

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF PENSION COSTS
CLAIMED FOR MEDICARE
REIMBURSEMENT BY ARKANSAS
BLUE CROSS AND BLUE SHIELD**



JUNE GIBBS BROWN
Inspector General

SEPTEMBER 1998
A-07-98-02525



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-07-98-02525

SEP 3 1998

Mr. Charles Clem
Vice President, Public Programs
Arkansas Blue Cross and Blue Shield
601 Gaines Street
Little Rock, Arkansas 72201

Dear Mr. Clem:

This report provides the results of an Office of Inspector General (OIG), Office of Audit Services (OAS) review titled *Review of Pension Costs Claimed for Medicare Reimbursement by Arkansas Blue Cross and Blue Shield*. The purpose of our review was to determine the allowability of pension costs claimed for Medicare reimbursement for Fiscal Years 1991 through 1996.

We determined that Arkansas Blue Cross and Blue Shield (Arkansas) underclaimed allowable Medicare pension costs for 1991 through 1996. During this period, the allowable Medicare pension costs were \$4,851,502. However, Arkansas claimed pension costs of \$3,094,560 for Medicare reimbursement. As a result, Arkansas did not claim \$1,756,942 of allowable pension costs. The underclaim occurred primarily because Arkansas did not base its claim on separately computed Cost Accounting Standards (CAS) pension costs for the Medicare segment.

We are recommending Arkansas revise its Final Administrative Cost Proposals (FACPs) to reflect the remaining allowable pension costs.

Arkansas concurred with our finding and recommendation. Their response to our draft audit report is included in its entirety as Appendix B.

INTRODUCTION

BACKGROUND

Arkansas has administered Medicare Parts A and B operations under cost reimbursement contracts since 1966. Medicare contractors must follow cost reimbursement principles contained in the CAS, the Federal Acquisition Regulations (FAR), and their Medicare contracts.

Since its inception, Medicare has reimbursed a portion of annual contributions paid into contractors' pension plans. To be allowable 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 consistent measurement and assignment of pension costs to contract periods. The CAS costs that are allowable as charges to Medicare include (1) the normal cost and (2) the amortization of the unfunded actuarial liability.

The FAR addresses allowability of pension costs and requires that pension costs assigned to contract periods be substantiated by funding.

In addition to CAS and FAR requirements, the Health Care Financing Administration (HCFA), starting with Fiscal Year 1988, incorporated specific segmentation language into Medicare contracts. To implement segmentation requirements, contracts stipulated procedures for identifying the Medicare segment and assigning pension assets to the segment.

Furthermore, the contracts required a separate calculation of pension costs for a segment if such a calculation (versus an allocation) materially affected pension costs charged to Medicare. Under a separate calculation method, a contractor identifies separately the normal costs and amortization for the Medicare segment. Under an allocation method, a contractor determines total plan CAS costs and allocates a share to Medicare. This allocation includes direct and indirect costs.

SCOPE

We made our examination in accordance with generally accepted government auditing standards. Our objective was to identify allowable CAS pension costs for Fiscal Years 1991 through 1996. Achieving the objective did not require a review of Arkansas' internal control structure.

This review was done in conjunction with our audits of pension segmentation (CIN: A-07-98-02524) and unfunded pension costs (CIN: A-07-98-02526). The information obtained and reviewed during those audits was also used in performing this review.

In performing the review, we used information provided by Hewitt Associates, Arkansas' consulting actuary. The information included liabilities, normal costs, contributions, and earnings. We reviewed Arkansas' accounting records, pension plan documents, annual actuarial valuation reports, and the Department of Labor/Internal Revenue Service Form 5500s. Using these documents, we computed CAS pension costs for the total company and the Medicare segment.

The HCFA Office of the Actuary developed the methodology used for computing allowable CAS pension costs based on Arkansas' historical practices. Appendix A contains the details of the CAS cost calculations.

We performed site work at Arkansas' corporate offices in Little Rock, Arkansas during March and April 1998. Subsequently, we performed audit work in our Jefferson City, Missouri office.

FINDING AND RECOMMENDATION

For Fiscal Years 1991 through 1996, Arkansas did not claim \$1,756,942 for pension costs which were allowable for Medicare reimbursement. The pension costs were allowable because the funded portion of CAS computed costs exceeded the costs claimed. The under claim occurred primarily because Arkansas did not base their claim on separately computed CAS pension costs for the Medicare segment. Arkansas should revise its FACPs to reflect the additional CAS pension costs which were allowable for reimbursement.

For years 1991 through 1996, Arkansas claimed pension costs for Medicare reimbursement on FACPs. Arkansas based its claims on an allocation of the total company pension cost, calculated in accordance with Financial Accounting Standard #87 (FAS 87). Arkansas assigned a portion of the FAS 87 pension costs to Medicare direct and indirect operations using cost center and line of business information.

We calculated the allowable CAS pension costs for the Medicare segment and for indirect Medicare operations. The calculations were based on separately computed CAS pension costs for the Medicare segment and total company CAS pension costs. See Appendix A for details.

We compared the allowable CAS pension costs to the pension costs claimed on Arkansas' FACPs and found:

<u>Fiscal Year</u>	<u>Allowable CAS Costs</u> (A)	<u>Costs Claimed</u> (B)	<u>Under (Over) Claim</u> (A)-(B)
1991	\$546,868	\$28,706	\$518,162
1992	\$718,370	\$764,500	(\$46,130)
1993	\$813,263	\$538,231	\$275,032
1994	\$843,671	\$423,610	\$420,061
1995	\$934,811	\$536,849	\$397,962
1996	\$994,519	\$802,664	\$191,855
Total	<u>\$4,851,502</u>	<u>\$3,094,560</u>	<u>\$1,756,942</u>

For 1991 through 1996, Arkansas claimed pension costs of \$3,094,560 for Medicare reimbursement. However, the allowable CAS pension costs were \$4,851,502. As a result, Arkansas could have claimed \$1,756,942 in additional CAS pension costs.

Recommendation

We recommend that Arkansas:

Revise its FACPs to claim additional allowable CAS pension costs of \$1,756,942.

Auditee Response

Arkansas concurred with our finding and recommendation. Their response to our draft audit report is included in its entirety as Appendix B.

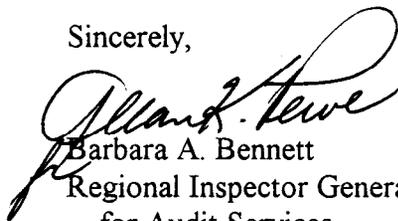
INSTRUCTIONS FOR AUDITEE RESPONSE

Final determinations as to actions to be taken on all matters reported will be made by the HHS action official identified on the following page. We request that you respond to the recommendation 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.

Page 5 - Mr. Charles Clem

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

Enclosure
HHS Action Official
Dr. James Farris
Regional Administrator, Region VI
Health Care Financing Administration
1301 Young Street, Room 714
Dallas, Texas 75204

ARKANSAS BLUE CROSS AND BLUE SHIELD
CIN: A-07-98-02525

STATEMENT OF ALLOWABLE CAS PENSION COSTS

FOR FISCAL YEARS 1991 THROUGH 1996

<u>Plan Year</u>	<u>Description</u>		<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare Segment</u>
1990	Plan Year Contributions	<u>1/</u>	\$0	\$0	\$0
	Discount for Interest	<u>2/</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>
	Present Value of Contributions	<u>3/</u>	\$0	\$0	\$0
	Prepayment Credit	<u>4/</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>
	Present Value of Funding	<u>5/</u>	\$0	\$0	\$0
	Normal Cost	<u>6/</u>	\$914,648	\$701,475	\$213,173
	Amortization Payment	<u>7/</u>	<u>\$144,999</u>	<u>\$67,602</u>	<u>\$77,397</u>
	CAS Pension Costs	<u>8/</u>	\$1,059,647	\$769,077	\$290,570
	Funded CAS Pension Costs	<u>9/</u>	\$0	\$0	\$0
	Allowable Interest	<u>10/</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>
	Allocable Pension Costs	<u>11/</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

ARKANSAS BLUE CROSS AND BLUE SHIELD
CIN: A-07-98-02525

STATEMENT OF ALLOWABLE CAS PENSION COSTS

FOR FISCAL YEARS 1991 THROUGH 1996

<u>Plan Year</u>	<u>Description</u>	<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare Segment</u>
1991	Plan Year Contributions	\$2,000,000	\$1,352,468	\$647,532
	Discount for Interest	<u>(\$165,138)</u>	<u>(\$111,672)</u>	<u>(\$53,466)</u>
	Present Value of Contributions	\$1,834,862	\$1,240,796	\$594,066
	Prepayment Credit	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>
	Present Value of Funding	\$1,834,862	\$1,240,796	\$594,066
	Normal Cost	\$1,333,042	\$881,809	\$451,233
	Amortization Payment	<u>\$181,886</u>	<u>\$39,053</u>	<u>\$142,833</u>
	CAS Pension Costs	\$1,514,928	\$920,862	\$594,066
	Funded CAS Pension Costs	\$1,514,928	\$920,862	\$594,066
	Allowable Interest	<u>\$96,577</u>	<u>\$58,705</u>	<u>\$37,872</u>
	Allocable Pension Costs	\$1,611,505	\$979,567	\$631,938
	Fiscal Year Pension Costs	<u>12/ \$1,208,629</u>	\$734,675	\$473,954
	Medicare LOB Percentage	<u>13/</u>	<u>16.75%</u>	<u>89.42%</u>
	Allowable Medicare Pension Costs	<u>14/ \$546,868</u>	<u>\$123,058</u>	<u>\$423,810</u>

ARKANSAS BLUE CROSS AND BLUE SHIELD
CIN: A-07-98-02525

STATEMENT OF ALLOWABLE CAS PENSION COSTS

FOR FISCAL YEARS 1991 THROUGH 1996

<u>Plan Year</u>	<u>Description</u>	<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare Segment</u>
1992	Plan Year Contributions	\$2,271,018	\$1,681,023	\$589,995
	Discount for Interest	<u>(\$115,828)</u>	<u>(\$85,737)</u>	<u>(\$30,091)</u>
	Present Value of Contributions	\$2,155,190	\$1,595,286	\$559,904
	Prepayment Credit	<u>\$348,728</u>	<u>\$208,617</u>	<u>\$140,111</u>
	Present Value of Funding	\$2,503,918	\$1,803,903	\$700,015
	Normal Cost	\$1,518,078	\$950,684	\$567,394
	Amortization Payment	<u>\$224,216</u>	<u>\$91,595</u>	<u>\$132,621</u>
	CAS Pension Costs	\$1,742,294	\$1,042,279	\$700,015
	Funded CAS Pension Costs	\$1,742,294	\$1,042,279	\$700,015
	Allowable Interest	<u>\$93,637</u>	<u>\$56,016</u>	<u>\$37,621</u>
	Allocable Pension Costs	\$1,835,931	\$1,098,295	\$737,636
	Fiscal Year Pension Costs	\$1,779,825	\$1,068,613	\$711,212
	Medicare LOB Percentage		<u>12.43%</u>	<u>82.33%</u>
	Allowable Medicare Pension Costs	<u>\$718,370</u>	<u>\$132,829</u>	<u>\$585,541</u>

ARKANSAS BLUE CROSS AND BLUE SHIELD
CIN: A-07-98-02525

STATEMENT OF ALLOWABLE CAS PENSION COSTS

FOR FISCAL YEARS 1991 THROUGH 1996

<u>Plan Year</u>	<u>Description</u>	<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare Segment</u>
1993	Plan Year Contributions	\$3,219,582	\$2,714,895	\$504,687
	Discount for Interest	<u>(\$167,037)</u>	<u>(\$140,853)</u>	<u>(\$26,184)</u>
	Present Value of Contributions	\$3,052,545	\$2,574,042	\$478,503
	Prepayment Credit	<u>\$830,170</u>	<u>\$530,247</u>	<u>\$299,923</u>
	Present Value of Funding	\$3,882,715	\$3,104,289	\$778,426
	Normal Cost	\$1,682,855	\$1,090,865	\$591,990
	Amortization Payment	<u>\$471,788</u>	<u>\$285,352</u>	<u>\$186,436</u>
	CAS Pension Costs	\$2,154,643	\$1,376,217	\$778,426
	Funded CAS Pension Costs	\$2,154,643	\$1,376,217	\$778,426
	Allowable Interest	<u>\$117,903</u>	<u>\$75,307</u>	<u>\$42,596</u>
	Allocable Pension Costs	\$2,272,546	\$1,451,524	\$821,022
	Fiscal Year Pension Costs	\$2,163,393	\$1,363,217	\$800,176
	Medicare LOB Percentage		<u>12.23%</u>	<u>80.80%</u>
	Allowable Medicare Pension Costs	<u>\$813,263</u>	<u>\$166,721</u>	<u>\$646,542</u>

ARKANSAS BLUE CROSS AND BLUE SHIELD
CIN: A-07-98-02525

STATEMENT OF ALLOWABLE CAS PENSION COSTS

FOR FISCAL YEARS 1991 THROUGH 1996

<u>Plan Year</u>	<u>Description</u>	<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare Segment</u>
1994	Plan Year Contributions	\$3,363,779	\$3,198,655	\$165,124
	Discount for Interest	<u>(\$171,254)</u>	<u>(\$162,848)</u>	<u>(\$8,406)</u>
	Present Value of Contributions	\$3,192,525	\$3,035,807	\$156,718
	Prepayment Credit	<u>\$1,866,319</u>	<u>\$1,121,436</u>	<u>\$744,883</u>
	Present Value of Funding	\$5,058,844	\$4,157,243	\$901,601
	Normal Cost	\$1,751,944	\$1,089,612	\$662,332
	Amortization Payment	<u>\$507,033</u>	<u>\$267,765</u>	<u>\$239,268</u>
	CAS Pension Costs	\$2,258,977	\$1,357,377	\$901,600
	Funded CAS Pension Costs	\$2,258,977	\$1,357,377	\$901,600
	Allowable Interest	<u>\$121,173</u>	<u>\$72,813</u>	<u>\$48,360</u>
	Allocable Pension Costs	\$2,380,150	\$1,430,190	\$949,960
	Fiscal Year Pension Costs	\$2,353,250	\$1,435,524	\$917,726
	Medicare LOB Percentage		<u>7.64%</u>	<u>79.98%</u>
	Allowable Medicare Pension Costs	<u>\$843,671</u>	<u>\$109,674</u>	<u>\$733,997</u>

ARKANSAS BLUE CROSS AND BLUE SHIELD
CIN: A-07-98-02525

STATEMENT OF ALLOWABLE CAS PENSION COSTS

FOR FISCAL YEARS 1991 THROUGH 1996

<u>Plan Year</u>	<u>Description</u>	<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare Segment</u>
1995	Plan Year Contributions	\$3,998,592	\$3,998,592	\$0
	Discount for Interest	<u>(\$208,400)</u>	<u>(\$208,400)</u>	<u>\$0</u>
	Present Value of Contributions	\$3,790,192	\$3,790,192	\$0
	Prepayment Credit	<u>\$2,744,062</u>	<u>\$1,791,294</u>	<u>\$952,768</u>
	Present Value of Funding	\$6,534,254	\$5,581,486	\$952,768
	Normal Cost	\$1,990,899	\$1,343,408	\$647,491
	Amortization_Payment	<u>\$753,163</u>	<u>\$447,886</u>	<u>\$305,277</u>
	CAS Pension Costs	\$2,744,062	\$1,791,294	\$952,768
	Funded CAS Pension Costs	\$2,744,062	\$1,791,294	\$952,768
	Allowable Interest	<u>\$98,493</u>	<u>\$98,493</u>	<u>\$0</u>
	Allocable Pension Costs	\$2,842,555	\$1,889,787	\$952,768
	Fiscal Year Pension Costs	\$2,726,954	\$1,774,888	\$952,066
	Medicare LOB Percentage		<u>7.31%</u>	<u>84.56%</u>
	Allowable Medicare Pension Costs	<u>\$934,811</u>	<u>\$129,744</u>	<u>\$805,067</u>

ARKANSAS BLUE CROSS AND BLUE SHIELD
CIN: A-07-98-02525

STATEMENT OF ALLOWABLE CAS PENSION COSTS

FOR FISCAL YEARS 1991 THROUGH 1996

<u>Plan Year</u>	<u>Description</u>	<u>Total Plan</u>	<u>Other Segment</u>	<u>Medicare Segment</u>
1996	Plan Year Contributions	\$4,792,258	\$4,792,258	\$0
	Discount for Interest	<u>(\$250,759)</u>	<u>(\$250,759)</u>	<u>\$0</u>
	Present Value of Contributions	\$4,541,499	\$4,541,499	\$0
	Prepayment Credit	<u>\$3,262,557</u>	<u>\$2,278,386</u>	<u>\$984,171</u>
	Present Value of Funding	\$7,804,056	\$6,819,885	\$984,171
	Normal Cost	\$2,296,763	\$1,684,774	\$611,989
	Amortization Payment	<u>\$965,794</u>	<u>\$593,612</u>	<u>\$372,182</u>
	CAS Pension Costs	\$3,262,557	\$2,278,386	\$984,171
	Funded CAS Pension Costs	\$3,262,557	\$2,278,386	\$984,171
	Allowable Interest	<u>\$125,801</u>	<u>\$125,801</u>	<u>\$0</u>
	Allocable Pension Costs	\$3,388,358	\$2,404,187	\$984,171
	Fiscal Year Pension Costs	\$3,251,907	\$2,275,587	\$976,320
	Medicare LOB Percentage		<u>4.97%</u>	<u>90.28%</u>
	Allowable Medicare Pension Costs	<u>\$994,519</u>	<u>\$113,097</u>	<u>\$881,422</u>

ARKANSAS BLUE CROSS AND BLUE SHIELD
CIN: A-07-98-02525

STATEMENT OF ALLOWABLE CAS PENSION COSTS

*FOR FISCAL YEARS 1991 THROUGH 1996*FOOTNOTES

- 1/ We assigned contributions to the Medicare segment based on a ratio of the Medicare segment's CAS funding target to the total company CAS funding target. The amount shown for the "other segment" represents the difference between the total company and the Medicare segment. If contributions exceeded the amount required to fund the CAS funding target, the excess contributions were assigned to the "other segment" as an unallocated prepayment credit (see footnote 4/).
- 2/ We subtracted interest that was included in the contributions deposited after January 1 of each year to discount the contributions back to their value at the beginning of the year. For purposes of this appendix, we computed the interest as the difference between the present value of contributions at the valuation interest rates, and the actual contribution amounts.
- 3/ The present value of contributions is the value of the contributions discounted from the date of deposit back to January 1. For purposes of this appendix, we deemed deposits made after the end of the plan year to have been made on the final day of the plan year.
- 4/ We applied the prepayment credits toward the funding of the CAS pension costs. The prepayment credit represents the premature funding from the previous year(s). Prepayment credits may be carried forward, with interest, to fund future CAS pension costs. The prepayment credits are reimbursable for the plan year in which they are used to fund the CAS pension costs.
- 5/ The present value of funding represents the present value of contributions plus prepayment credits. This is the amount of funding that was available to cover the CAS funding target measured at January 1 of each year.
- 6/ We obtained the normal cost for the total company, and for the Medicare segment, from data files provided by Arkansas' consulting actuary.
- 7/ We based the amortization payment on a CAS amortization schedule developed from information obtained from Arkansas' valuation reports and IRS Form 5500 reports.
- 8/ The CAS pension costs represents the sum of the amortization payment and the normal cost. We separately calculated CAS pension costs for years 1990 through 1996.

ARKANSAS BLUE CROSS AND BLUE SHIELD
CIN: A-07-98-02525

STATEMENT OF ALLOWABLE CAS PENSION COSTS

FOR FISCAL YEARS 1991 THROUGH 1996

- 9/ The CAS pension cost for the qualified plan must be funded by current or prepaid contributions to satisfy the funding requirement of FAR 31.205-6(j)(3)(i). Only the funded CAS pension costs of the qualified plan are eligible for Medicare reimbursement.
- 10/ We assumed interest on the funded CAS pension cost accrues in the same proportion as the interest on contributions bears to the present value of funding. However, we limited interest by FAR 31.205-6(j)(3)(iii) which does not permit the allowable interest to exceed the interest that would accrue if the CAS funding target were funded in four equal installments deposited within 30 days of the end of each quarter. The allowable interest was \$0 in those instance where the entire CAS funding target was funded by prepayment credits.
- 11/ The allocable CAS pension costs are the amount of pension costs for the qualified plan which may be allocated for contract cost purposes, on a plan year basis.
- 12/ We converted CAS pension costs allocable to the plan year to a fiscal year basis (October 1 through September 30). Costs charged to the Medicare contract should consist of the Medicare segment's pension costs plus an allocable portion of the other segment's pension costs attributable to indirect Medicare operations.
- 13/ We calculated allowable plan pension costs for Medicare and other segments based on the Medicare line of business (LOB) percentage of the segments. We obtained the percentages from documents provided by Arkansas.
- 14/ The Medicare pension costs are the amounts of CAS pension costs which may be claimed for Medicare reimbursement for the segment and indirect Medicare operations.



Arkansas
BlueCross BlueShield

601 S. Gaines St.
P.O. Box 2181
Little Rock, Arkansas 72203-2181

August 24, 1998

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

SUBJECT: CIN A -07-98-02524

Dear Ms. Bennett:

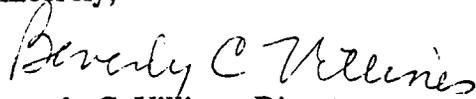
We are in receipt of the draft report of the recent reviews of our pension plan. We are in agreement with the recommendations presented and find them to properly reflect the results of actions discussed during the field work by your staff. We had previously used a rather strict definition for cost centers to include in the Medicare segment so the recommendation to decrease the value of assets assigned to the segment was expected. Further, we have forwarded to the HCFA Central Office all of the required documentation related to approval for reassignment of the unfunded pension costs, but, as you stated, this has not been finalized at this time.

These audit results have been sent on to our pension plan actuaries for their inclusion in valuation data associated with these time periods. Also, we will be working with our regional office on the cost reimbursement issues raised in the report titled "Review of Pension Costs Claimed for Medicare Reimbursement by Arkansas Blue Cross and Blue Shield".

Ms. Barbara A. Bennett
August 24, 1998
Page Two

I would like to express my thanks to your staff for the very cordial manner in which they conducted this audit. Please let me know what other actions are necessary at this time.

Sincerely,



Beverly C. Villines, Director
Corporate Accounting

cc: Charles Clem, Vice President, Public Programs
Steven Short, Vice President, Financial Services
David Greenwood, Government Programs Accounting
Sylvia Shaw, Human Resources Administration
Faye Deacon, Hewitt Associates