

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW
OF
MEDICARE CONTRACTOR'S
PENSION SEGMENTATION
BLUE CROSS AND BLUE SHIELD
OF FLORIDA**



JUNE GIBBS BROWN
Inspector General

DECEMBER 1995
CIN: A-07-94-01107



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

CIN: A-07-94-01 107

December 7, 1995

Mr. Rick Kibler
Director of Internal Audit
Blue Cross and Blue Shield of Florida
P.O. Box 1798 - JMA-3
Jacksonville, Florida 32231-0014

Dear Mr. Kibler:

This report provides the results of an Office of Inspector General (OIG), Office of Audit Services (OAS) review titled *Review of Medicare Contractor's Pension Segmentation, Blue Cross and Blue Shield of Florida*. The purpose of our review was to evaluate whether Blue Cross and Blue Shield of Florida (Florida) complied with the pension segmentation requirements of its Medicare contract. The audit addressed the update of pension assets during the period January 1, 1990 to January 1, 1994.

Our review showed that Florida understated Medicare segment pension assets as of January 1, 1990 by \$432,579. The understatement occurred because Florida did not fully implement the recommendations of our prior segmentation audit report. Florida's update of the Medicare segment assets from Plan Year 1990 to Plan Year 1994 understated segment assets by an additional \$380,543. The understatement occurred primarily because Florida used incorrect participant data in their update of pension assets.

We recommend that Florida increase the January 1, 1994 assets of the Medicare segment by \$813,122 (\$432,579 plus \$380,543). Florida agreed with the recommendation. Florida's response is included in its entirety as Appendix B.

INTRODUCTION

BACKGROUND

Florida has administered Medicare Parts A and B under cost reimbursement contracts since the start of the Medicare program. The contracts, the Federal Acquisition Regulations (FAR), which superseded the Federal Procurement Regulations (FPR), and the Cost Accounting Standards (CAS) contain reimbursement principles for cost reimbursement contracts.

Since its inception, Medicare has paid a portion of the annual contributions made by contractors to their pension plans. These payments represented allowable pension costs under the FPR and/or the FAR. In 1980, both the FPR and Medicare contracts incorporated CAS 412 and 413.

The CAS 412 regulates the determination and measurement of the components of pension costs. It also regulates the assignment of pension costs to appropriate accounting periods. The CAS 413 regulates the valuation of pension assets, allocation of pension costs to segments of an organization, adjustment of pension costs for actuarial gains and losses, and assignment of gains and losses to cost accounting periods.

The Health Care Financing Administration (HCFA) incorporated segmentation requirements into Medicare contracts starting with Fiscal Year 1988. The contractual language specifies segmentation requirements and also provides for the separate identification of the pension assets for a Medicare segment.

Florida's contract required (1) computing the Medicare segment's actuarial liability, (2) determining the ratio of the Medicare segment's actuarial liability to the total plan actuarial liability (asset fraction), (3) allocating a portion of total pension assets as of 1986 based on the above ratio, (4) updating Medicare pension assets annually, and (5) assessing if Medicare's pension costs should be separately calculated.

The Medicare contracts identify a Medicare segment as:

*... any organizational component **of** the contractor, such as a division, department, or other similar subdivision, having a significant degree of responsibility and accountability **for** the Medicare contract/agreement, in which.*

- I. The majority **of** the salary dollars is allocated to the Medicare agreement/contract; or*
- 2. Less than a majority **of** the salary dollars is allocated to the Medicare agreement/contract, and these salary dollars represent 40 percent or more **of** the total salary dollars allocated to the Medicare agreement/contract.*

The contracts also provide for separate identification of the pension assets of the Medicare segment. The identification involves the allocation of assets to the Medicare segment as of the first pension plan year after December 31, 1985 in which the salary criterion was met. The allocation was to use the ratio of the actuarial liabilities of the Medicare segment to the actuarial liabilities of the total plan, as of the later of the first day of the first plan year starting after December 31, 1980, or the first day of the first pension plan year following the date such Medicare segment first existed.

Our previous segmentation review (CIN: A-07-91-00473) addressed the computation of the asset fraction, the identification of the segment's assets as of January 1, 1986, and the update of the segment's assets to January 1, 1990.

In reports provided for our current review, Florida identified total pension assets of \$98,730,170 and Medicare segment assets of \$17,338,906 as of January 1, 1994. Florida also concluded that separate valuations for the Medicare segment were required.

Florida participates in the National Retirement Program administered by the Blue Cross/Blue Shield National Employee Benefits Administration (NEBA). The Wyatt Company, NEBA's actuarial firm, played a major role in the preparation of Florida's segmentation calculations.

SCOPE

We made our examination in accordance with generally accepted government auditing standards. Our objective was to determine Florida's compliance with pension segmentation requirements of its Medicare contract. Achieving our objective did not require a review of Florida's internal control structure. The audit addressed the update of pension assets during the period January 1, 1990 to January 1, 1994.

We performed this review in conjunction with our audits of unfunded pension costs (CIN: A-07-95-01 126) and pension costs claimed for Medicare reimbursement (CIN: A-07-95-01 125). The information obtained and reviewed during those audits was also used in performing this review.

We reviewed Florida's identification of the Medicare segment and its update of Medicare assets from January 1, 1990 to January 1, 1994.

In performing our review, we used information provided by NEBA and NEBA's pension actuary. The information included liabilities, normal costs, contributions, expenses, and earnings. We reviewed Florida's accounting records, pension plan documents, annual actuarial valuation reports, and the Department of Labor/Internal Revenue Service Forms 5500. Using these documents, we updated the Medicare segment assets to January 1, 1994. The HCFA pension actuarial staff reviewed our methodology and calculations.

We performed site work at Florida's corporate offices in Jacksonville, Florida during September 1994. Subsequently, we performed audit work in our Jefferson City, Missouri office.

FINDINGS AND RECOMMENDATION

As of January 1, 1994 pension assets for Florida's Medicare segment were understated by \$813,122.

The understatement of pension assets resulted because Florida:

- did not implement recommendations contained in our previous report (\$432,579)
- misclassified participants and transfers as to segment and non-segment (\$166,678)
- improperly identified benefit payments to retirees (\$27,339)
- inequitably assigned pension contributions (\$66,314)
- incorrectly allocated investment earnings and expenses (\$120,212).

Prior Audit Recommendations

We determined that Florida's calculations understated the January 1, 1990 Medicare segment assets by \$432,579. The understatement occurred because Florida did not fully implement the recommendations contained in our previous segmentation report. We reviewed correspondence between Florida and HCFA as well as audit clearance documents which noted that Florida concurred with all the findings and recommendations of our previous segmentation report. However, Florida did not instruct their consulting actuary to implement the report recommendations.

The following schedule shows the details of the calculations.

	<u>Florida</u>	<u>OIG</u>	<u>Variance</u>
January 1, 1990 Medicare Segment Assets	\$13,769,938	\$14,202,517	\$432,579

Participants and Transfers

In the update of pension assets, Florida misidentified Medicare segment participants. Florida incorrectly included participants in non-Medicare segment cost centers and incorrectly excluded participants in Medicare segment cost centers.

Since the identification of the segment participants was incorrect, transfers (representing the movement into and out of the segment each year) in the updates were also incorrect. The following table compares computations of transfer amounts:

Transfer Adjustments To The Medicare Segment

<u>Year</u>	<u>Florida</u>	<u>OIG</u>
1990	\$ (318,486)	\$ (447,133)
1991	(888,727)	(74,862)
1992	761,370	(256,742)
1993	<u>(1,790,556)</u>	<u>(1,290,984)</u>
Total	<u><u>\$(2,236,399)</u></u>	<u><u>\$(2,069,721)</u></u>

We corrected the identification of the segment participants and transfer amounts in updating the Medicare segment pension assets. See Appendix A. Our corrections to the transfer amounts increased the Medicare segment assets by \$166,678 (\$2,236,399 less \$2,069,721).

Payments to Retirees

Due to incorrect identification of the Medicare segment, Florida's update of segment assets did not properly identify benefit payments to retirees that were segment participants. We matched benefit payments to individual retirees and included them in our update of segment assets. A comparison of Florida's and our computed benefit amounts are shown on the following schedule.

Benefit Payments to Medicare Segment Retirees

<u>Year</u>	<u>Florida</u>	<u>OIG</u>	<u>Variance</u>
1990	\$ (130,524)	\$ (131,445)	\$ (921)
1991	(242,419)	(226,477)	15,942
1992	(270,223)	(268,654)	1,569
1993	<u>(599,314)</u>	<u>(588,565)</u>	<u>10,749</u>
Total	<u><u>\$(1,242,480)</u></u>	<u><u>\$(1,215,141)</u></u>	<u><u>\$27,339</u></u>

We corrected the benefit payment amounts in updating the Medicare segment assets as shown in Appendix A. This resulted in a net increase of \$27,339 in the Medicare segment assets.

Assignment of Pension Contributions

Florida's update methodology did not equitably assign pension contributions to the Medicare segment. As a result, Florida understated Medicare segment assets by \$66,314. The understatement primarily occurred because Florida only assigned contributions to the segment for 1992 and 1993 equal to the segment's computed pension costs.

For 1992 and 1993, Florida's consulting actuary calculated pension costs separately for the total company and the Medicare segment. For 1992, Florida's actual contribution to the pension trust fund exceeded the total company pension cost calculated by its actuary. However, Florida did not assign any portion of the excess contribution to the Medicare

segment. Instead, Florida assigned all of the excess contribution to the "other" segment (total company less the Medicare segment). Conversely, Florida's 1993 contribution was less than the total company pension cost calculated by their actuary. Florida's methodology credited the segment with a contribution exactly equal to the segment's pension cost. The balance of the 1993 contribution was assigned to the "other" segment.

We assigned an equitable portion of the total company contributions to the Medicare segment, based on a ratio of the Medicare segment CAS funding target to the total company CAS funding target. See Appendix A. Our calculations increased Medicare segment assets by \$66,314.

Allocation of Earnings and Expenses

Florida's update methodology allocated investment earnings and administrative expenses to the Medicare segment based on a ratio of segment assets to total company assets. Because Florida's asset amounts were incorrect, it understated the segment's earnings and expenses for each year of the update. Except for correcting **asset** amounts, as previously described, we used Florida's allocation methodology in our update and increased the Medicare segment assets by \$120,212.

Summary

We updated pension assets of the Medicare segment from January 1, 1990 to January 1, 1994 (See Appendix A). Our calculation showed that assets of the Medicare segment increased \$813,122 as of January 1, 1994. This increase resulted from starting with the proper assets as of January 1, 1990 (\$432,579 increase), correcting the transfer adjustments (\$166,678 increase), correcting the benefit payments (\$27,339 increase), correcting the allocation of contributions (\$66,314 increase), and calculating the update with corrected asset amounts (\$120,212 increase).

Recommendation:

We recommend that Florida:

- 0 Increase the pension assets of the Medicare segment by \$813,122 (\$432,579 plus \$380,543) as of January 1, 1994.

Auditee Response

Florida agreed with the recommendation.

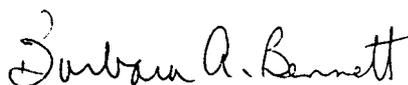
INSTRUCTIONS FOR AUDITEE RESPONSE

Final determination 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 within 30 days from the date of this report to the HHS action official, presenting any comments or additional information that you believe may have a bearing on final determination.

- - - - -

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 in the Act which the Department chooses to exercise. (See 45 CFR Part 5.)

Sincerely,



Barbara A. Bennett
Regional Inspector General for
Audit Services, Region VII

Enclosures

HHS Action Official:

Mr. Clarence J. Boone
Acting Regional Administrator, Region IV
Health Care Financing Administration
101 Marietta Street
Atlanta, Georgia 30023

BLUE CROSS AND BLUE SHIELD OF FLORIDA
JACKSONVILLE, FLORIDA

STATEMENT OF MEDICARE PENSION ASSETS

FOR THE PERIOD
JANUARY 1, 1990 TO JANUARY 1, 1994

Description		Total Company	Other Segment	Medicare Segment
Assets January 1, 1990	<u>1/</u>	\$71,493,976	\$57,291,459	\$14,202,517
Contributions	<u>2/</u>	\$ 0	\$ 0	\$ 0
Earnings	<u>3/</u>	(1,804,141)	(1,445,742)	(358,399)
Benefits	<u>4/</u>	(2,047,867)	(1,916,422)	(131,445)
Expenses	<u>5/</u>	(371,526)	(297,721)	(73,805)
Participant Transfers	<u>6/</u>	0	447,133	(447,133)
Assets January 1, 1991		\$67,270,442	\$54,078,707	\$13,191,735
Contributions		\$ 0	\$ 0	\$ 0
Earnings		14,764,868	11,869,477	2,895,391
Benefits		(2,392,846)	(2,166,369)	(226,477)
Expenses		(460,678)	(370,339)	(90,339)
Participant Transfer		0	74,862	(74,862)
Assets January 1, 1992		\$79,181,786	\$63,486,338	\$15,695,448
Contributions		\$ 5,571,012	\$ 4,298,228	\$ 1,272,784
Earnings		3,135,297	2,513,817	62 1,480
Benefits		(1,947,159)	(1,678,505)	(268,654)
Expenses		(388,391)	(3 11,404)	(76,987)
Participants Transfers		0	256,742	(256,742)
Assets January 1, 1993		\$85,552,545	\$68,565,216	\$16,987,329
Contributions		\$ 6,996,899	\$ 5,504,329	\$ 1,492,570
Earnings		8,407,869	6,738,401	1,669,468
Benefits		(1,633,922)	(1,045,357)	(588,565)
Expenses		(593,221)	(475,43 1)	(117,790)
Participants Transfers		0	1,290,984	(1,290,984)
Assets January 1, 1994		\$98,730,170	\$80,578,142	\$18,152,028
Assets Per Florida	<u>7/</u>	\$98,730,170	\$81,391,264	\$17,338,906
Asset Variance	<u>8/</u>	\$ 0	\$ (813,122)	\$ 813,122

BLUE CROSS AND BLUE SHIELD OF FLORIDA
JACKSONVILLE, FLORIDA

STATEMENT OF MEDICARE PENSION ASSETS

FOR THE PERIOD
JANUARY 1, 1990 TO JANUARY 1, 1994

FOOTNOTES

1/ We calculated the January 1, 1990 Medicare segment assets during our previous segmentation review. The amounts shown for the "other" segment represent the difference between the total company and the Medicare segment.

2/ We obtained total contribution amounts from IRS Form 5500 reports. Florida did not make contributions to the pension trust fund for years 1990 and 1991. For years 1992 and 1993, we allocated contributions to the Medicare segment based on the ratio of the segment's CAS funding target to the total company CAS funding target. The CAS funding target is computed in our report of unfunded pension costs (CIN: A-07-95-01126).

3/ We obtained investment earnings from actuarial valuation reports. We allocated earnings to the Medicare segment based on the ratio of beginning of year market value of Medicare assets to the beginning of year market value of total assets. Florida used this same methodology.

4/ We obtained total benefit payments from actuarial valuation reports. We based the Medicare segment's benefit payments on actual payments to Medicare segment retirees.

5/ We obtained administrative expenses from actuarial valuation reports. We allocated administrative expenses to the Medicare segment on the ratio of beginning of year market value of Medicare assets to the beginning of year market value of total assets. Florida used this same methodology.

6/ We identified participant transfers between segments by comparing annual participant valuation listings provided by Florida. The listings contained the actuarial liability of each participant at year-end. Our transfer adjustment considered each participant's actuarial liability and the funding level of the segment from which the participant transferred. We calculated the funding level as the assets divided by the liabilities. If the funding level ratio was greater than one, we transferred assets equal to the participant's liability. Florida used this same methodology.

7/ We obtained the total asset amounts as of January 1, 1994 from Florida's update of assets provided by its actuary.

8/ The asset variance represents the difference between the OIG calculation of assets as of January 1, 1994 and the assets calculated by Florida's actuary.



P O Box 1798, JMA-3
Jacksonville FL 32231-0014
(904) 791-6111

July 7, 1995

Ms. Barbara A. Bennett
Regional Inspector General for Audit Services, Region VII
Office of Inspector General
Office of Audit Services
601 East 12th Street
Kansas City, Missouri 64106

Re: Review of Pension Costs Claimed For Medicare Reimbursement CIN: A-07-95-01125
Review of Unfunded Pension Costs CIN: A-07-95-01 126
Review of Medicare Contractor's Pension Segmentation CIN: A-07-94-01 107

Dear Ms. Bennett:

We have reviewed the drafts of the three audit reports referenced above. This letter will serve to document Blue Cross and Blue Shield of Florida's response. Due to the technical nature of the review, we have relied heavily on our consultants from the National Employee Benefits Administration (NEBA) and our actuary from The Wyatt Company. The page numbers below correspond to the page numbers in the draft reports.

- o CIN: A-07-95-01 125 Pension Costs Claimed For Medicare Reimbursement (Recommendation - page 4) We recommend that Florida:
Revise its FACPs for Fiscal Years 1992 and 1993 to claim \$216,113 in allowable CAS pension costs.

Response: The Plan agrees that it did not fully claim its pension costs for Fiscal Year 1992. It anticipates that it will request reimbursement for those costs for which it is entitled to submit claims. Additionally it is continuing to review whether it agrees with the finding that \$853,847 in pension costs should be disallowed for Fiscal Year 1993.

- o CIN: A-07-95-01126 Unfunded Pension Costs (Recommendation - page 5) We recommend that Florida:
Identify \$6,428,087 (\$2,378,198 determined in prior audit plus \$4,049,889) as an unallowable component of direct pension costs as of January 1, 1994.

Annually update the unallowable pension cost component related to the accumulated unfunded CAS costs as of January 1, 1994.

Update unfunded pension costs for any subsequent years unallowable costs are identified.

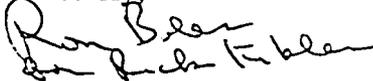
Response: The Plan agrees that it did not make contributions in 1990 and 1991 and that it under-funded the 1993 CAS pension costs by \$59,808. In accord with recent changes to the Cost Accounting Standards, BCBSF anticipates filing a request to amortize the eligible unfunded pension costs. It also agrees that it should identify, as an unallowable component of direct pension costs as of January 1, 1994, those pension costs that will remain unfunded following resolution of its request. Additionally, the Plan agrees with the last two recommendations.

- 0 CIN: A-07-94-01 107 Medicare Contractor's Pension Segmentation
(Recommendation - page 6) We recommend that Florida:
Increase the pension assets of the Medicare segment by \$813,122 (\$432,579 plus \$380,543) as of January 1, 1994.

Response: The Plan agrees with the recommendation.

If you have additional questions, please do not hesitate to call me at (904) 363-4661 or Ken Perkins at (904) 363-4662.

Sincerely,



Rick Kibler
Audit Director
Internal Audit Division

RAB/rab
(RAB05552)