

**Department of Health and Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**AUDIT OF ADMINISTRATIVE  
COSTS CLAIMED UNDER PART B  
OF THE HEALTH INSURANCE FOR  
THE AGED AND DISABLED PROGRAM**



**JUNE GIBBS BROWN  
Inspector General**

DECEMBER 1996  
A-07-96-02001



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

DEC 3 1 1996

CIN A-07-96-02001

Mr. David Kikumoto  
Chief Executive Officer  
Rocky Mountain Health Care Corporation  
700 Broadway  
Denver, Colorado 80273

Dear Mr. Kikumoto:

This report provides the results of our *Audit of Administrative Costs Claimed Under Part B of the Health Insurance for the Aged and Disabled Program (Medicare)*. The objective of our audit was to determine the allowability, allocability, and reasonableness of the final administrative costs claimed by Blue Cross Blue Shield of Colorado for processing Medicare Part B claims during the period October 1, 1989 through December 1, 1994.

Our audit of administrative costs totaling \$58,837,734 determined that \$4,244,570 was unallowable. Blue Cross Blue Shield claimed \$4,244,570 in excess of approved budgets, of which \$258,534 was also questioned for other reasons. This \$258,534 was made up of excess executive compensation \$141,554 and unallowable cafeteria costs \$116,980. We are recommending the final administrative cost proposals be reduced by a total of \$4,244,570.

Blue Cross Blue Shield did not concur with our findings and recommendations. The Blue Cross Blue Shield did not dispute that costs were incurred in excess of approved budgets. Rather, Blue Cross Blue Shield maintained that the Health Care Financing Administration (HCFA) did not negotiate budgets or respond to proposals to reduce contracts as required by the contract. In addition, Blue Cross Blue Shield indicated that HCFA would not accept claims in excess of approved budgets and would have penalized them if claims in excess of approved budgets had been submitted. Further, Blue Cross Blue Shield asserted that their contract allowed them to claim costs in excess of approved budgets and that HCFA was required by the contract to reimburse the excess costs. The Blue Cross Blue Shield response is summarized following each recommendation along with our comments concerning the Blue Cross Blue Shield comments. The complete text of the Blue Cross Blue Shield response is included as Appendix B.

## BACKGROUND

The Medicare program is administered by the Health Care Financing Administration (HCFA), an agency of the Department of Health and Human Services (Department). Public or private organizations, known as carriers for Part B services, assist HCFA in the

administration of the Medicare program. The Secretary enters into contracts (agreements) with the carriers to administer Medicare claims processing functions and reimburses them for the allowable administrative costs incurred in their performance.

Each participating carrier submits an annual prospective budget of administrative costs to be incurred to the HCFA regional office for review and approval. Final administrative cost proposals (FACP) and supporting data serve as the basis for settlement of allowable administrative costs.

On August 2, 1994, Blue Cross Blue Shield notified HCFA that they would not renew the contract. They served as the Part B carrier until December 1, 1994.

#### SCOPE OF AUDIT

We examined \$58,837,734 in Medicare Part B administrative costs claimed for the period October 1, 1989 through December 1, 1994. The objectives of our audit were to determine whether the costs claimed by Blue Cross Blue Shield were allowable, allocable, and reasonable in accordance with the contractual agreement and the Federal Acquisition Regulations (FAR) Part 31. We performed our audit in accordance with generally accepted government auditing standards.

Our review included an evaluation of the accounting system and related internal controls, tests of the accounting records, and the application of auditing procedures contained in the *Audit Guide for the Review of Administrative Costs Incurred by Medicare Intermediaries and Carriers Under Title XVIII of the Social Security Act*, issued by the Department, Office of the Inspector General in February 1991. Because the contract was discontinued, our internal control review was limited to those controls related to accumulation and reporting of costs on the FACP. Also, we did not audit Blue Cross Blue Shield's pension plan.

Audit procedures also included:

- Reconciling audited financial statements and claimed costs to the accounting records.
- Comparing the claimed costs to the approved budget ceiling.
- Verifying the accuracy of cost center allocations to the contract.
- Reviewing supporting documentation for a judgmental sample of charges.
- Evaluating the allocation of costs to ensure fairness.
- Comparing executive salary increases with the Employment Cost Index.

- Reviewing cafeteria costs to determine if they were in compliance with FAR.

The field work was performed at the offices of Blue Cross Blue Shield, Denver, Colorado during November 1995 through July 1996.

## RESULTS OF REVIEW

Blue Cross Blue Shield claimed costs of \$58,837,734 for the audit period. We accepted \$54,593,164 and are recommending a reduction of \$4,244,570 to the FACP because costs exceeded the approved budgets. Of this reduction, \$258,534 was also questioned due to unreasonable executive compensation (\$141,554) and unallowable cafeteria costs (\$116,980).

### COSTS IN EXCESS OF APPROVED BUDGETS

The Medicare contract limits expenditures to the budget approved by HCFA. For the period October 1, 1989 through December 1, 1994, Blue Cross Blue Shield claimed \$4,244,570 in excess of approved budgets. Approved and claimed costs are shown by fiscal year in the following schedule.

<i>Fiscal Year</i>	<i>Approved Budget</i>	<i>Amount Claimed</i>	<i>Excess Amount</i>
1990	\$ 9,412,281	\$10,024,865	\$ 612,584
1991	10,740,583	10,827,145	86,562
1992	11,831,700	12,254,871	423,171
1993	10,951,700	12,638,071	1,686,371
1994	9,822,900	11,157,867	1,334,967
1995	<u>1,834,000</u>	<u>1,934,915</u>	<u>100,915</u>
Totals	<u>\$54,593,164</u>	<u>\$58,837,734</u>	<u>\$4,244,570</u>

Blue Cross Blue Shield did not claim these excess costs until after the Medicare contract was terminated December 1, 1994. The approval must be obtained before costs are incurred in excess of the negotiated budget ceiling, as stated in the Medicare contract, Article XVI, Paragraph C:

*The Secretary and the Carrier shall negotiate the amount of the annual budget, and amendments thereto, based on the amount submitted by the Carrier in an amount calculated to pay the costs of administering the Carrier's contract. After the negotiations between the Secretary and the Carrier on the amount of the annual budget and any amendments thereto, the Secretary shall issue a notice to the Carrier specifying such budgeted amount. Such budgeted amount for the purpose of obligation of funds by the Secretary shall be a ceiling which the Carrier may not exceed without prior approval of the Secretary.. (emphasis added)*

Article XVI, Paragraph H required Blue Cross Blue Shield to notify (notification in any form followed by written notification) HCFA no less than 60 days prior to the date budgeted funds would be exhausted. The notification was to include proposals on ways to reduce costs. The 60 day period was to provide time for Blue Cross Blue Shield and HCFA to resolve the budget deficit problem by increasing the approved budget, reduce functions to be performed by Blue Cross Blue Shield, or a combination of increased budget and function reduction. Blue Cross Blue Shield made supplemental budget requests for additional funding. However, HCFA did not approve any supplemental budget requests which exceeded amounts shown in the above schedule.

Of the \$4,244,570 claimed in excess of approved budgets, a total of \$258,534 was also questioned for other reasons. As such, Appendix A shows a net questioned cost of \$3,986,036 because of the budget excess.

#### RECOMMENDATION

We recommend that final administrative cost proposals be reduced by a total of \$4,244,570. The recommended adjustments by fiscal year are shown in Appendix A.

#### Blue Cross Blue Shield Response

Blue Cross Blue Shield raised three issues relative to our first finding and recommendation.

Issue One. It was Blue Cross Blue Shield's opinion that HCFA did not fulfill contract requirements to negotiate budgets. Blue Cross Blue Shield stated HCFA allocated budgets between Medicare contractors based on the amount of funds that were made available to Regional HCFA authorities from the HCFA Central Office.

OIG Comments - Issue One. In our opinion, HCFA fulfilled its negotiating requirements by issuing the notices of budget approvals. The notices adequately identified the amount of funds that HCFA determined were necessary to accomplish work required under the contract and provided Blue Cross Blue Shield with adequate notice concerning operating funds available to do contract work.

Furthermore, contract terms required Blue Cross Blue Shield to notify HCFA within 60 calendar days of when the budgeted funds would be exhausted. Blue Cross Blue Shield made no such notifications. The 60 day advance notification was necessary so that steps to reduce functions or increase funding could be taken. Instead of giving the advance notice to HCFA, Blue Cross Blue Shield continued to conduct work at a level that exceeded funding availability. HCFA was unaware of each annual funding problem until after the contract was terminated in December 1994. Consequently, HCFA was not given the opportunity to reject increased funding in favor of options to reduce contract functions.

Issue Two. Blue Cross Blue Shield also stated that Article XV, paragraph A of the Contract required payment for cost incurred under the principle of neither profit or loss; i.e. a cost reimbursable contract.

OIG Comments - Issue Two. It is true that Article XV, paragraph A intended the Contract to be cost reimbursable. However, paragraph A is only one paragraph of Article XV and must be interpreted within context with the other paragraphs of Article XV and the entire contract. The provisions of paragraphs C, G and H are important to the overall interpretation of Article XV. These paragraphs (1) prohibited Blue Cross Blue Shield from exceeding the approved budgets, (2) allowed Blue Cross Blue Shield to discontinue performance under the contract, and (3) required Blue Cross Blue Shield to notify HCFA of budget shortfalls within 60 days of the occurrence. If Blue Cross Blue Shield had complied with the provisions of paragraphs (C, G, or H), HCFA would have had the opportunity to take steps adjust work requirements or provide additional funds. Blue Cross Blue Shield, however, continued to incur costs in excess of authorized amounts on their own volition without giving HCFA the required notification.

Issue Three. Blue Cross Blue Shield indicated that Article XVI, paragraph G. 2 states that Blue Cross Blue Shield has the right to claim costs in excess of the approved budget and the claim shall not be held in prejudice. Blue Cross Blue Shield also pointed out that Article XVI, paragraph I of the contract says that costs incurred in excess approved budgets will be paid (upon final settlement) if they are determined to be allowable.

OIG Comments - Issue Three. Paragraph G. 2 states that Blue Cross Blue Shield's right to claim costs in excess of approved budgets under paragraph I will not be prejudiced. However, paragraph I required Blue Cross Blue Shield to comply with reporting provisions under paragraph H. Blue Cross Blue Shield failed to give HCFA the 60 day notice of impending budget shortfall required by paragraph H. In addition, Article XVI, paragraph K required Blue Cross Blue Shield to submit reports of allowable costs within the close of each Federal fiscal year. Blue Cross Blue Shield did not submit reports of allowable costs in excess of approved budgets for any of the years involved until December 1, 1994.

## EXECUTIVE COMPENSATION

Blue Cross Blue Shield executives, whose compensation was charged to Medicare cost centers, received salary increases that exceeded the Department of Labor's Employment Cost Index (ECI) during calendar years 1990 through 1993. As a result, Medicare was charged \$141,554 in excess of reasonable costs.

Section 31.201-2(a) of the FAR states that reasonableness is one of the factors to be considered in determining whether a cost is allowable. With regard to reasonableness, FAR Section 31.205-6 (b) further states, in part,

*Based on an initial review of the facts, contracting officers or their representatives may challenge the reasonableness of any individual element or the sum of the individual elements of compensation paid or accrued to particular employees or classes of employees. In such cases, there is no presumption of reasonableness and, upon challenge, the contractor must demonstrate the reasonableness of the compensation item in question.*

The ECI provides the average salary increases received by executive, administrative, and managerial positions each year. We used the ECI to determine the reasonableness of increases given to five Blue Cross Blue Shield executives -- (1) Chief Executive Officer, (2) Senior Vice President for Finance, (3) Senior Vice President for Operations, (4) General Counsel, and (5) Quality Executive.<sup>1</sup>

From calendar year 1990 through 1993, the five executive positions received salary increases averaging 14.9 percent per year while the ECI increased an average of 3.63 percent per year.

#### RECOMMENDATION

We recommend that final administrative cost proposals be reduced by \$141,554. The recommended adjustments by fiscal year are shown in Appendix A.

#### Blue Cross Blue Shield Response

Blue Cross Blue Shield stated that the Medicare contract and applicable Federal regulations did not refer to the Department of Labor's ECI as a limit for salary increases of executive staff. Blue Cross Blue Shield also pointed out that Federal regulations (FAR, section 31.205-6, paragraph (a)(3)) states compensation must be based on, and conform to, the terms and conditions of the contractor's established compensation plan or practice followed so consistently as to imply, in effect, an agreement to make the payment.

#### OIG Comments

FAR section 31.205-6 paragraph a.3 is prefaced with the statement "Compensation for personal services in allowable subject to the following general criteria and additional requirements contained in other parts of this cost principle." In our opinion, the principle of reasonable cost set forth in FAR section 31.205-6 (b) is more specific and outweighs the general guidance provided by FAR section 31.205-6 (a)(3). A factor commonly used to measure the reasonableness of pay increases is the Department of Labor's ECI.

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<sup>1</sup> The Quality Executive position was not established until calendar year 1992

## CAFETERIA

During the period October 1, 1989 through November 30, 1994, cafeteria costs of \$116,980 were unallowable because Blue Cross Blue Shield did not try to break even on the cafeteria operation. Section 31.205-13 of FAR states, in part:

*The aggregate **of** costs incurred on activities designed to improve working conditions, employer-employee relations, employee morale, and employee performance (less income generated by these activities) are allowable, except as limited by paragraph (b), (c), and (d). . . Some examples are. . . food and dormitory services, which include cafeterias. . . vending machines.*

The paragraph (b) exception states, in part, that:

*(b) Losses from operating food and dormitory services may be included as costs only if the contractor's objective is to operate such services on a break-even basis.*

The Blue Cross Blue Shield contracted with a food service company (vendor) to manage cafeteria and vending machines operations. The contract provided that Blue Cross Blue Shield would receive 60 percent of net profits exceeding eight percent of gross sales after deducting a management fee equal to two percent of sales. Our review of unaudited financial statements of the vendor showed that while a profit was made, the profit did not exceed the required eight percent. However, the contract also required Blue Cross Blue Shield to donate the space and utilities for the cafeteria to the vendor at no cost. Blue Cross Blue Shield did incur costs for cafeteria space and charged \$116,980 to Medicare on the FACP.

Even though the contract commenced in 1985, there was no evidence that Blue Cross Blue Shield attempted to renegotiate the contract during the 9 years of operation to recover space costs and operate the cafeteria on a break-even basis as required by the FAR.

## RECOMMENDATION

We recommend that final administrative cost proposals be reduced by \$116,980. The recommended adjustments by fiscal year are shown in Appendix A.

### Blue Cross Blue Shield Response

Blue Cross Blue Shield's position on this finding is that the cafeteria costs questioned by our audit do not represent a loss to Blue Cross Blue Shield in the context of Far 31.205-13 because they did not directly operate the cafeteria.

OIG Comments

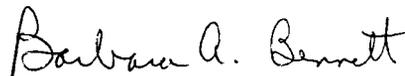
We disagree. In our opinion, FAR 3 1.205-13 requires Blue Cross Blue Shield to attempt to manage the cafeteria on a break-even basis whether it is operated directly by Blue Cross Blue Shield or under contract with a food service vendor. Blue Cross Blue Shield could have monitored the contract with the food services vendor more closely to ensure it recovered donated space costs that was charged to the Medicare function.

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

Sincerely,



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

Appendices

HHS Action Official:

Regional Administrator, Region VIII  
Health Care Financing Administration

BLUE CROSS BLUE SHIELD OF COLORADO  
DENVER, COLORADO

STATEMENT OF ADMINISTRATIVE COSTS CLAIMED  
AND RESULTS OF AUDIT  
OCTOBER 1, 1989 THROUGH DECEMBER 1, 1994

<u>Cost Category</u>	<u>Claimed</u>	<u>Results of Audit</u>		
		<u>Accepted</u>	<u>Questioned</u>	
Salaries and Wages	<b>\$26,715,184</b>	<b>\$26,573,630</b>	\$141,554	<u>1/</u>
Fringe Benefits	<b>5,990,906</b>	<b>5,990,906</b>	0	
Facilities & Occupancy	<b>2,085,308</b>	<b>1,968,328</b>	116,980	<u>2/</u>
EDP Equipment	<b>1,665,564</b>	<b>1,665,564</b>	0	
Subcontracts	<b>9,268,933</b>	<b>9,268,933</b>	0	
Consultants	725,001	725,001	0	
Telephone	<b>1,011,844</b>	<b>1,011,844</b>	0	
Postage	<b>5,255,640</b>	<b>5,255,640</b>	0	
Furniture & Equipment	<b>2,100,403</b>	<b>2,100,403</b>	0	
Material & Supplies	<b>2,089,004</b>	<b>2,089,004</b>	0	
Travel	459,272	459,272	0	
Return on Investment	<b>1,103,148</b>	<b>1,103,148</b>	0	
Miscellaneous	534,454	534,454	0	
Other	3512,798	<b>3,512,798</b>	0	
Credits	<u><b>(3,679,725)</b></u>	<u><b>(3,679,725)</b></u>	<u><b>0</b></u>	
Subtotal Claimed	<b>58,837,734</b>	<b>58,579,211</b>	258,533	
Budget Excess	<u>                    </u>	<u><b>(3,986,036)</b></u>	<u><b>3,986,036</b></u>	<u>3/</u>
Total	<u><b>\$58,837,734</b></u>	<u><b>\$54,593,164</b></u>	<u><b>\$4,244,570</b></u>	

1/ Salary increases in excess of reasonable amounts.

2/ Unallowable cafeteria costs.

3/ The total in excess of approved budget was **\$4,244,570**. We have offset this amount by the amount of costs questioned (\$258,534) for reasons indicated above.

BLUE CROSS BLUE SHIELD OF COLORADO  
DENVER, COLORADO

STATEMENT OF ADMINISTRATIVE COSTS CLAIMED  
AND RESULTS OF AUDIT  
OCTOBER 1, 1989 THROUGH SEPTEMBER 30, 1990

<u>Cost Category</u>	<u>Claimed</u>	<u>Results of Audit</u>		
		<u>Accepted</u>	<u>Questioned</u>	
Salaries and Wages	<b>\$4,642,055</b>	<b>\$4,606,700</b>	\$35,355	<u>1/</u>
Fringe Benefits	<b>1,021,766</b>	<b>1,021,766</b>	0	
Facilities & Occupancy	428,415	404,638	23,777	<u>2/</u>
EDP Equipment	131,256	131,256	0	
Subcontracts	<b>1,517,139</b>	<b>1,517,139</b>	0	
Consultants	113,239	113,239	0	
Telephone	167,548	167,548	0	
Postage	956,683	956,683	0	
Furniture & Equipment	332,084	332,084	0	
Material & Supplies	379,617	379,617	0	
Travel	73,331	73,331	0	
Return on Investment	0	0	0	
Miscellaneous	272,489	272,489	0	
Other	645,172	645,172	0	
Credits	<u>(655,929)</u>	<u>(655,929)</u>	<u>0</u>	
Subtotal	<b>10,024,865</b>	<b>9,965,733</b>	59,532	
Budget Excess		<u>(553,452)</u>	<u>553,452</u>	
Total	<b><u>\$10,024,865</u></b>	<b><u>\$9,412,281</u></b>	<b><u>\$612,584</u></b>	

1/ Salary increases in excess of reasonable amounts.

2/ Unallowable cafeteria costs.

3/ The total in excess of approved budget was \$612,584. We have offset this amount by the amount of costs questioned (\$59,132) for reasons indicated above.

BLUE CROSS BLUE SHIELD OF COLORADO  
DENVER, COLORADO

STATEMENT OF ADMINISTRATIVE COSTS CLAIMED  
AND RESULTS OF AUDIT  
OCTOBER 1, 1990 THROUGH SEPTEMBER 30,1991

<u>Cost Category</u>	<u>Claimed</u>	<u>Accepted</u>	<u>Questioned</u>	
Salaries and Wages	<b>\$5,049,322</b>	<b>\$5,019,126</b>	\$30,196	<u>1/</u>
Fringe Benefits	<b>1,097,032</b>	<b>1,097,032</b>	0	
Facilities & Occupancy	408,286	386,287	21,999	<u>2/</u>
EDP Equipment	159,359	159,369	0	
Subcontracts	<b>1,683,678</b>	<b>1,683,678</b>	0	
Consultants	144,231	144,231	0	
Telephone	210,659	210,659	0	
Postage	941,765	941,765	0	
Furniture & Equipment	363,723	363,723	0	
Material & Supplies	335,479	335,479	0	
Travel	100,631	100,631	0	
Return on Investment	336,463	336,463	0	
Miscellaneous	43,387	43,387	0	
Other	669,084	669,084	0	
Credits	<u>(715,954)</u>	<u>(715,954)</u>	<u>0</u>	
Subtotal Claimed	<b>10,827,145</b>	<b>10,774,950</b>	52,195	
Budget Excess	<u>                    </u>	<u>(34,367)</u>	<u>34,367</u>	
Total	<b><u>\$10,827,145</u></b>	<b><u>\$10,740,583</u></b>	<b><u>\$86,562</u></b>	

1/ Salary increases in excess of reasonable amounts.

2/ Unallowable cafeteria costs.

3/ The total in excess of approved budget was \$86,562. We have offset this amount by the amount of costs questioned (\$52,195) for reasons indicated above.

BLUE CROSS BLUE SHIELD OF COLORADO  
DENVER, COLORADO

STATEMENT OF ADMINISTRATIVE COSTS CLAIMED  
AND RESULTS OF AUDIT  
OCTOBER 1, 1991 THROUGH SEPTEMBER 30,1992

<u>Cost Category</u>	<u>Claimed</u>	<u>Results of Audit</u>		
		<u>Accepted</u>	<u>Questioned</u>	
Salaries and Wages	<b>\$5,464,178</b>	<b>\$5,428,339</b>	\$35,839	<u>1/</u>
Fringe Benefits	<b>1,228,145</b>	<b>1,228,145</b>	0	
Facilities & Occupancy	427,423	404,129	23,294	<u>2/</u>
EDP Equipment	256,388	256,388	0	
Subcontracts	<b>2,108,846</b>	<b>2,108,846</b>	0	
Consultants	142,079	142,079	0	
Telephone	189,842	189,842	0	
Postage	<b>1,182,596</b>	<b>1,182,596</b>	0	
Furniture & Equipment	406,925	406,925	0	
Material & Supplies	493,992	493,992	0	
Travel	85,580	85,580	0	
Return on Investment	305,402	305,402	0	
Miscellaneous	8,883	8,883	0	
Other	587,166	587,166	0	
Credits	<u>(632,574)</u>	<u>(632,574)</u>		
Subtotal Claimed	<b>12,254,871</b>	<b>12,195,738</b>	59,533	
Budget Excess		<u>(364,038)</u>	<u>364,038</u>	
Total	<b><u>\$12,254,871</u></b>	<b><u>\$11,831,700</u></b>	<u>\$423,171</u>	

1/ Salary increases in excess of reasonable amounts.

2/ Unallowable cafeteria costs.

3/ The total in excess of approved budget was \$423,171. We have offset this amount by the amount of costs questioned (\$59,133) for reasons indicated above.

BLUE CROSS BLUE SHIELD OF COLORADO  
DENVER, COLORADO STATEMENT OF ADMINISTRATIVE COSTS CLAIMED  
AND RESULTS OF AUDIT  
OCTOBER 1, 1992 THROUGH **SEPTEMBER 30,1993**

<u>Cost Category</u>	<u>Claimed</u>	<u>Results of Audit</u>		
		<u>Accepted</u>	<u>Questioned</u>	
Salaries and Wages	<b>\$5,773,219</b>	<b>\$5,733,055</b>	\$40,164	<u>1/</u>
Fringe Benefits	<b>1,229,582</b>	<b>1,229,582</b>	0	
Facilities & Occupancy	400,186	375,668	24,518	<u>2/</u>
EDP Equipment	372,224	372,224	0	
Subcontracts	<b>1,987,371</b>	<b>1,987,371</b>	0	
Consultants	134,305	134,305	0	
Telephone	214,052	214,052	0	
Postage	<b>1,192,924</b>	<b>1,192,924</b>	0	
Furniture & Equipment	446,247	446,247	0	
Material & Supplies	432,152	432,152	0	
Travel	112,247	112,247	0	
Return on Investment	229,030	229,030	0	
Miscellaneous	106,893	106,893	0	
Other	784,885	784,885	0	
Credits	<u>(777,246)</u>	<u>(777,246)</u>	<u>0</u>	
Subtotal Claimed	<b>12,638,071</b>	<b>12,573,389</b>	64,682	
Budget Excess	<u>                    </u>	<u>(1,621,689)</u>	<b>1,621,689</b>	<u>3/</u>
Total	<b><u>\$12,638,071</u></b>	<b><u>\$10,951,700</u></b>	<b><u>\$1,686,371</u></b>	

1/ Salary increases in excess of reasonable amounts.

2/ Unallowable cafeteria costs.

3/ The total in excess of approved budget was **\$1,686,371**. We have offset this amount by the amount of costs questioned (\$64,682) for reasons indicated above.

BLUE CROSS BLUE SHIELD OF COLORADO  
DENVER, COLORADO

STATEMENT OF ADMINISTRATIVE COSTS CLAIMED  
AND RESULTS OF AUDIT  
OCTOBER 1, 1993 THROUGH SEPTEMBER 30, 1994

<u>Cost Category</u>	<u>Claimed</u>	<u>Results of Audit</u>		
		<u>Accepted</u>	<u>Questioned</u>	
Salaries and Wages	<b>\$4,963,256</b>	<b>\$4,963,256</b>	\$0	<u>1/</u>
Fringe Benefits	<b>1,225,923</b>	<b>1,225,923</b>	0	
Facilities & Occupancy	360,699	340,433	20,266	<u>2/</u>
EDP Equipment	575,709	359,985	0	
Subcontracts	<b>1,687,761</b>	<b>1,687,761</b>	0	
Consultants	151,713	151,713	0	
Telephone	205,547	205,547	0	
Postage	821,552	821,552	0	
Furniture & Equipment	467,426	467,426	0	
Material & Supplies	377,998	377,998	0	
Travel	80,913	80,913	0	
Return on Investment	203,849	203,849	0	
Miscellaneous	88,998	88,998	0	
Other	706,618	706,618	0	
Credits	<u>(760,095)</u>	<u>(760,095)</u>	<u>          </u>	
Subtotal Claimed	<b>11,157,867</b>	<b>11,137,601</b>	20,266	
Budget Excess	<u>          </u>	<b><u>(1,314,701)</u></b>	<b><u>1,314,701</u></b>	<u>3/</u>
Total	<b><u>\$11,157,867</u></b>	<b><u>\$9,822,900</u></b>	<b><u>\$1,334,967</u></b>	

1/ Salary increases in excess of reasonable amounts.

2/ Unallowable cafeteria costs.

3/ The total in excess of approved budget was **\$1,334,967**. We have offset this amount by the amount of costs questioned (\$20,266) for reasons indicated above.

BLUE CROSS BLUE SHIELD OF COLORADO  
DENVER, COLORADO

STATEMENT OF ADMINISTRATIVE COSTS CLAIMED  
AND RESULTS OF AUDIT  
OCTOBER 1, 1994 THROUGH DECEMBER **1,1994**

<u>Cost Category</u>	<u>Claimed</u>	<u>Results of Audit</u>		
		<u>Accepted</u>	<u>Questioned</u>	
Salaries and Wages	\$823,154	\$823,154	\$0	<u>1/</u>
Fringe Benefits	188,458	188,458	0	
Facilities & Occupancy	60,299	57,173	3,126	<u>2/</u>
EDP Equipment	170,628	59,998	0	
Subcontracts	284,138	284,138	0	
Consultants	39,434	39,434	0	
Telephone	24,196	24,196	0	
Postage	160,120	160,120	0	
Furniture & Equipment	83,998	83,998	0	
Material & Supplies	69,766	69,766	0	
Travel	6,570	6,570	0	
Return on Investment	28,404	28,404	0	
Miscellaneous	13,804	13,804	0	
Other	119,873	119,873	0	
Credits	<u>(137,927)</u>	<u>(137,927)</u>		
Subtotal Claimed	<b>1,934,915</b>	<b>1,931,789</b>	3,126	
Budget Excess		<u>(97,789)</u>	<u>97,789</u>	
Total	<b><u>\$1,934,915</u></b>	<b><u>\$1,834,000</u></b>	<b><u>\$100,915</u></b>	

1/ Salary increases in excess of reasonable amounts.

2/ Unallowable cafeteria costs.

3/ The total in excess of approved budget was \$100,915. We have offset this amount by the amount of costs questioned (\$3,126) for reasons indicated above.



700 Broadway  
Denver, Colorado 80273-0002

December 16, 1996

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

RE: CIN: A-07-96-02001

Dear Ms. Bennett:

On October 30, 1996 we received the above referenced "draft" report related to the Office of Inspector General (OIG) audit of Blue Cross and Blue Shield of Colorado's (BCBSCO) administrative costs claimed under Part B of the Health Insurance for the Aged and Disabled Program for FY 1990 through FY 1995.

Our responses are in order of the findings and recommendations presented in the draft audit report.

**RECOMMENDATION:**

We recommend that the final administrative cost proposals be reduced by a total of \$4,244,570. The recommended adjustments by fiscal year are shown in Appendix A.

**RESPONSE:**

The draft audit reports cites Article XVI, Paragraphs C and H of the Medicare Part B contract as the basis for reducing the final administrative cost proposals. Paragraph C pertains to the requirement that the Secretary and Carrier negotiate annual budgets and paragraph H pertains to the requirement that the Carrier notify HCFA within 60 days prior to budget funds being exhausted.

Barbara A. Bennett  
December 16, 1996  
Page 2

Our initial response to this finding was set forth in a memorandum dated September 13, 1996 from Tom Gillgannon, Director, Government Operations to Mr. Terry Eddleman, Department of Health and Human Services, Office of Audit Services in response to a fact sheet finding - costs in excess of **NOBAs**. Our initial response is resubmitted with this letter as Attachment 1, to be made part of our official response to the audit findings and recommendations related to costs in excess of approved budgets.

We would like to also reaffirm our strong belief that HCFA did not negotiate budgets with the contractor as required by Article XVI, Paragraph C, nor did HCFA respond to proposals on ways to reduce costs. For the most part, HCFA allocated or apportioned budgets to contractors within Region VIII based on the Regional Office's budget allocation from the HCFA Central Office in Baltimore. During this audit review period, HCFA developed multiple strategies, which changed from year-to-year, to allocate budget funding to Carriers without regard to the Carriers' right to recover allowed incurred costs in accordance with the Medicare Part B contract. The strategies for distributing budgets to Carriers ranged from "market basket pricing", to "Equivalent Work Units (EWUs)", to a Bottom Line Unit Cost (BLUC) target used in FY 1994. In utilizing these budget distribution strategies, in addition to others during the audit review period, we feel HCFA inappropriately engaged in unilateral fixed price contracting in violation of the Medicare Part B contract.

Article XV, paragraph A, of the Medicare Part B contract, states that the contractor shall be paid for the costs incurred (i.e., cost of administration) for the functions performed under the contract and that the principle of neither profit nor loss is applied. The refiled FACPs for fully allocated and allowable costs represent the costs incurred to administer the Medicare Part B contract for the audit periods being reviewed and does not include any new costs or profit items. The contract clearly states that the Medicare Part B contract is a cost reimbursement arrangement.

Article XVI, Paragraph G. 2 of the Medicare Part B contract states, that the contractor has the right to claim costs in excess of the **NOBA** amount and that this claim of excess costs shall not be held in prejudice against the contractor.

Article XVI, Paragraph I., of the Medicare Part B contract states, that if the costs incurred are determined to be allowable upon final settlement and if these allowable costs exceed the **NOBA**, then the Secretary shall pay such costs.

Barbara A. Bennett  
December 16, 1996  
Page 3

With exception of costs claimed for "excess executive compensation" and "excess cafeteria costs", which are addressed below, the auditors determined that the costs which exceeded the NOBAs during the fiscal years 1990 through 1995 are allowable.

Therefore, BCBSCO strongly believes that it is entitled to be reimbursed for its allowable costs which exceeded the NOBAs during fiscal years 1990 through 1995 in accordance with Articles XV and XVI of our Medicare Part B contract. BCBSCO respectfully disagrees with the findings and does not accept the recommendation.

#### RECOMMENDATION:

We recommend that the final administrative cost proposals be reduced by \$141,554. The recommended adjustments by fiscal year are shown in Appendix A.

#### RESPONSE:

The findings and resulting recommendation pertain to the auditors determination that BCBSCO claimed \$141,554 in "excess executive compensation" for FY 1990 through FY 1993. The auditors used the Department of Labor's Employment Cost Index (ECI) to calculate what they determined to be excessive executive compensation. The difference between certain executives actual salary increases and the ECI were determined by the auditors to be in excess of reasonable costs.

BCBSCO's initial response to this finding was set forth in a memorandum dated September 13, 1996 from Tom Gillgannon, Director, Government Operations to Mr. Terry Eddleman, Department of Health and Human Services, Office of Audit Services. The September 13, 1996 memorandum is resubmitted with this letter as Attachment 1, to be made part of our official response to the audit findings and recommendation pertaining to "excess executive compensation." BCBSCO respectfully disagrees with the findings and does not accept the recommendation.

The Medicare Part B contract and the FAR do not refer to the Department of Labor's ECI or use of the ECI as a limit in the amount of salary increases for executive staff. The language within the Medicare Part B contract and the FAR does not provide authority to exclusively employ the ECI to determine executive compensation increases. The FAR, Section 31.205-6, paragraph a.3, specifically states that "compensation must be based on and conform to the terms and conditions of the contractor's established compensation plan or practice followed so consistently as to imply, in effect, an agreement to make the payment." We believe BCBSCO's method for allocating executive costs is both reasonable and allowable.

Barbara A. Bennett  
December 16, 1996  
Page 4

RECOMMENDATION:

We recommend that the final administrative cost proposals be reduced by \$116,980. The recommended adjustments by fiscal year are shown in Appendix A.

RESPONSE:

The findings and resulting recommendation pertain to the auditors disallowance of \$16,980 in occupancy costs charged to Medicare based on Paragraph (b) of the FAR, Section 31.205-1.3, which states in part that, "losses from operating food and dormitory services may be included as costs only if the contractor's objective is to operate such services on a break-even basis." BCBSCO respectfully disagrees with the findings and does not accept the recommendation.

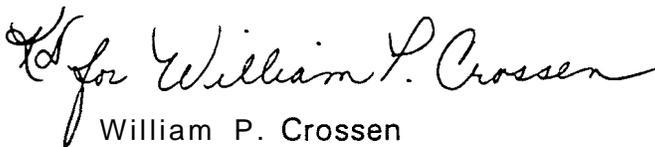
BCBSCO initially responded to this issue as a fact sheet finding, cafeteria cost, in a memorandum dated May 28, 1996 from Troy Stauber, BCBSCO Cost/Budget, to Mr. Phillip Wells, HHS-OIG-OAS. BCBSCO is resubmitting its May 28, 1996 memorandum as Attachment 2 to this letter as our official response to the cafeteria findings and recommendation. We believe BCBSCO's method for allocating cafeteria costs is both reasonable and allowable.

It is BCBSCO's intent to negotiate a final settlement with the HCFA upon completion of the outstanding audits for Medicare Part B termination costs and pension costs.

Thank you for the opportunity to review and comment on the draft audit report. I apologize for the unavoidable delay in responding to you earlier.

If you have any questions, please contact Troy Stauber at (303) 831-2205.

Sincerely,



William P. Crossen  
Chief Financial Officer

Attachments (2)

cc: Thomas J. Gillgannon  
Troy Stauber

Phillip Wells - Denver Regional Office  
Terry Eddleman - Kansas City Regional Office

700 Broadway  
Denver, Colorado 80273



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**M E M O R A N D U M**

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**TO:** Mr. Terry Eddleman  
Department of Health & Human Services  
Office of Audit Services

**FROM:** Tom Gillgannon  
Director, Government Operations

**DATE:** September 13, 1996

**SUBJECT:** BCBSCO Response to 2 Fact Sheet Findings  
Medicare B Contract

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Enclosed are the responses to the Audit Fact Sheet findings on:

- 1). Costs exceeding NOBA
- 2). Executive Compensation

If there are any questions, please contact me at (303) 831-2788 or Troy Stauber at (303) 831-2205.

Sincerely,

A handwritten signature in black ink that reads 'Tom Gillgannon' followed by a checkmark and the word 'for'.

Tom Gillgannon  
Director, Government Operations

Contractor: BCBS Colorado, #0550  
Medicare B Audit  
FY '90 thru FY '95

Response to:  
Fact Sheet on Costs in Excess of **NOBA**

1. BCBSCO has responded to this issue with many lengthy memos to the HHS/OIG Medicare B Audit explaining the actual steps in the Budget/NOBA process. The language in the fact sheet continues to ignore the information that has been provided during the audit.

2. HCFA does not negotiate the amount of the NOBA with the contractor. A Budget Request is submitted to HCFA several months prior to the start of the upcoming fiscal year. An initial, full-year NOBA is never issued until after the start of the new fiscal year. Often, the initial, full-year NOBA is received after the first quarter of the fiscal year has been completed.

HCFA does not hold discussions on the amount of the NOBA. The NOBA is predicated by the funding available for the entire region, Region VIII in this instance. These limited funds are distributed to the contractors within the region. Other than the submission of the Budget Request, the amount of funding is determined solely by HCFA.

3. The only avenue open to the contractor to change the amount of the NOBA is through the Supplemental Budget Request process. Again, there are no negotiations. The contractor submits a request and HCFA either approves or disapproves the supplemental request. BCBSCO submitted many supplemental budget requests during the audit period to address shortfalls in the NOBA.

4. As explained in the many memos to the HHS/OIG Medicare B Audit, the contractor is not allowed to submit costs in excess of NOBA within the IER/FACP process. HCFA will literally not accept an FACP that is higher than the NOBA. In addition, HCFA imposes performance penalties on the contractor if the FACP is submitted higher than the NOBA. Given the above environment, the contractor has no other possible avenue other than to submit costs at NOBA.

The argument used in the fact sheet is misleading and ignores the evidence provided during the audit. BCBSCO submitted FACP fully allocated costs from the SNAP system after contract termination because this was the only time that it could be done. When HCFA doesn't accept fully allocated costs and penalizes the contractor for attempting to do so, the fact sheet cannot imply that the contractor was somehow lax in filing fully allocated costs.

5. Article XV, paragraph A, of the Medicare B Contract states that the contractor shall be paid for the costs incurred (i.e., cost of administration) for the functions performed under the contract and that the principle of neither profit nor loss is applied. The refiled fully allocated and allowable costs represents the costs incurred to administer the Medicare B Contract and does not

**Contractor:** BCBS Colorado, #0550  
Medicare B Audit  
FY '90 thru FY '95

Response to:  
Fact Sheet on Costs in Excess of **NOBA**

include any new costs or profit items. The contract paragraph clearly states that the Medicare B Contract is a cost reimbursement arrangement.

Article XVI, paragraph G.2, of the Medicare B Contract states that the contractor has the right to claim costs in excess of the NOBA amount and that this claim of excess costs shall not be held in prejudice against the contractor.

Article XVI, paragraph I, of the Medicare B Contract states that if the costs incurred are determined to be allowable upon final settlement and if these allowable costs exceed the NOBA, then the HHS Secretary shall pay them. Since the audit process involves final settlement, BCBSCO's filing of actual, fully allocated and allowable costs incurred is appropriate at this time and juncture of the process.

Contractor: BCBS Colorado, #0550  
Medicare B Audit  
FY '90 thru FY '95

Response to:  
Fact Sheet on Executive Compensation

1. The Medicare B Contract and the FARs do not refer to the Department of Labor's ECI nor to using the ECI as a limit in the amount of salary increase for executive staff. The language within the Contract/FAR does not provide authority to exclusively employ the ECI index to determine executive compensation increases or even to determine regular employee compensation increases.

The FARs and the Medicare B contract do not even discuss the level of executive compensation increases nor the resulting allocations of executive compensation. The fact sheet finding is unprecedented and has no basis within the language of the FARs and the Medicare B Contract.

FAR, Section 3 1.205-6, paragraph a.3 specifically states "that compensation must be based upon and conform to the terms & conditions of the contractor's established compensation plan or practice followed so consistently as to imply, in effect, an agreement to make the payment."

2. Executive compensation is determined by BCBSCO corporate policy that is established and administered by the Human Resources department. BCBSCO's HR department utilizes data from the health care/insurance industry and various nationally based surveys in establishing executive compensation levels. This process assures that BCBSCO will be able to compete for the leadership talent required to develop & execute the corporate strategy. BCBSCO has followed an established policy over the audit years and has not changed its policy that would result in changes to the allocation of expenses.

3. This particular issue came up in an limited audit specifically reviewing executive compensation and was completed in June 1994. Even though it was requested, BCBSCO did not receive any written findings from this June 1994 audit nor could the auditors provide a copy of the Department of Labor's ECI nor could the audit provide an explanation of the basis for the ECI. In fact, the recently received fact sheet is the first time BCBSCO has seen this issue as an official finding.

4. BCBSCO does not believe that a "standard" (i.e., the ECI) can be suddenly imposed on the contractor at the end of the contract period nor be expected to be held to a standard the contractor knew nothing about. The rules & regulations that the contractor must perform to are established in the Medicare B Contract. In Article XV of the Medicare B Contract, allowable costs incurred in the performance of the contract are payable to the carrier and allowable costs are determined by FAR, Section 3 1. As noted above, paragraph a.3 of Section 3 1.205-6 states that compensation

Contractor: BCBS Colorado, #0550  
Medicare B Audit  
FY '90 thru FY '95

Response to:  
Fact Sheet on Executive Compensation

must be based on the contractor's established compensation plan. There is no mention of limiting increases to the ECI.

The audit cannot expect to hold BCBSCO to a standard that is not being formally imposed on other contractors nor is part of the contract, guidelines and manuals that the contractors utilize in determining the allocation process and the reporting of costs on the IER/FACP. The issue of executive compensation increases and the ECI appears to come up only during contractor audits and is not part of the dialogue between the contractor and HCFA.

5. The ECI does not reflect regional nor industry specific information. The ECI is based on an average increase from businesses across the U.S. The executive compensation increases arrived at BCBSCO are based on local market conditions and insurance industry trends. In some instances, executive increases are a result of expanding areas of responsibility. In other cases, new staff is brought in due to turnover or newly created functions within the corporation.

During this time period there was considerable turnover and restructuring of the executive staff. The audit does not take into consideration that new executives were replaced externally and that this turnover would contribute to the 15.5% increase referenced in the fact sheet. The analysis of the audit has not taken this into consideration nor has the audit considered any promotions to executive level status.

6. BCBSCO does not believe that the executive compensation increases are unreasonable. BCBSCO has complied fully with the language of the FAR and that the executive compensation increases are reasonable and therefore the resulting allocations are allowable.

700 Broadway  
Denver, Colorado 80273



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## MEMORANDUM

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TO: Phillip Wells  
HBS-OIG-OAS

FROM: Troy Stauber  
BCBSCO Cost/Budget

DATE: May 28, 1996

SUBJECT: Fact Sheet, Cafeteria Costs

REF : OIG memo, 5/13/96, Request for Response

*This memo is for:*      ACTION      DECISION      INFORMATION

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In response to the OIG memo:

A. FAR 31.205-13:

1. Paragraph a), FAR 31.205-13:

- Paragraph a) specifically states that aggregate costs are allowable after income generated by these activities have been applied **against** collected costs. Account 6325, CC 3235, does indeed apply income from vending machine sales to collected costs. As an example, in CY 1993 CC 3235 shows 5% of the cost center expense Total being in the form of revenues from **vending** machine sales.

Vending machine sales are not the only income generated in the agreement between BCBSCO and Canteen. An agreement exists that revenues from cafeteria sales will be shared between **BCBSCO** and Canteen if certain thresholds are met. Had Canteen met the thresholds laid out in the contract, then Medicare B would have received less allocated costs from CC 3235 (i.e. Medicare would share in the revenues BCBSCO obtained). The thresholds were not met, however, the potential still existed and the FAR does not disallow the expense as a result of not meeting thresholds.

- Except for food & dormitory services, the other examples of allowable costs listed in paragraph a) do not generate income or revenues. House publications, recreation & counseling services are not going to be operated on a revenue generating situation; the allowable cost examples in the FAR will be an expense only situation. By including these expense only examples in the paragraph, the **FAR's** intent must allow for expense only situation

as found in CC 3235.

In summary, CC 3235 is an expense only situation as described in paragraph a) and BCBSCO has complied with the FAR by netting any income (i.e. vending sales) **against any** expense. BCBSCO has fully complied with paragraph a) of FAR 31.205-13.

2. Paragraph b), FAR 31.205-13:

- The costs represented in CC 3235, Cafeteria, are not losses as discussed in FAR 31.205-13, paragraph b) and Appendix B, Section V of the Medicare B Contract. The losses discussed in paragraph b) are accounting losses **as** determined by the net income/loss line on the income statement. If BCBSCO was operating a food/dormitory service, losses would be defined only when the following variables were taken into account:

sales generated less cost of goods sold less variable overhead expense less fixed costs less income taxes paid.

- The intent of paragraph b) is quite different than the situation shown in CC 3235. Paragraph b)'s intent is to prevent the US Government from directly subsidizing food for the contractor's employees at taxpayer expense or adding to the profit line of a contractor's food/dormitory service. This situation described in paragraph b) does apply to CC 3235.

The audit finding tries to impose the intent of paragraph b) to a different situation and arrangement found in CC 3235 and between BCBSCO and Canteen Corporation. BCBSCO is not operating a food service and therefore losses mentioned in paragraph b) are not the same as the administrative expense found in CC 3235. BCBSCO believes the argument made in the Fact Sheet mixes 2 completely different accounting concepts with an operating situation that just doesn't exist.

- Paragraph b) also refers to losses resulting from operating a food service or dormitory service because the service is given away for free, without charge or at very low prices (i.e., low prices are inferred in the FAR language). The situation would only apply if a contractor operated a food service cafeteria and then proceeded to give the food away for free to its employees thereby creating a loss. This is not the situation that describes CC 3235.

BCBSCO is not giving away floor space to Canteen Corporation without charge and thereby creating a loss. The agreement calls for BCBSCO to provide space for Canteen to operate a cafeteria **in** exchange for sharing in revenues.

BCBSCO may have been able at the time of the agreement to settle for a rent payment for the space from the Canteen Corporation. However, the upside potential to share in revenues was probably much greater than receiving a static monthly rent payment. In

retrospection, the static rent payment would have been more secure, however, retrospection doesn't make the expense suddenly non-allowable.

Just because those expectations have not materialized does not mean that the situation in CC 3235 is described by paragraph b). BCBSO believes that the audit finding is ignoring the actual relationship and is forcing paragraph b) to fit an argument for non-allowableness.

B. Summary:

1. The intent of FAR 31.205-13:

BCBSO believes the intent and spirit of FAR 31.205-13 and Appendix B, Section V allows costs associated with the cafeteria as a result of providing an improved working **atmosphère** and builds upon employee performance by providing a convenient place to obtain food. Non-exempt employees with lunch breaks of 1/2 hour would find an on-site cafeteria a benefit. Employees who prefer to utilize the cafeteria to avoid the costs of traveling to a restaurant and the usually higher food costs at such establishments would find the on-site cafeteria a benefit. In times of inclement weather, the on-site cafeteria would provide a benefit to all BCBSO employees, including those who prefer to eat off-site.

BCBSO believes that intent of FAR 31.205-13 is to allow for such expenses for activities that provide a benefit to the employee population. The cafeteria concept falls easily within this concept and has been specifically listed as an example of allowable expense within the FAR and Appendix B. BCBSO believes that the on-site cafeteria leads to improved working conditions, better and stronger relationships between employees and BCBSO and supports a stronger performance from its employees. BCBSO believes it fully meets the intent and spirit of FAR 31.205-13.

2. The Audit Findings:

The entire audit finding and resulting Fact Sheet conclusion for costs being non-allowable is based on a narrow view and interpretation of FAR 31.205-13 and does not take the FAR in its entirety.

In order to arrive at the Fact Sheet conclusions, BCBSO would have to be the operator of a food/dormitory service. BCBSO is not currently operating nor has operated a food/dormitory service during the audit period. The operator of the "cafeteria" is Canteen Corporation.

BCBSO has entered into a contract with Canteen Corporation. That contract provides for BCBSO to supply space for Canteen Corporation to operate a cafeteria. In exchange for space, BCBSO has the opportunity to share in revenues. BCBSO has simply

substituted a monthly rent payment for an opportunity to share in revenues generated by **Canteen**. Had such revenue sharing materialized, the Medicare **B** LOB would have received a portion of that revenue in the allocation of CC 3235.

The audit finding is mixing terminology that incorrectly associates administrative expense with accounting losses, implies that expenses from CC 3235 are operating losses and incorrectly describes the nature of **BCBSCO's** role. The FAR discusses a specific operating situation that does not apply to the situation entered into between BCBSCO and the Canteen Corporation.

BCBSCO disagrees with the conclusions drawn and firmly believes that the expenses allocated in CC 3235 are allowable.