



JUL 15 1994

Memorandum

Date

From

June Gibbs Brown
June Gibbs Brown
Inspector General

Subject Review of Unfunded Pension Costs of Health Care Service Corporation
(A-07-94-00762)

To Bruce C. Vladeck
Administrator
Health Care Financing Administration

This memorandum is to alert you to the issuance on July 19, 1994 of our final audit report. A copy is attached.

Our review showed that as of January 1, 1992, Health Care Service Corporation (HCSC) had accumulated \$1.2 million in pension costs that are unallowable for Medicare reimbursement.

This is one of a series of pension audits requested by the Health Care Financing Administration (HCFA) of Medicare contractors. The audits are conducted as joint efforts using Office of Inspector General auditors and HCFA pension actuarial staff. We are alerting you to the issuance of this particular report because of the dollar amount involved. The general issue of funding for pension costs is highly technical. The report contains the details needed by your program staff to settle this issue with HCSC. As a basic rule, however, for Medicare reimbursement, pension costs must be annually calculated in accordance with established Federal contracting criteria. Only appropriate costs funded by actual contributions to a pension trust fund are allowable under Medicare.

We found HCSC only partially funded their pension costs for Plan Years 1986 through 1991. For each of those years, we considered the unfunded portion of the pension costs to be unallowable. The accumulated unallowable costs amounted to \$1.2 million (including interest) as of January 1, 1992 that must be separately identified and excluded in future calculations of Medicare pension costs.

We are recommending that HCSC make proper accounting adjustments to repay Medicare for the unallowable unfunded pension costs.

Page 2 - Bruce C. Vladeck

The HCSC disagreed with our calculation of \$1.2 million for unfunded pension costs. They stated they wish to discuss the potential waiver of the established Federal pension rules with HCFA officials. Regional HCFA officials declined to comment on our draft report.

For further information contact:

Barbara A. Bennett
Regional Inspector General for
Audit Services, Region VII
(816) 426-3591

Attachment

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF
UNFUNDED PENSION COSTS OF
HEALTH CARE SERVICE CORPORATION**



JUNE GIBBS BROWN
Inspector General

JULY 1994
A-07-94-00762



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General
Office of Audit Services

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

CIN: A-07-94-00762

Mr. Richard J. Giba
Internal Audit/Controls Consultant
Health Care Service Corporation
233 North Michigan Avenue, 17th Floor
Chicago, Illinois 60601

Dear Mr. Giba:

This report provides you with the results of an Office of Inspector General (OIG), Office of Audit Services (OAS) review titled "REVIEW OF UNFUNDED PENSION COSTS OF HEALTH CARE SERVICE CORPORATION." The purpose of our review was to determine whether pension costs for Plan Years 1986 through 1991 were funded in accordance with the Federal Acquisition Regulations (FAR).

As of January 1, 1992, Health Care Service Corporation (HCSC) had accumulated \$657,538 in Medicare A pension costs and \$575,799 in Medicare B pension costs which are unallowable for Medicare reimbursement. Pension costs assigned to an accounting period, but not funded by the tax filing deadlines, may not be reassigned to or claimed in subsequent accounting periods. Also, interest on the portion not funded in a period can not be a component of pension costs of any future cost accounting periods.

The HCSC made contributions to the pension trust fund for Plan Years 1986 through 1991. However, HCSC did not fully fund the pension costs identifiable with its Medicare segments for Plan Years 1988 through 1990. As a result, HCSC accumulated unfunded Medicare pension costs of \$1,233,337 (Medicare segment A of \$657,538 and Medicare segment B of \$575,799) as of January 1, 1992. The HCSC must separately identify and eliminate this amount from the amortization components of future pension costs.

The HCSC disagreed with our calculated amount for unfunded pension costs as of January 1, 1992. This difference resulted from HCSC's use of another funding methodology. In contrast to our more equitable approach, HCSC used a funding methodology that fully covered the segments' CAS pension cost for 1988 and 1989 even though the total Plan was only partially funded. The response to our draft report is included as Appendix B.

INTRODUCTION

BACKGROUND

For Medicare reimbursement, pension costs must be (1) measured, assigned, and allocated in accordance with Cost Accounting Standards (CAS) 412 and 413, and (2) funded as specified by part 31 of the FAR. The CAS deals with stability between contract periods and requires that pension costs be consistently measured and assigned to contract periods. The FAR addresses the allowability of pension costs and requires that pension costs assigned to contract periods be substantiated by funding.

The FAR funding requirement has traditionally been satisfied by trust fund deposits qualifying for tax-exemptions under the Employees Retirement Income Security Act of 1974 (ERISA). The ERISA provided for a minimum and a maximum deposit to pension funds as determined each year. The minimum represented a required deposit while the maximum represented the upper limit that could be deducted for income tax purposes for the year for which the deposit was applicable.

Pension costs computed in accordance with CAS represented an assignment of pension costs to specific accounting periods. The CAS pension costs often fell between ERISA minimum and maximum contributions. If contractors deposited the minimum ERISA contribution in their qualified trust funds, and the CAS pension costs exceeded the ERISA minimum, the contractors could only claim the funded portion of the CAS amount as allowable contract costs. Additionally, the excess of the CAS costs over the ERISA minimum contribution could not be carried forward as a component of future CAS pension costs.

In contrast, before 1986, if CAS pension costs were greater than maximum ERISA contributions, contractors could deposit the CAS amounts in qualified trust funds, claim them as allowable contract costs, and take ERISA maximums as tax deductions. The excess of the CAS amount over the ERISA maximum could be carried forward to future years for tax deductibility. Similarly, if contractors deposited ERISA maximums that were larger than CAS computed amounts, differences could be carried forward to fund allowable contract costs for future years.

The Tax Reform Act of 1986 (TRA 86) changed the effect of making pension plan contributions in excess of ERISA maximums. The ERISA maximum was still the tax deductible limit and the excess could still be carried forward to future years for deductibility. However, TRA 86 imposed an excise tax of 10 percent on contributions in excess of ERISA maximums. The excise tax is cumulative from year to year and applied on a first-in/first-out basis considering carry-forwards and current year contributions.

With the Omnibus Budget Reconciliation Act of 1987 (OBRA 87), the Congress took additional action affecting contractors' pension plan contributions to qualified trust funds. Prior to OBRA 87, ERISA's full funding limitation traditionally considered accumulated assets and the actuarial liability. If assets equalled or exceeded the actuarial liability, then the tax deductible amount was limited to zero.

The OBRA 87 imposes a second more restrictive test to the full funding limitation. It considers the accumulated assets and 150 percent of the amount designated "current liability." The actuarial liability under the pre-OBRA 87 test was based on projected benefits and conservative valuation assumptions. The current liability test of OBRA 87 considers only currently accrued benefits and values the liability using interest rates based on Treasury rates. The effect was that most pension plans that were already in full funding would remain there longer. Also, the same effect would push additional plans into full funding.

SCOPE

We made our examination in accordance with generally accepted government auditing standards. Our objective was to identify unfunded CAS costs, plus appreciation on the unfunded costs, from January 1, 1986 to January 1, 1992. Achieving our objective did not require that we review the internal control structure of HCSC.

This review was done in conjunction with our audit of pension segmentation (CIN: A-07-94-00763) at HCSC. The information obtained and reviewed during that audit was also used in performing this review.

The Health Care Financing Administration (HCFA) Office of the Actuary developed the methodology used for computing the CAS pension costs based on HCSC's historical practices.

We performed site work during September 1993 at HCSC's corporate offices in Chicago, Illinois. Subsequently, we performed audit work in the OIG, OAS, Jefferson City, Missouri Office.

FINDING AND RECOMMENDATIONS

As of January 1, 1992, HCSC had accumulated \$1,233,337 in unallowable direct pension costs (Medicare A segment costs of \$657,538 and Medicare B segment costs of \$575,799). These costs are unallowable because the pension costs were not funded within specific time periods set by regulation. Imputed interest on the unfunded costs is also unallowable. These costs represent unfunded pension costs and imputed interest for Plan Years 1988

through 1990. The HCSC cannot claim any of these unfunded costs in future cost accounting periods.

For Medicare reimbursement, pension costs must be (1) measured, assigned, and allocated in accordance with CAS 412 and 413 and (2) funded as specified by part 31 of the FAR. The CAS deals with stability between contract periods and requires that pension costs be consistently measured and assigned to contract periods. The FAR addresses the allowability of pension costs and requires that pension costs assigned to contract periods be substantiated by funding.

The FAR, 48 CFR 31.205-6(j)(3)(i) and (iii), states:

"***costs of pension plans not funded in the year incurred, and all other components of pension costs***assignable to the current accounting period but not funded during it, shall not be allowable in subsequent years***."

"Increased pension costs caused by delay in funding beyond 30 days after each quarter of the year to which they are assignable are unallowable."

Furthermore, the CAS within 48 CFR 30.412-50(a)(7) states:

"If any portion of the pension costs computed for a cost accounting period is not funded in that period, no amount for interest on the portion not funded in that period shall be a component of pension cost of any future cost accounting period."

In addition, the CAS within 48 CFR 30.412-50(a)(2) states:

"Pension costs applicable to prior years that were specifically unallowable in accordance with then existing Government contractual provisions shall be separately identified and eliminated from any unfunded actuarial liability being amortized***."

We compared CAS pension costs for the Medicare segments, computed by HCFA Office of the Actuary, to actual contributions to the Medicare segments and found the following:

	<u>Medicare A Segment</u>					
	<u>1/1/86</u>	<u>1/1/87</u>	<u>1/1/88</u>	<u>1/1/89</u>	<u>1/1/90</u>	<u>1/1/91</u>
CAS Pension Costs	\$365,187	\$403,421	\$441,365	\$425,425	\$443,641	\$482,259
Interest to End of Year	31,954	35,299	36,413	35,098	36,600	39,786
Less:						
Actual Contribution	397,141	438,720	396,654	197,465	242,840	573,710
Interest to End of Year	-0-	-0-	2,329	3,670	3,096	5,708
Under (Over) funding	\$ -0-	\$ -0-	\$ 78,795	\$259,388	\$234,305	\$(57,373)

Medicare B Segment

	<u>1/1/86</u>	<u>1/1/87</u>	<u>1/1/88</u>	<u>1/1/89</u>	<u>1/1/90</u>	<u>1/1/91</u>
CAS Pension Costs	\$296,192	\$266,317	\$377,102	\$353,224	\$416,353	\$485,083
Interest to End of Year	25,917	23,303	31,111	29,141	34,349	40,019
Less:						
Actual Contribution	322,109	289,620	338,901	163,952	227,903	577,070
Interest to End of Year	-0-	-0-	1,990	3,047	2,905	5,741
Under (Over) funding	\$ -0-	\$ -0-	\$ 67,322	\$215,366	\$219,894	\$(57,709)

Appendix A provides additional information on the CAS pension costs.

For Plan Years 1988 through 1990, HCSC had not fully funded the CAS pension costs within the required time periods. For these years, HCSC made contributions to the pension trust fund based on the ERISA minimum contribution amounts.

The CAS pension costs not funded are unallowable as a component of pension costs for any future years. Interest related to these unfunded costs is also unallowable as a component of future years' pension costs.

The following table shows the unfunded amounts, plus interest, which are unallowable on a cumulative basis. We computed the unfunded amounts for each year as shown on the previous schedules. We increased the unfunded amounts by the assumed rate of interest used in the valuation reports. Our computation of the unfunded amounts plus interest considers those costs which should have been funded for the applicable years. In other words, if HCSC funded the costs, the assets of the Medicare segments would have been greater at the specified time periods.

Medicare A Segment Unfunded Pension Costs and Interest

<u>Date</u>	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>	<u>Total</u>
1/1/89	\$ 78,795	\$ -0-	\$ -0-	\$ -0-	\$ 78,795
1/1/90	85,296	259,388	-0-	-0-	344,684
1/1/91	92,333	280,788	234,305	-0-	607,426
1/1/92	99,950	303,953	253,635	-0-	657,538

Medicare B Segment Unfunded Pension Costs and Interest

<u>Date</u>	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>	<u>Total</u>
1/1/89	\$ 67,322	\$ -0-	\$ -0-	\$ -0-	\$ 67,322
1/1/90	72,876	215,366	-0-	-0-	288,242
1/1/91	78,888	233,134	219,894	-0-	531,916
1/1/92	85,396	252,368	238,035	-0-	575,799

Recommendations

We recommend that HCSC:

- o Identify \$1,233,337 (Medicare A segment costs of \$657,538 and Medicare B segment costs of \$575,799) as an unallowable component of direct pension costs as of January 1, 1992.

- o Update annually the unallowable pension cost component related to the unfunded CAS costs for Plan Years 1988 through 1990.
- o Identify and update unfunded pension costs for any later years in a similar manner.

Auditee Comments

The HCSC disagreed with the results of our review: "Your report states that HCSC has accumulated unfunded Medicare pension costs for Segment A and Segment B of \$1,233,337. We do not agree.

"Contributions to the plan are allocated first to Medicare Segments A and B in order to fully cover the CAS pension cost. As a result of funding the total CAS pension costs for fiscal 1987 through fiscal 1991 for Medicare Segments A and B, there will be no unfunded Medicare pension costs."

OIG Response

As stated in the report, HCSC did not fund the total company CAS pension costs for Plan Years 1988 through 1990. Since HCSC only partially funded the CAS costs, we allocated the contributions among the Medicare segments and other segment using each segment's CAS computed pension costs in relation to total CAS computed pension costs.

Both the Medicare contracts and CAS provide for the consistent treatment of costs among different cost objectives. For example, Paragraph B, Section II, Appendix B of the Medicare contracts state "***the criteria for determining the allocation of costs***should be the same for all similar objectives." The CAS 413.50(c)(1) and (10) state "***the base to be used for allocating such costs shall be representative of the factors [on] which the pension benefits are based." and "where pension cost is separately calculated for one or more segments, the actuarial cost method shall be the same for all segments***."

The HCSC made several deposits into the pension trust fund during the period 1988 through 1990. We found no evidence that the deposits were specifically dedicated to a particular cost objective or group of employees. As such, our proration of the funded costs is appropriate as it provides consistent and equitable treatment of the funded costs among the segments. Therefore, we did not change our computation of the unfunded pension costs.

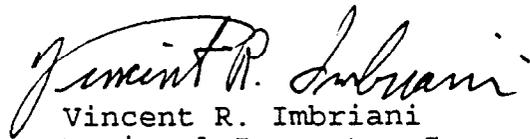
INSTRUCTIONS FOR AUDITEE RESPONSE

Final determinations as to actions to be taken on all matters reported will be made by the HHS action official identified below. We request that you respond to each of the recommendations in this report to the HHS action official, presenting any comments or additional information that you believe may have a bearing on the final determination.

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In accordance with the principles of the Freedom of Information Act (Public Law 90-23), OIG, OAS reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act which the Department chooses to exercise. (See 45 CFR part 5.)

Sincerely,



Vincent R. Imbriani
Regional Inspector General for
Audit Services, Region VII

Enclosures

HHS Action Official:

Mr. Chester Stroyny
Regional Administrator, Region V
Health Care Financing Administration
105 West Adams Street, 15th Floor
Chicago, Illinois 60603

HEALTH CARE SERVICE CORPORATION
CHICAGO, ILLINOIS

STATEMENT OF CAS PENSION COSTS AND FUNDING

FOR THE PERIOD
JANUARY 1, 1986 TO JANUARY 1, 1992

		Total Plan	Other Segment	Medicare A Segment	Medicare B Segment
01/01/86 Normal Cost	1/	\$ 3,022,569	-	-	\$ 239,044
Amortization Payment	2/	<u>2,850,422</u>	-	-	<u>57,148</u>
01/01/86 CAS Pension Cost	3/	5,872,991	\$ 5,211,612	\$ 365,187	296,192
Interest to 12/31/86	4/	<u>513,887</u>	<u>456,016</u>	<u>31,954</u>	<u>25,917</u>
12/31/86 CAS Funding Target	5/	6,386,878	5,667,628	397,141	322,109
Contribution	6/	(6,386,878)	(5,667,628)	(397,141)	(322,109)
Interest on Contribution	7/	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
12/31/86 Unfunded Pension Cost	8/	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
01/01/87 Normal Cost		\$ 3,475,698	-	-	\$ 209,371
Amortization Payment		<u>3,087,214</u>	-	-	<u>56,946</u>
01/01/87 CAS Pension Cost		6,562,912	\$ 5,893,174	\$ 403,421	266,317
Interest to 12/31/87		<u>574,255</u>	<u>515,653</u>	<u>35,299</u>	<u>23,303</u>
12/31/87 CAS Funding Target		7,137,167	6,408,827	438,720	289,620
Contribution		(7,137,167)	(6,408,827)	(438,720)	(289,620)
Interest on Contribution		<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
12/31/87 Unfunded Pension Cost		<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
01/01/88 Normal Cost		\$ 4,275,446	\$ 3,716,411	\$ 263,604	\$ 295,431
Amortization Payment		<u>3,270,394</u>	<u>3,010,962</u>	<u>177,761</u>	<u>81,671</u>
01/01/88 CAS Pension Cost		7,545,840	6,727,373	441,365	377,102
Interest to 12/31/88		<u>622,532</u>	<u>555,008</u>	<u>36,413</u>	<u>31,111</u>
12/31/88 CAS Funding Target		8,168,372	7,282,381	477,778	408,213
Contribution		(6,781,427)	(6,045,872)	(396,654)	(338,901)
Interest on Contribution		<u>(39,825)</u>	<u>(35,506)</u>	<u>(2,329)</u>	<u>(1,990)</u>
12/31/88 Unfunded Pension Cost		<u>\$ 1,347,120</u>	<u>\$ 1,201,003</u>	<u>\$ 78,795</u>	<u>\$ 67,322</u>
01/01/89 Normal Cost		\$ 3,788,919	\$ 3,239,945	\$ 262,930	\$ 286,044
Amortization Payment		<u>2,580,107</u>	<u>2,350,432</u>	<u>162,495</u>	<u>67,180</u>
01/01/89 CAS Pension Cost		6,369,026	5,590,377	425,425	353,224
Interest to 12/31/89		<u>525,445</u>	<u>461,206</u>	<u>35,098</u>	<u>29,141</u>
12/31/89 CAS Funding Target		6,894,471	6,051,583	460,523	382,365
Contribution		(2,956,245)	(2,594,828)	(197,465)	(163,952)
Interest on Contribution		<u>(54,943)</u>	<u>(48,226)</u>	<u>(3,670)</u>	<u>(3,047)</u>
12/31/89 Unfunded Pension Cost		<u>\$ 3,883,283</u>	<u>\$ 3,408,529</u>	<u>\$ 259,388</u>	<u>\$ 215,366</u>

HEALTH CARE SERVICE CORPORATION
CHICAGO, ILLINOIS

STATEMENT OF CAS PENSION COSTS AND FUNDING

FOR THE PERIOD
JANUARY 1, 1986 TO JANUARY 1, 1992

	<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare A Segment</u>	<u>Medicare B Segment</u>
01/01/90 Normal Cost	\$ 4,382,417	\$ 3,743,580	\$ 283,556	\$ 355,281
Amortization Payment	<u>2,508,122</u>	<u>2,286,965</u>	<u>160,085</u>	<u>61,072</u>
01/01/90 CAS Pension Cost	6,890,539	6,030,545	443,641	416,353
Interest to 12/31/90	<u>568,469</u>	<u>497,520</u>	<u>36,600</u>	<u>34,349</u>
12/31/90 CAS Funding Target	7,459,008	6,528,065	480,241	450,702
Contribution	(3,771,737)	(3,300,994)	(242,840)	(227,903)
Interest on Contribution	<u>(48,079)</u>	<u>(42,078)</u>	<u>(3,096)</u>	<u>(2,905)</u>
12/31/90 Unfunded Pension Cost	<u>\$ 3,639,192</u>	<u>\$ 3,184,993</u>	<u>\$ 234,305</u>	<u>\$ 219,894</u>
01/01/91 Normal Cost	\$ 4,982,377	\$ 4,283,479	\$ 297,545	\$ 401,353
Amortization Payment	<u>2,895,754</u>	<u>2,627,310</u>	<u>184,714</u>	<u>83,730</u>
01/01/91 CAS Pension Cost	7,878,131	6,910,789	482,259	485,083
Interest to 12/31/91	<u>649,946</u>	<u>570,141</u>	<u>39,786</u>	<u>40,019</u>
12/31/91 CAS Funding Target	8,528,077	7,480,930	522,045	525,102
Contribution	(9,372,073)	(8,221,293)	(573,710)	(577,070)
Interest on Contribution	<u>(93,246)</u>	<u>(81,797)</u>	<u>(5,708)</u>	<u>(5,741)</u>
12/31/91 Unfunded Pension Cost	<u>\$ (937,242)</u>	<u>\$ (822,160)</u>	<u>\$ (57,373)</u>	<u>\$ (57,709)</u>

HEALTH CARE SERVICE CORPORATION
CHICAGO, ILLINOIS

STATEMENT OF CAS PENSION COSTS AND FUNDING

FOR THE PERIOD
JANUARY 1, 1986 TO JANUARY 1, 1992

FOOTNOTES

- 1/ We obtained the total company normal costs from HCSC's actuarial valuation reports. Except for the 1986 Medicare B normal cost, we obtained the Medicare segments' normal costs from the participant data files provided by HCSC's consulting actuary. The 1986 Medicare B normal cost was estimated by HCFA, Office of the Actuary.
- 2/ We based the amortization payment on a CAS amortization schedule developed from information obtained from HCSC's valuation reports and IRS Form 5500 reports. We developed a separate CAS amortization schedule for the Medicare A segment starting in 1988. For the Medicare B segment, we developed a separate amortization schedule starting in 1986.
- 3/ The CAS pension cost represents the sum of the normal cost and amortization payment. For 1986 and 1987, our computation of the Medicare A segment's CAS pension costs is the product of the formula (total company CAS cost - Medicare B segment CAS cost) x (Medicare A segment covered payroll / (total company covered payroll - Medicare B segment covered payroll)). We separately calculated Medicare A CAS pension costs for 1988 through 1991. For the Medicare B segment, we separately calculated the 1986 through 1991 CAS pension costs.

The amounts shown for the "other segment" represent the difference between the total company and the Medicare segments.

- 4/ We applied one year's interest at the assumed rate reported in the actuarial valuation reports. For 1986 and 1987, the interest rate is 8.75 percent. For 1988 through 1991, the interest rate is 8.25 percent.
- 5/ The annual CAS pension cost, adjusted with interest to the end of the year, must be funded by current and prepaid contributions to satisfy the allowability criteria of FAR, section 31.205-6(j).
- 6/ We obtained total company contributions from IRS Form 5500 reports. We allocated contributions to the Medicare segments based on the CAS funding target at the end of the year.

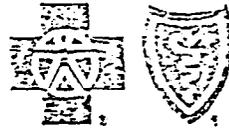
HEALTH CARE SERVICE CORPORATION
CHICAGO, ILLINOIS

STATEMENT OF CAS PENSION COSTS AND FUNDING .

FOR THE PERIOD
JANUARY 1, 1986 TO JANUARY 1, 1992

- 7/ We applied interest on the contributions at the assumed rate from the date of deposit to the end of the year.

- 8/ We computed the unfunded pension cost by subtracting the value of contributions and interest at year-end from the CAS funding target. We calculated a prepayment credit (a negative value) in those instances where our computed CAS pension costs are less than the contributions for the Medicare segments. The HCSC may carry forward a prepayment credit to fund future CAS pension costs.



233 North Michigan Avenue
Chicago, Illinois 60601-5655
312/938-6000

March 14, 1994

Mr. James Aasmundstad
Department of Health and Human Services
Office of the Inspector General
Office of Audit Services
Region VII
601 East 12th Street
Room 284A
Kansas City, Missouri 64106

Re: **A-07-94-00761**
A-07-94-00762
A-07-94-00763

Dear Mr. Aasmundstad:

I am writing in response to the three reports prepared by the Office of the Inspector General, Office of Audit Services reviewing:

- Pension costs claimed for Medicare reimbursement by Health Care Service Corporation, CIN: A-07-94-00761,
- Unfunded pension costs of Health Care Service Corporation, CIN: A-07-94-00762, and
- Medicare Contractor's pension segmentation, Health Care Service Corporation, CIN: A-07-94-00763.

Pension Costs Claimed

Your report states that HCSC has received reimbursement for \$2,811,890 in Medicare pension costs from the Health Care Financing Administration (HCFA) for fiscal years 1987 through 1991. We agree. The funded portion of CAS computed pension costs was reported as \$3,137,403. On this amount, we disagree. HCSC fully funds all CAS

Mr. James Aasmundstad
March 14, 1994
Page 2.

pension costs for the Medicare Part A and Part B segments and, thus, the amount funded was actually \$4,286,117.

Our amounts differ for two reasons:

1. For fiscal years 1987 through 1991, HCSC actually funded the total CAS pension cost for Medicare Segments A and B, and
2. The calculation of the indirect allowable pension cost should multiply the Medicare indirect percentage by the CAS pension cost rather than the allocable pension cost.

Attached is Exhibit I, which shows revised calculations of Appendix A to report CIN: A-07-94-00761.

As a result, HCSC claims an additional \$1,474,227 in allowable CAS pension costs for fiscal years 1987 through 1991, rather than the additional \$325,513 as stated in your report.

Unfunded Pension Costs

Your report states that HCSC has accumulated unfunded Medicare pension costs for Segment A and Segment B of \$1,233,337. We do not agree.

Contributions to the plan are allocated first to Medicare Segments A and B in order to fully cover the CAS pension cost. As a result of funding the total CAS pension costs for fiscal 1987 through fiscal 1991 for Medicare Segments A and B, there will be no unfunded Medicare pension costs.

Attached is Exhibit II which shows revised calculations of Appendix A to report CIN: A-07-94-00762.

Pension Segmentation

Your report states that HCSC has understated Medicare Segment A assets by \$129,177 and Medicare Segment B assets by \$926,231. We do not agree.

HEALTH CARE SERVICE CORPORATION
CHICAGO, ILLINOIS

EXHIBIT
Revised Appendix A
CIN: A-07-94-00761

STATEMENT OF ALLOWABLE CAS PENSION COSTS
FOR FISCAL YEARS 1987 THROUGH 1991

	<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare A Segment</u>	<u>Medicare B Segment</u>
1986 Plan Year Contributions	\$6,366,878	\$5,667,628	\$997,141	\$322,109
Discount for Interest	<u>(513,637)</u>	<u>(455,016)</u>	<u>(31,954)</u>	<u>(25,917)</u>
Present Value of Funding	5,872,991	5,211,612	365,187	296,192
CAS Pension Costs	<u>5,872,991</u>	<u>5,211,612</u>	<u>365,187</u>	<u>296,192</u>
Percentage of Costs Funded	100%	100%	100%	100%
Funded CAS Pension Cost	5,872,991	5,211,612	365,187	296,192
Allowable Interest	<u>364,003</u>	<u>323,011</u>	<u>22,634</u>	<u>18,358</u>
		0		
Allocable Pension Cost	6,236,994	5,534,623	387,821	314,550
Medicare Segment Percentage	<u>n/a</u>	<u>n/a</u>	<u>100%</u>	<u>100%</u>
Allowable Segment Pension Cost			387,821	n/a
Medicare Indirect Percentage			1.6112%	n/a
Allowable Indirect Pension Cost			63,969	n/a
Calendar Year Pension Cost			471,790	n/a
1987 Plan Year Contributions	\$7,137,167	\$6,408,827	\$438,720	\$289,620
Discount for Interest	<u>(574,255)</u>	<u>(515,653)</u>	<u>(35,299)</u>	<u>(23,303)</u>
Present Value of Funding	6,562,912	5,893,174	403,421	266,317
CAS Pension Costs	<u>6,562,912</u>	<u>5,893,174</u>	<u>403,421</u>	<u>266,317</u>
Percentage of Costs Funded	100%	100%	100%	100%
Funded CAS Pension Cost	6,562,912	5,893,174	403,421	266,317
Allowable Interest	<u>406,764</u>	<u>365,254</u>	<u>25,004</u>	<u>16,506</u>
		0		
Allocable Pension Cost	6,969,676	6,258,428	428,425	282,823
Medicare Segment Percentage	<u>n/a</u>	<u>n/a</u>	<u>100%</u>	<u>100%</u>
Allowable Segment Pension Cost			428,425	n/a
Medicare Indirect Percentage			1.3374%	n/a
Allowable Indirect Pension Cost			78,615	n/a
Calendar Year Pension Cost			507,240	n/a
Fiscal Year Pension Cost			493,673	n/a

HEALTH CARE SERVICE CORPORATION
CHICAGO, ILLINOIS

STATEMENT OF ALLOWABLE CAS PENSION COSTS

FOR FISCAL YEARS 1987 THROUGH 1991

	<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare A Segment</u>	<u>Medicare B Segment</u>
1988 Plan Year Contributions	\$6,781,427	\$5,900,609	\$474,968	\$405,830
Discount for Interest	<u>(460,039)</u>	<u>(417,688)</u>	<u>(33,623)</u>	<u>(28,722)</u>
Present Value of Funding	6,301,388	5,482,921	441,365	377,102
CAS Pension Costs	<u>7,545,840</u>	<u>6,727,373</u>	<u>441,365</u>	<u>377,102</u>
Percentage of Costs Funded	83.51%	81.50%	100%	100%
Funded CAS Pension Cost	6,301,388	5,482,921	441,365	377,102
Allowable Interest	<u>368,237</u>	<u>320,408</u>	<u>25,792</u>	<u>22,037</u>
		0		
Allocable Pension Cost	6,669,625	5,803,329	467,157	399,139
Medicare Segment Percentage	<u>n/a</u>	<u>n/a</u>	<u>100%</u>	<u>100%</u>
Allowable Segment Pension Cost			467,157	n/a
Medicare Indirect Percentage			1.8858%	n/a
Allowable Indirect Pension Cost			126,865	n/a
Calendar Year Pension Cost			594,022	n/a
Fiscal Year Pension Cost			572,327	n/a
1989 Plan Year Contributions	\$2,956,245	\$2,128,737	\$452,120	\$375,388
Discount for Interest	<u>(174,547)</u>	<u>(125,688)</u>	<u>(26,693)</u>	<u>(22,164)</u>
Present Value of Funding	2,781,698	2,003,049	425,425	353,224
CAS Pension Costs	<u>6,369,026</u>	<u>5,590,377</u>	<u>425,425</u>	<u>353,224</u>
Percentage of Costs Funded	43.68%	35.83%	100%	100%
Funded CAS Pension Cost	2,781,698	2,003,049	425,425	353,224
Allowable Interest	<u>162,555</u>	<u>117,053</u>	<u>24,861</u>	<u>20,641</u>
		0		
Allocable Pension Cost	2,944,253	2,120,102	450,286	373,865
Medicare Segment Percentage	<u>n/a</u>	<u>n/a</u>	<u>100%</u>	<u>100%</u>
Allowable Segment Pension Cost			450,286	373,865
Medicare Indirect Percentage			1.6246%	2.0280%
Allowable Indirect Pension Cost			90,921	113,373
Calendar Year Pension Cost			541,107	437,233
Fiscal Year Pension Cost			554,336	243,619

HEALTH CARE SERVICE CORPORATION
CHICAGO, ILLINOIS

STATEMENT OF ALLOWABLE CAS PENSION COSTS
FOR FISCAL YEARS 1987 THROUGH 1991

	<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare A Segment</u>	<u>Medicare B Segment</u>
1990 Plan Year Contributions	\$3,771,737	\$2,652,511	\$474,197	\$445,029
Discount for Interest	<u>(243,039)</u>	<u>(183,607)</u>	<u>(30,556)</u>	<u>(28,676)</u>
Present Value of Funding	3,528,698	2,668,704	443,641	416,353
CAS Pension Costs	<u>6,890,539</u>	<u>6,030,545</u>	<u>443,641</u>	<u>416,353</u>
Percentage of Costs Funded	51.21%	44.25%	100%	100%
Funded CAS Pension Cost	3,528,698	2,668,704	443,641	416,353
Allowable Interest	<u>206,208</u>	<u>155,952</u>	<u>25,925</u>	<u>24,331</u>
		0		
Allocable Pension Cost	3,734,906	2,824,656	469,566	440,684
Medicare Segment Percentage	<u>n/a</u>	<u>n/a</u>	<u>100%</u>	<u>100%</u>
Allowable Segment Pension Cost			469,566	440,684
Medicare Indirect Percentage			2.0200%	2.5105%
Allowable Indirect Pension Cost			121,817	151,397
Calendar Year Pension Cost			591,383	592,080
Fiscal Year Pension Cost			578,814	565,870
1991 Plan Year Contributions	\$9,372,073	\$8,335,241	\$516,903	\$519,929
Discount for Interest	<u>(628,129)</u>	<u>(558,639)</u>	<u>(34,644)</u>	<u>(34,846)</u>
Present Value of Funding	8,743,944	7,776,602	482,259	485,083
CAS Pension Costs	<u>7,878,131</u>	<u>6,910,789</u>	<u>482,259</u>	<u>485,083</u>
Percentage of Costs Funded	100%	100%	100%	100%
Funded CAS Pension Cost	7,878,131	6,910,789	482,259	485,083
Allowable Interest	<u>460,378</u>	<u>403,849</u>	<u>28,182</u>	<u>28,347</u>
		0		
Allocable Pension Cost	8,338,509	7,314,638	510,441	513,430
Medicare Segment Percentage	<u>n/a</u>	<u>n/a</u>	<u>100%</u>	<u>100%</u>
Allowable Segment Pension Cost			510,441	513,430
Medicare Indirect Percentage			1.8237%	2.2087%
Allowable Indirect Pension Cost			126,032	152,639
Calendar Year Pension Cost			636,473	666,069
Fiscal Year Pension Cost			625,201	647,572

HEALTH CARE SERVICE CORPORATION
CHICAGO, ILLINOIS

Exhibit II
Revised Appendix A
CIN: A-07-54-00762

STATEMENT OF CAS PENSION COSTS AND FUNDING

FOR THE PERIOD
JANUARY 1, 1986 TO JANUARY 1, 1992

		<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare A Segment</u>	<u>Medicare B Segment</u>
01/01/86	Normal Cost	\$3,022,559	n/a	n/a	\$289,044
	Amortization Payment	<u>2,650,422</u>	<u>n/a</u>	<u>n/a</u>	<u>57,148</u>
01/01/86	CAS Pension Cost	5,872,991	5,211,612	365,187	296,192
	Interest to 12/31/86	<u>513,887</u>	<u>456,016</u>	<u>31,954</u>	<u>25,917</u>
12/31/86	CAS Funding Target	6,386,878	5,667,628	397,141	322,109
	Contribution	(6,386,878)	(5,667,628)	(397,141)	(322,109)
	Interest on Contribution	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
12/31/86	Unfunded Pension Cost	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
01/01/87	Normal Cost	\$3,475,698	n/a	n/a	\$209,371
	Amortization Payment	<u>3,087,214</u>	<u>n/a</u>	<u>n/a</u>	<u>56,945</u>
01/01/87	CAS Pension Cost	6,562,912	5,893,174	403,421	266,317
	Interest to 12/31/87	<u>574,255</u>	<u>515,653</u>	<u>35,299</u>	<u>23,303</u>
12/31/87	CAS Funding Target	7,137,167	6,408,827	439,720	289,620
	Contribution	(7,137,167)	(6,408,827)	(439,720)	(289,620)
	Interest on Contribution	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
12/31/87	Unfunded Pension Cost	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
01/01/88	Normal Cost	\$4,275,446	\$3,716,411	\$253,604	\$295,431
	Amortization Payment	<u>3,270,394</u>	<u>\$3,010,962</u>	<u>\$177,761</u>	<u>81,671</u>
01/01/88	CAS Pension Cost	7,545,840	6,727,373	441,365	377,102
	Interest to 12/31/88	<u>622,532</u>	<u>555,008</u>	<u>35,413</u>	<u>31,111</u>
12/31/88	CAS Funding Target	8,168,372	7,282,381	477,778	408,213
	Contribution	(6,781,427)	(5,900,609)	(474,988)	(405,830)
	Interest on Contribution	<u>(39,625)</u>	<u>(34,652)</u>	<u>(2,790)</u>	<u>(2,383)</u>
12/31/88	Unfunded Pension Cost	<u>1,347,120</u>	<u>1,347,120</u>	<u>0</u>	<u>0</u>
01/01/89	Normal Cost	\$3,783,919	\$3,239,945	\$262,930	\$266,044
	Amortization Payment	<u>2,580,107</u>	<u>\$2,350,432</u>	<u>\$162,495</u>	<u>67,190</u>
01/01/89	CAS Pension Cost	6,369,026	5,590,377	425,425	353,224
	Interest to 12/31/89	<u>525,445</u>	<u>451,206</u>	<u>35,093</u>	<u>29,141</u>
12/31/89	CAS Funding Target	6,894,471	6,051,553	460,523	382,365
	Contribution	(2,956,245)	(2,123,737)	(452,120)	(375,388)
	Interest on Contribution	<u>(54,943)</u>	<u>(39,666)</u>	<u>(3,406)</u>	<u>(3,977)</u>

HEALTH CARE SERVICE CORPORATION
CHICAGO, ILLINOIS

EXHIBIT II
Revised Appendix A
CIN: A-07-94-00762

STATEMENT OF CAS PENSION COSTS AND FUNDING

FOR THE PERIOD
JANUARY 1, 1986 TO JANUARY 1, 1992

		<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare A Segment</u>	<u>Medicare B Segment</u>
01/01/90	Normal Cost	\$4,382,417	\$3,743,550	\$283,556	\$355,281
	Amortization Payment	<u>2,508,122</u>	<u>\$2,235,965</u>	<u>\$160,025</u>	<u>61,072</u>
01/01/90	CAS Pension Cost	6,890,539	6,030,545	443,641	416,353
	Interest to 12/31/90	<u>568,459</u>	<u>497,520</u>	<u>36,600</u>	<u>34,349</u>
12/31/90	CAS Funding Target	7,459,008	6,528,065	480,241	450,702
	Contribution	(3,771,737)	(2,852,511)	(474,197)	(445,029)
	Interest on Contribution	<u>(48,079)</u>	<u>(36,361)</u>	<u>(6,044)</u>	<u>(5,673)</u>
12/31/90	Unfunded Pension Cost	<u>3,639,192</u>	<u>3,639,192</u>	<u>0</u>	<u>0</u>
01/01/91	Normal Cost	\$4,982,377	\$4,283,479	\$297,545	\$401,353
	Amortization Payment	<u>2,895,754</u>	<u>\$2,627,310</u>	<u>\$184,714</u>	<u>83,730</u>
01/01/91	CAS Pension Cost	7,878,131	6,910,789	482,259	485,083
	Interest to 12/31/91	<u>649,946</u>	<u>570,140</u>	<u>39,786</u>	<u>40,019</u>
12/31/91	CAS Funding Target	8,528,077	7,480,929	522,045	525,102
	Contribution	(9,372,073)	(8,335,241)	(516,903)	(519,929)
	Interest on Contribution	<u>(93,246)</u>	<u>(82,930)</u>	<u>(5,142)</u>	<u>(5,173)</u>
12/31/91	Unfunded Pension Cost	<u>(937,242)</u>	<u>(937,242)</u>	<u>0</u>	<u>0</u>

HEALTH CARE SERVICE CORPORATION
CHICAGO, ILLINOIS

EXHIBIT III
Revised Appendix A
CIN: A-07-94-00783

STATEMENT OF MEDICARE PENSION ASSETS

FOR THE PERIOD
JANUARY 1, 1986 TO JANUARY 1, 1992

Description	Total Plan	Other Segment	Medicare A Segment	Medicare B Segment
Assets January 1, 1986	\$0	\$0	\$0	\$0
Contributions	6,386,878	5,667,628	397,141	322,109
Benefits	0	0	0	0
Expenses	0	0	0	0
Earnings	0	0	0	0
Net Transfers	0	49,496	(44,560)	(4,936)
Assets January 1, 1987	\$6,386,878	\$5,717,124	\$352,581	\$317,173
Contributions	7,137,167	6,408,827	438,720	289,620
Benefits	(438,757)	(391,512)	(31,421)	(15,824)
Expenses	(40,799)	(36,521)	(2,252)	(2,026)
Earnings	(254,639)	(227,937)	(14,057)	(12,645)
Net Transfers	0	(195,674)	117,162	78,492
Assets January 1, 1988	\$12,789,650	\$11,274,307	\$660,753	\$654,790
Contributions	6,761,427	5,900,609	474,968	405,830
Benefits	(1,940,168)	(1,872,269)	(60,160)	(7,745)
Expenses	(66,447)	(56,573)	(4,472)	(3,402)
Earnings	627,213	552,891	42,211	32,111
Net Transfers	0	(69,919)	22,907	47,012
Assets January 1, 1989	\$18,191,875	\$15,727,052	\$1,336,227	\$1,128,596
Contributions	2,956,245	2,128,737	452,120	375,368
Benefits	(619,045)	(611,854)	0	(7,191)
Expenses	(149,817)	(130,715)	(10,359)	(8,743)
Earnings	5,162,938	4,463,410	379,227	320,301
Asset Transfer	77,633	77,633	0	0
Net Transfers	0	(36,070)	(136,547)	172,617
Assets January 1, 1990	\$25,619,829	\$21,618,193	\$2,020,569	\$1,560,958
Contributions	3,771,737	2,852,511	474,197	445,029
Benefits	(975,726)	(840,012)	(10,596)	(125,120)
Expenses	(171,090)	(148,725)	(11,122)	(11,243)
Earnings	1,058,406	893,090	83,478	81,838
Net Transfers	0	8,339	(257,669)	249,350
Assets January 1, 1991	\$29,303,154	\$24,363,396	\$2,298,937	\$2,620,821
Contributions	9,372,073	8,335,241	516,903	519,929
Benefits	(699,404)	(784,591)	(84,225)	(30,566)
Expenses	(214,141)	(186,432)	(12,406)	(15,303)
Earnings	8,988,260	7,479,222	705,162	603,896
Net Transfers	0	(12,951)	(25,164)	38,135
Assets January 1, 1992	\$46,549,962	\$39,213,665	\$3,399,167	\$3,936,890
Assets Per HCSC	\$46,549,962	\$41,629,421	\$2,541,140	\$2,379,401
Asset Variance	\$0	(\$2,415,756)	\$858,027	\$1,557,489

Notes: Earnings are reported for the delay periods in GAS 413 80 only. Earnings are