



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General  
Offices of Audit Services

December 29, 2003

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

Report Number: A-07-03-03045

Ms. Pamela T. Miller, Esq.  
Vice President Enterprise Strategy and Quality  
Horizon Blue Cross Blue Shield of New Jersey  
3 Penn Plaza East  
Newark, New Jersey 07105

Dear Ms. Miller:

Enclosed are two copies of the U.S. Department of Health and Human Services (HHS), Office of Inspector General report entitled "*Review of Pension Costs Claimed for Medicare Reimbursement by Horizon Blue Cross Blue Shield of New Jersey* ."

The objective of our review was to determine allowability of pension costs claimed for Medicare reimbursement for Fiscal Years (FY) 1986 through 2000.

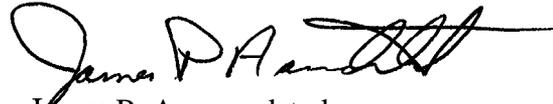
For FYs 1986 through 2000, we determined that Horizon over claimed allowable Medicare pension costs. During this period, the allowable Medicare pension costs were \$1,232,376. However, Horizon claimed pension costs of \$1,605,828 for Medicare reimbursement. As a result, Horizon over claimed allowable pension costs by \$373,452. This over claim of pension costs was the result of Horizon claiming pension costs that it had not funded for the years 1993 and 1997 through 2000. We are recommending Horizon remit the over claimed pension costs of \$373,452 to the Federal Government.

Final determination as to actions taken on all matters reported will be made by the HHS action official named below. We request that you respond to the HHS action 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.

In accordance with the principles of the Freedom of Information Act (5 U.S.C. 552, as amended by Public Law 104-231), Office of Inspector General reports issued to the Department's grantees and contractors are made available 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.)

If you have any questions or comments about this report, please do not hesitate to call me or Gregory Tambke, Audit Manager at (573) 893-8338, ext. 30 or through e-mail at gtambke@oig.hhs.gov. To facilitate identification, please refer to Report Number A-07-03-03045 in all correspondence relating to this report.

Sincerely yours,



James P. Aasmundstad  
Regional Inspector General  
for Audit Services

Enclosures - as stated

**Directly Reply to HHS Action Official:**

Ms. Judith Berek  
Regional Administrator, Region II  
Centers for Medicare & Medicaid Services  
26 Federal Plaza, 38<sup>th</sup> Floor  
New York, New York 10278

**Department of Health and Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF PENSION COSTS CLAIMED  
FOR MEDICARE REIMBURSEMENT BY  
HORIZON BLUE CROSS BLUE SHIELD  
OF NEW JERSEY**



**DECEMBER 2003  
A-07-03-03045**

# *Office of Inspector General*

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

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The OIG's Office of Audit Services (OAS) provides all 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 in order to reduce waste, abuse, and mismanagement and to promote economy and efficiency throughout the Department.

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# ***Notices***

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In accordance with the principles of the Freedom of Information Act, 5 U.S.C. 552, as amended by Public Law 104-231, Office of Inspector General, Office of Audit Services, reports are made available to members of the public to the extent information contained therein is not subject to exemptions in the Act. (See 45 CFR Part 5.)

## **OAS FINDINGS AND OPINIONS**

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



## EXECUTIVE SUMMARY

### Objective

The objective of our review was to determine allowability of pension costs claimed for Medicare reimbursement for FYs 1986 through 2000.

### Summary of Findings

For FYs 1986 through 2000, we determined that Horizon over claimed allowable Medicare pension costs. During this period, the allowable Medicare pension costs were \$1,232,376. However, Horizon claimed pension costs of \$1,605,828 for Medicare reimbursement. As a result, Horizon over claimed allowable pension costs by \$373,452. This over claim of pension costs was the result of Horizon claiming pension costs that it had not funded for the years 1993 and 1997 through 2000.

### Recommendations

We are recommending Horizon remit the over claimed pension costs of \$373,452 to the Federal Government.

### Auditee's Comments

Horizon disagreed with our report and stated:

*"In summary, we disagree with (1) the inconsistencies between the Draft Pension Costs Report and the Draft Pension Surplus Report, specifically in regard to 1989 and 1990 costs and the Medicare LOB percentages, and (2) your statement that the primary cause for the over claim was that Horizon did not fully fund the costs claimed for the years 1993 and 1997 through 2000. We request that the two reports be consistent in their treatment of these issues."*

### OIG Response

We do not agree with Horizon's comments about (1) the inconsistencies between this report and Report Number: A-07-02-03028, specifically in regard to the 1989 and 1990 costs and the Medicare LOB percentages, and (2) our statement that the primary cause for the over claim was that Horizon did not fully fund the costs claimed for the years 1993 and 1997 through 2000. Horizon has not presented any arguments that would cause us to reconsider our findings.

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## **BACKGROUND**

### ***Medicare***

Horizon administered Medicare Part A under its cost reimbursement contract until the contractual relationship was terminated in 2000. In claiming costs, contractors were to follow cost reimbursement principles contained in the Federal Procurement Regulations (FPR), which were superseded by the Federal Acquisition Regulations (FAR), the Cost Accounting Standards (CAS), and the Medicare contracts.

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

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.

Additionally, the Centers for Medicare & Medicaid Services (CMS), formerly the Health Care Financing Administration, incorporated specific segmentation language into Medicare contracts. The contracts provide for either an allocation or a separate calculation of pension costs. Under an allocation method, a contractor determines total plan CAS costs and allocates a share to Medicare. Under the separate calculation method, a contractor separately identifies the normal costs and amortization for the Medicare segment. The separate calculation method must be used if there is a material difference between the two methods.

### ***Horizon Blue Cross Blue Shield of New Jersey***

Horizon was awarded a Medicare Part A contract in 1987. On July 31, 2000 Horizon terminated its Medicare operations.

## **OBJECTIVES, SCOPE AND METHODOLOGY**

### ***Objective***

The objective of our review was to determine allowability of pension costs claimed for Medicare reimbursement for FYs 1986 through 2000.

### ***Scope***

This review was done in conjunction with our review of Horizon's pension segmentation closing (Report Number: A-07-02-03028). The information obtained and reviewed during that audit was also used in performing this review.

We identified Horizon's CAS pension costs for the total company and for the Medicare segment. We also determined the extent to which Horizon funded CAS pension costs with contributions to the pension trust fund. Using this information, we calculated CAS pension costs that are allowable for Medicare reimbursement for FYs 1986 through 2000. Appendix A contains the details on the pension costs and contributions. Achieving the objective did not require a review of Horizon's internal control structure.

### ***Methodology***

We made our examination in accordance with generally accepted government auditing standards. The CMS Office of the Actuary developed the methodology used for computing allowable CAS pension costs based on Horizon's historical practices. We performed site work at Horizon's corporate offices in Newark, New Jersey during April 2002. Subsequently, we performed audit work in the Office of Inspector General, Jefferson City, Missouri Field Office.

## **FINDINGS IN DETAIL**

For FYs 1986 through 2000, Horizon claimed \$373,452 in pension costs that are not allowable for Medicare reimbursement. The pension costs are unallowable because the costs claimed exceeded the funded portion of CAS computed costs. The over claim primarily occurred because Horizon claimed pension costs that were not funded.

### **CRITERIA**

The determination and allocation of pension costs are addressed by the Medicare contract which states:

*The calculation of and accounting for pension costs charged to this agreement/contract are governed by the Federal Acquisition Regulation and Cost Accounting Standards 412 and 413.*

## CONDITION AND CAUSE

For FYs 1986 through 2000, Horizon charged \$1,605,828 of pension costs to Medicare. However, the allowable CAS pension costs were \$1,232,376 for the same period. Therefore, Horizon over claimed \$373,452 in pension costs.

The primary cause for the over claim was that Horizon did not fully fund the costs claimed for the years 1993 and 1997 through 2000.

Horizon could not provide documentation regarding costs it may have incurred from its non-Medicare segment. Additionally, Horizon waived its right to reimbursement for any indirect pension costs attributable to Medicare. We therefore only calculated the allowable CAS pension costs for the Medicare segment. The calculations were based on separately computed CAS pension costs. See Appendix A.

We compared our calculated allowable CAS pension costs to the pension costs claimed on Horizon's FACPs and found:

### PENSION COSTS CLAIMED VARIANCE

<b>FISCAL YEAR</b>	<b>PER HORIZON</b>	<b>PER OIG</b>	<b>DIFFERENCE</b>
1986	\$0	\$0 <sup>1</sup>	\$0
1987	0	0	0
1988	0	0	0
1989	0	0 <sup>2</sup>	0
1990	0	0	0
1991	138,939	199,345	(60,406)
1992	150,556	173,900	(23,344)
1993	186,168	52,301	133,867
1994	146,595	201,482	(54,887)
1995	191,512	311,351	(119,839)
1996	149,303	236,015	(86,712)
1997	167,352	57,982	109,370
1998	171,091	0	171,091
1999	176,073	0	176,073
2000	128,239	0	128,239
	<u>\$1,605,828</u>	<u>\$1,232,376</u>	<u>\$373,452</u>

<sup>1</sup> Horizon could not provide supporting documentation for the years 1986 and 1987. Also, for the years 1986 to 1988, Horizon did not make contributions to the pension plan per its reconstructed Update of Segment Assets and did not claim pension costs per its computation of CAS pension costs.

<sup>2</sup> Horizon did not claim pension costs per its FACPs for the years 1989 and 1990. Horizon did make contributions to the Medicare segment of its Management Plan for these years. Based on these contributions, we have computed allocable costs for Horizon. See Appendix A. However, because Horizon could not supply documentation to verify that it in fact had not claimed pension costs for the years 1989 and 1990, we cannot express an opinion on any potential under claim of pension costs for these years.

## **EFFECT**

For FYs 1986 through 2000, Horizon claimed pension costs of \$1,605,828 for Medicare reimbursement. However, the allowable CAS pension costs were \$1,232,376. As a result, Horizon claimed \$373,452 in excess of the allowable CAS pension costs.

## **RECOMMENDATION**

We recommend that Horizon remit the over claimed pension costs of \$373,452 to the Federal Government.

## **AUDITEE'S COMMENTS**

Horizon's comments are summarized in the following paragraphs and presented in detail at Appendix B.

Horizon disagreed with our report and stated:

*"In summary, we disagree with (1) the inconsistencies between the Draft Pension Costs Report and the Draft Pension Surplus Report, specifically in regard to 1989 and 1990 costs and the Medicare LOB percentages, and (2) your statement that the primary cause for the over claim was that Horizon did not fully fund the costs claimed for the years 1993 and 1997 through 2000. We request that the two reports be consistent in their treatment of these issues."*

### **Inconsistencies**

Horizon disputed our findings concerning costs claimed for 1989 and 1990. Horizon stated that it presented FACPs for these years as documentation of costs claimed, the OIG audited the FACPs, and no findings were expressed for pension costs. According to Horizon, it was unaware of any requests for additional documentation to verify that no costs were claimed for those years. Horizon stated that if in our final determination we maintain that Horizon could not claim these costs then:

*"...consistency requires these amounts (with compounded investment return through the contract settlement date) to be removed from the resulting Medicare surplus."*

Horizon also stated that it is inconsistent for us to apply Medicare LOB percentages for the years 1991 through 1997 to allowable pension costs for this report and to use the average of 1994 through 2000 percentages to compute the aggregate Medicare percentage to determine the excess Medicare pension assets for Report Number: A-07-02-03028. Horizon stated that:

*"We submit that consistent application of the Medicare percentages requires that: (1) the percentage applied in the Draft Pension Surplus Report reflect only the years for which there were Allowable Pension Costs and (2) higher weights be given to the earlier years' percentages since these years costs contributed to a larger share of the resulting surplus (due to the additional years of compounded investment return which applied)."*

## **Unfunded Costs Claimed**

Concerning our finding that Horizon's over claim was the result of pension costs claimed not being fully funded for the years 1993 and 1997 through 2000, Horizon claimed that it had fully funded the pension costs for these years and that its actuary had determined that the segment was in an "overfunded position."

## **OIG RESPONSE**

We do not agree with Horizon's comments about (1) the inconsistencies between this report and Report Number: A-07-02-03028, specifically in regard to the 1989 and 1990 costs and the Medicare LOB percentages, and (2) our statement that the primary cause for the over claim was that Horizon did not fully fund the costs claimed for the years 1993 and 1997 through 2000. Horizon has not presented any arguments that would cause us to reconsider our findings.

## **Inconsistencies**

We believe that Horizon is aware that documentation was requested to verify that no costs were claimed for 1989 and 1990 on its FACP's for all years. The documentation was initially requested in October 2001 when a list of required data was presented to Horizon that included a request for:

*"An accounting for Medicare pension costs and assets from the initial allocation to present (the asset "roll-up"). The information should include for each year:*

- A. Total pension cost charged to the FACP.*
- B. The pension cost for the Medicare Segment charged to the FACP.*
- C. A description of how the pension costs for the segment were determined, including the actuarial cost method, actuarial assumptions, and amortization schedules."*

In November 2002, we requested an accounting of pension costs for 1997 and another year, "preferably the earliest date possible." During a January 2003 phone conference with Horizon's staff and legal counsel, we requested information to aid in determining pension costs of its two pension plans. In a February 3, 2003 letter sent by Horizon, we were informed that the earliest data available to verify the segmented pension costs was 1994.

Horizon provided audited FACP's for 1989 and 1990 as supporting documentation. However, the Administrative Cost Audits performed scoped out pension costs for our review and are not officially closed until the completion of our review of those costs. Therefore, there would have been no findings and the audited FACP's do not serve as supporting documentation. Furthermore, we do not consider FACP's as adequate support for Medicare pension costs. We consider supporting documentation to be the source used to prepare the FACP's.

Because Horizon could not supply adequate supporting documentation for 1989 and 1990 Pension Costs claimed for Medicare reimbursement on the FACPs, we were not able to verify whether Horizon allocated claimed pension costs to the contract for these years. Since, we have no way of knowing whether Medicare reimbursed Horizon for these costs, we can't recommend that Horizon be allowed to claim these pension costs. If Horizon supplied us with the requested documentation and it showed Horizon had not claimed pension costs for FYs 1989 and 1990, we would have adjusted our finding for these years. However, because there is no support for the pension costs, we cannot express an opinion concerning any potential under or over claim of costs.

Throughout our review we requested information to use in determining the percentage of Medicare work that was performed by the Provider Audit unit. Horizon acknowledged this in a February 3, 2003 letter when it quoted us as requesting data "for the earlier years (mid to late 1980's)" and only provided data for 1991 through 2000. Horizon informed us that it could not produce the required information by pension plan prior to 1994. For 1991 through 1993, Horizon was able to provide allocation data in the aggregate for both plans.

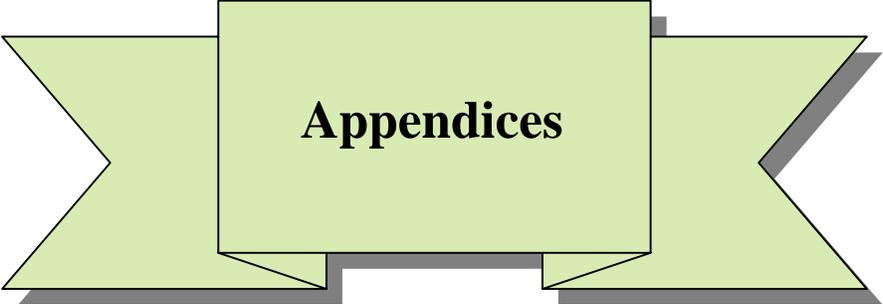
For those years that Horizon provided us with data to verify the costs claimed on its FACPs (FYs 1991 to 2000), we materially agreed that the pension costs shown on the cost classification report were the costs allocated to the contract. For those years that Horizon could not provide data (FYs 1986 to 1990), we expressed no opinion on the accuracy of the claimed pension costs shown on the cost classification report since we were not supplied with support for the allocation of pension costs to the contract. Therefore, we were not able to verify percentages prior to 1991 and were not able to determine if those costs actually contributed to a larger share of the resulting surplus.

### **Unfunded Costs Claimed**

We do not agree with Horizon's assertion that its pension plans were over funded. The pension expense reported and allocated to the contract by Horizon's cost accounting department was not related to the funded allowable costs. Therefore, Horizon inadvertently did not fully fund its claimed pension costs.

## **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 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.



**Appendices**

## HORIZON BLUE CROSS BLUE SHIELD OF NEW JERSEY

Report Number: A-07-02-03028

STATEMENT OF MEDICARE

AGGREGATE PERCENTAGES

JANUARY 1, 1986 TO JULY 31, 2000

Description	1986 To						
	1988	1989	1990	1991	1992	1993	1994
	<u>1/</u>						
	<u>2/</u>						
Contribution Value at EOY	<u>3/</u>	\$81,759	\$70,334	\$331,725	\$215,830	\$0	\$371,436
Discount for Interest	<u>4/</u>	<u>(6,231)</u>	<u>(5,360)</u>	<u>(25,282)</u>	<u>(16,449)</u>		<u>(29,099)</u>
Pres Val Contributions	<u>5/</u>	75,528	64,974	306,443	199,381		342,337
Prepayment Credit	<u>6/</u>			2,520			2,022
Pres Value of Funding	<u>7/</u>	<u>75,528</u>	<u>64,974</u>	<u>308,963</u>	<u>199,381</u>		<u>344,359</u>
CAS Funding Target	<u>8/</u>	77,157	62,646	314,192	197,655		348,471
% Funded	<u>9/</u>	97.89%	100.00%	98.34%	100.00%		98.82%
Funded Pension Costs	<u>10/</u>	75,528	62,646	308,963	197,655		344,359
Allowable Interest	<u>11/</u>	<u>4,414</u>	<u>3,661</u>	<u>18,055</u>	<u>11,550</u>		<u>20,733</u>
Allocable Pension Cost	<u>12/</u>	79,942	66,307	327,018	209,205		365,092
FY Pension Costs	<u>13/</u>			261,840	238,659	52,301	273,819
Medicare LOB%	<u>14/</u>			76.1322%	72.8654%	100.0000%	73.5823%
Allowable Pension Cost	<u>15/</u>			<u>\$199,345</u>	<u>\$173,900</u>	<u>\$52,301</u>	<u>\$201,482</u>

Description	1995	1996	1997	1998	1999	2000
Contribution Value at EOY	\$417,633	\$280,673	\$0	\$0	\$0	\$0
Discount for Interest	<u>(32,718)</u>	<u>(21,988)</u>				
Pres Val Contributions	384,915	258,685				
Prepayment Credit						
Pres Value of Funding	<u>384,915</u>	<u>258,685</u>				
CAS Funding Target	394,938	265,420				
% Funded	<u>97.46%</u>	<u>97.46%</u>				
Funded Pension Costs	384,915	258,685				
Allowable Interest	<u>23,175</u>	<u>15,575</u>				
Allocable Pension Cost	408,090	274,260				
FY Pension Costs	397,341	307,717	68,565			
Medicare LOB%	78.3588%	76.6986%	84.5649%			
Allowable Pension Cost	\$311,351	\$236,015	\$57,982			

**HORIZON BLUE CROSS BLUE SHIELD OF NEW JERSEY**  
**Report Number: A-07-02-03028**  
**STATEMENT OF MEDICARE**  
**AGGREGATE PERCENTAGES**  
**JANUARY 1, 1986 TO JULY 31, 2000**

**FOOTNOTES**

- 1/ Horizon could not provide documentation for the years 1986 and 1987. Also, for the years 1986 through 1988, Horizon did not make contributions to the pension plan per its Update of Segment Assets and did not claim pension costs per its computation of CAS pension costs.
- 2/ Horizon did not claim pension costs per its FACPs for the years 1989 and 1990. Horizon did make contributions to the Medicare segment of its Management Plan for these years. Based on these contributions, we have computed allocable costs for Horizon. However, because Horizon could not supply documentation to verify that it in fact had not claimed the pension costs for the years 1989 and 1990, we cannot express an opinion on any potential under claim of pension costs for these years.
- 3/ We obtained Medicare segment contribution amounts from Horizon's reconstructed Update of Segment Assets that were reviewed and accepted by the CMS actuaries. The contributions included deposits made during the plan year and accrued contributions deposited after the end of the plan year but within the time allowed for filing tax returns.
- 4/ We subtracted interest that is included in the contributions deposited after January 1 of each year to discount the contributions back to their beginning of the year value. For purposes of this appendix, we computed the interest as the difference between the present value of contributions, at the valuation interest rate, and the actual contribution amounts.
- 5/ 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.
- 6/ A prepayment credit represents the premature funding from the previous year(s). A prepayment credit is created when contributions, plus interest, exceed the end-of-year CAS funding target. A prepayment credit may be carried forward, with interest, to fund future CAS pension costs.
- 7/ The present value of funding represents the present value of contributions plus prepayment credits. This is the amount of funding that is available to cover the CAS funding target measured at January 1 of each year.

**HORIZON BLUE CROSS BLUE SHIELD OF NEW JERSEY**  
**Report Number: A-07-02-03028**  
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**JANUARY 1, 1986 TO JULY 31, 2000**

- 8/ The CAS funding target must be funded by current or prepaid contributions to satisfy the funding requirement of FAR 31.205-6(j)(3)(I).
- 9/ The percentage of costs funded is a measure of the portion of the CAS funding target that was funded during the plan year. Since any funding in excess of the CAS funding target is considered premature funding in accordance with CAS 412.50(a)(7), we determined that the funded ratio may not exceed 100 percent. We computed the percentage funded as the present value of funding divided by the CAS funding target. For purposes of illustration, the percentage of funding has been rounded to four decimals.
- 10/ We computed the funded CAS pension cost as the CAS funding target multiplied by the percent funded.
- 11/ We assumed interest on the funded CAS pension cost is to accrue 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 the quarter.
- 12/ The allocable CAS pension cost is the amount of pension cost that may be allocated for contract cost purposes.
- 13/ We converted the plan year allowable CAS pension costs to a fiscal year basis (October 1 through September 30). We calculated the fiscal year pension costs as one-fourth (1/4) of the prior year's costs plus three-fourths (3/4) of the current year's costs. Costs charged to the Horizon's Medicare contract should consist of the Medicare segment's direct pension costs. Horizon chose not to claim costs for its indirect segment.
- 14/ We calculated allowable pension costs for the Medicare segment based on the direct Medicare line of business (LOB) percentage for the segment. We obtained the direct percentage from documents provided by Horizon.
- 15/ We computed the allowable Medicare pension cost as the Fiscal Year pension cost multiplied by the Medicare LOB percentage.



Horizon Blue Cross Blue Shield of New Jersey

**William J. Frantel**  
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November 6, 2003

*Via Facsimile and Federal Express*

Mr. James P. Aasmundstad  
Regional Inspector General for Audit Services  
Office of Inspector General  
Offices of Audit Services  
Department of Health & Human Services  
Region VII  
601 East 12<sup>th</sup> Street  
Room 284A  
Kansas City, MO 64106

Re: Report Number A-07-03-03045

Dear Mr. Aasmundstad:

Horizon Blue Cross Blue Shield of New Jersey ("Horizon") submits this letter in response to the above-referenced draft report entitled "Review of Pension Costs Claimed for Medicare Reimbursement by Horizon Blue Cross Blue Shield of New Jersey," dated October 2003 (hereafter "Draft Pension Costs Report"). This response is timely in that it is submitted on November 6, 2003, prior to the November 9, 2003 due date for the response. This response also addresses the earlier draft report number A-07-02-03028 entitled "Audit of the Pension Plan at a Terminated Medicare contractor, Horizon Blue Cross Blue Shield of New Jersey" for the period January 1, 1986 through July 31, 2000 (hereafter "Draft Pension Surplus Report"), because some of the government's audit comments are inconsistent between the two reports. In its September 12, 2002 response to the Draft Pension Surplus Report, Horizon reserved the right to provide additional comments following receipt of the Draft Pension Costs Report. (Letter from Pamela T. Miller to James Aasmundstad dated September 12, 2003, at page 3.)

On page 3 of the Draft Pension Costs Report, footnote number two (under the *Pension Cost Claimed Variance* table) you indicate that cost claims for the years 1989 and 1990 were not recognized because Horizon could not supply documentation to verify that it had not claimed pension costs for those years. You state:

Horizon did not claim pension costs per its FACPs for the years 1989 and 1990. Horizon did make contributions to the Medicare segment of its Management Plan for these years. Based on these contributions, we have computed allocable costs for Horizon. See Appendix A. However, because Horizon could not supply documentation to verify that it in fact had not claimed pension costs for the years 1989 and 1990, we cannot express any opinion on any potential claim of pension costs for those years. (Draft Pension Costs Report, at footnote 2.)

Horizon did in fact supply the government with the FACPs for the 1989 and 1990 years. On those filings, Horizon clearly indicated that it was not claiming any pension costs for these two years. Those filings were audited by the OIG and there were no findings related to the inclusion of pension costs in any other expense categories. We are unaware of any request from the auditors for additional documentation to verify that Horizon had not claimed costs for these years. Horizon's position is that it should be allowed to claim the pension costs for these two years. However, if the final OIG determination is that the amounts are not eligible to be claimed, Horizon submits that consistency requires these amounts (with compounded investment return through the contract settlement date) to be removed from the resulting Medicare surplus.

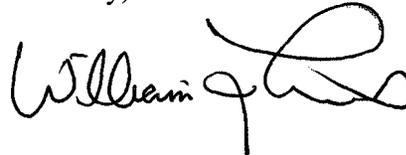
On page 5 of the Draft Pension Costs Report, Medicare LOB percentages are applied to the annual Allocable Pension Costs to determine the annual Allowable Pension Costs. We believe that this is an inconsistent application of the percentages used in this Draft Pension Costs Report as compared to those used in the Draft Pension Surplus Report. Although Medicare percentages are used in the Draft Pension Costs Report for the years 1991 through 1997, where there are allowable pension costs (for the Horizon Management Plan only), the Draft Pension Surplus Report for the Horizon Management Plan uses an average of the 1994 through 2000 Medicare percentages. We submit that consistent application of the Medicare percentages requires that: (1) the percentage applied in the Draft Pension Surplus Report reflect only the years for which there were Allowable Pension Costs and (2) higher weights be given to the earlier years' percentages since these years costs contributed to a larger share of the resulting surplus (due to the additional years of compounded investment return which applied).

Finally, within the "Summary of Findings" of the Executive Summary and in the second paragraph on page 3 of the Draft Pension Costs Report, you identify the primary cause for the cost "over claim" was that Horizon did not fully fund the costs claimed for the years 1993 and 1997 through 2000. Specifically, you state "The primary cause for the over claim was that Horizon did not fully fund the costs claimed for the years 1993 and 1997 through 2000." (Draft Pension Costs Report, at page 3.) We do not agree with this reasoning. Horizon did in fact fund the pension plans during these years. The over claim is primarily the result of having the costs that were originally claimed on the annual Final Administrative Cost Proposals ("FACPs") disallowed during the audit process. During the audit of the annual pension costs, the annual costs were recomputed by Horizon's actuary and several years were then determined to have no pension cost allocable to the Medicare segment due to the segment's overfunded position.

In summary, we disagree with (1) the inconsistencies between the Draft Pension Costs Report and the Draft Pension Surplus Report, specifically in regard to 1989 and 1990 costs and the Medicare LOB percentages, and (2) your statement that the primary cause for the over claim was that Horizon did not fully fund the costs claimed for the years 1993 and 1997 through 2000. We request that the two reports be consistent in their treatment of these issues.

If you have any questions regarding this response, please contact me at (973) 466-8600. We appreciate your consideration of the issues raised in our response.

Sincerely,

A handwritten signature in black ink, appearing to read "William Frantel". The signature is fluid and cursive, with a large, stylized initial "W".

William Frantel

cc: Scott Englund, Department of Health and Human Services  
Christine Simpson, Esq., CMS  
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**AUDIT REPORT NUMBER: A-07-03-03045**  
**Horizon Blue Cross Blue Shield of New Jersey**

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INFORMATION REGARDING THIS AUDIT REPORT**

Greg Tambke, Audit Manager  
Scott Englund, Senior Auditor  
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Office Administrative Personnel