



**DEPARTMENT OF HEALTH AND HUMAN SERVICES**

Office of Inspector General

Office of Audit Services  
1100 Commerce, Room 632  
Dallas, Texas 75242

April 2, 2009

Report Number: A-06-08-00016

Mr. Dan Bloodworth  
Senior Vice President and CFO  
Pinnacle Business Solutions, Inc.  
515 Pershing Boulevard.  
North Little Rock, Arkansas 72114

Dear Mr. Bloodworth:

Enclosed is the U.S. Department of Health and Human Services (HHS), Office of Inspector General (OIG), final report entitled "Audit of Pinnacle Business Solutions, Inc.'s, Medicare Part B Final Administrative Cost Proposals for Fiscal Years 2005 through 2007." We will forward a copy of this report to the HHS action official noted on the following page for review and any action deemed necessary.

The HHS action official will make final determination as to actions taken on all matters reported. We request that you respond to this official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

Pursuant to the Freedom of Information Act, 5 U.S.C. § 552, OIG reports generally are made available to the public to the extent that information in the report is not subject to exemptions in the Act. Accordingly, this report will be posted on the Internet at <http://oig.hhs.gov>.

If you have any questions or comments about this report, please do not hesitate to call me, or contact Paul Chesser, Audit Manager, at (501) 225-8114 or through e-mail at [Paul.Chesser@oig.hhs.gov](mailto:Paul.Chesser@oig.hhs.gov). Please refer to report number A-06-08-00016 in all correspondence.

Sincerely,

A handwritten signature in black ink that reads "Gordon L. Sato".

Gordon L. Sato  
Regional Inspector General  
for Audit Services

Enclosure

**Direct Reply to HHS Action Official:**

Nanette Foster Reilly  
Consortium Administrator  
Consortium for Financial Management & Fee for Service Operations  
Centers for Medicare & Medicaid Services  
601 East 12<sup>th</sup> Street, Room 235  
Kansas City, Missouri 64106  
rokcmora@cms.hhs.gov

Department of Health and Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**AUDIT OF PINNACLE BUSINESS  
SOLUTIONS, INC.'S MEDICARE  
PART B FINAL ADMINISTRATIVE  
COST PROPOSALS FOR FISCAL  
YEARS 2005 THROUGH 2007**



Daniel R. Levinson  
Inspector General

April 2009  
A-06-08-00016

# ***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 and 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:

## ***Office of Audit Services***

The Office of Audit Services (OAS) provides auditing services for HHS, either by conducting audits with its own audit resources or by overseeing audit work done by others. Audits examine the performance of HHS programs and/or its grantees and contractors in carrying out their respective responsibilities and are intended to provide independent assessments of HHS programs and operations. These assessments help reduce waste, abuse, and mismanagement and promote economy and efficiency throughout HHS.

## ***Office of Evaluation and Inspections***

The Office of Evaluation and Inspections (OEI) conducts national evaluations to provide HHS, Congress, and the public with timely, useful, and reliable information on significant issues. These evaluations focus on preventing fraud, waste, or abuse and promoting economy, efficiency, and effectiveness of departmental programs. To promote impact, OEI reports also present practical recommendations for improving program operations.

## ***Office of Investigations***

The Office of Investigations (OI) conducts criminal, civil, and administrative investigations of fraud and misconduct related to HHS programs, operations, and beneficiaries. With investigators working in all 50 States and the District of Columbia, OI utilizes its resources by actively coordinating with the Department of Justice and other Federal, State, and local law enforcement authorities. The investigative efforts of OI often lead to criminal convictions, administrative sanctions, and/or civil monetary penalties.

## ***Office of Counsel to the Inspector General***

The Office of Counsel to the Inspector General (OCIG) provides general legal services to OIG, rendering advice and opinions on HHS programs and operations and providing all legal support for OIG's internal operations. OCIG represents OIG in all civil and administrative fraud and abuse cases involving HHS programs, including False Claims Act, program exclusion, and civil monetary penalty cases. In connection with these cases, OCIG also negotiates and monitors corporate integrity agreements. OCIG renders advisory opinions, issues compliance program guidance, publishes fraud alerts, and provides other guidance to the health care industry concerning the anti-kickback statute and other OIG enforcement authorities.

# *Notices*

---

## **THIS REPORT IS AVAILABLE TO THE PUBLIC**

at <http://oig.hhs.gov>

Pursuant to the Freedom of Information Act, 5 U.S.C. § 552, Office of Inspector General reports generally are made available to the public to the extent that information in the report is not subject to exemptions in the Act.

## **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.

## **EXECUTIVE SUMMARY**

### **BACKGROUND**

Title XVIII of the Social Security Act established the Medicare Program, which provides for a hospital insurance program (Part A) and a supplementary medical insurance program (Part B). The Centers for Medicare & Medicaid Services (CMS) administers the Medicare program through contractors, including Part B carriers that process and pay Medicare claims. Contracts between CMS and the Medicare contractors define the functions to be performed and provide for the reimbursement of allowable administrative costs incurred in the processing of Medicare claims.

At the close of each fiscal year (FY), contractors submit to CMS a Final Administrative Cost Proposal (cost proposal), which reports the costs incurred in performing Medicare functions during the year. For FYs 2005 through 2007, CMS contracted with Pinnacle Business Solutions, Inc. (Pinnacle), to serve as the Medicare Part B contractor for Arkansas, Louisiana, Missouri, New Mexico, Oklahoma, and Rhode Island. Pinnacle reported Medicare administrative costs totaling \$174,424,088 in its cost proposals for FYs 2005 through 2007.

### **OBJECTIVE**

Our objective was to determine whether the administrative costs Pinnacle reported in its cost proposals were reasonable, allowable, and allocable in accordance with part 31 of the Federal Acquisition Regulations (FAR) and the Medicare contract.

### **SUMMARY OF FINDINGS**

Pinnacle reported expenditures in its cost proposals that substantially complied with FAR and Medicare contract provisions. However, Pinnacle reported \$247,040 in unallowable costs: (1) \$172,477 in overstated costs related to subcontracts (\$149,089), fringe benefits (\$21,324), and executive compensation (\$2,064) and (2) \$74,563 in FY 2004 costs that it reported on the FY 2005 cost proposal. Pinnacle also reported \$594,079 in professional and consulting services costs and \$223,193 in subcontractor services costs that may be unallowable. We are setting aside the potentially unallowable costs for the CMS contracting officer to review for allowability.

Pinnacle had no forward funding remaining for FYs 2005 through 2007; i.e., Pinnacle had performed all of the services for which it had received funding.

## **RECOMMENDATIONS**

We recommend that Pinnacle:

- decrease its FY 2005 cost proposal by \$94,079 and its FY 2006 cost proposal by \$152,961 to reflect the unallowable costs and
- work with the CMS contracting officer to determine the allowability of \$817,272 in costs related to professional and consulting services and subcontractor services.

## **PINNACLE COMMENTS**

In written comments on our draft report, Pinnacle agreed that it had reported unallowable costs. Pinnacle said that it had made or would make adjustments or offsets to decrease its FY 2005 cost proposal by \$94,079 and its FY 2006 cost proposal by \$152,961. Pinnacle said that it would work with CMS to determine the allowability of costs relating to professional and consulting services and subcontractor services.

Pinnacle's response to our draft report is included as Appendix D. We excluded the attachments to Pinnacle's comments because they contained personally identifiable information.

## **OFFICE OF INSPECTOR GENERAL RESPONSE**

In addition to its comments, Pinnacle provided additional documentation supporting a portion of the unallowable costs and a portion of the potentially unallowable costs. We adjusted our draft findings and recommendations based on the additional documentation.

# TABLE OF CONTENTS

|   | <u>Page</u> |
|---|-------------|
| <b>INTRODUCTION</b> .....   | 1           |
| <b>BACKGROUND</b> .....   | 1           |
| <b>OBJECTIVE, SCOPE, AND METHODOLOGY</b> .....  | 1           |
| Objective .....   | 1           |
| Scope.....  | 1           |
| Methodology .....   | 2           |
| <b>FINDINGS AND RECOMMENDATIONS</b> .....   | 2           |
| <b>UNALLOWABLE COSTS</b> .....  | 3           |
| Subcontractor Costs .....   | 3           |
| Fiscal Year 2004 Costs .....  | 3           |
| Fringe Benefit Costs .....  | 3           |
| Executive Compensation .....  | 4           |
| <b>POTENTIALLY UNALLOWABLE COSTS</b> .....  | 4           |
| Professional and Consulting Services .....  | 4           |
| Subcontractor Services.....   | 5           |
| <b>RECOMMENDATIONS</b> .....  | 5           |
| <b>PINNACLE COMMENTS</b> .....  | 5           |
| <b>OFFICE OF INSPECTOR GENERAL RESPONSE</b> .....   | 5           |
| <b>APPENDIXES</b>   |             |
| A – FINAL ADMINISTRATIVE COST PROPOSALS AND RECOMMENDED<br>DISALLOWANCE, SET-ASIDE, AND ACCEPTANCE AMOUNTS FOR<br>FISCAL YEARS 2005, 2006, and 2007 |             |
| B – RECOMMENDED COST DISALLOWANCE AND SET-ASIDE AMOUNTS   |             |
| C – COMPARISON OF ADMINISTRATIVE COSTS CLAIMED TO BUDGET<br>AUTHORIZATION   |             |
| D – PINNACLE COMMENTS   |             |

## **INTRODUCTION**

### **BACKGROUND**

Title XVIII of the Social Security Act established the Medicare Program, which provides for a hospital insurance program (Part A) and a supplementary medical insurance program (Part B). The Centers for Medicare & Medicaid Services (CMS) administers the Medicare program through contractors, including Part B carriers that process and pay Medicare claims. Contracts between CMS and the Medicare contractors define the functions to be performed and provide for the reimbursement of allowable administrative costs incurred in the processing of Medicare claims.

At the close of each fiscal year (FY), contractors submit to CMS a Final Administrative Cost Proposal (cost proposal), which reports the costs incurred in performing Medicare functions during the year. The cost proposal and supporting data provide the basis for an administrative costs audit and final settlement of allowable costs.

For FYs 2005 through 2007, CMS contracted with Pinnacle Business Solutions, Inc. (Pinnacle), to serve as the Medicare Part B contractor for Arkansas, Louisiana, Missouri, New Mexico, Oklahoma, and Rhode Island. Pinnacle reported Medicare administrative costs totaling \$174,424,088 in its cost proposals for FYs 2005 through 2007.

### **OBJECTIVE, SCOPE, AND METHODOLOGY**

#### **Objective**

Our objective was to determine whether the administrative costs Pinnacle reported in its cost proposals were reasonable, allowable, and allocable in accordance with part 31 of the Federal Acquisition Regulations (FAR) and the Medicare contract.

#### **Scope**

Our review covered the period October 1, 2004, through September 30, 2007 (FYs 2005 through 2007). For this period, Pinnacle reported Medicare administrative costs of \$174,424,088.

We performed a limited review of the internal controls and procedures Pinnacle had in place to allocate costs in accordance with the FAR and Medicare contract. We performed the review to help us accomplish our objectives, not to provide assurance on the internal control structure.

We conducted fieldwork at the Pinnacle campus in North Little Rock, Arkansas, from November 2007 through May 2008.

## **Methodology**

To accomplish our objectives, we:

- reviewed applicable Medicare laws, regulations, and guidelines;
- reviewed the applicable sections of the FAR and the Pinnacle contract with CMS;
- reviewed the independent auditor's reports for FYs 2005 and 2006;
- reviewed Pinnacle internal audit reports for FYs 2005 through 2007;
- reconciled line-item expenses on cost proposals and cost classification reports to the contractor's subsidiary record of expenses;
- reviewed journal entries, invoices, expense reports, contracts and agreements, and additional supporting documentation;
- interviewed Pinnacle officials regarding the cost accumulation processes for cost proposals and cost allocation systems;
- reviewed payroll and personnel records; and
- tested costs for reasonableness, allowability, and allocability.

Regarding top Pinnacle executives who had salaries allocated to Medicare, we:

- reviewed established personnel and accounting policies and procedures to determine Pinnacle's practices for allocating compensation costs to Medicare,
- compared a sample of executives' compensation to benchmark compensation amounts published in the Federal Register, and
- identified excessive executive compensation costs.

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.

## **FINDINGS AND RECOMMENDATIONS**

Pinnacle reported expenditures in its cost proposals that substantially complied with FAR and Medicare contract provisions. However, Pinnacle reported \$247,040 in unallowable costs: (1) \$172,477 in overstated costs related to subcontracts (\$149,089), fringe benefits (\$21,324), and

executive compensation (\$2,064), and (2) \$74,563 in FY 2004 costs that it reported on the FY 2005 cost proposal. Pinnacle also reported \$594,079 in professional and consulting services costs and \$223,193 in subcontractor services costs that may be unallowable. We are setting aside the potentially unallowable costs for the CMS contracting officer to review for allowability.

Pinnacle had no forward funding remaining for FYs 2005 through 2007; i.e., Pinnacle had performed all of the services for which it had received funding.

## **UNALLOWABLE COSTS**

### **Subcontractor Costs**

The carrier contract, Appendix B, section IV, states: “All contractors must depreciate all items of equipment having a useful life of more than 1 year. The cost of equipment may not be charged off as an expense in the year of purchase.”

Pinnacle overstated subcontractor costs by \$149,089 in its FY 2006 cost proposal. The overstatement occurred because Pinnacle accounted for an equipment purchase as an expense rather than an asset. As a result, the FY 2006 cost proposal contains unallowable costs of \$149,089.

### **Fiscal Year 2004 Costs**

FAR 31.201-2(a)(3) states: “A cost is allowable when the cost complies with . . . generally accepted accounting principles and practices appropriate to the circumstances.” Also, the “Medicare Financial Management Manual,” chapter 2, section 130, states that the final administrative cost proposals (FACP) “shall not include adjustments related to prior years’ costs on the current FACP.”

Pinnacle incorrectly reported \$74,563 in FY 2004 costs in its FY 2005 cost proposal because the FY 2004 cost proposal was closed for adjustments. The costs included contract labor, tuition reimbursement credits, subcontractor costs, and outside professional services

### **Fringe Benefit Costs**

Pinnacle reported unallowable fringe benefit costs totaling \$21,324 in its FY 2005 and FY 2006 cost proposals.

### *State Unemployment Tax Refund*

FAR 31.201-5 states: “The applicable portion of any income, rebate, allowance, or other credit relating to any allowable cost and received by or accruing to the contractor shall be credited to the Government either as a cost reduction or by cash refund.”

Pinnacle received a \$15,559 State unemployment tax refund that was not included in the FY 2005 and FY 2006 cost proposals. Because the refund was not deducted from costs, the FY 2005 and FY 2006 cost proposals contain unallowable costs of \$15,559.

### *Lobbying Costs*

FAR 31.205-22(c) states: “When a contractor seeks reimbursement for indirect costs, total lobbying costs shall be separately identified in the indirect cost rate proposal, and thereafter treated as other unallowable activity costs.”

Pinnacle reported unallowable costs totaling \$5,765 in its FY 2005 and FY 2006 cost proposals for lobbying activities related to corporate membership in a trade organization.

### **Executive Compensation**

FAR 31.205-6(p) states: “Costs incurred after January 1, 1998, for compensation of a senior executive in excess of the benchmark compensation amount determined applicable for the contractor fiscal year by the Administrator, Office of Federal Procurement Policy (OFPP), under Section 39 of the OFPP Act (41 U.S.C. 435) are unallowable . . . .” Effective January 2, 1999, senior executives are “. . . the five most highly compensated employees in management positions at each home office and each segment of the contractor, whether or not the home office or segment reports directly to the contractor’s headquarters.”

Pinnacle overstated executive compensation costs by \$2,064 in its FY 2005 cost proposal. Pinnacle made a calculation error that understated the adjustment made to eliminate excess executive compensation in the cost proposal.

## **POTENTIALLY UNALLOWABLE COSTS**

### **Professional and Consulting Services**

The carrier contract, section II, part I, B, states: “The prior written approval of the Contracting Officer shall be required: . . . (b) for the utilization of the services of any consultant under this contract where such reimbursement exceeds or may exceed \$400.00 per day or \$100,000 per year, exclusive of travel costs.” In addition, the carrier contract, section I, article XVII, G, states: “If, with respect to any subcontract entered into under this Article requiring the prior written approval of the Secretary, such required approval is not obtained, the United States shall not be obligated to reimburse the Carrier for any costs incurred, relative to such subcontract, prior to the date of the Secretary’s approval unless so stipulated.”

Pinnacle reported costs totaling \$594,079 in its FY 2005 and FY 2006 cost proposals for professional and consulting services for which it was unable to provide written approval. Without prior written approval, CMS is not required to reimburse these costs.

## **Subcontractor Services**

The carrier contract, section I, article XVII, A, states: “The Carrier shall not enter into any subcontract with a third party to perform any of the functions set forth in this contract unless such subcontract received the prior written approval of the Secretary.” In addition, the carrier contract, section I, article XVII, G, states: “If, with respect to any subcontract entered into under this Article requiring the prior written approval of the Secretary, such required approval is not obtained, the United States shall not be obligated to reimburse the Carrier for any costs incurred, relative to such subcontract, prior to the date of the Secretary’s approval unless so stipulated.”

Pinnacle reported costs totaling \$223,193 in its FY 2005 and FY 2006 cost proposals for subcontracting services for which it was unable to provide written approval. Without prior written approval, CMS is not required to reimburse these costs.

## **RECOMMENDATIONS**

We recommend that Pinnacle:

- decrease its FY 2005 cost proposal by \$94,079 and its FY 2006 cost proposal by \$152,961 to reflect the unallowable costs and
- work with the CMS contracting officer to determine the allowability of \$817,272 in costs related to professional and consulting services and subcontractor services.

## **PINNACLE COMMENTS**

In written comments on our draft report, Pinnacle agreed that it had reported unallowable costs. Pinnacle said that it had made or would make adjustments or offsets to decrease its FY 2005 cost proposal by \$94,079 and its FY 2006 cost proposal by \$152,961. Pinnacle said that it would work with CMS to determine the allowability of costs relating to professional and consulting services and subcontractor services.

Pinnacle’s response to our draft report is included as Appendix D. We excluded the attachments to Pinnacle’s comments because they contained personally identifiable information.

## **OFFICE OF INSPECTOR GENERAL RESPONSE**

In addition to its comments, Pinnacle provided additional documentation supporting a portion of the unallowable costs and a portion of the potentially unallowable costs. We adjusted our draft findings and recommendations based on the additional documentation.

# **APPENDIXES**

**APPENDIX A**

**FINAL ADMINISTRATIVE COST PROPOSALS AND RECOMMENDED  
DISALLOWANCE, SET-ASIDE, AND ACCEPTANCE AMOUNTS FOR FISCAL  
YEARS 2005, 2006, and 2007**

| <b>Cost Category</b>                  | <b>FY 2005</b>      | <b>FY 2006</b>      | <b>FY 2007</b>      | <b>Total</b>         |
|---------------------------------------|---------------------|---------------------|---------------------|----------------------|
| Salaries/wages                        | \$38,171,162        | \$37,126,933        | \$34,035,939        | \$109,334,034        |
| Fringe benefits                       | 12,121,891          | 12,395,585          | 11,115,698          | 35,633,174           |
| Facilities or occupancy               | 3,359,260           | 3,555,009           | 3,176,944           | 10,091,213           |
| Data processing equipment             | 2,531,103           | 2,355,797           | 1,945,339           | 6,832,239            |
| Subcontractors                        | 2,880,947           | 3,337,666           | 2,189,376           | 8,407,989            |
| Outside professional services         | 1,353,005           | (2,399,439)         | (1,831,841)         | (2,878,275)          |
| Telephone and telegraph               | 798,573             | 1,023,912           | 791,191             | 2,613,676            |
| Postage and express                   | 6,556,027           | 5,772,859           | 4,978,481           | 17,307,367           |
| Furniture and equipment               | 4,298,047           | 4,436,600           | 2,592,614           | 11,327,261           |
| Materials and supplies                | 1,383,307           | 1,018,576           | 976,946             | 3,378,829            |
| Travel                                | 620,134             | 456,066             | 376,423             | 1,452,623            |
| Return on investment                  | 498,122             | 226,530             | 0                   | 724,652              |
| Miscellaneous                         | 778,621             | 3,986,744           | 3,410,158           | 8,175,523            |
| Other                                 | 0                   | (2,751)             | 0                   | (2,751)              |
| Subtotal                              | 75,350,199          | 73,290,087          | 63,757,268          | 212,397,554          |
| Other adjustments (credits)           | (13,350,795)        | (12,981,129)        | (11,641,542)        | (37,973,466)         |
| <b>Total</b>                          | <b>\$61,999,404</b> | <b>\$60,308,958</b> | <b>\$52,115,726</b> | <b>\$174,424,088</b> |
| Forward funding                       | 0                   | 0                   | 0                   | 0                    |
| <b>Total claimed on cost proposal</b> | <b>\$61,999,404</b> | <b>\$60,308,958</b> | <b>\$52,115,726</b> | <b>\$174,424,088</b> |
| Recommended disallowance*             | 94,079              | 152,961             | 0                   | 247,040              |
| Recommended set-aside*                | 550,412             | 266,860             | 0                   | 817,272              |
| Recommended for acceptance            | \$61,354,913        | \$59,889,137        | \$52,115,726        | \$173,359,776        |

\*See Appendix B

## RECOMMENDED COST DISALLOWANCE AND SET-ASIDE AMOUNTS

| <b>Disallowance Category</b>         | <b><u>Fiscal Year 2005</u></b> |                  |
|--------------------------------------|--------------------------------|------------------|
|                                      | <b>Disallowance</b>            | <b>Set-Aside</b> |
| State unemployment tax refund        | \$14,620                       |                  |
| Lobbying costs                       | 2,832                          |                  |
| Executive compensation               | 2,064                          |                  |
| Fiscal year 2004 costs               | 74,563                         |                  |
| Professional and consulting services |                                | \$409,601        |
| Subcontractor services               |                                | 140,811          |
| <b>Total</b>                         | <b>\$94,079</b>                | <b>\$550,412</b> |

| <b>Disallowance Category</b>         | <b><u>Fiscal Year 2006</u></b> |                  |
|--------------------------------------|--------------------------------|------------------|
|                                      | <b>Disallowance</b>            | <b>Set-Aside</b> |
| Subcontractor costs/services         | \$149,089                      | \$82,382         |
| State unemployment tax refund        | 939                            |                  |
| Lobbying costs                       | 2,933                          |                  |
| Professional and consulting services |                                | 184,478          |
| <b>Total</b>                         | <b>\$152,961</b>               | <b>\$266,860</b> |

**COMPARISON OF ADMINISTRATIVE COSTS CLAIMED  
TO BUDGET AUTHORIZATION**

**Fiscal Year 2005**

| <b>Operation</b>                            | <b>Budget<br/>Authorization</b> | <b>Administrative<br/>Costs Claimed</b> | <b>Variance—<br/>Favorable<br/>(Unfavorable)</b> |
|---|---------------------------------|---|--|
| <b>Program Management (PM)</b>              |                                 |   |  |
| Bills/claims payment                        | \$43,855,126                    | \$43,260,395                            | \$594,731  |
| Appeals/reviews                             | 6,730,518                       | 6,710,373                               | 20,145   |
| Beneficiary inquiries                       | 4,015,077                       | 4,024,474                               | (9,397)  |
| PM provider communications                  | 109,182                         | 109,174                                 | 8  |
| Participating physician                     | 290,128                         | 290,502                                 | (374)  |
| Productivity investment                     | 349,862                         | 114,761                                 | 235,101  |
| Provider enrollment                         | 2,906,010                       | 2,939,044                               | (33,034)   |
| Provider telephone inquiries                | 4,368,466                       | 4,335,220                               | 33,246   |
| Credits                                     | (13,213,142)                    | (13,127,766)                            | (85,376)   |
| Subtotal                                    | 49,411,227                      | 48,656,177                              | 755,050  |
| <b>Medicare Integrity Program<br/>(MIP)</b> |                                 |   |  |
| Medical review                              | 4,566,919                       | 4,620,076                               | (53,157)   |
| MSP <sup>1</sup> prepayment                 | 672,706                         | 672,667                                 | 39   |
| Benefits integrity                          | 263,771                         | 257,589                                 | 6,182  |
| Provider education and training             | 1,102,021                       | 1,080,857                               | 21,164   |
| Provider communications                     | 1,567,654                       | 1,531,055                               | 36,599   |
| MSP postpayment                             | 3,271,076                       | 3,253,613                               | 17,463   |
| Subtotal                                    | 11,444,147                      | 11,415,857                              | 28,290   |
| MMA <sup>2</sup> fee-for-service            | 69,000                          | 68,632                                  | 368  |
| MMA regulatory reform                       | 1,871,487                       | 1,858,738                               | 12,749   |
| <b>Total</b>                                | <b>\$62,795,861</b>             | <b>\$61,999,404</b>                     | <b>\$796,457</b>                                 |

NOTE: All amounts taken from Final Administrative Cost Proposal (Supplement No. 7) and Notice of Budget Approval (Supplement No. 13).

<sup>1</sup>MSP – Medicare secondary payer

<sup>2</sup>MMA – Medicare Prescription Drug, Improvement, and Modernization Act

**COMPARISON OF ADMINISTRATIVE COSTS CLAIMED  
TO BUDGET AUTHORIZATION**

**Fiscal Year 2006**

| <b>Operation</b>                  | <b>Budget<br/>Authorization</b> | <b>Administrative<br/>Costs Claimed</b> | <b>Variance—<br/>Favorable<br/>(Unfavorable)</b> |
|-----------------------------------|---------------------------------|---|--|
| <b>Program Management</b>         |                                 |   |  |
| Bills/claims payment              | \$40,222,900                    | \$39,756,328                            | \$466,572  |
| Appeals/reviews                   | 7,725,400                       | 7,758,753                               | (33,353)   |
| Beneficiary inquiries             | 3,961,600                       | 3,572,254                               | 389,346  |
| PM provider communications        | 601,900                         | 563,666                                 | 38,234   |
| Participating physician           | 317,600                         | 361,164                                 | (43,564)   |
| Productivity investment           | 158,000                         | 103,838                                 | 54,162   |
| Provider enrollment               | 3,127,100                       | 3,177,845                               | (50,745)   |
| Provider telephone inquiries      | 6,406,000                       | 6,265,116                               | 140,884  |
| Credits                           | (13,316,100)                    | (12,801,433)                            | (514,667)  |
| Subtotal                          | 49,204,400                      | 48,757,531                              | 446,869  |
| <b>Medicare Integrity Program</b> |                                 |   |  |
| Medical review                    | 4,692,000                       | 4,404,624                               | 287,376  |
| MSP prepayment                    | 696,700                         | 931,489                                 | (234,789)  |
| Benefits integrity                | 326,000                         | 353,805                                 | (27,805)   |
| Provider education and training   | 1,156,100                       | 1,134,963                               | 21,137   |
| Provider communications           | 1,288,200                       | 1,249,288                               | 38,912   |
| MIP productivity investment       | 126,300                         | 126,300                                 | 0  |
| MSP postpayment                   | 3,063,300                       | 3,006,783                               | 56,517   |
| Subtotal                          | 11,348,600                      | 11,207,252                              | 141,348  |
| <b>Nonactivity Summary</b>        |                                 |   |  |
| Nonrenewal                        | 0                               | 344,175                                 | (344,175)  |
| <b>Total</b>                      | <b>\$60,553,000</b>             | <b>\$60,308,958</b>                     | <b>\$244,042</b>                                 |

NOTE: All amounts taken from Final Administrative Cost Proposal (Supplement No. 4) and Notice of Budget Approval (Supplement No. 21).

**COMPARISON OF ADMINISTRATIVE COSTS CLAIMED  
TO BUDGET AUTHORIZATION**

**Fiscal Year 2007**

| <b>Operation</b>                    | <b>Budget<br/>Authorization</b> | <b>Administrative<br/>Costs Claimed</b> | <b>Variance<br/>Favorable<br/>(Unfavorable)</b> |
|-------------------------------------|---------------------------------|---|---|
| <b>Program Management</b>           |                                 |   |   |
| Bills/claims payment                | \$38,528,600                    | \$37,643,396                            | \$885,204                                       |
| Appeals/reviews                     | 4,712,000                       | 4,726,146                               | (14,146)  |
| Beneficiary inquiries               | 1,091,000                       | 837,994                                 | 253,006   |
| Participating physician             | 82,600                          | 78,893                                  | 3,707   |
| Productivity investment             | 79,400                          | 0                                       | 79,400  |
| Provider enrollment                 | 5,160,600                       | 4,862,835                               | 297,765   |
| Provider telephone inquiries        | 6,538,200                       | 6,301,558                               | 236,642   |
| Provider outreach and education     | 150,400                         | 147,525                                 | 2,875   |
| Credits                             | (12,297,100)                    | (11,603,877)                            | (693,223)                                       |
| Subtotal                            | 44,045,700                      | 42,994,470                              | 1,051,230                                       |
| <b>Medicare Integrity Program</b>   |                                 |   |   |
| Medical review                      | 4,691,000                       | 4,461,994                               | 229,006   |
| MSP prepayment                      | 867,400                         | 488,041                                 | 379,359   |
| Benefits integrity                  | 300,000                         | 238,562                                 | 61,438  |
| MSP postpayment                     | 2,159,000                       | 2,091,851                               | 67,149  |
| MIP provider outreach and education | 2,030,800                       | 1,840,813                               | 189,987   |
| Subtotal                            | 10,048,200                      | 9,121,261                               | 926,939   |
| <b>Total</b>                        | <b>\$54,093,900</b>             | <b>\$52,115,731</b>                     | <b>\$1,978,169</b>                              |

NOTE: All amounts taken from Final Administrative Cost Proposal (Supplement No. 00) and Notice of Budget Approval (Supplement No. 11).



MEDICARE  
Part A Intermediary  
Part B Carrier

March 4, 2009

Report Number: A-06-08-00016

Mr. Gordon L. Sato  
Regional Inspector General for Audit Services  
Department of Health & Human Services  
Office of Inspector General  
Office of Audit Services  
1100 Commerce, Room 632  
Dallas, TX 75242

**Office of Inspector General Note:** Portions of this response are no longer applicable because we reduced the unallowable costs and the potentially unallowable costs based on additional documentation submitted by the auditee.

Dear Mr. Sato,

This letter represents Pinnacle Business Solutions, Inc.'s (PBSI) response to draft Report Number A-06-08-00016 dated February 3, 2009. This report was issued as a result of the Office of Inspector General's (OIG) audit of PBSI's Fiscal Years 2005, 2006, and 2007 final administrative cost proposals (FACP).

Below you will find PBSI's written comments in response to each of the findings included within the draft report. An excel sheet summarizing these findings as well as the status of adjustments has been included as Attachment A for reference. The status of adjustments and actions necessary to remediate agreed upon findings is included in both Attachment A as well as discussions below.

**Unallowable Costs:**

- *Subcontractor Costs:* PBSI agrees with the OIG finding that costs were overstated in its FY 2006 cost proposal in the amount of \$149,089 due to the fact that a piece of equipment was improperly expensed rather than being capitalized and depreciated. PBSI made an adjustment to its FY 2006 FACP supplement #06 dated July 31, 2008 to remove this cost. Therefore, no further adjustment is necessary.
- *Fiscal Year 2004 Costs:* PBSI agrees that FY 2004 costs were recognized on the FY 2005 FACP in the amount of \$74,563. These were allowable costs recognized inaccurately in FY 2005 rather than FY 2004. A settlement agreement has been finalized for the FY 2004

Mr. Gordon L. Sato  
March 4, 2009  
Page 2 of 3

FACP; therefore, an adjustment to increase the FY 2004 expenses is not possible. PBSI will remove these costs in the next FY 2005 FACP submission.

- Fringe Benefit Costs:
  - *State Unemployment Tax Refund:* PBSI agrees that unallowable costs in the amount of \$15,559 were included in the FY 2005 and FY 2006 FACP's related to a tax refund that was not applied. PBSI made an adjustment to the FY 2005 FACP supplement #09 dated July 31, 2008 and FY 2006 FACP supplement #06 dated July 31, 2008 to remove these costs. Therefore, no further adjustment is necessary.
  - *Lobbying Costs:* PBSI agrees that unallowable costs in the total amount of \$5,765 were included in the FY 2005 and FY 2006 FACP's (FY 2005 - \$2,832 / FY 2006 - \$2,933). PBSI did not file \$331,285 of its Program Management costs in FY 2006 (see Attachment B) in order to stay within notice of budget approval (NOBA); therefore, PBSI proposes to offset the FY 2006 finding amount of \$2,933 by these unfiled costs and remove the FY 2005 amount of \$2,832 in the next FY 2005 FACP submission.

- *Electronic Data Processing Costs:* The audit report indicates that these costs have been considered unallowable due to the fact that they were reported without maintaining records in accordance with Federal regulations. PBSI has provided a copy of the invoice related to the expense in question to the audit team, and have also attached the invoice to this letter for further reference as Attachment C. This expense is incurred as an annual maintenance charge for front-end claims receipt software. PBSI believes this invoice substantiates the validity of the expense and documents the benefit to the Medicare Program for the incurrence of the expense. PBSI does not agree that the \$10,267 should be considered non-allowable cost.

- *Executive Compensation:* PBSI agrees that FY 2005 cost was overstated by \$2,064 in association with executive compensation. PBSI reviews and makes an adjustment for executive compensation in accordance with CMS guidelines in each fiscal year. PBSI had worked with the OIG on previous audits to improve the process associated with the adjustment calculation. The \$2,064 adjustment is the result of a miscalculation on a spreadsheet, and the necessary adjustment to remove this cost was made to PBSI's FY 2005 FACP supplement #09 dated July 31, 2008. Therefore, no further adjustment is necessary.

**Potentially Unallowable Costs:**

The audit report recommends that PBSI work with the CMS contracting officer to determine the allowability of \$862,446 in set aside costs related to professional and consulting services, subcontractor services and electronic data processing costs. Upon initial review of the detailed listing of vendor payments, PBSI has determined that \$53,344 of the expenses identified in the audit report were not included on the 2006 FACP; therefore, the total set aside amount should be adjusted downward by this amount, leaving a balance of \$809,102. PBSI does believe those

Mr. Gordon L. Sato  
March 4, 2009  
Page 3 of 3

remaining expenses to be allowable, and we will work with the CMS contracting officer to validate the allowability of those expenses.

We look forward to continuing our work with you to finalize this audit. If you have any questions or comments about our response please feel free to contact me at 501-210-9105.

Sincerely,

A handwritten signature in black ink, appearing to read "Dan Bloodworth". The signature is fluid and cursive, with a long horizontal stroke at the end.

Dan Bloodworth  
Sr. VP & CFO

/db

Attachments

cc: Kathy Markman  
Janie Fenton  
Amy Green