



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Office of Audit Services, Region VII
601 East 12th Street, Room 0429
Kansas City, MO 64106

March 25, 2010

Report Number: A-07-09-00312

Ms. Sandy Coston
President and Chief Executive Officer
First Coast Service Options, Inc.
532 Riverside Avenue
Jacksonville, FL 32202

Dear Ms. Coston:

Enclosed is the U.S. Department of Health & Human Services (HHS), Office of Inspector General (OIG), final report entitled *Review of Pension Costs Claimed for Medicare Reimbursement by First Coast Service Options, Inc., for Fiscal Years 2004 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.

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If you have any questions or comments about this report, please do not hesitate to call me at (816) 426-3591, or contact Jenenne Tambke, Audit Manager, at (573) 893-8338 or through email at Jenenne.Tambke@oig.hhs.gov. Please refer to report number A-07-09-00312 in all correspondence.

Sincerely,

/Patrick J. Cogley/
Regional Inspector General
for Audit Services

Enclosure

Direct Reply to HHS Action Official:

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

Department of Health & Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF PENSION COSTS
CLAIMED FOR MEDICARE
REIMBURSEMENT BY
FIRST COAST SERVICE OPTIONS,
INC., FOR FISCAL YEARS
2004 THROUGH 2007**



Daniel R. Levinson
Inspector General

March 2010
A-07-09-00312

Office of Inspector General

<http://oig.hhs.gov>

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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

During our audit period, First Coast Service Options, Inc. (FCSO), administered Medicare Part A and Part B operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS).

FCSO participates in a defined benefit pension plan, which is a deferred compensation plan in which an employer makes actuarially determined contributions to fund an employee's retirement benefit as defined by the plan's terms.

CMS reimburses a portion of the annual contributions that contractors make to their pension plans. In claiming costs, contractors must follow cost reimbursement principles contained in the Federal Acquisition Regulation, Cost Accounting Standards (CAS), and Medicare contracts.

OBJECTIVE

Our objective was to determine the allowability of pension costs that FCSO claimed for Medicare reimbursement for fiscal years (FY) 2004 through 2007.

SUMMARY OF FINDING

FCSO did not claim \$124,189 of pension costs that were allowable for Medicare reimbursement for FYs 2004 through 2007. The underclaim occurred primarily because FCSO based its pension cost calculations on misstated Medicare segment pension assets. FCSO used the incorrect pension cost calculations to claim \$20,878,353 for Medicare reimbursement. We calculated allowable pension costs for FYs 2004 through 2007 in accordance with CAS 412 and 413, as required by the Medicare contracts, to be \$21,002,542, a difference of \$124,189.

RECOMMENDATIONS

We recommend that FCSO:

- increase its Final Administrative Cost Proposal pension costs by \$124,189 and
- ensure that future pension cost claims are in accordance with the Medicare contracts.

AUDITEE COMMENTS

In written comments on our draft report, FCSO agreed with our recommendations. FCSO's comments are included in their entirety as Appendix B.

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INTRODUCTION

BACKGROUND

First Coast Service Options, Inc.

During our audit period, First Coast Service Options, Inc. (FCSO), administered Medicare Part A and Part B operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS).¹

FCSO participates in a defined benefit pension plan, which is a deferred compensation plan in which an employer makes actuarially determined contributions to fund an employee's retirement benefit as defined by the plan's terms.²

Medicare Reimbursement of Pension Costs

CMS reimburses a portion of the annual contributions that contractors make to their pension plans. To be allowable for Medicare reimbursement, pension costs must be (1) measured, assigned, and allocated in accordance with Cost Accounting Standards (CAS) 412 and 413 and (2) funded as specified by part 31 of the Federal Acquisition Regulation (FAR).

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to determine the allowability of pension costs that FCSO claimed for Medicare reimbursement for fiscal years (FY) 2004 through 2007.

Scope

We reviewed \$20,878,353 of pension costs that FCSO claimed for Medicare reimbursement on its Final Administrative Cost Proposals (FACP) for FYs 2004 through 2007. Achieving our objective did not require that we review FCSO's overall internal control structure. However, we reviewed the internal controls related to the pension costs claimed for Medicare reimbursement to ensure that the pension costs were allocable in accordance with the CAS and allowable in accordance with the FAR.

We performed fieldwork at FCSO's office in Jacksonville, Florida, in February and March 2009.

¹ FCSO's parent company, Blue Cross Blue Shield of Florida, Inc., novated the contracts to FCSO effective October 1, 2003. Prior to that, FCSO managed the contracts by special power of attorney on behalf of its parent company.

² FCSO participates in employee benefit plans of its parent company, such as the defined benefit pension plan.

Methodology

We reviewed the applicable portions of the FAR, CAS, and Medicare contracts. Additionally, we reviewed FCSO's FACPs to identify the amount of pension costs claimed for Medicare reimbursement for FYs 2004 through 2007. We also determined the extent to which FCSO funded CAS pension costs with contributions to the pension trust fund and accumulated prepayment credits. We based our calculations on separately computed CAS pension costs for the Medicare segment and the "Other" segment. The CMS Office of the Actuary calculated the allocable CAS pension costs based on FCSO's historical practices and on the results of our segmentation review, *Review of Medicare Contractor's Pension Segmentation Requirements at First Coast Service Options, Inc., for the Period January 1, 2003, to January 1, 2008* (A-07-09-00311).

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

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 finding and conclusions based on our audit objective.

FINDING AND RECOMMENDATIONS

FCSO did not claim \$124,189 of pension costs that were allowable for Medicare reimbursement for FYs 2004 through 2007. The underclaim occurred primarily because FCSO based its pension cost calculations on misstated Medicare segment pension assets. FCSO used the incorrect pension cost calculations to claim \$20,878,353 for Medicare reimbursement. We calculated allowable pension costs for FYs 2004 through 2007 in accordance with CAS 412 and 413, as required by the Medicare contracts, to be \$21,002,542, a difference of \$124,189.

FEDERAL REQUIREMENTS

The Medicare contracts address the determination and allocation of pension costs. The contracts state: "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."

FAR 31.205-6(j) addresses allowability of pension costs and requires that plan contributions substantiate pension costs assigned to contract periods.

CAS 412 addresses the determination and measurement of pension cost components. It also addresses the assignment of pension costs to appropriate accounting periods.

CAS 413 addresses 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.

ALLOWABLE PENSION COSTS NOT CLAIMED

FCSO did not claim \$124,189 of allowable Medicare pension costs for FYs 2004 through 2007. During that period, FCSO claimed pension costs of \$20,878,353 for Medicare reimbursement. We calculated allowable pension costs based on separately computed CAS pension costs for the Medicare segment and the “Other” segment in accordance with CAS 412 and 413. Based on the terms of the Medicare contracts, the allowable CAS pension costs for this period totaled \$21,002,542.

The following table compares allowable CAS pension costs with the pension costs claimed on FCSO’s FACPs. Appendix A contains details on allowable pension costs and contributions.

Comparison of Allowable Pension Costs and Claimed Pension Costs

	Medicare Pension Costs		
	Allowable	Claimed	
Fiscal Year	Per Audit	By FCSO	Difference
2004	\$4,842,392	\$4,824,359	\$18,033
2005	5,125,910	5,019,900	106,010
2006	5,480,423	5,376,181	104,242
2007	5,553,817	5,657,913	(104,096)
Total	\$21,002,542	\$20,878,353	\$124,189

The Medicare contracts require FCSO to calculate pension costs for Medicare reimbursement pursuant to CAS 412 and 413. However, due to misstated Medicare segment pension assets, FCSO based its claim on incorrect pension cost calculations. As a result, FCSO underclaimed \$124,189 of allowable pension costs.

RECOMMENDATIONS

We recommend that FCSO:

- increase its Final Administrative Cost Proposal pension costs by \$124,189 and
- ensure that future pension cost claims are in accordance with the Medicare contracts.

AUDITEE COMMENTS

In written comments on our draft report, FCSO agreed with our recommendations. FCSO’s comments are included in their entirety as Appendix B.

APPENDIXES

**APPENDIX A: ALLOWABLE MEDICARE PENSION COSTS FOR
FIRST COAST SERVICE OPTIONS, INC.,
FOR FISCAL YEARS 2004 THROUGH 2007**

Date	Description	Total Company	"Other" Segment	Medicare Segment	Total Medicare
2003	Plan Year Allowable Pension Cost <u>1/</u>		\$809,240	\$3,933,548	
2004	Contributions <u>2/</u>	\$66,154,448	\$66,154,448	\$0	
7.50%	Discount for Interest <u>3/</u>	(\$4,615,427)	(\$4,615,427)	\$0	
January 1, 2004	Present Value Contributions <u>4/</u>	\$61,539,021	\$61,539,021	\$0	
	Prepayment Credit Applied <u>5/</u>	\$37,453,330	\$32,796,089	\$4,657,241	
	Present Value of Funding <u>6/</u>	\$98,992,351	\$94,335,110	\$4,657,241	
January 1, 2004	CAS Funding Target <u>7/</u>	\$37,453,330	\$32,796,089	\$4,657,241	
	Percentage Funded <u>8/</u>		100.00%	100.00%	
	Funded Pension Cost <u>9/</u>		\$32,796,089	\$4,657,241	
	Allowable Interest <u>10/</u>		\$0	\$0	
	Allocable Pension Cost <u>11/</u>		\$32,796,089	\$4,657,241	
	Medicare LOB* Percentage <u>12/</u>		1.87%	91.52%	
	Plan Year Allowable Pension Cost <u>13/</u>		\$613,287	\$4,262,307	
2004	Fiscal Year Allowable Pension Cost <u>14/</u>		\$662,275	\$4,180,117	\$4,842,392
2005	Contributions	\$53,032,360	\$53,032,360	\$0	
7.50%	Discount for Interest	(\$3,699,932)	(\$3,699,932)	\$0	
January 1, 2005	Present Value Contributions	\$49,332,428	\$49,332,428	\$0	
	Prepayment Credit Applied	\$42,719,885	\$37,543,336	\$5,176,549	
	Present Value of Funding	\$92,052,313	\$86,875,764	\$5,176,549	
January 1, 2005	CAS Funding Target	\$42,719,885	\$37,543,336	\$5,176,549	
	Percentage Funded		100.00%	100.00%	
	Funded Pension Cost		\$37,543,336	\$5,176,549	
	Allowable Interest		\$0	\$0	
	Allocable Pension Cost		\$37,543,336	\$5,176,549	
	Medicare LOB* Percentage		1.40%	90.48%	
	Plan Year Allowable Pension Cost		\$525,607	\$4,683,742	
2005	Fiscal Year Allowable Pension Cost		\$547,527	\$4,578,383	\$5,125,910
2006	Contributions	\$15,000,000	\$15,000,000	\$0	
7.50%	Discount for Interest	(\$1,046,512)	(\$1,046,512)	\$0	
January 1, 2006	Present Value Contributions	\$13,953,488	\$13,953,488	\$0	
	Prepayment Credit Applied	\$44,346,100	\$38,641,861	\$5,704,239	
	Present Value of Funding	\$58,299,588	\$52,595,349	\$5,704,239	
January 1, 2006	CAS Funding Target	\$44,346,100	\$38,641,861	\$5,704,239	
	Percentage Funded		100.00%	100.00%	
	Funded Pension Cost		\$38,641,861	\$5,704,239	
	Allowable Interest		\$0	\$0	
	Allocable Pension Cost		\$38,641,861	\$5,704,239	
	Medicare LOB* Percentage		1.46%	87.77%	
	Plan Year Allowable Pension Cost		\$564,171	\$5,006,611	
2006	Fiscal Year Allowable Pension Cost		\$554,530	\$4,925,893	\$5,480,423

Date	Description	Total Company	"Other" Segment	Medicare Segment	Total Medicare
2007	Contributions	\$0	\$0	\$0	
7.50%	Discount for Interest	\$0	\$0	\$0	
January 1, 2007	Present Value Contributions	\$0	\$0	\$0	
	Prepayment Credit Applied	\$46,710,129	\$40,954,639	\$5,755,490	
	Present Value of Funding	\$46,710,129	\$40,954,639	\$5,755,490	
January 1, 2007	CAS Funding Target	\$46,710,129	\$40,954,639	\$5,755,490	
	Percentage Funded		100.00%	100.00%	
	Funded Pension Cost		\$40,954,639	\$5,755,490	
	Allowable Interest		\$0	\$0	
	Allocable Pension Cost		\$40,954,639	\$5,755,490	
	Medicare LOB* Percentage		1.19%	87.93%	
	Plan Year Allowable Pension Cost		\$487,360	\$5,060,802	
2007	Fiscal Year Allowable Pension Cost		\$506,563	\$5,047,254	\$5,553,817

* Line of business.

FOOTNOTES

- 1/ We obtained the 2003 plan year (PY) (January 1 - December 31) allowable pension costs from our prior review (A-07-04-00180; issued February 8, 2005).
- 2/ We obtained Total Company contribution amounts and dates of deposit from Internal Revenue Service Form 5500 reports. The contributions included deposits made during the PY and accrued contributions deposited after the end of the PY but within the time allowed for filing tax returns. We determined the contributions allocated to the Medicare segment during the pension segmentation review (A-07-09-00311). The amounts shown for the "Other" segment represent the difference between the Total Company and the Medicare segment.
- 3/ We subtracted the interest that was included in the contributions deposited after the beginning of the valuation 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.
- 4/ The present value of contributions is the value of the contributions discounted from the date of deposit back to the first day of the PY. For purposes of this Appendix, we deemed deposits made after the end of the PY to have been made on the final day of the PY, consistent with the method mandated by the Employee Retirement Income Security Act.
- 5/ 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 Cost Accounting Standards (CAS) funding target. A prepayment credit is carried forward, with interest, to fund future CAS pension costs.
- 6/ 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 the first day of the PY.
- 7/ The CAS funding target must be funded by current or prepaid contributions to satisfy the funding requirement of the Federal Acquisition Regulation (FAR) 31.205-6(j)(2)(i).
- 8/ The percentage of costs funded is a measure of the portion of the CAS funding target that was funded during the PY. Because any funding in excess of the CAS funding target is accounted for as a prepayment in accordance with CAS 412.50(c)(1) (as amended), 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.
- 10/ We assumed that interest on the funded CAS pension cost, less the prepayment credit, accrues in the same proportion as the interest on contributions bears to the present value of contributions. However, we limited the interest in accordance with FAR 31.205-6(j)(2)(iii), which does not permit the allowable interest to exceed the interest that would accrue if the CAS funding target, less the prepayment credit, were funded in four equal installments deposited within 30 days after 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 calculated PY allowable pension costs of the Medicare and “Other” segments based on the Medicare line of business (LOB) percentage of each segment. We determined the LOB percentages based upon information provided by FCSO.
- 13/ We computed the PY allowable Medicare pension cost as the allocable pension cost multiplied by the Medicare LOB percentage.
- 14/ We converted the PY allowable pension costs to a fiscal year (FY) basis (October 1 through September 30). We calculated the FY pension costs as 1/4 of the prior year’s costs plus 3/4 of the current year’s costs. Pursuant to CAS 412 and 413, the total Medicare allowable pension costs charged to the Medicare contract consisted of the Medicare segment’s direct pension costs plus “Other” segment pension costs attributable to indirect Medicare operations.

APPENDIX B: AUDITEE COMMENTS



MEDICARE

Sandy Coston
CEO & President
First Coast Service Options, Inc.
Sandy.Coston@fcsso.com

March 12, 2010

Mr. Patrick J. Cogley
Regional Inspector General for Audit Services
Office of Inspector General
Office of Audit Services
601 East 12th Street, Room 0429
Kansas City, Missouri 64106

Dear Mr. Cogley:

Reference: A-07-09-00312

The purpose of this letter is to submit our response to the Department of Health and Human Services Office of Inspector General's draft report for the review of the Medicare pension costs claimed by First Coast Service Options (FCSO) for fiscal years 2004-2007.

We agree with the report finding regarding the under claimed pension costs of \$124,189 and will take the following actions to ensure the report recommendations are implemented:

- 1) Follow CMS guidelines for fiscal years 2004-2007 to increase the claimed pension costs by \$124,189.
- 2) Update Medicare segment assets in accordance with the appropriate cost accounting standards.

Additionally, we are working with our actuaries to ensure that Medicare segment assets are updated in accordance with Medicare contractual requirements.

We appreciate the opportunity to review and provide our comments prior to release of the final report. If you have any questions regarding our response, please contact Mr. Gregory England at 904-791-8364.

Sincerely,

Sandy Coston

cc: Jonathan Hogan, VP & CFO, FCSO
Gregory England, Director of Internal Audit, FCSO
Brenda Francisco, Director of Medicare Reporting, FCSO
Cheryl Mose, VP & Corporate Controller, BCBSF
Jay Pinkerton, VP, JP Morgan

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