



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General
Offices of Audit Services

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

APR 11 2006

Report Number: A-07-06-00198

R. Paul Warburton, CPA, Director of Finance
Regence Blue Cross Blue Shield of Utah
2890 East Cottonwood Parkway
Salt Lake City, Utah 84121-7035

Dear Mr. Warburton:

Enclosed are two copies of the U.S. Department of Health and Human Services (HHS), Office of the Inspector General (OIG) report titled "Audit of Blue Cross Blue Shield of Utah's Unfunded Pension Costs for 1986 Through 1997." A copy of this report will be forwarded to the HHS action official noted on the next page for his review and any action deemed necessary.

The HHS 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 to the public 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, or Jenenne Tambke, Audit Manager, at (573) 893-8338, extension 21, or through email at Jenenne.Tambke@oig.hhs.gov. Please refer to report number A-07-06-00198 in all correspondence.

Sincerely,

Patrick J. Cogley
Regional Inspector General
for Audit Services

Enclosures

Page 2 – Mr. R. Paul Warburton

Direct Reply to HHS Action Official:

Mr. Alex Trujillo
Regional Administrator, Region VIII
Centers for Medicare & Medicaid Services
Colorado State Bank Building
1600 Broadway, Suite 700
Denver, Colorado 80202

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**AUDIT OF BLUE CROSS BLUE SHIELD
OF UTAH'S UNFUNDED PENSION
COSTS FOR 1986 THROUGH 1997**



**Daniel R. Levinson
Inspector General**

**APRIL 2006
A-07-06-00198**

Office of Inspector General

<http://oig.hhs.gov>

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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 HHS divisions will make final determination on these matters.



EXECUTIVE SUMMARY

BACKGROUND

Blue Cross Blue Shield of Utah (Utah) administered Medicare Parts A and B operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS) until Utah merged with The Regence Group on January 1, 1998.

Starting with fiscal year 1988, CMS incorporated segmentation requirements into Medicare contracts. The contracts specify segmentation requirements and require separate identification of unfunded costs for the Medicare segment and the business units comprising the rest of the company, which are aggregated and identified as the “Other” segment.

OBJECTIVES

Our objectives were to:

- determine if pension costs for plan years 1986 through 1997 were funded in accordance with the Federal Acquisition Regulations and the Cost Accounting Standards and
- identify and properly account for any accumulated unfunded pension costs, including unallowable and reassignable portions.

SUMMARY OF FINDING

Utah did not properly fund the pension costs allocable to the Medicare contracts for plan years 1993 and 1995. In addition, Utah did not identify or properly account for accumulated unfunded pension costs. As a result, Utah understated the January 1, 1998, accumulated unallowable pension costs by \$202,066 (\$174,774 for the Other segment plus \$27,292 for the Medicare segment).

RECOMMENDATION

We recommend that Utah identify accumulated unallowable pension costs of \$202,066 (\$174,774 for the Other segment plus \$27,292 for the Medicare segment) as of January 1, 1998.

AUDITEE’S COMMENTS

Utah concurred with our recommendation. Utah’s comments are included in their entirety as the appendix.

OFFICE OF INSPECTOR GENERAL’S RESPONSE

We commend Utah for its action to address the recommendation.

INTRODUCTION

BACKGROUND

Utah and Medicare

Blue Cross Blue Shield of Utah (Utah) administered Medicare Parts A and B operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS) until Utah merged with The Regence Group on January 1, 1998. In claiming costs, contractors must follow cost reimbursement principles contained in the Federal Acquisition Regulations (FAR), Cost Accounting Standards (CAS), and Medicare contracts.

Since its inception, Medicare has paid a portion of the annual contributions made by contractors to their pension plans. The payments are allowable pension costs under the FAR and its predecessor, Federal Procurement Regulations (FPR). In 1980, the Medicare contracts and the FPR incorporated CAS 412 and 413.

Cost Accounting Standards

The CAS deals with stability between contract periods and requires pension costs to be consistently measured, assigned to contract periods, and allocated to cost objectives, including Federal contracts. On March 30, 1995, the Office of Federal Procurement Policy, Cost Accounting Standards Board, revised the CAS relating to accounting for pension costs applicable with the start of the first accounting period thereafter.

The revised CAS removed the regulatory conflict between the funding limits of the Employees Retirement Income Security Act of 1974 (ERISA) and the period assignment provisions of CAS. The transition provisions of the new rule (48 CFR § 9904.412-64) allow the reassignment of prior period pension costs, with interest, which were not funded because they lacked tax deductibility.

The CAS revision does not remove the requirement to fund pension costs with contributions that are not in conflict with ERISA. If a contractor could have funded pension costs and chose not to, the costs and any accrued interest are unallowable in future periods. The unallowable portion of pension costs must be updated, with interest, per the FAR and CAS.

Federal Acquisition Regulations

The FAR addresses the allowability of pension costs and requires pension costs assigned to contract periods to be substantiated by funding. The FAR, as found at 48 CFR § 31.205-6(j)(3)(i) and (iii), states:

. . . costs of pension plans not funded in the year incurred, and all other components of pension costs . . . assignable to the current accounting period but not funded during it, shall not be allowable in subsequent years . . . Increased pension costs caused by delay in

funding beyond 30 days after each quarter of the year to which they are assignable are unallowable.

OBJECTIVES, SCOPE, AND METHODOLOGY

Objectives

Our objectives were to:

- determine if pension costs for plan years 1986 through 1997 were funded in accordance with the FAR and CAS and
- identify and properly account for any accumulated unfunded pension costs, including unallowable and reassignable portions.

Scope

Our review covered January 1, 1986, to January 1, 1998. Achieving our objectives did not require that we review Utah's overall internal control structure. However, we did review the controls with regard to the funding of pension costs to ensure that the pension costs had been funded in accordance with the CAS and FAR.

We performed this review in conjunction with our audits of Medicare segmentation of pension assets (A-07-05-00190) and pension costs claimed for Medicare reimbursement (A-07-06-00199). We used the information obtained and reviewed during those audits in performing this review.

We performed fieldwork at Utah's office in Salt Lake City, UT, during May 2005.

Methodology

The CMS Office of the Actuary developed the methodology used to compute CAS pension costs based on Utah's historical practices.

In performing this review, we used information provided by Utah's actuarial consulting firms. The information included assets, liabilities, normal costs, contributions, benefit payments, investment earnings, and administrative expenses. We reviewed Utah's accounting records, pension plan documents, annual actuarial valuation reports, and Department of Labor/Internal Revenue Service Form 5500s. Using the documents, CMS pension actuarial staff calculated the assignable CAS pension costs for each year 1986 through 1997 for both the Medicare segment and the Other segment. Additionally, CMS pension actuarial staff determined the extent to which Utah funded the pension costs with contributions to the pension trust fund and prepayment credits. The CMS pension actuarial staff also determined the unallowable and reassignable portions of unfunded pension costs. We reviewed the methodology for the calculations and updated Utah's unfunded pension costs for 1986 through 1997 for both the Medicare segment and the Other segment.

We performed our review in accordance with generally accepted government auditing standards.

FINDING AND RECOMMENDATION

Utah did not properly fund the pension costs allocable to the Medicare contracts for plan years 1993 and 1995. In addition, Utah did not identify or properly account for accumulated unfunded pension costs. As a result, Utah understated the January 1, 1998, accumulated unallowable pension costs by \$202,066 (\$174,774 for the Other segment plus \$27,292 for the Medicare segment).

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. The Medicare contract states that: “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.”

The revised CAS states that if a contractor could have funded pension costs and chose not to, the costs and any accrued interest are unallowable in future periods. The unallowable portion of pension costs must be updated, with interest, per the FAR and CAS.

For plan years 1993 and 1995, we identified \$144,531 and \$4,659, respectively, of pension costs that Utah could have funded with contributions per ERISA, but chose not to. As of January 1, 1998, Utah had accumulated \$202,066 in unallowable pension costs (\$174,774 for the Other segment plus \$27,292 for the Medicare segment). The pension costs are unallowable because they were not funded within specific time periods set by FAR regulations. Imputed interest on the unfunded costs is also unallowable per CAS regulations. The \$202,066 represents unfunded pension costs and imputed interest for years 1993 through 1997.

RECOMMENDATION

We recommend that Utah identify accumulated unallowable pension costs of \$202,066 (\$174,774 for the Other segment plus \$27,292 for the Medicare segment) as of January 1, 1998.

AUDITEE’S COMMENTS

Utah concurred with our recommendation. Utah’s comments are included in their entirety as the appendix.

OFFICE OF INSPECTOR GENERAL’S RESPONSE

We commend Utah for its action to address the recommendation.

APPENDIX

MAILING ADDRESS
 Regence BlueCross BlueShield of Utah
 P. O. Box 30270
 Salt Lake City, Utah 84130-0270



**Regence
 BlueCross BlueShield
 of Utah**

An Independent Licensee of the Blue Cross and Blue Shield Association

2890 East Cottonwood Parkway
 Salt Lake City, Utah 84121-7035
 Tel (801) 333-2000
 Customer Service (801) 333-2100
 www.regence.com

March 31, 2006

Patrick, J. Cogley
 Regional Inspector General for Audit Services
 Dept. of Health & Human Services Region VII
 601 East 12th Street
 Kansas City, Missouri 64106

Re: Report Number: A-07-05-00190
 Report Number: A-07-06-00198
 Report Number: A-07-06-00199

Dear Mr. Cogley

We have reviewed the referenced draft audit reports and include the following written comments for your consideration;

Report Number: A-07-05-00190

"Review of Medicare Contractor's Pension Segmentation Requirements, Blue Cross Blue Shield of Utah for the Period Covering January 1, 1986 to January 1, 1998"

Recommendation: We recommend that Utah identify pension assets of \$2,040,174 for the Medicare segment as of January 1, 1998.

Response: We agree with the recommendation. Regence BlueCross and BlueShield of Utah terminated its Medicare contract effective November 30, 2005.

Report Number: A-07-06-00198

"Audit of BlueCross BlueShield of Utah's Unfunded Pension Cost for 1986 through 1997"

Recommendation: We recommend that Utah identify accumulated unallowable pension costs of \$202,066 (\$174,774 for the other segment plus \$27,292 for the Medicare segment) as of January 1, 1998).

Response: We agree with the recommendation. Regence BlueCross and BlueShield of Utah terminated its Medicare contract effective November 30, 2005.

Report Number: A-07-06-00199

"Review of Pension Costs Claimed for Medicare Reimbursement by Blue Cross Blue Shield of Utah for Fiscal Years 1987 Through 1997."

Recommendation: We recommend that Utah revise its Final Administrative Cost Proposals (FACP) to claim allowable CAS pension cost of \$756,509 for FYs 1987 through 1997.

Response: We agree with the finding. Regence BlueCross and BlueShield of Utah (RBCBSU) terminated its Medicare contract effective November 30, 2005 and will include allowable pension costs of \$756,509 as a part of our global settlement with CMS.

If you have questions or comments concerning our response, please feel free to call me at (801) 333-5294.

Sincerely,

R Paul Warburton
 Director of Finance