
Department of Liquor Licenses and Control	
Liquor Licenses Fund	$8,600
Audit Surcharge Fund	800
Enforcement Surcharge - Enforcement Unit Fund	1,000
Enforcement Surcharge - Multiple Complaints Fund	1,000
Subtotal	$11,400
Arizona State Lottery Commission	
State Lottery Fund	$24,800
Subtotal	$24,800
Arizona State Parks Board	
State Lake Improvement Fund	$45,800
Subtotal	$45,800
State Personnel Board	
Personnel Board Subaccount of the Personnel Division Fund	$600
Subtotal	$600
Arizona Pioneers' Home	
Miners' Hospital Fund	$12,100
Subtotal	$12,100
Commission for Postsecondary Education	
Family College Savings Program Trust Fund	$1,800
Subtotal	$1,800
Department of Public Safety	
Highway Patrol Fund	$155,400
Highway User Revenue Fund	522,000
Subtotal	$677,400
Arizona Department of Racing	
Racing Regulation Fund	$2,300
Subtotal	$2,300
Radiation Regulatory Agency	
State Radiologic Technologist Certification Fund	$3,800
Subtotal	$3,800

FY 2014 Legal Services Charges

Agencies and Fund Sources	Legal Services Charge
Arizona State Retirement System	
State Retirement System Administration Account	$69,100
Subtotal	$69,100
Department of Revenue	
Department of Revenue Administrative Fund	$4,634
Tobacco Tax and Health Care Fund	150
Liability Setoff Revolving Fund	96
IGA and ISA Fund	20
Subtotal	$4,900
Department of State - Secretary of State	
Data Processing Acquisition Fund	$1,800
Subtotal	$1,800
State Treasurer	
State Treasurer's Operating Fund	$9,200
Subtotal	$9,200
Department of Veterans' Services	
Home for Veterans' Trust Fund	$52,700
Subtotal	$52,700
Department of Weights and Measures	
Air Quality Fund	$3,430
Motor Vehicle Liability Insurance Enforcement Fund	770
Subtotal	$4,200
Total Reported Legal Services Charges	**$1,809,500**
Total Legal Services Charges in FY 2014 General Appropriation Act	**$1,809,500**

STATE OF ARIZONA

Joint Legislative Budget Committee

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MICHELLE UGENTI

DATE: October 23, 2013

TO: Representative Jon Kavanagh, Chairman
Members, Joint Legislative Budget Committee

THRU: Richard Stavneak, Director RS

FROM: Ben Henderson, Fiscal Analyst BH

SUBJECT: Arizona Department of Administration - Review of the Arizona Public Safety Communication Advisory Commission

Request

Pursuant to A.R.S. § 41-3542C, the Arizona Department of Administration (ADOA) has submitted for review its FY 2013 annual report of expenditures and progress for the statewide interoperability design project.

Recommendation

The Committee has at least the following 2 options:

1. A favorable review of the department's FY 2013 annual report.

2. An unfavorable review of the department's submission.

Under either option, the JLBC Staff recommends that by March 28, 2014 ADOA provide the Committee for its review, an update on the status of the $3.0 million grant from the State and Local Implementation Grant Program (SLIGP). This funding is part of the federal government's National Public Safety Broadband Network (NPSBN) initiative.

FY 2013 expenditures totaled $446,300 of the $546,300 appropriated from the General Fund. Pursuant to A.R.S. § 41-3014.16, the PSCC terminates on July 1, 2014.

Analysis

Background
The Arizona Public Safety Communication Advisory Commission (PSCC) was established to develop a statewide, standard-based interoperability system that allows public safety personnel from one agency to

(Continued)

communicate, via mobile radio, with personnel from other agencies. An interoperable system enhances the ability of various public safety agencies to coordinate their actions in the event of a large-scale emergency, as well as daily emergencies. Traditionally, local jurisdictions and emergency response agencies are largely responsible for the construction costs, while PSCC receives state and federal funding for coordination and oversight activities.

FY 2013 Accomplishments
PSCC is staffed by the Public Safety Interoperable Communications (PSIC) office. Day to day work of the PSIC office includes analyzing and assisting in the approval of interoperability projects around the state, providing guidance to a variety of public safety communications stakeholders, staff and facilitate the annual meetings for the PSCC and the Statewide Interoperability Executive Committee (SIEC), as well as present at conferences and workgroups and updating a variety of policies and procedures. Broadly these activities fall into the following categories:

- Governance
- Standard Operating Procedures
- Technology
- Training

Governance
Following September 11, 2001, the 9/11 Commission recommended the establishment of a nationwide, interoperable public safety communications network to provide solutions to communications challenges facing first responders. In 2012, Congress passed legislation creating the National Public Safety Broadband Network (NPSBN) initiative. This initiative is an effort to build a nationwide, standards-based, high-speed data network by reserving a part of the electromagnetic spectrum specifically for public safety, the 700 MHz broadband spectrum, or the "D Block."

The NPSBN initiative is being administered and implemented by the First Responders Network Authority (FirstNet), an independent authority within the U.S. Department of Commerce's National Telecommunications and Information Administration (NTIA). FirstNet is comprised of members of both the public and private sectors, representing interests in state and local governments as well as public safety, finance and technology. More than $7 billion has been allocated for the NPSBN initiative, with a majority of funding being raised through the sale of rights to transmit signals over specific bands of the electromagnetic spectrum that were surrendered by television broadcasters during the transition from analog to digital television.

Part of the $7 billion allocated for this initiative includes a grant program for state and local governments, the State and Local Implementation Grant Program (SLIGP). Approximately $118 million in formula-based grants are available to assist regional, state, local, and tribal government entities in preparing for the implementation of the NPSBN initiative. This initial funding is not intended to purchase new equipment, but will instead focus on planning.

The PSIC office is charged with leading the state's efforts in adopting and implementing the NPSBN initiative. In March of 2013, they submitted Arizona's request to the federal government's SLIGP grant program. The state was awarded $3.0 million in grant funds in August 2013. One requirement of the grant is that Arizona and local governments additionally contribute at least $745,200 in in-kind contributions to the project.

The $3.0 million grant will be spent in 2 phases. During the first phase, $1.5 million will be spent on approximately 145 meetings over 2.5 years for education and outreach to tribal and local governments. PSIC intends to inform public safety stakeholders statewide to determine how the new technology may impact governance and operations, and to determine possible participants. During the second phase, $1.5

(Continued)

million would be spent on data collection. As part of the federal initiative, PSIC intends to collect data regarding specific participating entities, coverage requirements, budget considerations, and possible shared infrastructure that FirstNet may utilize during implementation.

The $3.0 million grant includes $2.2 million for 6 FTE Positions, including 3 FTE Positions for program contract staff, and an additional 3 FTE Positions working part-time as vendors and contractors for the project. In addition, $449,000 would be spent on travel, $213,000 would be spent on program support services and web development, and $104,000 would be spent on equipment and supplies.

PSIC has reported that the next steps include developing a detailed education and outreach plan, including the content that will be included in this plan as well as content related to data collection based on FirstNet specifications which have yet to be released. Due to the variability involved in developing this content, the JLBC Staff recommends that by April 29, 2013, the PSIC office return to the Committee to provide a 6-month update on the status of this initiative and the spending of these Federal Funds.

PSIC also pursued additional governance efforts in FY 2013. They held 7 workshops in multiple counties to assist in the development and update of counties' Tactical Interoperable Communications Plans (TICP). These plans align with the National Emergency Communication Plan, as well as the state's Statewide Communications Interoperable Plan, as well as assists local jurisdictions to enhance and implement adequate governance structures. By the end of FY 2013, 11 counties had approved TICPs.

PSIC administers the Communications Assets Survey and Mapping Tool (CASM), which collects information from a variety of agencies about their need and available resources for interoperability, inventory assessments, and provides the tools to analyze the current status of interoperability statewide. An additional 35 agencies began reporting to CASM in FY 2013, for a total of 395 participants to date.

Standard Operating Procedures
As part of the Statewide Communications Interoperability Plan (SCIP), PSIC is charged with establishing a set of standards and procedures to ensure consistent implementation across the state. PSIC updated a variety of these operating procedures regarding land mobile radio equipment standards, interagency radio systems, communication unit training procedures, all-hazards communications recognition procedures, and National Incident Management System (NIMS) workgroup policies. In addition, PSIC developed videos showing how each piece of equipment is deployed, utilized, and shut down when operating Mobile Communications Units (MCU).

Technology
As part of SCIP, PSIC is charged with overseeing technology-based solutions to interoperability. For example, PSIC manages a project along the southern Arizona border, which assists a variety of law enforcement agencies that operate in this region. In FY 2013, the 6th and final transmitter site for this project went online. Throughout the year, PSIC worked with the Yuma Regional Communications System (YRCS), select law enforcement dispatch centers, and a variety of Public Safety Answering Points (PSAP) on equipment installation. This project is funded through $2.2 million in federal Racketeer Influenced and Corrupt Organizations (RICO) funds.

On January 1, 2013, all Federal Communications Commission (FCC) licensees were required to implement equipment designed to operate on channel bandwidths of 12.5 kHz or less. For many licensees, this required a transition from the previous VHF and UHF spectrum systems, which operate on 25 kHz. PSIC assisted many entities in this transition. As of June 30, 2013, 7,067 of the 7,454 transmitters are in compliance with these new requirements.

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Training
As part of SCIP, PSIC is charged with providing a variety of trainings and exercises for different stakeholders across the state. In FY 2013, PSIC provided a variety of 11 different training events to a total of 160 participants.

Expenditures
In FY 2013, PSCC expended $446,300 of the $546,300 General Fund appropriation.

In addition, PSCC utilized $344,300 in federal homeland security grants to help advance interoperable communications throughout Arizona. In addition, $686,500 of the Anti-Racketeering Fund set aside was expended in FY 2013. Of the original $2.2 million set aside, $49,400 in non-lapsing Anti-Racketeering funds remain. These funds are planned to be spent in FY 2014 on equipment. A footnote in the FY 2008 General Appropriation Act specifies legislative intent to use the Anti-Racketeering funds for the detailed design of a long-term interoperability solution.

Total expenditures from all fund sources was $1.5 million. *Table 1* displays expenditures for FY 2013. These amounts exclude the newly awarded $3.0 million federal grant.

Table 1

FY 2013 Expenditures

	FY 2013 Expenditures
General Fund	
Personal Services	$199,600
Employee Related Expenditures	67,900
Professional & Outside Services	30,100
Travel - In State	900
Travel - Out of State	4,900
Other Operating Expenditures	101,700
Equipment	12,500
Transfers	28,700
Subtotal	**$446,300**
Federal Homeland Security Grant	**$344,300**
RICO - Southern Border	**$686,500**
Total Budget	**$1,477,100**

BH/RS:kp

Janice K. Brewer
Governor

Brian C. McNeil
Director

ARIZONA DEPARTMENT OF ADMINISTRATION

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JOINT BUDGET COMMITTEE

October 8, 2013

The Honorable John Kavanagh, Chair
Joint Legislative Budget Committee
Arizona House of Representatives
1700 West Washington St.
Phoenix, AZ 85007

The Honorable Don Shooter, Vice Chair
Joint Legislative Budget Committee
Arizona State Senate
1700 West Washington St.
Phoenix, AZ 85007

Dear Representative Kavanagh and Senator Shooter:

Pursuant to A.R.S. § 41-3542(C), the Arizona Department of Administration (ADOA[1]) is pleased to submit its FY2013 annual report of expenditures and progress of the Public Safety Communications Advisory Commission (PSCC or Commission), including a review of staff operations, to the Joint Legislative Budget Committee (JLBC). This annual report covers the activities of the Public Safety Interoperable Communications Office (PSIC), the PSCC and the Statewide Interoperability Executive Committee (SIEC), which is the operational/technical sub-committee of the PSCC.

The PSCC was established to make recommendations to PSIC on the development of standards-based systems that provide interoperability of public safety agencies' communications statewide. PSIC, PSCC and SIEC help to ensure that Arizona's public safety personnel, at all levels of government and within non-governmental organizations, have access to quality interoperable communication systems, are adequately trained, and utilize such systems effectively in multi-disciplinary, multi-jurisdictional incident response.

Emergency responders need to share vital voice and data information across disciplines and jurisdictions to successfully respond to critical emergencies as well as day-to-day incidents. Emergency responders must be able to communicate (via voice and data paths) as needed, on

[1] Please see Attachment I: Definitions of Acronyms for a complete list of acronyms used in this report.

demand, as authorized, and at all levels of government and across all disciplines. With more than 500 fire, police, and emergency medical service agencies in Arizona responding daily to emergency and life-threatening incidents, public safety communications interoperability is a significant challenge.

Compatible technology between jurisdictions alone will not make an agency interoperable; the jurisdictions must connect policies, procedures, technology, and people to achieve interoperability. Arizona's strategic initiatives leading to a statewide interoperability system are focused in five key areas as defined by the U.S. Department of Homeland Security (DHS) Interoperability Continuum. The continuum (*Attachment A: SAFECOM Interoperability Continuum*) is used by all states in the U.S. and identifies the five critical areas that must be addressed to achieve true interoperability:

- Governance
- Standard Operating Procedures
- Technology
- Training and Exercise
- Usage and Outreach

Strategic initiatives in these five areas are defined in Arizona's strategic plan for interoperability entitled the Statewide Communications Interoperability Plan (SCIP)[2]. These initiatives are listed in *Attachment B: SCIP Initiatives Alignment with AZ Statutes and National Emergency Communications Plan Requirements*. Key FY2013 accomplishments in each of these areas are outlined below with additional detail included in the attachments to this report.

Governance (SCIP Initiatives #1-3)
Governance is a formalized system that provides a unified approach to decision-making to reflect shared objectives across multiple disciplines and jurisdictions. Strong governance is essential to interoperability because it provides a framework for planning, collaboration and implementation between and among multiple disparate communication systems and stakeholders.

Arizona has well-established interoperable communications governance bodies and plans, which include:

- A statewide governance body for interoperability (PSCC) established in statute[3].
- A technical/operational subcommittee (SIEC) operating in support of PSCC.
- A Statewide Interoperability Coordinator (SWIC) in the PSIC Office.
- A strong group of engaged stakeholders who participate in interoperability workgroups (that support development of policies and programs).
- A statewide plan for interoperability (SCIP) that is aligned with the national plan for interoperability (National Emergency Communications Plan or NECP).
- A plan for the SWIC Office (PSIC Office Plan) in support of SWIC activities.

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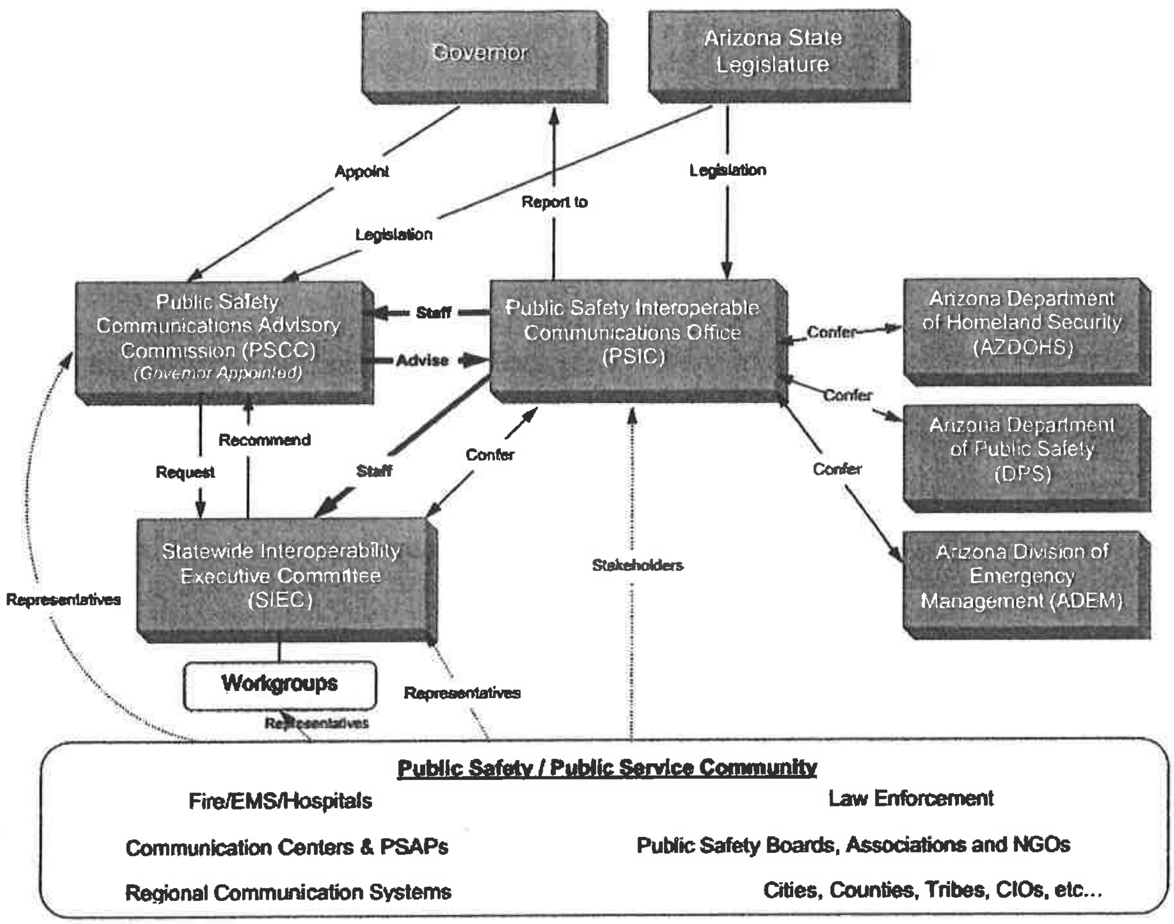
[2] www.azpsic.gov/SCIP/
[3] http://www.azleg.state.az.us/FormatDocument.asp?inDoc=/ars/41/03541.htm&Title=41&DocType=ARS

State of Arizona Governance Structure for Public Safety Interoperable Communications



Regional Governance: In FY2013, PSIC focused our governance efforts on advancing governance at the regional level. Seven workshops were held in multiple counties to assist in the development or update of Tactical Interoperable Communications Plans (TICP). These plans follow a national framework, align with the NECP and the Arizona SCIP, and assist local jurisdictions to evolve governance structures in support of interoperability on the regional level. Further, the plans document the interoperable communications governance structures, technology assets, and usage policies and procedures for a jurisdiction. In support of this effort, the PSIC Office also provides an Arizona specific TICP template which has been prepopulated with Arizona specific language. As of the end of FY2013, eleven Arizona counties had approved TICPs.

PSIC also administers the Communications Assets Survey and Mapping Tool (CASM) to collect and maintain information on State and local Public Safety/First Responder communications. CASM is a web-based single repository to support interoperable communications analysis to:

- Facilitate information sharing
- Hold communication assets inventory assessment (agency, region, statewide)

- Foster inter-agency interoperability analysis
- Enable development of Tactical Interoperable Communication Plans (TICPs)
- Evaluate an agency's Need vs. Ability to communicate

As part of the TICP development process, PSIC continued our multi-year project to collect data on local interoperable communication assets. During FY2013, an additional 35 agencies started sharing data within CASM, for a total of 395 participating agencies.

Public Safety Broadband: In FY2013, PSIC continued efforts to position Arizona to take advantage of the upcoming National Public Safety Broadband Network (NPSBN) initiative. The NPSBN is an effort to build a nationwide, standards-based, high-speed data network with dedicated spectrum for the needs of public safety users (primary and secondary). The utilization of 4G Long Term Evolution (LTE) standards-based technology will provide reliability, resiliency, security, and interoperability.

The NPSBN will be a self-sustaining, fee-based network with potential for public/private partnerships and sharing of tribal, state, and local infrastructure to lower costs. The network will be built and operated by FirstNet - an independent authority within the National Telecommunications & Information Administration (NTIA). On a national basis, there is up to $7 billion available for the build out of the NPSBN; including $135 million that has been made available to states as part of the State and Local Implementation Grant Program (SLIGP).

The PSIC Office, under the direction of the State Chief Information Officer (CIO) and in conjunction with the PSCC, has been designated as the lead in developing public safety broadband strategy and recommendations for the Governor's Office. Monthly briefings have been sent to the Governor's public safety advisor and representatives of the Department of Public Safety (DPS), Arizona Department of Homeland Security (AZDOHS), ADOA and ADOA-ASET on an ongoing basis since March of 2012.

The PSIC Office submitted Arizona's SLIGP grant request on March 19, 2013. This program is to provide education, outreach and data collection activities in support of the NSPBN in Arizona. Arizona's grant application has been favorably reviewed by the NTIA and $2,911,147 in grant funds were awarded in August 2013.

The PSIC Office team and their partners continue to track activities at the national level and develop plans at the state level relative to Arizona's portion of the planned network.

Additional governance related activities included:

- An annual update to the PSIC Office Plan[4] which details how this office will use its resources in alignment with its Arizona State statute and in advancement of Arizona's SCIP.

[4] http://www.azpsic.gov/plans/FY2013_PSIC_Office_Plan_FINAL.pdf

- Development of a SCIP Implementation Report[5] for Federal DHS to track Arizona's progress.
- Input to Federal Emergency Management Agency (FEMA), Arizona Division of Emergency Management (ADEM), and AZDOHS to assure that their plans for Arizona (FEMA's Emergency Communications Plan (ECP), ADEM's State Emergency Response and Recovery Plan (SERRP), and AZDOHS's State Homeland Security Strategy (SHSS)) are in alignment with Arizona's SCIP.
- Participation in the Regional Emergency Communications Coordinators Working Group (RECCWG)

Please also see *Attachment C: Governance Accomplishments* for additional details regarding these Governance efforts.

Standard Operating Procedures (SOP) (SCIP Initiative #4)
A reliable Policies, Standards and Procedures (PSPs) framework enables stakeholders to implement interoperability projects consistently across the state. The PSIC Office has established a framework for interoperable communications PSPs in accordance with SCIP Initiative #4, *Establish a Policies, Standards and Procedures (PSP) Framework, and Implement PSPs, Including SOPs, for Statewide Interoperable Communications Solutions.*

The policies, standards and procedures established by the Commission enable emergency responders to successfully coordinate an incident response across disciplines and jurisdictions. Clear and effective PSPs are essential in the development and deployment of interoperable communications solutions. There are currently nine PSPs approved by either the PSCC or SIEC in the areas of Governance, Training, and Technology. These PSPs are consistent with the Commissions legislative mandate to make recommendations to ADOA-ASET on the development of standards-based systems that provide interoperability of public safety agencies' communications statewide.

PSIC has established a standard annual review cycle for all PSPs to ensure each document is kept up to date and stakeholders have an opportunity to request changes and provide input. All documents are subject to an internal review, subject matter expert workgroup review, and public comment prior to drafts being presented to the PSCC or SIEC for approval, as appropriate. The PSIC Office has also established a standardized template and style guide to provide consistency when creating PSP documentation.

Statewide policies, standards and procedures updated this year include:

- Land Mobile Radio Minimum Equipment Standards Update - establishes minimum standards for certain radio features that are nationally recognized to promote and maintain a higher level of interoperable communications among and between public safety jurisdictions and disciplines.

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[5] http://www.azpsic.gov/library/reports/2012/AZ_SCIP_Implementation_Report_FFY2012.pdf

- Arizona Interagency Radio System (AIRS) Improvement and Sustainability Plan – establishes requirements for the integration of locally procured AIRS site communications infrastructure into the AIRS system in order to improve the overall coverage of AIRS in Arizona. The procedure provides guidance for initial requests for new AIRS site approvals and documents ongoing maintenance responsibilities if new sites are approved.
- Arizona Communication Unit Training Coordination Procedure – a statewide procedure developed by PSIC (with input from ADEM and SIEC) to coordinate All-Hazards Communications Unit Training in Arizona. The procedure defines appropriate instructors for the All-Hazards Communications Unit position courses, how Arizona will develop a cadre of such Instructors, and how communications unit training courses can be requested.
- Arizona Regional All-Hazards Communications Unit Recognition Procedure – documents the process for requesting Arizona regional recognition for communications unit positions that align with associated Federal DHS approved curriculum and task book.
- National Incident Management System (NIMS) Communications Unit Workgroup (NIMS-CU) Policies and Procedures – documents the procedures that will be followed by the workgroup and the PSIC Office to review the qualifications of individuals seeking Arizona regional recognition for All-Hazards Communications Unit positions.

PSIC also worked with the ADEM to develop a detailed Standard Operating Procedure (SOP) and Concept of Operations Plan (CONOPS) for the State's five Mobile Communications Units (MCU). MCU's are vehicles equipped with specialized radio and communications equipment to support public safety operations in remote areas. The documents will also be made available to local agencies for customization and use with their MCU's. As a result of this effort, ADEM, PSIC, and the Gila County Emergency Manager's office worked with the federal Office of Emergency Communications (OEC) to create a video version of the MCU SOP. Videos were created to show how each piece of equipment is deployed, utilized, and shut down. The videos were put together in a similar fashion to the written SOP.

Please also see *Attachment D: SOP Accomplishments* for details regarding SOP related efforts.

Technology (SCIP Initiatives #5-9)
Arizona is currently pursuing a system-of-systems approach to interoperability, coordinating and encouraging interconnection of operability and interoperability communications assets to one another in order to provide communications between state, regional and local systems. Existing interoperability assets include shared systems, shared channels, gateways, radio caches and other communications technologies.

During FY2013, PSIC and its partners continued advancing technology related SCIP Initiative #s 5 to 9 as described below and in more detail in *Attachment E: Technology Accomplishments*:

- Enhance and Promote the AIRS Interoperable Communications Solution, including development of the AIRS Improvement and Sustainability Plan (SCIP Initiative #5)

- Implement, Enhance and Promote Functional Regional Voice and Data Systems in Support of Interoperable Communications (SCIP Initiative #6)
- Upgrade the Statewide Microwave Backbone Infrastructure to Digital Technology (DPS) (SCIP Initiative #7)
- Sustain the State Strategic Technology Reserve (STR) (ADEM) (SCIP Initiative #8)
- Upgrade Operable Voice and Data Communication Systems for State Agencies in Support of Interoperable Communications (SCIP Initiative #9)

RICO Project: The PSIC Office continued to manage the implementation of the project (approved by JLBC) which utilizes $2.2 million in Racketeer Influenced and Corrupt Organizations (RICO) funds for the advancement of communications interoperability along the southern Arizona border. The project deployed standards-based P25 communications capabilities at six key transmitter sites supported by the DPS upgraded digital microwave system, and supports hardware and software upgrades to the Yuma Regional Communications System (YRCS) infrastructure. The project provides high-level connectivity for existing and developing communication systems thus increasing interoperability capabilities during multi-jurisdictional, multi-agency response and recovery, and mitigating impacts from critical incidents in the border region.

Additionally, the RICO Project provides communications equipment to selected law enforcement dispatch centers and Public Safety Answering Points (PSAP) in the region. Through the creation of a Southeastern Arizona Communications Center Talk Group, the dispatch centers will be able to share information and coordinate efforts between participating agencies in the border region. This will alleviate the need for dispatchers to make a phone call or send a teletype every time they need to relay information to, or coordinate with, a neighboring jurisdiction. The talk group may also be used for situations such as requesting resource assistance (e.g., K9, helicopter, officers), broadcasting critical attempts to locate (e.g., missing children, carjacking, pursuit) and immediate notification of PSAP equipment failures/evacuations.

During FY2013, the sixth transmitter site was activated and the PSIC Office continued to meet with YRCS, selected law enforcement dispatch centers, and PSAPs in the region on equipment installation. The System Wide Calling channel was created. Three agencies have already completed the Memorandum of Understanding (MOU) process, with nine additional agencies working through their internal process to gain approval.

Narrowbanding: On or before January 1, 2013, all existing Federal Communications Commission (FCC) licensees on the VHF and UHF Spectrum were required to implement equipment designed to operate on channel bandwidths of 12.5 kHz or less or that meets a specific efficiency standard. Licensees were required to convert or replace their existing VHF and UHF wideband (25 kHz) systems.

The FCC narrowbanding requirements impact public safety operability and as a result are important for interoperability. Since 2009, the PSIC Office has continuously provided education and outreach to the Arizona Public Safety community on the pending narrowband deadline.

Activities include direct stakeholder outreach, monthly updates to the PSCC and SIEC, providing online resources, and communications to our e-mail distribution list of over 850 public safety stakeholders. As of June 30, 2013, 94.9% of transmitter licenses in Arizona (7067 out of 7454 transmitters) are in compliance with the FCC requirements. Some Arizona licensees, such as Pima County, requested and received waivers from the FCC for a designated time-frame, allowing additional time to narrowband or move off of existing VHF/UHF systems.

Training & Exercise (SCIP Initiatives #10-11)
Implementing effective training and exercise programs is essential for ensuring that technology actually works as planned and that responders are able to demonstrate that they can effectively communicate using that technology.

Communications Unit Training and Recognition Program: During all-hazards emergency response operations, radio communication among multiple jurisdictions and disciplines is essential. Trained communications professionals working to achieve interoperability among responding agencies can significantly improve communications during an emergency incident. The PSIC office coordinates training opportunities for individuals to serve as All-Hazards Communications Unit Leaders (COML) or All-Hazards Communications Unit Technicians (COMT) consistent with SCIP Initiative #10.

The COML heads the Communications Unit and is responsible for integrating communications and ensuring that operations are supported by communications. The COML must understand Incident Command System (ICS) and local response systems to support the efforts of incident personnel. To date, 253 Arizona students have completed the All-Hazards COML Course. The PSIC Office collaborated with ADEM and county emergency management offices in FY2013 for seven COML courses training 88 students:

- Yuma, AZ – October 22-25, 2012
- Phoenix, AZ – January 26-27 and February 2-3, 2013 (weekend course)
- Tucson, AZ – April 30 - May 2, 2013
- Casa Grande, AZ – May 6 - 8, 2013
- Phoenix, AZ – May 10 - 12, 2013
- Prescott, AZ – May 13 - 15, 2013
- Globe, AZ – May 14 - 16, 2013

The role of the COMT is to provide for the technical implementation of incident communications systems, which include providing for equipment distribution, tracking equipment, training users on use of equipment, verifying proper programming of equipment, and assisting the COML in the development of the Incident Radio Communications Plan. To date, 82 students have been trained in practices and procedures common to COMTs during all hazards emergency operations. Due to the technical nature of the training, course enrollment is limited to 15 students and is offered by invitation only. Three All-Hazards COMT courses were conducted in FY2013 as follows:

- Maricopa County – November 26 - 30, 2012
- Coconino County – April 22 - 26, 2013

- Yuma County –April 29 - May 3, 2013

Arizona's first Communications Unit Training Field Day was held on February 20, 2013. A total of 27 trainees participated, representing 19 agencies from 5 counties. The Field Day provided attendees with necessary specialized COML and COMT training and hands-on experience. The field day was open to individuals who completed the initial COML or COMT classroom training and wished to get their taskbooks signed off in order to become recognized as a regional COML or COMT. The successful event could not have been accomplished without the volunteer help of the Field Day Event Planning Team. The twenty individuals on the planning team contributed their time and years of first-hand operational public safety and emergency management experience at no cost to the State to plan and staff the Field Day.

Additional accomplishments during FY2013 regarding Training and Exercise initiatives and objectives are outlined in *Attachment F: Training & Exercise Accomplishments* and include:

- Development and delivery of a workshop on Effectively Incorporating Communications into Public Safety Exercises.
- Continued implementation of the communications unit training and recognition program consistent with national standards and ADEM requirements.
- Continued support for statewide AIRS Training program, including a DVD, lesson plan and other training materials to promote the use of AIRS frequencies statewide.
- Participated in three communications focused exercises in support of Arizona communities.

Usage & Outreach (SCIP Initiative #12)

The PSCC and SIEC each met four times in FY2013 and in these meetings approved interoperability projects and policies, heard updates from regional systems, provided guidance to and received technical advice from its workgroups and provided significant feedback to PSIC regarding advancement of SCIP initiatives.

PSIC staff regularly attended and presented at conferences, workshops, expos, taskforces, and national, multi-state, state, regional, local and working group meetings. PSIC also conducted in-person meetings, web and telephonic conferences, posted updates to its website and communicated regularly by e-mail to its extensive (850+) interested parties list.

The PSIC Office promoted collaboration among members of public safety and service agencies/organizations by updating the *Statewide Education and Outreach Plan Regarding Public Safety Communications Interoperability*[6]. The Plan highlighted specific targeted interoperability topics of significant importance in 2013:

- FCC Narrowbanding Compliance
- Public Safety Broadband

[6] http://www.azpsic.gov/plans/Education_and_Outreach_Plan_2012_Approved_07172012.pdf

- NECP Gap Closure (including Regional Interoperability Planning, Communications Asset Survey and Mapping (CASM), TICPs, Strategic Communication Migration Plans (SCMPs) and other resources)

These and other activities are outlined in *Attachment G: Usage and Outreach Accomplishments.*

Reports
Annual Report to Governor and Legislature – PSIC presented a draft annual report to PSCC at its November 13, 2012, meeting. The PSCC approved the report for transmission to the Governor and the Legislature. The report was submitted on December 1, 2012, and is available on the PSIC website.

Annual SCIP Implementation Report - On October 31, 2012, PSIC submitted Arizona's annual report to Federal DHS Office of Emergency Communications covering progress in achieving the initiatives and strategic vision identified in Arizona's SCIP. The report is available on the PSIC website.

Quarterly Programmatic Grant Reports – As a recipient of Federal Homeland Security grants, PSIC submits quarterly grant reports to AZDOHS.

Budget
For FY2013, $542,700 was appropriated from the general fund for the public safety communications program. PSIC continued to utilize vacancy savings and maximize federal grants to support its goal of advancing interoperable communications in Arizona in the most fiscally responsible manner. In addition, the PSIC Office was able to successfully leverage volunteer subject matter experts and workgroup members for many of the accomplishments listed in this report resulting in reduced expenditures for the State. As of June 30, 2013, $446,286 had been expended or encumbered. A breakdown of expenditures by category is attached as *Attachment H: FY2013 PSIC Expenditures.*

In addition to general fund expenditures, $344,349 was spent by the PSIC Office from Federal Homeland Security grants during FY2013 to support achievement of the results outlined in this report.

The Technology section above describes the use of $2.2 million of non-lapsing Anti-Racketeering (RICO) Fund monies. As detailed above, the project is proceeding well. During FY2013, $686,477 of these RICO funds was expended. The remaining RICO Fund monies of $49,425 will be used in FY2014 on equipment installation at selected dispatch centers.

Federal Technical Assistance Awards
OEC's Interoperable Communications Technical Assistance Program (ICTAP) works to ensure, accelerate, and attain operable and interoperable emergency communications nationwide through the offering of non-monetary Technical Assistance (TA) grants to the states.

TA requests are submitted annually by PSIC on behalf of the State after solicitation of stakeholder input and consultation with the PSCC, SIEC, and the Arizona Department of Homeland Security (AZDOHS). Each state can apply for up to five (5) TA offerings. Arizona received the following five TA awards in 2013:

- Communications Focused Table Top Exercise (OP-TTX) – Coconino County – Complete
- NIMS ICS All-Hazards Communications Unit Technician Course (TRG-COMT) - Flagstaff - Complete
- Mobile Communications Unit Support (OP-MCUS) - Statewide
    - Concept of Operations Document – Complete
    - Video SOP Development – Complete
- Outreach, planning, and data collection for Broadband (ENG-BRDBND)– Statewide - In progress

In addition, the City of Yuma received the following TA assistance through the Border Interoperability Demonstration Project:

- Tactical Interoperable Communications Field Operations Guide (TIC-FOG) Development – Complete
- Communications-Focused Functional Exercise (OP-FE) – In progress
- Communications-Focused Exercise Workshop (OP-TEPW) – Complete
- Standard Operating Procedure (SOP) Development (SOP-DEV) – In progress

Please contact me with any questions regarding the activities of the PSCC, SIEC and PSIC Office.

Sincerely,

Aaron V. Sandeen
Deputy Director & State CIO
Chairman Designee, Public Safety Communications Advisory Commission

Enclosures

cc: Richard Stavneak, Director, Joint Legislative Budget Committee
Ben Henderson, Analyst, Joint Legislative Budget Committee
John Arnold, Director, Office of Strategic Planning and Budgeting
Ken Matthews, Budget Analyst, Office of Strategic Planning and Budgeting
Philip D. Manfredi, Chief Strategy Officer, ADOA-ASET
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