



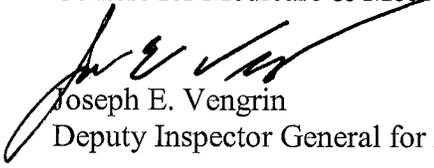
DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Washington, D.C. 20201

OCT 18 2007

TO: Kerry Weems
Acting Administrator
Centers for Medicare & Medicaid Services

FROM: 
Joseph E. Vengrin
Deputy Inspector General for Audit Services

SUBJECT: Review of Supplemental Executive Retirement Plan Costs Claimed by Blue Cross Blue Shield of South Carolina for Medicare Reimbursement for Fiscal Years 1999–2004 (A-07-07-00234)

Attached is an advance copy of our final report on Supplemental Executive Retirement Plan (SERP) costs claimed by Blue Cross Blue Shield of South Carolina (South Carolina) for Medicare reimbursement. We will issue this report to South Carolina within 5 business days.

Our objective was to determine the allowability of the SERP costs that South Carolina claimed for Medicare reimbursement for fiscal years (FY) 1999–2004.

South Carolina's claim for \$5,920,947 in SERP costs for FYs 1999–2004 included some costs that were unreasonable and therefore unallowable for Medicare reimbursement. Specifically, executive salaries used to calculate SERP costs were \$15,614,436 greater than the executive compensation limits established in Federal regulations. However, we were unable to determine the impact of these unallowable compensation costs on SERP costs because South Carolina did not provide us with the necessary documentation to support its SERP calculations. Therefore, we are setting aside the \$5,920,947 in claimed SERP costs for adjudication by the Centers for Medicare & Medicaid Services (CMS).

We recommend that South Carolina work with CMS to determine the allowability of \$5,920,947 in SERP costs claimed for FYs 1999–2004.

In written comments on our draft report, South Carolina concurred with our recommendation.

If you have any questions or comments about this report, please do not hesitate to call me, or your staff may contact George M. Reeb, Assistant Inspector General for the Centers for Medicare & Medicaid Audits, at (410) 786-7104 or through e-mail at George.Reeb@oig.hhs.gov. Please refer to report number A-07-07-00234 in all correspondence.

Attachment

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF SUPPLEMENTAL
EXECUTIVE RETIREMENT PLAN
COSTS CLAIMED BY BLUE CROSS
BLUE SHIELD OF SOUTH
CAROLINA FOR MEDICARE
REIMBURSEMENT FOR FISCAL
YEARS 1999–2004**



Daniel R. Levinson
Inspector General

October 2007
A-07-07-00234

Office of Inspector General

<http://oig.hhs.gov>

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OAS FINDINGS AND OPINIONS

The designation of financial or management practices as questionable or a recommendation for the disallowance of costs incurred or claimed, as well as other conclusions and recommendations in this report, represent the findings and opinions of the HHS/OIG/OAS. Authorized officials of the HHS divisions will make final determination on these matters.





DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General
Offices of Audit Services

OCT 19 2007

Region VII
601 East 12th Street
Room 284A
Kansas City, Missouri 64106

Report Number: A-07-07-00234

Mr. Joseph D. Wright, CPA
Vice President and Chief Financial Officer
Blue Cross Blue Shield of South Carolina
P.O. Box 100134, AG-A15
Columbia, South Carolina 29202-3134

Dear Mr. Wright:

Enclosed is the U.S. Department of Health and Human Services (HHS), Office of Inspector General (OIG), final report entitled "Review of Supplemental Executive Retirement Plan Costs Claimed by Blue Cross Blue Shield of South Carolina for Medicare Reimbursement for Fiscal Years 1999 Through 2004." We will forward a copy of this report to the HHS action official noted on the following page for review and any action deemed necessary.

The HHS action official will make final determination as to actions taken on all matters reported. We request that you respond to this official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

Pursuant to the principles of the Freedom of Information Act, 5 U.S.C. § 552, as amended by Public Law 104-231, OIG reports generally are made available to the public to the extent the information is not subject to exemptions in the Act (45 CFR part 5). Accordingly, within 10 business days after the final report is issued, it will be posted on the Internet at <http://oig.hhs.gov>.

If you have any questions or comments about this report, please do not hesitate to call me at (816) 426-3591, or contact Jenenne Tambke, Audit Manager, at (573) 893-8338, extension 21, or through e-mail at Jenenne.Tambke@oig.hhs.gov. Please refer to report number A-07-07-00234 in all correspondence.

Sincerely,

Patrick J. Cogley
Regional Inspector General
for Audit Services

Enclosure

Direct Reply to HHS Action Official:

Mr. Roger Perez
Regional Administrator, Region IV
Centers for Medicare & Medicaid Services
Atlanta Federal Center
61 Forsyth Street SW., Suite 4T20
Atlanta, Georgia 30303-8909

EXECUTIVE SUMMARY

BACKGROUND

Blue Cross Blue Shield of South Carolina (South Carolina) administers Medicare Part A and Part B operations in its Palmetto Government Benefit Administrators (Palmetto) and TrailBlazer Health Enterprises (TrailBlazer) subsidiaries under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS).

South Carolina maintains a Supplemental Executive Retirement Plan (SERP), which is a nonqualified pension plan designed to provide supplemental benefits to a select group of highly compensated employees. SERP benefits are in addition to those under the qualified pension plan and the nonqualified excess benefit plan. In claiming SERP costs, contractors must follow cost reimbursement principles contained in the Federal Acquisition Regulation (FAR), the Cost Accounting Standards, and their Medicare contracts.

OBJECTIVE

Our objective was to determine the allowability of the SERP costs that South Carolina claimed for Medicare reimbursement for fiscal years (FY) 1999–2004.

SUMMARY OF FINDING

South Carolina's claim for \$5,920,947 in SERP costs for FYs 1999–2004 included some costs that were unreasonable and therefore unallowable for Medicare reimbursement. Specifically, executive salaries used to calculate SERP costs were \$15,614,436 greater than the executive compensation limits established in Federal regulations. However, we were unable to determine the impact of these unallowable compensation costs on SERP costs because South Carolina did not provide us with the necessary documentation to support its SERP calculations. Therefore, we are setting aside the \$5,920,947 in claimed SERP costs for adjudication by CMS.

RECOMMENDATION

We recommend that South Carolina work with CMS to determine the allowability of \$5,920,947 in SERP costs claimed for FYs 1999–2004.

AUDITEE'S COMMENTS

In written comments on our draft report, South Carolina concurred with our recommendation. South Carolina's comments are included in their entirety as the Appendix.

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Glossary of Abbreviations and Acronyms

CAS	Cost Accounting Standards
CMS	Centers for Medicare & Medicaid Services
FAR	Federal Acquisition Regulation
FY	fiscal year
SERP	Supplemental Executive Retirement Plan

INTRODUCTION

BACKGROUND

Blue Cross Blue Shield of South Carolina (South Carolina) administers Medicare Part A and Part B operations in its Palmetto Government Benefit Administrators (Palmetto) and TrailBlazer Health Enterprises (TrailBlazer) subsidiaries under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS).¹

South Carolina maintains a Supplemental Executive Retirement Plan (SERP), which is a nonqualified pension plan designed to provide supplemental benefits to a select group of highly compensated employees. SERP benefits are in addition to the retirement benefits provided under the qualified pension plan and the nonqualified excess benefit plan. South Carolina determined SERP costs for Medicare reimbursement on an accrual basis.

To be allowable for Medicare reimbursement, costs claimed for nonqualified defined-benefit pension plans must be in compliance with Cost Accounting Standard (CAS) 412. CAS 412 (48 CFR § 9904.412-50(c)(3)) states that a contractor may use accrual accounting to measure and assign nonqualified defined-benefit pension plan costs if the contractor so elects, the plan is funded, and the pension benefits are nonforfeitable. If the plan does not meet all of these requirements, the contractor must assign the plan's costs using the pay-as-you-go method.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to determine the allowability of the SERP costs that South Carolina claimed for Medicare reimbursement for fiscal years (FY) 1999–2004.

Scope

We reviewed the \$5,920,947 in SERP costs that South Carolina claimed for Medicare reimbursement on its Final Administrative Cost Proposals for FYs 1999–2004. The objective did not require that we review South Carolina's overall internal control structure. However, we did review the controls relating to the SERP costs claimed for Medicare reimbursement to ensure that costs were allowable pursuant to the Federal Acquisition Regulation (FAR).

We performed fieldwork at South Carolina's corporate office in Columbia, South Carolina, in January 2007.

Methodology

We obtained information from South Carolina and its consulting actuary regarding South Carolina's SERP costs for FYs 1999–2004. We identified Palmetto's and TrailBlazer's SERP costs that South Carolina claimed for Medicare reimbursement.

¹South Carolina acquired TrailBlazer from Blue Cross Blue Shield of Texas in October 1999.

We performed our review in accordance with generally accepted government auditing standards.

FINDING AND RECOMMENDATION

SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN COSTS

FAR 31.201-2(a) states, in part, that a cost must be reasonable to be allowable. In addition, FAR 31.205-6(b)(2) provides that comparable market data be used to evaluate the reasonableness of compensation. Furthermore, FAR 31.201-6(a) states: “When an unallowable cost is incurred, its directly associated costs are also unallowable.” SERP pension benefits are directly associated with compensation because the benefit is based on the salary history of the recipient.

Additionally, FAR 31.205-6(p) states: “Costs incurred . . . for compensation of a senior executive in excess of the benchmark compensation amount determined applicable for the contractor fiscal year . . . are unallowable.”

Supplemental Executive Retirement Plan Costs Claimed

South Carolina claimed a total of \$5,920,947 in accrued SERP costs for Medicare reimbursement, as shown in Table 1.

Table 1: Accrued SERP Costs Claimed

FY	Palmetto	TrailBlazer	Total
1999	\$309,247	\$0	\$309,247
2000	207,794	257,322	465,116
2001	490,233	475,181	965,414
2002	561,627	616,718	1,178,345
2003	723,372	523,162	1,246,534
2004	1,014,543	741,748	1,756,291
Total	\$3,306,816	\$2,614,131	\$5,920,947

Unreasonable Compensation Costs

We determined that these accrued costs were based on unreasonable associated compensation. Using the executive compensation limit specified in FAR 31.205-6(p) as a benchmark for evaluating the reasonableness of the compensation, we determined that the salaries used to calculate SERP costs for the six senior executives were \$15,614,436 greater than the executive compensation limit for FYs 1999–2004, as shown in Table 2 on the next page.

Table 2: Unreasonable Executive Compensation

FY	Actual Compensation	Executive Compensation Limit	Unreasonable Compensation
1999	\$2,274,391	\$2,057,916	\$216,475
2000	3,193,324	2,118,060	1,075,264
2001	3,994,971	2,245,368	1,749,603
2002	4,984,980	2,326,698	2,658,282
2003	6,987,158	2,431,638	4,555,520
2004	7,956,398	2,597,106	5,359,292
Total	\$29,391,222	\$13,776,786	\$15,614,436

Impact of Unreasonable Compensation Costs on Supplemental Retirement Plan Costs Claimed

Compensation costs are used in the calculation of allowable SERP costs. Because it did not limit the associated compensation to a reasonable level, South Carolina overstated its allowable SERP costs. This resulted in an overclaim of SERP costs for Medicare reimbursement.

South Carolina did not provide supporting documentation for its benefit formula, its computations of actuarial liabilities and normal costs, or its allocation of assignable costs, although we requested that it do so. Without this documentation, we were unable to determine the impact of the \$15,614,436 in unallowable compensation costs on SERP costs. Therefore, we are setting aside the \$5,920,947 in claimed SERP costs for adjudication by CMS.

RECOMMENDATION

We recommend that South Carolina work with CMS to determine the allowability of \$5,920,947 in SERP costs claimed for FYs 1999–2004.

AUDITEE’S COMMENTS

In written comments on our draft report, South Carolina concurred with our recommendation. South Carolina’s comments are included in their entirety as the Appendix.

APPENDIX



Palmetto GBA
Post Office Box 100134
Columbia, South Carolina 29202-3134

Joe Wright
Vice President and CFO

July 20, 2007

Patrick J. Cogley
Regional Inspector General for Audit Services
Region VII
601 East 12th Street
Room 284A
Kansas City, Missouri 64106

RE: Audit Report Number A-07-07-00234

Dear Mr. Cogley:

We are responding to your draft audit report dated June 14, 2007 entitled "Review of Supplemental Executive Retirement Plan Costs Claimed by Blue Cross Blue Shield of South Carolina for Medicare Reimbursement for Fiscal Years 1999 Through 2004."

The audit contained the following recommendation with which we concur.

Recommendation:

We recommend that South Carolina work with CMS to determine the allowability of \$5,920,947 in SERP costs claimed for FYs 1999 through 2004.

Comment:

As recommended, we plan to work with CMS to determine the allowability of the SERP costs set aside during the audit.

If you have any questions, please feel free to contact me at 803-763-5544.

Sincerely,

A handwritten signature in black ink that reads "Joe Wright".

Joe Wright

CC: Eric Shipley, OACT-CMS
William R. Horton, BCBSSC
Bruce Hughes, Palmetto GBA
Marti Mahaffey, Trailblazer
Bob Leichtle, BCBSSC
