



June 2, 2010

Report Number: A-07-10-00326

Ms. Jean Rush  
President  
CIGNA Government Services  
Two Vantage Way  
Nashville, TN 37228

Dear Ms. Rush:

Enclosed is the U.S. Department of Health & Human Services (HHS), Office of Inspector General (OIG), final report entitled *Review of Medicare Contractor's Pension Segmentation Requirements at CIGNA Government Services, LLC, for the Period January 1, 2004, to January 1, 2008*. 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.

Section 8L of the Inspector General Act, 5 U.S.C. App., requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at <http://oig.hhs.gov>.

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, extension 21, or through email at [Jenenne.Tambke@oig.hhs.gov](mailto:Jenenne.Tambke@oig.hhs.gov). Please refer to report number A-07-10-00326 in all correspondence.

Sincerely,

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

Enclosure

**Direct Reply to HHS Action Official:**

Ms. Deborah Taylor  
Acting Director & Chief Financial Officer  
Office of Financial Management  
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Department of Health & Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF MEDICARE CONTRACTOR'S  
PENSION SEGMENTATION  
REQUIREMENTS AT CIGNA  
GOVERNMENT SERVICES, LLC, FOR THE  
PERIOD JANUARY 1, 2004, TO  
JANUARY 1, 2008**



Daniel R. Levinson  
Inspector General

June 2010  
A-07-10-00326

# *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**

#### **CIGNA Government Services and Medicare**

During our audit period, CIGNA Government Services, LLC (CGS), administered Medicare Part B and durable medical equipment operations for Connecticut General Life Insurance Company (CGLIC), the legal entity that entered into these cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS). In addition, CGS administered Medicare operations under a Medicare administrative contractors contract with CMS. CGS and CGLIC are wholly owned subsidiaries of CIGNA Corporation.

CGS 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.

Since its inception, Medicare has paid a portion of contractors' contributions to their pension plans. These contributions are allowable Medicare costs subject to the criteria set forth in the Federal Acquisition Regulation, Cost Accounting Standards (CAS), and Medicare contracts.

In resolution of our prior pension segmentation audit, CGLIC executed a pension closing agreement with CMS to establish a final settlement of the January 1, 2004, Medicare segment asset base.

#### **Pension Segmentation**

Beginning with fiscal year 1988, CMS incorporated specific segmentation requirements into the Medicare contracts to ensure conformance with CAS 413. The Medicare contracts define a segment and specify the methodology for the identification and initial allocation of pension assets to the segment. Additionally, the contracts require Medicare segment assets to be updated for each year after the initial allocation in accordance with CAS 412 and 413.

### **OBJECTIVE**

Our objective was to determine whether CGS complied with Federal requirements and the Medicare contracts' pension segmentation requirements when:

- implementing the January 1, 2004, Medicare segment asset base established by an executed pension closing agreement between CGLIC and CMS, and
- updating the Medicare segment's assets from January 1, 2004, to January 1, 2008.

## **SUMMARY OF FINDINGS**

CGS properly implemented the January 1, 2004, Medicare segment asset base established by an executed pension closing agreement between CGLIC and CMS. However, CGS did not always comply with the Medicare contracts' pension segmentation requirements when updating Medicare segment assets to January 1, 2008. CGS identified Medicare segment pension assets of \$17,014,151; however, we determined that the Medicare segment pension assets were \$16,671,408 as of January 1, 2008. Thus, CGS overstated the Medicare segment pension assets by \$342,743. The overstatement occurred primarily because CGS did not properly assign earnings, less administrative expenses, to the Medicare segment.

## **RECOMMENDATION**

We recommend that CGS:

- decrease Medicare segment assets as of January 1, 2008, by \$342,743, and
- implement controls to ensure that the Medicare segment's assets are updated in accordance with the Medicare contracts.

## **AUDITEE COMMENTS**

In written comments on our draft report, CGS agreed with our findings and described corrective actions that it planned to implement. CGS's comments are included in their entirety as Appendix B.

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## **Glossary of Abbreviations and Acronyms**

CAS	Cost Accounting Standards
CGLIC	Connecticut General Life Insurance Company
CGS	CIGNA Government Services, LLC
CMS	Centers for Medicare & Medicaid Services
DME	durable medical equipment
FAR	Federal Acquisition Regulation
MAC	Medicare administrative contractor
WAV	weighted average value

## INTRODUCTION

### BACKGROUND

#### **CIGNA Government Services, LLC, and Medicare**

During our audit period, CIGNA Government Services, LLC (CGS), administered Medicare Part B and durable medical equipment (DME) operations for Connecticut General Life Insurance Company (CGLIC), the legal entity that entered into these cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS).<sup>1</sup> In addition, CGS administered Medicare operations under a Medicare administrative contractors (MAC) contract with CMS.<sup>2</sup> CGS and CGLIC are wholly owned subsidiaries of CIGNA Corporation.

CGS 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.<sup>3</sup>

Since its inception, Medicare has paid a portion of contractors' contributions to their pension plans. These contributions are allowable Medicare costs subject to the criteria set forth in the Federal Acquisition Regulation (FAR), Cost Accounting Standards (CAS), and Medicare contracts.

In resolution of our prior pension segmentation audit (A-07-05-00189, issued January 11, 2007), CGLIC executed a pension closing agreement with CMS to establish a final settlement of the January 1, 2004, Medicare segment asset base.

#### **Federal Requirements**

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.

#### **Pension Segmentation**

CMS incorporated CAS 412 and 413 into the Medicare contracts effective October 1, 1980. Beginning with fiscal year 1988, CMS incorporated segmentation requirements into Medicare contracts. The Medicare contracts define a segment and specify the methodology for the

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<sup>1</sup> The DME contractual relationship was terminated on September 29, 2006.

<sup>2</sup> CGS assumed full DME Jurisdiction C MAC operations on June 1, 2007.

<sup>3</sup> CGS participates in employee benefit plans, such as the defined benefit pension plan, of its parent company, CIGNA Corporation.

identification and initial allocation of pension assets to the segment. The contracts require Medicare segment assets to be updated for each year after the initial allocation in accordance with CAS 412 and 413. In claiming costs, contractors must follow cost reimbursement principles contained in the FAR, CAS, and the Medicare contracts.

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

### **Objective**

Our objective was to determine whether CGS complied with Federal requirements and the Medicare contracts' pension segmentation requirements when:

- implementing the January 1, 2004, Medicare segment asset base established by an executed pension closing agreement between CGLIC and CMS, and
- updating the Medicare segment's assets from January 1, 2004, to January 1, 2008.

### **Scope**

We reviewed CGS's implementation of the pension closing agreement, identification of its Medicare segment and update of the Medicare segment's assets from January 1, 2004, to January 1, 2008.

Achieving our objectives did not require us to review CGS's overall internal control structure. However, we reviewed controls relating to the implementation of the pension closing agreement, the identification of the Medicare segment, and the update of the Medicare segment's assets.

We performed fieldwork at CGS's office in Nashville, Tennessee, during June 2009 and February 2010.

### **Methodology**

To accomplish our objective, we did the following:

- We reviewed the applicable portions of the FAR, CAS, and Medicare contracts.
- We reviewed Closing Agreement No. PEN-01 executed between CGLIC and CMS. We used this information to identify the Medicare segment assets as of January 1, 2004.
- We reviewed annual actuarial valuation reports prepared by CGS's actuarial consulting firms, which included the pension plan's assets, liabilities, normal costs, contributions, benefit payments, investment earnings, and administrative expenses. We used this information to calculate the Medicare segment assets.

- We obtained and reviewed the pension plan documents and Department of Labor/Internal Revenue Service Forms 5500 used in calculating the Medicare segment assets.
- We interviewed CGS staff responsible for identifying the Medicare segment to determine whether the segment was properly identified in accordance with the Medicare contracts.
- We reviewed CGS's accounting records to verify the segment identification and benefit payments made to the Medicare segment.
- We provided the CMS Office of the Actuary with the actuarial information necessary for it to calculate the Medicare segment assets as of January 1, 2008.
- We reviewed the CMS actuaries' methodology and calculations.

We performed this review in conjunction with our audit of CGS's pension costs claimed for Medicare reimbursement (A-07-10-00327) and used the information obtained during that audit in this review.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

### **FINDINGS AND RECOMMENDATIONS**

CGS properly implemented the January 1, 2004, Medicare segment asset base established by an executed pension closing agreement between CGLIC and CMS. However, CGS did not always comply with the Medicare contracts' pension segmentation requirements while updating Medicare segment assets to January 1, 2008. CGS identified Medicare segment pension assets of \$17,014,151; however, we determined that the Medicare segment pension assets were \$16,671,408 as of January 1, 2008. Thus, CGS overstated the Medicare segment pension assets by \$342,743. The overstatement occurred primarily because CGS did not properly assign earnings, less administrative expenses, to the Medicare segment.

Appendix A presents details of the Medicare segment's pension assets from January 1, 2004, to January 1, 2008, as determined during our audit. Table 1 summarizes the audit adjustments required to update Medicare segment pension assets in accordance with Federal requirements.

<b>Table 1: Summary of Audit Adjustments</b>			
	<b>Per OIG</b>	<b>Per CGS</b>	<b>Difference</b>
<b>Update of Medicare Segment Assets</b>			
Earnings, Net Expenses	\$6,476,742	\$6,792,385	(\$315,643)
Contributions and Transferred Prepayment Credits	3,438,890	3,465,990	(27,100)
<b>Overstatement of Medicare Segment Assets</b>			<b>(\$342,743)</b>

## **PENSION CLOSING AGREEMENT**

CGLIC executed a pension closing agreement with CMS to establish a final settlement of the January 1, 2004, Medicare segment asset base. CGS properly used the January 1, 2004, Medicare segment asset base, established by the executed pension closing agreement with CMS, in its computations.

## **UPDATE OF MEDICARE SEGMENT ASSETS**

### **Federal Requirements**

The Medicare contracts state that "... the pension assets allocated to each Medicare Segment shall be adjusted in accordance with CAS 413.50(c)(7)." CAS 413.50(c)(7) requires that the asset base be adjusted by contributions, permitted unfunded accruals, income, benefit payments, and expenses. For plan years beginning after March 30, 1995, the CAS requires investment income and expenses to be allocated among segments based on the ratio of the segment's weighted average value (WAV) of assets to Total Company WAV of assets.

In addition, CAS 413.50(c)(8) requires an adjustment to be made for transfers (participants who enter or leave the segment) if the transfers materially affect the segment's ratio of pension plan assets to actuarial accrued liabilities. For plan years beginning after March 30, 1995, the CAS requires that the amount of assets transferred equal the actuarial accrued liabilities as determined using the accrued benefit cost method.

Furthermore, CAS 412.50(a)(4) requires that contributions in excess of the pension cost assigned to the period be recognized as prepayment credits and accumulated at the assumed valuation interest rate until applied to future period costs. Prepayment credits that have not been applied to fund pension costs are excluded from the value of assets used to compute pension costs. Prepayment credits are accounted for as part of the "Other" segment only for purposes of allocating investment earnings and expenses between the segments.

### **Earnings, Net Expenses Overstated**

CGS overstated investment earnings, less administrative expenses, by \$315,643 for the Medicare segment because it improperly omitted prepayment credits in the computation of the WAV of assets when assigning the net investment earnings to the segment.

In our audited update, we allocated net investment earnings based on the applicable CAS requirements. This included accounting for prepayment credits as part of the “Other” segment for purposes of allocating net investment earnings between the segments, pursuant to CAS 412.50(a)(4). The inclusion of prepayment credits with the assets of the “Other” segment for the purpose of allocating investment returns is consistent with the premise that prepayment credits are the result of the plan sponsor’s investment decision to fund amounts in excess of the assigned costs. Accordingly, the Federal Government should not share in the investment risk/reward associated with those funds.

Based on our computations, we determined that CGS overstated the Medicare segment assets by \$315,643.

### **Contributions and Transferred Prepayment Credits Overstated**

CGS overstated contributions and transferred prepayment credits for the Medicare segment by \$27,100. The overstatement occurred because CGS overstated the segment’s assignable pension costs for the audit period. As a result, CGS overstated the Medicare segment assets by \$27,100.

### **RECOMMENDATIONS**

We recommend that CGS:

- decrease Medicare segment assets as of January 1, 2008, by \$342,743, and
- implement controls to ensure that the Medicare segment’s assets are updated in accordance with the Medicare contracts.

### **AUDITEE COMMENTS**

In written comments on our draft report, CGS agreed with our findings and described corrective actions that it planned to implement. CGS’s comments are included in their entirety as Appendix B.

# **APPENDIXES**

**APPENDIX A: STATEMENT OF MARKET VALUE OF PENSION ASSETS FOR  
CIGNA GOVERNMENT SERVICES, LLC,  
FOR THE PERIOD JANUARY 1, 2004, TO JANUARY 1, 2008**

Description	Total Company	"Other" Segment	Medicare Segment
Assets January 1, 2004	1/ \$2,425,988,220	\$2,414,921,503	\$11,066,717
Transferred Prepayment Credits	2/ 0	(841,641)	841,641
Contributions	3/ 60,000,000	60,000,000	0
Earnings, Net Expenses	4/ 259,163,398	257,879,386	1,284,012
Benefit Payments	5/ (224,929,194)	(224,386,124)	(543,070)
Transfers	6/ 0	(107,463)	107,463
Assets January 1, 2005	2,520,222,424	2,507,465,661	12,756,763
Transferred Prepayment Credits	0	(844,386)	844,386
Contributions	543,000,000	542,912,647	87,353
Earnings, Net Expenses	259,024,427	257,716,453	1,307,974
Benefit Payments	(230,078,171)	(229,342,608)	(735,563)
Transfers	0	(324,308)	324,308
Assets January 1, 2006	3,092,168,680	3,077,583,459	14,585,221
Transferred Prepayment Credits	0	(1,027,220)	1,027,220
Contributions	0	0	0
Earnings, Net Expenses	479,190,883	476,850,707	2,340,176
Benefit Payments	(244,180,210)	(241,964,667)	(2,215,543)
Transfers	0	52,272	(52,272)
Assets January 1, 2007	3,327,179,353	3,311,494,551	15,684,802
Transferred Prepayment Credits	0	(638,290)	638,290
Contributions	0	0	0
Earnings, Net Expenses	317,943,453	316,398,873	1,544,580
Benefit Payments	(249,245,553)	(247,715,616)	(1,529,937)
Transfers	0	(333,673)	333,673
Assets January 1, 2008	\$3,395,877,253	\$3,379,205,845	\$16,671,408
Per CGS	7/ \$3,395,877,253	\$3,378,863,102	\$17,014,151
Asset Variance	8/ \$0	\$342,743	(\$342,743)

**FOOTNOTES**

1/ We obtained the Medicare segment assets as of January 1, 2004, from Closing Agreement No. PEN-01. The Centers for Medicare & Medicaid Services (CMS) and Connecticut General Life Insurance Company entered into and executed this closing agreement in order to establish a final settlement of the January 1, 2004, Medicare segment asset base. The amounts shown for the "Other" segment represent the difference between the Total Company and the Medicare segment. All pension assets are shown at market value.

2/ Prepayment credits represent funds available to satisfy future funding requirements and are applied to future funding requirements before current year contributions in order to reduce interest costs to the Federal Government. Prepayment credits are transferred to the Medicare segment as needed to cover funding requirements.

- 3/ We obtained Total Company contribution amounts from the actuarial valuation reports and Department of Labor/Internal Revenue Service Forms 5500. We accepted CIGNA Government Services, LLC's (CGS), methodology whereby only contributions actually made during a plan year were considered as funding for that year. We allocated Total Company contributions to the Medicare segment based on the ratio of the Medicare segment funding target divided by the Total Company funding target. Contributions in excess of the funding targets were treated as prepayment credits and accounted for in the "Other" segment until needed to fund pension costs in the future.
- 4/ We obtained net investment earnings from actuarial valuation reports and documents prepared by CGS's actuarial consulting firms. We allocated net investment earnings based on the ratio of the segment's weighted average value (WAV) of assets to Total Company WAV of assets as required by the Cost Accounting Standards (CAS).
- 5/ We based the Medicare segment's benefit payments on actual payments to Medicare segment retirees. We obtained information on the benefit payments from documents provided by CGS. We reviewed and accepted CGS's benefit payments to Medicare segment retirees.
- 6/ We identified participant transfers between segments by comparing valuation data files provided by CGS. Asset transfers were equal to the actuarial liability determined under the accrued benefit cost method in accordance with the CAS. We reviewed and accepted CGS's participant transfers.
- 7/ We obtained total asset amounts as of January 1, 2008, from documents prepared by CGS's actuarial consulting firms.
- 8/ The asset variance represents the difference between our calculation of Medicare segment assets and CGS's calculation of Medicare segment assets.

## APPENDIX B: AUDITEE COMMENTS

Steve Bishop  
Accounting Director



CIGNA Government  
Services

May 14, 2010

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Patrick J. Cogley  
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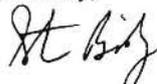
Dear Mr. Cogley:

This letter is in response to Audit Report No. A-07-10-00326, which noted an overstatement of the Medicare segment assets of \$342,743, and A-07-10-00327, which cited unallowable pension costs of \$12,130 for the fiscal years 2005 – 2007, in accordance with CAS 412 and 413.

CIGNA Government Services, LLC (“CGS”) agrees with the findings in both reports and will make the appropriate adjustment to our FACP and reimburse CMS accordingly. We will also instruct our actuaries to adjust the Medicare segment assets as noted.

Please feel free to contact Kara Fitzgerald at 615.782.4687 or myself at 615.782.4616 if you have questions regarding this response.

Sincerely,



Steve Bishop