



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General
Offices of Audit Services

November 5, 2004

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

Report Number: A-07-04-00171

Donald L. Fisher
Vice President
Compensation, Benefits, HRIS, and Risk Management
Highmark, Inc.
1800 Center Street
P.O. Box 890089
Camp Hill, Pennsylvania 17089-0089

Dear Mr. Fisher:

Enclosed are two copies of the Department of Health and Human Services (HHS), Office of Inspector General (OIG) report entitled "Review of Pension Costs Claimed for Medicare Reimbursement by Pennsylvania Blue Shield for Fiscal Years 1992 Through 1997." A copy of this report will be forwarded to the HHS action official noted on the next page for her review and any action deemed necessary.

The action official will make final determination regarding actions taken on all matters in the report. 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), OIG reports are made available publicly to the extent information contained therein is not subject to exemptions of the Act that 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 at (816) 426-3591, ext. 225, or Jenenne Tambke, Audit Manager, at (573) 893-8338, ext. 21, or through email at Jenenne.Tambke@oig.hhs.gov. Please refer to report number A-07-04-00171 in all correspondence.

Sincerely yours,

A handwritten signature in black ink, appearing to read "James P. Aasmundstad".

James P. Aasmundstad
Regional Inspector General
for Audit Services

Enclosure - as stated

Direct Reply to HHS Action Official:

Nancy B. O'Connor
Acting Regional Administrator, Region III
Centers for Medicare & Medicaid Services
Public Ledger Building, Suite 216
150 South Independence Mall West
Philadelphia, Pennsylvania 19106

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF PENSION COSTS
CLAIMED FOR MEDICARE
REIMBURSEMENT BY PENNSYLVANIA
BLUE SHIELD FOR FISCAL YEARS
1992 THROUGH 1997**



**NOVEMBER 2004
A-07-04-00171**

Office of Inspector General

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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

BACKGROUND

Pennsylvania Blue Shield (PBS) administered Medicare Part B operations under cost reimbursement contract with the Centers for Medicare & Medicaid Services (CMS) until it merged with Veritus, Inc. (Veritus) on December 6, 1996, to form Highmark, Inc. (Highmark).

On December 31, 1997, Highmark merged the Veritus pension plan into the PBS pension plan. Effective January 1, 1998, the PBS plan was amended and restated, and became the pension plan for Highmark. For the purposes of this report, the term PBS will be used to address the findings concerning the Part B pension costs claimed for fiscal years (FY) 1992 through 1997.

Medicare reimburses it's a portion of contractors' annual pension costs. In claiming costs, contractors are to follow cost reimbursement principles contained in Federal Acquisition Regulations (FAR), Cost Accounting Standards (CAS), and the Medicare contracts.

The Medicare contracts provide for either an allocation or a separate calculation of pension costs. However, the separate calculation method must be used if there is a material difference between the two methods.

OBJECTIVE

The objective of our review was to determine the allowability of pension costs claimed for Medicare reimbursement for FY 1992 through 1997.

FINDING

The PBS did not incur nor claim pension costs for FY 1992 and 1993. However, PBS underclaimed allowable Medicare pension costs for FY 1994 through 1997. During this period, the allowable Medicare pension costs were \$8,271,992. However, PBS claimed pension costs of \$4,978,167 for Medicare reimbursement. The underclaim occurred because PBS did not correctly identify its Medicare segment in accordance with its Medicare contract. As a result, PBS did not claim \$3,293,825 of allowable pension costs.

RECOMMENDATION

We recommend that PBS revise its Final Administrative Cost Proposals (FACP) to claim allowable CAS pension costs of \$3,293,825 for FY 1994 through 1997.

AUDITEE'S COMMENTS

The PBS's comments are summarized in the following paragraphs, and its redacted comments are presented in its entirety on appendix B.

The PBS disagreed with our report and stated that it:

“... does not concur that PBS should decrease the accumulated reassignable pension costs of the Medicare segment by \$2,154,481 as of December 31, 1996, because PBS did not have adequate controls in place to ensure that reassignable pension costs were identified and properly accounted for in accordance with CAS requirements.”

The PBS contends that:

- OIG assigned certain participants to incorrect segments
- most of the OIG’s findings concerning the understatement of segment assets was due to a retroactive application of a recent decision handed down by the U.S. Court of Appeals concerning reassignable pension costs
- OIG incorrectly identified PBS’s Medicare segment cost centers

Additionally, PBS disputed our identification of pension costs it claimed per its FACP and provided restated pension costs.

OIG RESPONSE

We partially disagree with PBS’s assertion concerning pension costs claimed by PBS for Medicare reimbursement for FY 1992 through 1997.

Our identification of the Medicare segment assets was in accordance with the Medicare contract, and the update of assets was in accordance with CAS 412 and 413. During the course of the audit, we reviewed our identification of the participants and cost centers comprising the Medicare segment with representatives of PBS and obtained their concurrence. The findings and recommendation of this report are based upon that identification.

Also, PBS could not provide documentation supporting the restated pension costs. Therefore, our position has not changed and we recommend that PBS revise its FACP to claim allowable CAS pension costs of \$3,293,825 for FY 1994 through 1997.

However, we acknowledge that a recent decision by the U.S. Court of Appeals affected the method used by PBS to measure and assign pension costs to periods. The method employed by CMS actuaries reflected this decision and did have a material impact upon the difference between claimed and allowable pension costs used to update the Medicare assets.

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Glossary of Abbreviations and Acronyms

CAS	Cost Accounting Standards
CMS	Centers for Medicare and Medicaid Services
FACP	Final Administrative Cost Proposal
FAR	Federal Acquisition Regulations
FY	Fiscal Year
HHS	U.S. Department of Health and Human Services
OIG	Office of Inspector General
PBS	Pennsylvania Blue Shield

INTRODUCTION

BACKGROUND

PBS

The PBS administered Medicare Part B operations under a cost reimbursement contract with CMS from the inception of Medicare until it merged with Veritus on December 6, 1996, to form Highmark.

On December 31, 1997, Highmark merged the Veritus pension plan into the PBS pension plan. Effective January 1, 1998, the PBS plan was amended and restated, and became the pension plan for Highmark. For the purposes of this report, the term PBS will be used to address the findings concerning the Part B pension costs for FY 1992 through 1997.

Medicare

Medicare reimburses a 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 FAR.

Additionally, CMS incorporated specific segmentation language into Medicare contracts starting with FY 1988. 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.

Regulations

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 Regulations and Cost Accounting Standards 412 and 413.”

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

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 gains and losses, and assignment of gains and losses to cost accounting periods.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

The objective of our review was to determine the allowability of pension costs claimed by PBS for Medicare reimbursement for FY 1992 through 1997.

Scope

We reviewed pension costs claimed on PBS's FACP's for Medicare reimbursement for FY 1992 through 1997. Achieving the objective did not require that we review the overall internal control structure of PBS. However, we did review the controls relating to the pension costs claimed for Medicare reimbursement to ensure that pension costs were allowable in accordance with CAS and funded in accordance with FAR.

We performed onsite audit work at PBS's corporate office in Camp Hill, PA.

Methodology

We identified PBS's CAS pension costs for the total company and for the Medicare segment. We also determined the extent to which PBS funded CAS pension costs with contributions to the pension trust fund and accumulated prepayment credits. Using this information, we calculated CAS pension costs that are allowable for Medicare reimbursement for FY 1992 through 1997. The calculations were based on separately computed CAS pension costs for the Medicare segment and total company CAS pension costs. The CMS Office of the Actuary developed the methodology used for computing allowable CAS pension costs based on PBS's historical practices. Appendix A contains the details on the pension costs and contributions.

In performing our review, we used information provided by PBS's actuarial consulting firm. The information included assets, liabilities, normal costs, contributions, benefit payments, investment earnings, and administrative expenses. We examined PBS's accounting records, pension plan documents, annual actuarial valuation reports, and Department of Labor/Internal Revenue Service Form 5500s.

This review was done in conjunction with our review of PBS's pension segmentation (A-07-04-00169) and unfunded costs (A-07-04-00173). The information obtained and reviewed during the audits also was used in performing this review.

Our review was performed in accordance with generally accepted government auditing standards.

FINDING AND RECOMMENDATION

The PBS did not incur nor claim pension costs for FY 1992 and 1993. However, PBS underclaimed allowable Medicare pension costs for FY 1994 through 1997. During this period, the allowable Medicare pension costs were \$8,271,992. However, PBS claimed pension costs of

\$4,978,167 for Medicare reimbursement. The underclaim occurred because PBS did not correctly identify its Medicare segment in accordance with its Medicare contract. As a result, PBS did not claim \$3,293,825 of allowable pension costs.

CRITERIA - MEDICARE CONTRACT

The Medicare contract states:

“The term “Medicare Segment” shall mean any organizational component of the contractor, such as a division, department, or other similar subdivision, having a significant degree of responsibility and accountability for the Medicare contract/agreement, in which:

1. The majority of the salary dollars is allocated to the Medicare agreement/contract; or
2. Less than a majority of the salary dollars is allocated to the Medicare agreement/contract, and these salary dollars represent 40 percent or more of the total salary dollars allocated to the Medicare agreement/contract.”

Furthermore, 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 Regulations and Cost Accounting Standards 412 and 413.”

CONDITION - UNDERCLAIM OF \$3,293,825

The PBS under claimed \$3,293,825 of allowable pension costs. For FY 1992 through 1997, PBS charged \$4,978,167 of pension costs to Medicare. However, the allowable CAS pension costs for the period were \$8,271,992.

We compared our calculated allowable CAS pension costs to the pension costs claimed on PBS’s FACP:

Pension Cost Claimed Variance			
FISCAL YEAR	PER OIG	PER PBS	DIFFERENCE
1992	\$0	\$0	\$0
1993	0	0	0
1994	303,825	122,679	181,146
1995	1,627,892	824,482	803,410
1996	2,848,166	1,331,495	1,516,671
1997	<u>3,492,109</u>	<u>2,699,511</u>	<u>792,598</u>
Total	<u>\$8,271,992</u>	<u>\$4,978,167</u>	<u>\$3,293,825</u>

CAUSE - LACK OF ADEQUATE CONTROLS

The PBS did not have adequate controls to ensure that the Medicare segment was identified in accordance with the Medicare contract and the Medicare segment pension assets were updated in accordance with CAS 412 and 413.

EFFECT - UNDERCLAIMED COSTS OF \$3,293,825

The PBS underclaimed \$3,293,825 of allowable CAS pension costs.

RECOMMENDATION

We recommend that PBS revise its FACP to claim allowable CAS pension costs of \$3,293,825 for FY 1994 through 1997.

AUDITEE'S COMMENTS

The PBS's comments are summarized in the following paragraphs and its redacted comments are presented in its entirety on Appendix B.

The PBS disagreed with our report and stated that it “. . .does not concur that it under claimed \$3,293,825 of allowable pension costs because PBS did not correctly identify its Medicare segment in accordance with its Medicare contract.”

The PBS contends that:

- OIG assigned certain participants to incorrect segments
- most of the OIG's findings concerning the understatement of segment assets was due to a retroactive application of a recent decision handed down by the U.S. Court of Appeals concerning reassignable pension costs
- OIG incorrectly identified PBS's Medicare segment cost centers

Additionally, PBS disputed our identification of pension costs it claimed per its FACPs and provided restated pension costs.

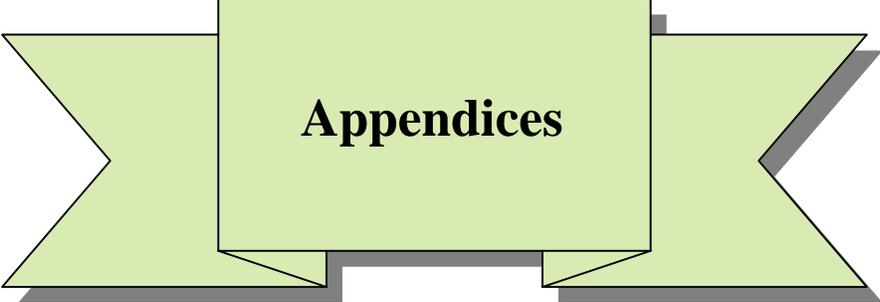
OIG RESPONSE

We partially disagree with PBS's assertion concerning pension costs claimed by PBS for Medicare reimbursement for FY 1992 through 1997.

Our identification of the Medicare segment assets was in accordance with the Medicare contract, and the update of assets was in accordance with CAS 412 and 413. During the course of the audit, we reviewed our identification of the participants and cost centers comprising the Medicare segment with representatives of PBS and obtained their concurrence. The findings and recommendation of this report are based upon that identification.

Also, PBS could not provide documentation supporting the restated pension costs. Therefore, our position has not changed and we recommend that PBS revise its FACP to claim allowable CAS pension costs of \$3,293,825 for FY 1994 through 1997.

However, we acknowledge that a recent decision by the U.S. Court of Appeals affected the method used by PBS to measure and assign pension costs to periods. The method employed by CMS actuaries reflected this decision and did have a material impact upon the difference between claimed and allowable pension costs used to update the Medicare assets.



Appendices

Pennsylvania Blue Shield
Statement of Allowable CAS Pension Costs
For Fiscal Years 1992 Through 1997

Date	Description	Total Company	Other Segment	Medicare Segment
1992	Contributions	<u>1/</u> \$0	\$0	\$0
8.50%	Discount For Interest	<u>2/</u> 0	0	0
1/1/92	Present Value	<u>3/</u> 0	0	0
1/1/92	Prepayment Credit	<u>4/</u> 0	0	0
1/1/92	Present Value Of Funding	<u>5/</u> 0	0	0
1/1/92	Assigned Pension Costs	<u>6/</u> 0	0	0
1/1/92	Absorbed Credit	0	0	0
1/1/92	CAS Funding Target	<u>7/</u> 0	0	0
1/1/92	Percentage Funded	<u>8/</u>	0.00%	0.00%
1/1/92	Funded Pension Cost	<u>9/</u>	0	0
	Allowable Interest	<u>10/</u>	0	0
	Allocable Pension Cost	<u>11/</u>	0	0
	Fiscal Year Pension Cost	<u>12/</u>	0	0
	Medicare LOB Percentage	<u>13/</u>	0.00%	0.00%
	Allowable Pension Cost	<u>14/</u> <u>\$0</u>	<u>\$0</u>	<u>\$0</u>

1993	Contributions	\$0	\$0	\$0
8.50%	Discount For Interest	0	0	0
1/1/93	Present Value	0	0	0
1/1/93	Prepayment Credit	0	0	0
1/1/93	Present Value Of Funding	0	0	0
1/1/93	Assigned Pension Costs	170,000	0	170,000
1/1/93	Absorbed Credit	0	0	0
1/1/93	CAS Funding Target	170,000	0	170,000
1/1/93	Percentage Funded		0.00%	0.00%
1/1/93	Funded Pension Cost		0	0
	Allowable Interest		0	0
	Allocable Pension Cost		0	0
	Fiscal Year Pension Cost		0	0
	Medicare LOB Percentage		0.00%	0.00%
	Allowable Pension Cost	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

Pennsylvania Blue Shield
Statement of Allowable CAS Pension Costs
For Fiscal Years 1992 Through 1997

Date	Description	Total Company	Other Segment	Medicare Segment
1994	Contributions	\$421,804	\$0	\$421,804
8.50%	Discount For Interest	(22,543)	0	(22,543)
1/1/94	Present Value	399,261	0	399,261
1/1/94	Prepayment Credit	0	0	0
1/1/94	Present Value Of Funding	399,261	0	399,261
1/1/94	Assigned Pension Costs	962,212	0	962,212
1/1/94	Absorbed Credit	0	0	0
1/1/94	CAS Funding Target	962,212	0	962,212
1/1/94	Percentage Funded		0.00%	41.49%
1/1/94	Funded Pension Cost		0	399,261
	Allowable Interest		0	22,543
	Allocable Pension Cost		0	421,804
	Fiscal Year Pension Cost		0	316,353
	Medicare LOB Percentage		25.54%	96.04%
	Allowable Pension Cost	<u>\$303,825</u>	<u>\$0</u>	<u>\$303,825</u>

1995	Contributions	\$7,981,344	\$6,879,231	\$1,102,113
8.50%	Discount For Interest	(422,243)	(363,937)	(58,306)
1/1/95	Present Value	7,559,101	6,515,294	1,043,807
1/1/95	Prepayment Credit	0	0	0
1/1/95	Present Value Of Funding	7,559,101	6,515,294	1,043,807
1/1/95	Assigned Pension Costs	4,658,123	3,614,316	1,043,807
1/1/95	Absorbed Credit	0	0	0
1/1/95	CAS Funding Target	4,658,123	3,614,316	1,043,807
1/1/95	Percentage Funded		100.00%	100.00%
1/1/95	Funded Pension Cost		3,614,316	1,043,807
	Allowable Interest		201,892	58,306
	Allocable Pension Cost		3,816,208	1,102,113
	Fiscal Year Pension Cost		2,862,156	932,036
	Medicare LOB Percentage		24.41%	99.70%
	Allowable Pension Cost	<u>\$1,627,892</u>	<u>\$698,652</u>	<u>\$929,240</u>

Pennsylvania Blue Shield
Statement of Allowable CAS Pension Costs
For Fiscal Years 1992 Through 1997

Date	Description	Total Company	Other Segment	Medicare Segment
1996	Contributions	\$4,717,604	\$3,644,402	\$1,073,202
8.50%	Discount For Interest	(251,611)	(194,372)	(57,239)
1/1/96	Present Value	4,465,993	3,450,030	1,015,963
1/1/96	Prepayment Credit	3,147,562	2,199,902	947,660
1/1/96	Present Value Of Funding	7,613,555	5,649,932	1,963,623
1/1/96	Assigned Pension Costs	6,521,985	4,558,362	1,963,623
	Absorbed Credit	0	0	0
	CAS Funding Target	6,521,985	4,558,362	1,963,623
1/1/96	Percentage Funded		100.00%	100.00%
1/1/96	Funded Pension Cost		4,558,362	1,963,623
	Allowable Interest		132,874	57,239
	Allocable Pension Cost		4,691,236	2,020,862
	Fiscal Year Pension Cost		4,674,979	1,791,175
	Medicare LOB Percentage		22.69%	99.79%
	Allowable Pension Cost	<u>\$2,848,166</u>	<u>\$1,060,753</u>	<u>\$1,787,413</u>

1997	Contributions	\$10,617,076	\$8,705,754	\$1,911,322
8.50%	Discount For Interest	(566,839)	(464,795)	(102,044)
1/1/97	Present Value	10,050,237	8,240,959	1,809,278
1/1/97	Prepayment Credit	1,184,353	940,942	243,411
1/1/97	Present Value Of Funding	11,234,590	9,181,901	2,052,689
1/1/97	Assigned Pension Costs	9,987,682	7,934,994	2,052,688
	Absorbed Credit	0	0	0
	CAS Funding Target	9,987,682	7,934,994	2,052,688
1/1/97	Percentage Funded		100.00%	100.00%
1/1/97	Funded Pension Cost		7,934,994	2,052,688
	Allowable Interest		394,469	102,044
	Allocable Pension Cost		8,329,463	2,154,732
	Fiscal Year Pension Cost		7,487,406	2,121,265
	Medicare LOB Percentage		18.32%	99.96%
	Allowable Pension Cost	<u>\$3,492,109</u>	<u>\$1,371,693</u>	<u>\$2,120,416</u>

Pennsylvania Blue Shield
Statement of Allowable CAS Pension Costs
For Fiscal Years 1992 Through 1997

FOOTNOTES

- 1/ We obtained total company contribution amounts and dates of deposit from IRS Form 5500 Reports. 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.
- 2/ 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 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/ A prepayment credit represents the accumulated value of 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.
- 5/ 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.
- 6/ The assigned pension costs, computed at January 1 of each year, provides the basis to compute the allowable pension cost that can be charged to Medicare.
- 7/ 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).
- 8/ 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), 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.
- 9/ We computed the funded CAS pension cost as the CAS funding target multiplied by the percent funded.

Pennsylvania Blue Shield
Statement of Allowable CAS Pension Costs
For Fiscal Years 1992 Through 1997

- 10/ 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 the interest per 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.
- 11/ The allocable CAS pension cost is the amount of pension cost that may be allocated for contract cost purposes.
- 12/ We converted the plan year allocable CAS pension costs to a Federal fiscal year basis (October 1 through September 30). We calculated the fiscal year pension costs as 1/4 of the prior year's costs plus 3/4 of the current year's costs. Costs charged to the Medicare contract should consist of the Medicare segment's direct pension costs plus pension costs attributable to indirect Medicare operations.
- 13/ We calculated the Medicare line of business (LOB), for the segment and indirect operations, based on individual cost center LOB percentages provided by PBS.
- 14/ We computed the allowable Medicare pension cost as the fiscal year pension cost multiplied by the Medicare LOB percentage.



October 14, 2004

Mr. James P. Aasmundstad
Regional Inspector General for Audit Services
DHHS, OIG
601 East 12th Street
Room 284A
Kansas City, Missouri 64106

RE: A-07-04-00169 (“Review of Medicare Contractor’s Pension Segmentation Requirements, Pennsylvania Blue Shield”)
A-07-04-00171 (“Review of Pension Costs Claimed for Medicare Reimbursement by Pennsylvania Blue Shield for Fiscal Year 1992 through 1997”)
A-07-04-00173 (“Audit of Pennsylvania Blue Shield’s Unfunded Pension Costs for the Period covering 1992 through 1996”)

Dear Mr. Aasmundstad:

Attached is our response to your letters dated August 18, 2004, requesting comments on your draft reports A-07-04-00169 entitled, “Review of Medicare Contractor’s Pension Segmentation Requirements, Pennsylvania Blue Shield” for the period covering January 1, 1992 to December 31, 1997; A-07-04-00171 entitled, “Review of Pension Costs Claimed for Medicare Reimbursement by Pennsylvania Blue Shield for Fiscal Year 1992 through 1997;” and A-07-04-00173 entitled, “Audit of Pennsylvania Blue Shield’s Unfunded Pension Costs for the period covering 1992 through 1996.”

If you have any questions, please feel free to contact me at 717-302-4175.

Sincerely,

Donald L. Fisher, Vice President
Compensation, Benefits, HRIS &
Risk Management

cc: James Chiado
Elizabeth Farbacher
Patrick Kiley
Anthony Lobato
Gayeta Porter

Corporate Offices:

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**Review of Pension Costs Claimed
For Medicare Reimbursement by
Pennsylvania Blue Shield**

Fiscal Year 1992 through 1997

**Highmark Comments to OIG Draft Report
A-07-04-00171**

Highmark's Comments on Report Number A-07-04-00171

Highmark does not concur that it under claimed \$3,293,825 of allowable pension costs because PBS did not correctly identify its Medicare segment in accordance with its Medicare contract. Highmark disagrees with OIG's segment assignment of certain participants identified in the attached Exhibits I and II and also believes that a significant portion of the under claim occurred as a result of OIG's retroactive application of a recent decision of the United States Court of Appeals for the Federal Circuit (*Eastman Kodak Company vs. Donald H. Rumsfeld, Secretary of Defense*). Highmark suggests that OIG's audit report should separately identify the amount due to the retroactive application of the recent Kodak "full funding limit" that was not a part of the measurement and assignment practices that were previously followed by either OIG or Highmark's pension actuary, and the amount due to the incorrect assignment of cost centers to the Medicare segment after revising their calculations for the participants identified in Exhibits I and II.

Highmark agrees that several cost centers were incorrectly assigned. Of 58 cost centers that OIG did not include in their identification of the Medicare segment, only 2 (cost centers 129 and 623) were inappropriately assigned to the Medicare segment by PBS. These two cost centers were identified by OIG during their previous pension audit that was completed in 1994. Following receipt of the audit reports in 1994, these cost centers were correctly assigned to the Indirect segment for future valuations.

In addition, OIG inappropriately excluded cost center 106, Medicare Systems Support and Development, from the Medicare segment for 1996 and 1997. This cost center was moved from Xact Medicare Services (Medicare B Business Unit) to the Information Services Group (Corporate Unit) in 1995, but continued to perform anywhere from 90-100% in support of Medicare B activity. The cost center was assigned to the Indirect segment in 1995 in error by Pennsylvania Blue Shield, but reassigned to the Medicare B segment in 1996 and 1997. OIG correctly reassigned the participants in cost center 106 to the Medicare B segment in 1995, but transferred them to the Indirect segment in 1996 and 1997 in error. The other cost centers, which were originally assigned to the Medicare segment, had not been closed in the Financial system, but were excluded by the PBS pension actuary prior to completing the pension valuation, because there were no participants in those cost centers.

There were 32 cost centers that OIG included in the identification of the Medicare segment that were missing for one or more years from the cost center listing that Highmark provided. Of the 32 cost centers identified by OIG, only 4 cost centers (031, 163, 250 and 384) that contained participants, were not appropriately assigned to the Medicare segment by Highmark's actuary. Cost center 005, SVP, Government Business, was transferred from the Medicare B segment during 1996 to the Indirect segment. Prior to August 1996, the cost center supported Medicare B but, after the transfer, no cost was allocated to the Medicare B line of business. Therefore, this cost center was appropriately assigned to the Indirect segment by Highmark's actuary for 1997. In addition, Highmark's pension actuary utilizes a segment indicator on all participants (actives, retirees and vested terms); therefore, it is not necessary to continue to identify cost centers for retirees or terminated participants. The segment indicator for retirees and vested terms doesn't change following termination. Most of the remaining cost centers, which were not assigned to the Medicare segment, had no active employees, or the employees were correctly assigned by Highmark's pension actuary.

In order to identify differences between OIG's and Pennsylvania Blue Shield's assignment of participants to the Medicare B segment, Highmark's pension actuary compared OIG participant listings for each year with their valuation files. Any differences were researched to determine the correct segment assignment, using the Medicare definition of segment as: "any organizational component of the contractor, such as, division, department, or other similar subdivision, having a significant degree of responsibility and accountability for the Medicare contract/agreement in which the majority of the salary dollars is allocated to the Medicare agreement/contract." Based on Highmark's research, Highmark believes that OIG was incorrect on the segment assignment for the participants listed on the attached Exhibits I and II. The exhibits identify the participants, the participant's cost center, the valuation years impacted, and an explanation for why Highmark believes that OIG should change their segment assignment and recalculate the impact on the allowable Medicare pension costs.

In addition, Highmark does not concur with the data presented in the "Per PBS" column contained in the "Pension Cost Claimed Variance" chart located on page 3 of the OIG report.

As disclosed to the OIG auditors, when reviewing our pension workpapers in relation to this audit, we uncovered several discrepancies in the compilation of information used to prepare the "informational breakout" pension figures listed on the FACP Cost Classification Reports.

The pension costs claimed in the FACP's were appropriate, however, the informational breakout numbers in several of the fiscal years contained misstatements. The chart below shows informational pension data consistent with that originally reported on the FACP Cost Classification Reports as well as restated informational pension data. We believe the data in column D in the chart below [restated pension data (column B) less non-qualified pension expense (column C)] is the appropriate amount to use in determining the over/under statement of expense in comparison to the OIG findings. This information was provided to the OIG auditors during the pension audit.

In addition, it appears that in FY 1994 & 1995, the "Per PBS" column in the OIG original chart includes both qualified and non-qualified pension, while the remaining years appear to include the qualified plan amount only. We believe this chart should reference only qualified pension amounts.

Comparison Schedule for Pension Amounts

	(a)	(b)	(c)	(d = b-c)
	<u>Total Pension Exp on FACP CCR</u>	<u>Total Pension Exp Restated</u>	<u>Less Non-Qualified Pension Exp</u>	<u>Qualified Pension Exp Claimed on FACP</u>
FY 1992	\$ 7,251	\$ 7,251	\$ 7,251	\$ -
FY 1993	-	-	-	-
FY 1994	121,662	122,679	29,156	93,523
FY 1995	824,482	795,225	15,619	779,606
FY 1996	1,540,703	1,533,957	209,208	1,324,749
FY 1997	2,874,829	2,697,974	211,038	2,486,936
	<u>\$ 5,368,927</u>	<u>\$ 5,157,086</u>	<u>\$ 472,272</u>	<u>\$ 4,684,814</u>

Participants not included in the Medicare B Segment by OIG that should be

Segment	Cost Center		Valuation Impacted	Explanation
	Number	Name		
Medicare B	186	Medicare Medical Director	1994 1995	Based on provisions of Pennsylvania Blue Shield's pension plan, became 100% vested when he reached age 65 in 1979, with 5 years of credited service from 1970-1975. He is an eligible retiree who terminated from a cost center that allocated more than 50% to Medicare B. was not considered an eligible participant prior to 1994 but, upon research, Pennsylvania Blue Shield determined that he was entitled to a benefit under the Plan. He was credited with 5 years of service, and a liability was established for his benefit in 1994.
Medicare B	020	Medicare Incoming Mail	1995 1996 1997	Participant is a retiree who terminated in 1986 from a cost center that allocated more than 50% to Medicare. Because participant was not identified as an exception during OIG's initial audit of Pennsylvania Blue Shield pension costs and segmentation, Highmark believes that Participant's assignment to the Medicare segment was appropriate.
Medicare B	399	Provider Telephone and General Inquiry Services	1995 1996 1997	Participant is a retiree who terminated in 1988 from a cost center that allocated more than 50% to Medicare. Because participant was not identified as an exception during OIG's initial audit of Pennsylvania Blue Shield pension costs and segmentation, Highmark believes that Participant's assignment to the Medicare segment was appropriate. Participant returned to work in a part-time position in 1995, but didn't accrue any additional service.
Medicare B	020	Medicare Incoming Mail	1995 1996	Participant is a retiree who terminated in 1979 from a cost center that allocated more than 50% to Medicare. Because participant was not identified as an exception during OIG's initial audit of Pennsylvania Blue Shield pension costs and segmentation, Highmark believes that Participant's assignment to the Medicare segment was appropriate.
Medicare B	398	Medicare Beneficiary Telephone Services	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.

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Participants not included in the Medicare B Segment by OIG that should be

Segment	Cost Center		Valuation Impacted	Explanation
	Number	Name		
Medicare B	914	Medicare Appeals	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	121	Medicare Microfilming	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	687	Medicare Medical Unit A	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	398	Medicare Beneficiary Telephone Services	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	185	Medicare Medical Review	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	211	Medicare Accounts Receivable	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	398	Medicare Beneficiary Telephone Services	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	431	Medicare Provider Telephone Services	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	686	Xact Medicare Clerical Specialties	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	431	Medicare Provider Telephone Services	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.

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Participants not included in the Medicare B Segment by OIG that should be

Segment	Cost Center		Valuation Impacted	Explanation
	Number	Name		
Medicare B	164	Xact Development Select Claims Adjudication	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	1049	Medical Unit B	1996	Participant is a vested termination who terminated in 1995 from a cost center that allocated more than 50% to Medicare.
Medicare B	020	Medicare Incoming Mail (Spouse)	1997	Surviving spouse of [redacted] who retired from cost center 020 in the Medicare B segment.
Medicare B	433	General Information	1997	Participant is a vested termination who terminated 1996 from a cost center that allocated more than 50% to Medicare.

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Participants not included in the Medicare B Segment by OIG that should be

	Segment	Cost Center		Valuation Impacted	Explanation
		Number	Name		
Data Redacted by OAS Auditors.	Medicare B	106	Medicare Systems Support and	1996	This cost center was moved from HGSA (Government Business Unit) to ISG (Corporate Unit) in 1995, but continued to perform anywhere from 90-100% in support of Medicare B activity. This cost center should be included in the Medicare B segment for 1996 and 1997. In 1998, it was moved to the Indirect segment as a consequence of the new cost allocation system, where it became part of the allocation of centralized services.
	Medicare B	106	Development	1996 & 1997	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1997	
	Medicare B	106		1996	
	Medicare B	106		1996	
	Medicare B	106		1996	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996	
	Medicare B	106		1996	
	Medicare B	106		1996	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996 & 1997	
	Medicare B	106		1996	
	Medicare B	106		1996	
	Medicare B	106		1996-1997	
Medicare B	106		1996		

Participants included in the Medicare B Segment by OIG that should not be

Segment	Cost Center		Valuation Impacted	Explanation
	Number	Name		
Indirect	005	SVP, Govt Business, thru July 1996. Name changed to SVP, Middle Atlantic Region, during August 1996.	1997	Cost center was transferred from Medicare B segment during 1996 to the Indirect Segment. Through July 1996, the cost center supported Medicare B, but after transfer, no cost was allocated to the Medicare B line of business. As of 12/31/96, the cost center should be assigned to the Indirect segment.
Indirect	005	SVP, Govt Business, thru July 1996. Name changed to SVP, Middle Atlantic Region, during August 1996.	1997	Cost center was transferred from Medicare B segment during 1996 to the Indirect Segment. Through July 1996, the cost center supported Medicare B, but after transfer, no cost was allocated to the Medicare B line of business. As of 12/31/96, the cost center should be assigned to the Indirect segment.
Indirect	189	PA/DE Champus	1994 1995 1996 1997	Participant is a retiree who terminated in 1981 from a cost center that allocated less than 50% to Medicare B. Because participant was not identified as an exception during OIG's initial audit of Pennsylvania Blue Shield pension cost and segmentation, Highmark believes that Participant's assignment to the Indirect segment was appropriate.
Indirect	077	Employee Relations	1994 1995 1996 1997	Participant is a retiree who terminated in 1984 from a cost center that allocated less than 50% to Medicare B. Because participant was not identified as an exception during OIG's initial audit of Pennsylvania Blue Shield pension cost and segmentation, Highmark believes that Participant's assignment to the Indirect segment was appropriate.
Indirect	375	Assistant Controller Cost Accounting	1996	The cost center moved in February 1996 from Xact (Director Medicare Financial Services) to Corporate Finance and supported the entire corporation. In 1996, less than 50% of this cost center was allocated to Medicare B.

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