COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER

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OSCAR VALDEZ
AUDITOR-CONTROLLER

CONNIE YEE
CHIEF DEPUTY AUDITOR-CONTROLLER

March 27, 2025

TO: Each Supervisor

FROM: Oscar Valdez
Auditor-Controller

Robert G. Campbell
Assistant Auditor-Controller / Chief Audit Executive

SUBJECT: **L.A. CARE HEALTH PLAN – FINANCIAL CONDITION REVIEW FOR FISCAL YEARS 2020-21 AND 2021-22**

NUMBER OF RECOMMENDATIONS	
PRIORITY 1	1 — CORRECTIVE ACTION REQUIRED WITHIN 90 DAYS
PRIORITY 2	0 — CORRECTIVE ACTION REQUIRED WITHIN 120 DAYS
PRIORITY 3	0 — CORRECTIVE ACTION REQUIRED WITHIN 180 DAYS

As required by the State of California Welfare and Institutions Code Section 14087, with the support and active participation of L.A. Care Health Plan (L.A. Care or Agency), we evaluated the Agency's financial condition for Fiscal Years (FY) 2020-21 and 2021-22, and assessed the outlook of their FYs 2021-22 and 2022-23 revenues and expenses.

Based on L.A. Care's Independent Auditor's Report, the Agency's combined financial statements for FYs 2020-21 and 2021-22 are presented fairly, in all material respects. In addition, opinions regarding going concern were *not* issued, which indicates the Agency was expected to have the resources to meet its financial obligations for at least one year after the issuance of their financial statements. Highlights include:

- L.A. Care's revenues exceeded their expenses by approximately $161 million ($9.210 billion in operating revenues less $9.049 billion in operating expenses) and $89 million ($9.012 billion in operating revenues less $8.923 billion in operating expenses) at the end of FYs 2020-21 and 2021-22, respectively. In addition, L.A. Care's net position was approximately $1.049 billion ($4.967 billion in total assets less $3.918 billion in total liabilities and deferred inflow of resources) in FY 2020-21 and $1.087 billion ($5.834 billion in total assets less $4.747 billion in total liabilities and deferred inflow of resources) in FY 2021-22.

FAST FACTS

L.A. Care is the Local Initiative Health Authority for the County of Los Angeles and the nation's Largest locally-based, publicly-operated health plan with approximately 2.6 million members, as of August 2024.

- L.A. Care's FY 2022-23 Operating and Capital Budget, as compared to their FY 2021-22 actual results, projects an increase in operating revenues and expenses to $10.165 billion and $10.085 billion, respectively, but a decrease in income from operations to approximately $80.7 million. Agency management indicated this is related to increased staffing and contracting for their medical cost centers, and increased Salaries and Employee Benefits.

However, we noted that L.A. Care's FY 2021-22 audited financial statements had understated liabilities by approximately $31.4 million ($30.6 million in current liabilities and $795,000 in long-term liabilities), due to an inadvertent mis-categorization of funds. Since the misstatement was less than 1% of total liabilities, it does not affect our evaluation of L.A. Care's overall financial health.

L.A. Care management indicated that they communicated our finding to their Audit Committee and will work with their independent auditors to ensure liabilities are appropriately reported in future years. We will assess and report on the status of our recommendation during our following annual financial condition review.

For details of our review, see Attachment I. The Agency's response, Attachment III, indicates general agreement with our findings and recommendations.

We thank L.A. Care management and staff for their cooperation and assistance during our review. If you have any questions please call us, or your staff may contact Jesse Urbano at jurbano@auditor.lacounty.gov..

OV:CY:RGC:JU:gcb

Attachments

c: Fesia A. Davenport, Chief Executive Officer
Edward Yen, Executive Officer, Board of Supervisors
Christina R. Ghaly, M.D., Director, Department of Health Services

L.A. CARE HEALTH PLAN
FINANCIAL CONDITION REVIEW
FISCAL YEARS 2020-21 AND 2021-22

BACKGROUND AND SCOPE

We have completed a review of L.A. Care Health Plan's (L.A. Care or Agency) annual financial condition for Fiscal Years (FY) 2020-21 and 2021-22. The County of Los Angeles (County) is required by the State of California (State) Welfare and Institutions Code (WIC) Section 14087.9675 to perform an annual financial condition review of its Local Initiative Health Authority (local initiative). We conducted our review in conformance with the *International Standards for the Professional Practice of Internal Auditing* and will continue to review L.A. Care's financial condition annually, as required.

Background

L.A. Care is the local initiative for the County. The Agency is an independent, tax-exempt public agency created by the County, and initially funded by the State and the Federal Government of the United States of America, to provide managed health care services to low-income residents. L.A. Care was developed in response to the State's plan to transition Medi-Cal recipients to managed care. In 1994, Senate Bill (SB) 2092 was enacted, which enabled the creation of L.A. Care. Shortly after the passage of SB 2092, the Board of Supervisors adopted an ordinance to establish L.A. Care as a separate legal entity from the County.

Scope and Objectives

We evaluated L.A. Care's financial condition for FYs 2020-21 and 2021-22, and assessed the outlook of their FYs 2021-22 and 2022-23 revenues and expenses. Our review included interviewing L.A. Care financial management, analyzing their independently audited financial statements and FYs 2021-22 and 2022-23 Operating and Capital Budgets (budgets), and reviewing regulatory agencies' reports issued on L.A. Care during FYs 2020-21 and 2021-22.

Our reviews of the Agency's financial condition for FYs 2020-21 and 2021-22 were delayed due to priority assignments, the COVID-19 public health emergency, which impacted operations countywide and inevitably required the reprioritization of all projects/workloads, and the need to complete the Agency's financial condition review for FY 2019-20. We conducted this consolidated financial condition review for two FYs to bring us closer to the current schedule of these annual reviews.

FINANCIAL CONDITION AND OUTLOOK

Operating Revenues and Expenses

We reviewed L.A. Care's independently audited financial statements for FYs 2020-21 and 2021-22, and noted that the Independent Auditor's Report opinion for each year asserts that L.A. Care's combined financial statements were presented fairly, in all material respects. In addition, opinions regarding going concern were *not* issued, which indicates that the Agency was expected to have the resources to meet its financial obligations for at least one year after the issuance of their financial statements.

We also conducted our own high-level financial analyses based on L.A. Care's audited financial statements and noted the following:

- **Operating Revenues -** The Agency's operating revenues totaled approximately $9.210 billion and $9.012 billion in FYs 2020-21 and 2021-22, respectively, and included funds from the State's Department of Health Care Services (DHCS), Centers for Medicare and Medicaid Services (CMS), State, County, and individual member premiums.

- **Operating Expenses -** L.A. Care's operating expenses totaled approximately $9.049 billion and $8.923 billion in FYs 2020-21 and 2021-22, respectively, and mainly consisted of health care expenses, such as capitation payments for professional services (e.g., office visits, immunizations, and medical procedures) and pharmacy claims.

- **FY 2020-21 Operating Changes -** In FY 2020-21, L.A. Care's operating revenues and expenses increased by $856.4 million (10.3%) and $564.1 million (6.7%), respectively from FY 2019-20, primarily due to increased revenues (i.e., 9.2% net increase in member months and annual rate increases for Medi-Cal, L.A. Care Covered, and Cal MediConnect), and offset by increases in all expense categories, such as capitation payments for professional services, inpatient/outpatient claims (e.g., hospital stays, emergency room visits, and Skilled Nursing Facility (SNF) stays), In-Home Supportive Services (IHSS) Program claims, and pharmacy claims.

- **FY 2021-22 Operating Changes -** In FY 2021-22, L.A. Care's operating revenues and expenses decreased by $197.9 million (2.2%) and $126.7 million (1.4%), respectively from FY 2020-21, primarily due to Proposition 56 (California Healthcare Research and Prevention Tobacco Tax Act) payment reductions by the State, and the transition of pharmacy service claims from L.A. Care to the State effective January 2022, which resulted in a reduction in revenues of approximately $530.7 million and $474.4 million, respectively, and was partially offset by an increase in member months of 2.3 million (i.e., $703.8 million increase in revenues).

Details of L.A. Care's revenues and expenses for FY 2018-19 through FY 2021-22 are provided in Table 2 of Attachment II.

Financial Analyses

We used L.A. Care's independently audited financial statements for FYs 2020-21 and 2021-22, and various financial ratios to determine the Agency's financial health and stability. We noted the following:

- **Short-term solvency, debt-paying capability, and ability to carry operating costs -** L.A. Care's current assets and liquid assets (i.e., cash, short-term securities, and accounts receivable) exceeded their current liabilities by 20% and 18% in FYs 2020-21 and 2021-22, respectively. This indicates that the Agency had sufficient current resources to cover short-term liabilities and was able to finance current operations and meet obligations as they became due in both FYs.

- **Ability to generate revenues in excess of expenses -** L.A. Care generated revenues in excess of expenses in both FYs 2020-21 and 2021-22. Specifically, L.A. Care generated approximately $161 million in net operating income ($9.210 billion in operating revenues less $9.049 billion in operating expenses) in FY 2020-21, and approximately $89 million ($9.012 billion in operating revenues less $8.923 billion in operating expenses) in FY 2021-22.

  Financial performance requirements - L.A. Care met the State's minimum tangible net equity (TNE) requirement of $154.4 million and $159.3 million in FYs 2020-21 and 2021-22, respectively, which the Agency calculates and reports directly to the State's Department of Managed Health Care (DMHC). Specifically, the Agency generated positive net positions of approximately $1.049 billion ($4.967 billion in total assets less $3.918 billion in total liabilities and deferred inflow of resources) and $1.087 billion ($5.834 billion in total assets less $4.747 billion in total liabilities and deferred inflow of resources) in FYs 2020-21 and 2021-22, respectively, which exceeded their minimum TNE requirement for each year. Title 28 of the California Code of Regulations (CCR) Section 1300.76 requires all health plans to maintain a minimum TNE equal to the greater of $1 million, a percentage of premium revenues, or a percentage of healthcare expenses, to ensure a health plan's financial viability. In addition, L.A. Care's total administrative expenses were approximately 5.1% and 5.6% of their total revenues for FYs 2020-21 and 2021-22, respectively, both of which remained below the 15% maximum administrative cost ratio (total administrative expenses over total revenue) required by Title 28 of CCR Section 1300.78(b).

- **Financial reporting requirements -** We noted that liabilities were understated in L.A. Care's FY 2021-22 audited financial statements by approximately $31.4 million ($30.6 million in current liabilities and $795,000 in long-term liabilities) due to being mis-categorized as deferred inflow of resources.

  During our review, we discussed regulatory changes and the presentation of financial statements with L.A. Care, including those related to liabilities and deferred inflow of resources, and noted discrepancies when we reviewed and compared what the Agency indicated is required by Governmental Accounting Standards Board Statement No. 65 (GASB 65) to what was reported in their audited financial statements. Specifically, GASB 65 requires that resources received before all funding eligibility requirements are met be reported as liabilities, and as deferred inflow of resources once all the eligibility requirements are met (excluding time requirements in either case).

  However, we reviewed the notes to L.A. Care's FY 2021-22 audited financial statements, which state that $30.6 million in Incentive Payment Program funds were received in advance of meeting eligibility requirements, yet they were mis-categorized as deferred inflow of resources (i.e., Deferred Revenue) on the Combined Statements of Net Position, instead of liabilities, as required by GASB 65. In addition, we further reviewed the total amounts reported as deferred inflow of resources and noted that an additional $795,000, received for the Student Behavioral Health Incentive Program, had not met all eligibility requirements and were also mis-categorized as deferred inflow of resources instead of a liability.

  Since both deferred inflow of resources and liabilities are subtracted from total assets to calculate net position, and the $31.4 million misstatement accounted for less than 1% of total liabilities (approximately $4.7 billion), this error does not affect our evaluation of L.A. Care's overall financial health, including our determination that they met their minimum TNE requirement for that year (as noted above). **(NOTE: We have adjusted all charts in this report, including ensuring our financial analyses and ratios appropriately account for the misstated liabilities, where applicable.)**

L.A. Care shared our findings with their external Certified Public Accountants (CPA), who confirmed the error was an inadvertent mis-categorization and that the amounts should have been reported as liabilities. However, L.A. Care and their CPAs determined that the error's impact to the Agency's financial statements was neither qualitatively nor quantitively material, and did not require a restatement.

Recommendation:

1. **Priority 1 - L.A. Care management work with their external Certified Public Accountants to ensure liabilities and deferred inflow of resources are appropriately reported, in accordance with applicable reporting standards.**

   Agency Response: Agree

We will assess and report on the status of our recommendation during our following annual financial condition review, including if any financial statement corrections were made or required.

Details on L.A. Care's assets, liabilities, and deferred inflow of resources for FY 2018-19 through FY 2021-22 are provided in Table 1 of Attachment II.

Outlook of Revenues and Expenses

We compared L.A. Care's FYs 2021-22 and 2022-23 financial budgets to their FYs 2020-21 and 2021-22 actual results, and noted that L.A. Care projected membership to decrease by approximately 69,500 (3%) to 2.39 million by fiscal year-end September 2022, but their actual membership that year increased by 252,800 (10%) to 2.72 million. In addition, we noted that L.A. Care projected membership to decrease by approximately 58,100 (2%) to 2.66 million by fiscal year-end 2023. L.A. Care indicated they expected the State would resume the Medi-Cal redetermination process (i.e., members' eligibility is reassessed) at two different points in time (i.e., January 2022 and February 2023), resulting in a gradual disenrollment of members over a 12 to 14-month period, which contributed to the Agency's projected decreases in membership. The State had suspended the redetermination process during the COVID-19 public health emergency, resulting in higher membership, since people who might have lost coverage during the normal annual process were not dropped. However, the State did not resume the redetermination process until April 2023, leading to a continued increase in membership to 2.72 million through September 2022, as mentioned above. The redetermination process will likely impact L.A. Care's membership in FY 2022-23, which we will assess and report on during our following annual financial condition review.

In addition, L.A. Care projected positive net positions for FYs 2021-22 and 2022-23, despite expecting operating revenues and expenses to decrease to $8.638 billion (6%) and $8.494 billion (6%), respectively in FY 2021-22, and increase to $10.165 (13%) billion and $10.085 (13%) billion, respectively in FY 2022-23. As of January 2022, Medi-Cal outpatient pharmacy service claims transitioned from L.A. Care to the State, resulting in the Agency no longer receiving or incurring the related revenue and expenses, which contributed to their projected decrease in FY 2021-22. However, their actual operating revenues and expenses only decreased by $197.9 million (2.15%) and $126.7 million (1.4%), respectively. The Agency also indicated that the projected increase in revenues and expenses in FY 2022-23 is primarily due to higher rates set by DHCS and increases in expenses for capitation payments for professional services, inpatient/outpatient claims, IHSS claims, and SNF claims.

Oversight by Governing Agencies

L.A. Care's operations are reviewed by various agencies, including DMHC, CMS, and DHCS. These regulatory agencies perform a variety of audits and reviews, including financial, operational, and administrative. Regulatory compliance findings in these audits and reviews may lead to corrective action plans, fines, penalties, and/or suspension or revocation of the State license, which could affect L.A. Care's financial condition.

In reviewing relevant reports issued on L.A. Care, we noted that DHCS and DMHC conducted coordinated investigations that resulted in $55 million in regulatory penalties ($20 million from DHCS and $35 million from DMHC) for L.A. Care. Both State agencies' investigations found several violations, including L.A. Care's mishandling of enrollee grievances, delayed processing of requests for authorization, and inadequate oversight and supervision of its contracted entities regarding timely access to health care services. In October 2024, the Agency reached a settlement agreement with DHCS and DMHC, which requires L.A. Care to work with a consultant to develop corrective actions over the related findings/violations. In addition, L.A. Care paid out a total of $27 million in financial penalties in October 2024 and agreed to spend the remaining $28 million on community investments over the course of three years.

We also noted that, although L.A. Care had accrued the total penalty amounts in FY 2021-22, the Agency still generated $89.5 million in income from operations and the Independent Auditor's Report opinion indicated that their combined financial statements were presented fairly, in all material respects (as noted above). In addition, the CPAs did *not* issue an opinion regarding going concern, which indicates they did not detect conditions or events that would raise substantial doubt about the Agency's ability to meet its financial obligations, such as the penalties mentioned above, for at least one year after the issuance of their financial statements.

We will continue to monitor, review, and report on L.A. Care's financial condition annually, as required by WIC Section 14087.9675.

STATUS OF PRIOR YEAR RECOMMENDATION(S)

Recommendation FY 2019-20 No.1:

Priority 1 - L.A. Care management should work with their Board of Governors to assess the feasibility and benefits of implementing a multi-year financial forecasting process.

Priority Ranking: Recommendations are ranked from Priority 1 to 3 based on the potential seriousness and likelihood of negative impact on the Agency's operations if corrective action is not taken.

Original Issue/Impact:

L.A. Care did not project financial outcomes beyond the following fiscal year. Although L.A. Care is not legislatively required to do so, it is a best practice to create multi-year (e.g., 3-5 years) financial forecasts to appropriately identify, track, and manage the effects of future trends (e.g., decreasing revenues, increasing expenses, and legislative or industry changes, such as ones noted in this report) that could have immediate or long-term impacts on operations. In addition, financial forecasting allows for the strategic planning and implementation of management's goals and objectives.

Recommendation Status: Partially Implemented

L.A. Care indicated that they have been working toward establishing the necessary foundational support that would allow the Agency to generate effective and meaningful multi-year financial forecasts, given the shifting components and demands of the healthcare industry. Specifically, L.A. Care management indicated they have been increasing their staffing levels, conducting preliminary multi-year forecasts to assess the capabilities and limitations of their current system(s), and most notably, implementing a new data analytics platform (i.e., Systems Applications and Products Analytics Cloud), which they believe will allow them to make more accurate financial projections due to its comprehensive capabilities (e.g., generative artificial intelligence, industry-specific analytics, and ability to process complex datasets).

The Agency plans to fully implement this recommendation by June 15, 2025. We will assess and report on the status of this recommendation during our following annual financial condition review.

Priority Ranking: Recommendations are ranked from Priority 1 to 3 based on the potential seriousness and likelihood of negative impact on the Agency's operations if corrective action is not taken.

Table 1
L.A. Care Assets, Liabilities, Deferred Inflow of Resources, and Net Position
Fiscal Years (FY) 2018-19 Through 2021-22

(In Thousands)	FY 2018-19	FY 2019-20	FY 2020-21	FY 2021-22
Current Assets:				
Cash and Cash Equivalents	$ 1,634,374	$ 1,144,914	$ 990,897	$ 1,239,407
Investments - At Fair Value	897,935	1,310,365	1,223,897	1,085,262
Capitation Receivable	2,420,401	2,490,434	2,464,340	2,824,384
Other Current Assets	7,093	52,595	103,304	514,415
Total Current Assets	**$ 4,959,803**	**$ 4,998,308**	**$ 4,782,438**	**$ 5,663,468**
Non-Current/Capital Assets	**$ 138,204**	**$ 110,928**	**$ 184,643**	**$ 170,432**
Total Assets	**$ 5,098,007**	**$ 5,109,236**	**$ 4,967,081**	**$ 5,833,900**
Current Liabilities:				
Accounts Payable and Accrued Liabilities	$ 50,138	$ 98,247	$ 116,251	$ 164,813
Sub-Capitation Payable	3,112,997	3,244,683	2,837,547	3,464,015
Medi-Cal Adult Expansion Payable	-	-	-	-
Grants Payable	11,841	11,977	15,411	13,415
Reserves for Claims	558,640	620,735	643,228	784,397
Other Accrued Medical Expenses	199,709	131,068	125,151	77,929
Reserves for Provider Incentives	88,247	68,396	86,852	98,376
Lease Liability	-	-	15,151	13,204
Deferred Revenue	-	-	-	30,618
Total Current Liabilities	**$ 4,021,572**	**$ 4,175,106**	**$ 3,839,591**	**$ 4,646,767**
Long-Term Liabilities	**$ 3,581**	**$ 3,474**	**$ 63,495**	**$ 58,802**
Total Liabilities	**$ 4,025,153**	**$ 4,178,580**	**$ 3,903,086**	**$ 4,705,569**
Deferred Inflow of Resources	**$ 18,739**	**$ 14,096**	**$ 14,540**	**$ 40,977**
Net Position:				
Invested in Capital Assets	$ 112,322	$ 106,386	$ 105,915	$ 98,723
Restricted	300	300	600	600
Unrestricted	941,493	809,874	942,940	988,031
Total Net Position	**$ 1,054,115**	**$ 916,560**	**$ 1,049,455**	**$ 1,087,354**
Total Liabilites, Deferred Inflow of Resources & Net Position	**$ 5,098,007**	**$ 5,109,236**	**$ 4,967,081**	**$ 5,833,900**

Source: L.A. Care's Audited Financial Statements (Adjusted for Misstatement of Liabilities)

Table 2
L.A. Care Revenues and Expenses
Fiscal Years (FY) 2018-19 Through 2021-22

(In Thousands)	FY 2018-19	FY 2019-20	FY 2020-21	FY 2021-22
Operating Revenues				
Capitation	$ 7,901,970	$ 8,353,703	$ 9,210,117	$ 9,012,228
Grant Income	-	-	-	-
Total Operating Revenues	**$ 7,901,970**	**$ 8,353,703**	**$ 9,210,117**	**$ 9,012,228**
Operating Expenses				
Capitation - Professional Services	$ 4,169,129	$ 4,461,443	$ 4,834,938	$ 4,661,634
Inpatient / Outpatient Claims	2,322,749	2,758,981	2,822,674	3,302,501
Pharmacy Claims	661,929	693,186	760,355	273,758
Administrative Expenses	415,719	451,660	466,510	506,108
Provider Incentives and Shared Risk	67,205	39,098	81,832	94,910
Medical Administrative Expenses	61,943	80,887	83,067	83,808
Total Operating Expenses	**$ 7,698,674**	**$ 8,485,255**	**$ 9,049,376**	**$ 8,922,719**
Income from Operations	**$ 203,296**	**$ (131,552)**	**$ 160,741**	**$ 89,509**
Non-Operating Revenue / (Expense)				
Investment / Income / Tax Revenue	$ 165,429	$ 146,486	$ 163,284	$ 157,756
Grant Income	13,304	1,667	9,657	11,840
Provision / Tax Expense	(145,399)	(154,155)	(200,787)	(221,208)
Total Non-Operating Revenue / (Expense)	**$ 33,334**	**$ (6,002)**	**$ (27,846)**	**$ (51,612)**
Increase / (Decrease) in Net Position	**$ 236,630**	**$ (137,554)**	**$ 132,895**	**$ 37,897**

Source: L.A. Care's Audited Financial Statements

March 21, 2025

County of Los Angeles
Department of Auditor – Controller
Attn: Oscar Valdez
500 West Temple Street, Room 525
Los Angeles, CA 90012-3873

RE: L.A. Care Health Plan – Financial Condition Review for Fiscal Year 2020-21 and 2021-22

Dear Mr. Valdez,

Thank you for your letter dated February 2025 and we appreciate the opportunity to work collaboratively on the financial condition review for Fiscal Year (FY) 2020-21 and 2021-22.

We have carefully reviewed the Department of Auditor-Controller's report and agree with the recommendations presented.

The first recommendation pertains to the appropriateness of reported liabilities and deferred revenue. To address this, we have conducted balance sheet reconciliations to verify the classification of transactions as liabilities or deferred revenue. Based on our review, we confirm that our balances are presented accurately in all material respects.

The second recommendation highlights the feasibility and benefits of implementing a multi-year financial forecasting process. We plan to work with our internal leadership to develop financial forecasts that incorporate both known variables—such as rate notices and legislative changes—and historical trends. Establishing a multi-year financial forecast will strengthen our strategic planning efforts. We recognize that factors such as contractual adjustments, rate changes, and executive administrative orders will significantly impact our financial projections, which we will address through periodic updates.

We are in agreement with the remainder of the report and appreciate the insights provided.

Sincerely,

Radiah Campbell
Controller, L.A. Care Health Plan