



DEPARTMENT OF HEALTH & HUMAN SERVICES

OFFICE OF INSPECTOR GENERAL

Office of Audit Services, Region IV
61 Forsyth Street, SW, Suite 3T41
Atlanta, GA 30303

April 29, 2011

Report Number: A-04-10-04005

Mr. Bruce W. Hughes
President & COO
Palmetto GBA
2300 Springdale Drive, Building One
Mail Code: AG-A03
Camden, SC 29020-1728

Dear Mr. Hughes:

Enclosed is the U.S. Department of Health & Human Services (HHS), Office of Inspector General (OIG), final report entitled *Audit of Palmetto Government Benefits Administrators' Medicare Part A Final Administrative Cost Proposals for Fiscal Years 2007 Through 2009*. We will forward a copy of this report to the HHS action official noted below.

Section 8L of the Inspector General Act, 5 U.S.C. App., requires that OIG post its publicly available reports on the OIG Web site. Accordingly, the report will be posted at <http://oig.hhs.gov>.

If you have any questions or comments about this report, please direct them to the HHS action official. Please refer to report number A-04-10-04005 in all correspondence.

Sincerely,

/Peter J. Barbera/
Regional Inspector General
for Audit Services

Enclosure

HHS Action Official:

Nanette Foster Reilly
Consortium Administrator
Consortium for Financial Management & Fee for Service Operations
Centers for Medicare & Medicaid Services
601 East 12th Street, Room 235
Kansas City, MO 64106

Department of Health & Human Services

**OFFICE OF
INSPECTOR GENERAL**

**AUDIT OF PALMETTO GOVERNMENT
BENEFITS ADMINISTRATORS' MEDICARE
PART A FINAL ADMINISTRATIVE
COST PROPOSALS FOR
FISCAL YEARS
2007 THROUGH 2009**



Daniel R. Levinson
Inspector General

April 2011
A-04-10-04005

Office of Inspector General

<http://oig.hhs.gov>

The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health & Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

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Notices

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Section 8L of the Inspector General Act, 5 U.S.C. App., requires that OIG post its publicly available reports on the OIG Web site.

OFFICE OF AUDIT SERVICES FINDINGS AND OPINIONS

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

INTRODUCTION

BACKGROUND

Title XVIII of the Social Security Act established the Health Insurance for the Aged and Disabled (Medicare) program, which provides for a hospital insurance program (Part A) and a related supplementary medical insurance program (Part B). The Centers for Medicare & Medicaid Services (CMS) administers the Medicare program through contracts with private organizations that process and pay Medicare claims.

The contracts with CMS provide for the reimbursement of allowable administrative costs incurred in processing Medicare claims. After the close of each fiscal year (FY), contractors submit a Final Administrative Cost Proposal (cost proposal) reporting Medicare costs. Once CMS accepts a cost proposal, the contractor and CMS negotiate a final settlement of allowable administrative costs.

During our audit period (FYs 2007 through 2009), CMS contracted with Palmetto Government Benefits Administrators (Palmetto) to serve as a Medicare contractor. Palmetto processed Part A claims for North Carolina and South Carolina and Regional Home Health Intermediary claims for Alabama, Arkansas, Florida, Georgia, Illinois, Indiana, Kentucky, Louisiana, Michigan, Mississippi, New Mexico, North Carolina, Ohio, Oklahoma, South Carolina, Tennessee, and Texas.

The contract between Palmetto and CMS set forth principles of reimbursement for administrative costs. The contract cited the Federal Acquisition Regulation (FAR) as the guiding regulatory principles for the Medicare contract and provided additional guidelines for specific cost areas.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to determine whether the administrative costs that Palmetto reported on its cost proposals were allowable, allocable, and reasonable in accordance with part 31 of the FAR and the Medicare contract.

Scope

Our audit covered the period October 1, 2006, through September 30, 2009 (FYs 2007 through 2009). For this period, Palmetto reported administrative costs to CMS totaling \$112,967,522. This total included pension costs of \$7,278,133 that will be the subject of a separate audit and, therefore, were excluded from this audit. We reviewed \$105,689,389 of administrative costs.

We limited our internal control review to controls related to the recording and reporting of costs on the cost proposals. We accomplished our objectives through substantive testing.

We conducted fieldwork at Palmetto's office in Columbia, South Carolina, from February through November 2010.

Methodology

To accomplish our objective, we:

- reviewed applicable Medicare laws, regulations, and guidelines, including the FAR section 31.201-2(d), the *Medicare Financial Management Manual*, chapter 2, section 190.3, and Palmetto's contract with CMS;
- interviewed Palmetto officials about their cost-accumulation processes for cost proposals and gained an understanding of their cost allocation systems;
- reconciled the cost proposals from FYs 2007 through 2009 to Palmetto's accounting records;
- performed analytical tests of Palmetto's general ledger;
- created a sampling frame of 21,499 employee pay periods totaling \$35,239,450 that included cost centers with total costs of \$100,000 or more and salaries of \$10,000 or more for FYs 2007 through 2009;
- selected a judgmental sample of 90 employee pay periods (30 from each FY) totaling \$175,640;
- verified that the amount paid was in accordance with the employee's pay rate, the salary was charged to the correct cost center, and the number of hours paid agreed with the time sheets for the 90 employee pay periods;
- reviewed payroll journals, corporate bonus plans, and personnel records;
- compared top executives' compensation to benchmark compensation amounts published in the Federal Register and tested for excessive compensation claimed;
- created a sampling frame totaling \$64,591,120 that consisted of cost classification line items other than salaries/wages and fringe benefits (i.e., nonsalary items) with total costs of \$1,000,000 or more for FYs 2007 through 2009;
- selected a judgmental sample of 90 nonsalary transactions (30 from each FY) totaling \$4,598,139; and
- tested the costs for allowability, allocability, and reasonableness.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient,

appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

RESULTS OF REVIEW

All of the \$105,689,389 in administrative costs that we reviewed for FYs 2007 through 2009 were allowable, allocable, and reasonable in accordance with the FAR and the Medicare contract. Consequently, this report contains no recommendations.

APPENDIX

**APPENDIX: FINAL ADMINISTRATIVE COST PROPOSALS WITH
RECOMMENDED COSTS FOR ACCEPTANCE
For Fiscal Years 2007, 2008, and 2009**

<u>Cost Category</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>Total</u>
Salaries & Wages	\$18,795,703	\$9,166,940	\$8,166,083	\$36,128,726
Fringe Benefits	8,891,184	2,897,065	2,900,360	14,688,609
Facilities or Occupancy	2,232,571	0	0	2,232,571
EDP Equipment	1,604,174	2,115	7,907	1,614,196
Subcontracts	5,463,895	5,341,831	2,694,571	13,500,297
Outside Professional Services	25,283	339,948	571,116	936,347
Telephone & Telegraph	520,304	4,859	11,139	536,302
Postage & Express	2,303,443	1,955,300	2,340,956	6,599,699
Furniture & Equipment	161,482	0	0	161,482
Materials & Supplies	595,956	19,619	64,989	680,564
Travel	503,666	302,417	305,205	1,111,288
Return on Investment	97,156	106,025	92,535	295,716
Miscellaneous	1,460,356	0	17,738,993	19,199,349
Other	0	20,242,366	0	20,242,366
Credits	(2,860,672)	(1,111,046)	(988,272)	(4,959,990)
Forward Funding	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total Costs Claimed on FACP	\$39,794,501	\$39,267,439	\$33,905,582	\$112,967,522
Pension Costs Not Reviewed	1,373,889	2,957,216	2,947,028	7,278,133
OIG Recommended for Acceptance	<u><u>\$38,420,612</u></u>	<u><u>\$36,310,223</u></u>	<u><u>\$30,958,554</u></u>	<u><u>\$105,689,389</u></u>