



Region VII
601 East 12th Street
Room 0429
Kansas City, Missouri 64106

July 14, 2011

Report Number: A-07-11-00358

Mr. Peter S. Moore
Vice President of Government Programs
GHI Medicare
25 Broadway
New York, NY 10004

Dear Mr. Moore:

Enclosed is the U.S. Department of Health & Human Services (HHS), Office of Inspector General (OIG), final report entitled *Review of the Pension Segmentation Requirements for the Local 153 Pension Plan at Group Health Incorporated for the Period of April 1, 1987, to January 1, 2009*. 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. Please refer to report number A-07-11-00358 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
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Department of Health & Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF THE PENSION
SEGMENTATION REQUIREMENTS FOR
THE LOCAL 153 PENSION PLAN AT
GROUP HEALTH INCORPORATED
FOR THE PERIOD OF
APRIL 1, 1987, TO JANUARY 1, 2009**



Daniel R. Levinson
Inspector General

July 2011
A-07-11-00358

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

Group Health Incorporated (GHI), an EmblemHealth Company, administered Medicare Part B operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS). These contracts terminated on July 18, 2008, but GHI continues to administer Medicare operations under a Coordination of Benefits contract with CMS.

During the audit period, GHI had three defined benefit pension plans: the GHI Local 153 Pension Plan; the GHI Cash Balance Pension Plan; and the EmblemHealth Services Company Employees' Retirement Plan. This report will address the pension assets for the Local 153 Pension Plan only.

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.

Pension Segmentation

Beginning with fiscal year 1988, CMS incorporated segmentation requirements into the Medicare contracts. The Medicare contracts define a segment and specify the methodology for the identification and initial allocation of pension assets to the segment. Accordingly, 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 GHI complied with Federal requirements and the Medicare contracts' pension segmentation requirements when:

- identifying the Medicare segment's pension asset base (initial allocation) as of April 1, 1987, and
- updating the Medicare segment's pension assets from April 1, 1987, to January 1, 2009.

SUMMARY OF FINDINGS

GHI did not always comply with Federal requirements and the Medicare contracts' pension segmentation requirements when identifying the Medicare segment's initial asset base and when updating Medicare segment assets to January 1, 2009. GHI identified Medicare segment pension assets of \$28,362,719; however, we determined that the Medicare segment pension assets were \$15,753,896 as of January 1, 2009. As a result, GHI overstated the Medicare segment pension assets by \$12,608,823 as of January 1, 2009.

RECOMMENDATIONS

We recommend that GHI:

- decrease Medicare segment pension assets as of January 1, 2009, by \$12,608,823 and recognize \$15,753,896 as the Medicare segment pension assets;
- allocate contributions and prepayment credits to the Medicare segment based on separately calculated pension costs; and
- establish controls to ensure compliance with Federal regulations and the Medicare contracts' pension segmentation requirements when allocating contributions and prepayment credits, benefit payments, participant transfers, and investment earnings and expenses.

AUDITEE COMMENTS

In written comments on our draft report, GHI agreed with our findings and recommendations for our first and third recommendations. However, GHI did not directly address our second recommendation. GHI's comments are included in their entirety as Appendix B.

OFFICE OF INSPECTOR GENERAL RESPONSE

Although GHI did not specifically address our second recommendation, its agreement with our third recommendation meant that GHI had also effectively agreed to allocate contributions and prepayment credits to the Medicare segment based on separately calculated pension costs, as stated in our second recommendation. Accordingly, we maintain that all of our findings and recommendations remain valid.

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Glossary of Abbreviations and Acronyms

CAS	Cost Accounting Standards
CMS	Centers for Medicare & Medicaid Services
FAR	Federal Acquisition Regulation
GHI	Group Health Incorporated
WAV	weighted average value

INTRODUCTION

BACKGROUND

Group Health Incorporated and Medicare

Group Health Incorporated (GHI), an EmblemHealth Company, administered Medicare Part B operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS). These contracts terminated on July 18, 2008, but GHI continues to administer Medicare operations under a Coordination of Benefits contract with CMS. GHI also performs Medicare work as subcontractor on the Medicare Secondary Payer Recovery and Retiree Drug Subsidy contracts.

During the audit period, GHI had three defined benefit pension plans: the GHI Local 153 Pension Plan; the GHI Cash Balance Pension Plan; and the EmblemHealth Services Company Employees' Retirement Plan. Effective August 31, 2003, benefits accrued under the Local 153 Pension Plan for management employees were frozen. On September 1, 2003, GHI established the GHI Cash Balance Pension Plan for management employees. On January 1, 2008, GHI froze the GHI Cash Balance Pension Plan and employees were given an opportunity to elect participation in the EmblemHealth Services Company Employees' Retirement Plan, effective January 1, 2008. This report will address the pension assets for the Local 153 Pension Plan only.

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.

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

Beginning with fiscal year 1988, CMS incorporated segmentation requirements into the Medicare contracts. 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. 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 GHI complied with Federal requirements and the Medicare contracts' pension segmentation requirements when:

- identifying the Medicare segment's pension asset base (initial allocation) as of April 1, 1987, and
- updating the Medicare segment's pension assets from April 1, 1987, to January 1, 2009.

Scope

We reviewed GHI's identification of its Medicare segment, computation of the initial assets allocated to the Medicare segment, and its update of Medicare segment pension assets from April 1, 1987, to January 1, 2009.

Achieving our objective did not require us to review GHI's overall internal control structure. We reviewed controls relating to the identification of the Medicare segment, computation of the initial assets allocated to the Medicare segment, and the update of the segment's assets to ensure adherence to the Medicare contracts, CAS 412, and CAS 413.

We performed fieldwork at GHI in New York, New York, during September 2008 and July 2010.

Methodology

To accomplish our objective, we did the following:

- We reviewed the applicable portions of the FAR, CAS, and the Medicare contracts.
- We reviewed the annual actuarial valuation reports prepared by GHI'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 GHI staff responsible for identifying the Medicare segment to determine whether the segment was properly identified in accordance with the Medicare contracts.
- We reviewed GHI'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 pension assets from April 1, 1987, to January 1, 2009.
- We reviewed the CMS actuaries' methodology and calculations.

We performed this review in conjunction with our audit of GHI's pension costs claimed for Medicare reimbursement, to be issued in a subsequent report, 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

GHI did not always comply with Federal requirements and the Medicare contracts' pension segmentation requirements when identifying the Medicare segment's initial asset base and when updating Medicare segment assets to January 1, 2009. GHI identified Medicare segment pension assets of \$28,362,719; however, we determined that the Medicare segment pension assets were \$15,753,896 as of January 1, 2009. As a result, GHI overstated the Medicare segment pension assets by \$12,608,823 as of January 1, 2009.

Appendix A presents details on the Medicare segment's pension assets from April 1, 1987, to January 1, 2009, as determined during our audit. Table 1 summarizes the audit adjustment required to update Medicare segment pension assets in accordance with Federal requirements.

Table 1: Summary of Audit Adjustments			
	Per Audit	Per GHI	Difference
Medicare Segment Asset Base (Initial Allocation)	\$3,916,166	\$6,696,841	(\$2,780,675)
Update of Medicare Segment Assets			
Contributions and Prepayment Credits	3,123,671	1,292,715	1,830,956
Benefit Payments	6,926,470	7,477,623	551,153
Transfers	822,966	0	822,966
Earnings, Net Expenses	14,817,563	27,850,786	(13,033,223)
Under/(Over)statement of Medicare Pension Segment Assets			(\$12,608,823)

MEDICARE SEGMENT ASSET BASE (INITIAL ALLOCATION)

The Medicare contracts provide for separate identification of the pension assets for the Medicare segment. The identification involves the allocation of assets to the Medicare segment as of the first pension plan year after December 31, 1985, in which the salary criterion was met. The allocation is to use the ratio of the actuarial liabilities of the Medicare segment to the actuarial liabilities of the total plan, as of the later of the first day of the first plan year after December 31, 1980, or the first day of the first pension plan year following the date such Medicare segment existed. This ratio is known as the asset fraction.

GHI did not always comply with Federal requirements and the Medicare contracts' pension segmentation requirements when identifying the Medicare segment's initial asset base. Specifically, GHI overstated the initial Medicare segment asset base by \$2,780,675 as of April 1, 1987, because it incorrectly included actuarial liabilities from its terminated Florida Medicare operations in the numerator of its asset fraction. GHI calculated an asset fraction of 21.1998 percent and identified \$6,696,841 as the Medicare segment asset base as of April 1, 1987. We calculated the asset fraction to be 12.3761 percent and identified \$3,916,166 as the initial Medicare segment pension asset base as of April 1, 1987. Thus, GHI overstated the initial Medicare segment pension assets by \$2,780,675 as of April 1, 1987.

UPDATE OF MEDICARE SEGMENT PENSION ASSETS

GHI did not always comply with Federal requirements and the Medicare contracts' pension segmentation requirements when updating Medicare segment assets to January 1, 2009.

Federal Requirements

The Medicare contracts identify a Medicare segment as:

. . . 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 are charged to the Medicare agreement/contract, and these salary dollars represent 40% or more of the total salary dollars charged to the Medicare agreement/contract.

Furthermore, 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. The CAS requires expenses to be allocated among the segments in proportion to the investment earnings. 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 on or before March 30, 1995, the CAS requires investment income and expenses to be allocated among segments in proportion to the beginning-of-year asset value. 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.

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.

Contributions and Prepayment Credits Understated

GHI understated contributions and prepayment credits by \$1,830,956 because its update methodology did not equitably assign pension contributions to the Medicare segment. More specifically, GHI did not comply with the Medicare contracts when it used allocated pension costs rather than segment pension costs to allocate contributions to the Medicare segment. As a result, GHI understated the Medicare segment pension assets by \$1,830,956.

Beginning with fiscal year 1988, the Medicare contracts require a separate calculation of pension costs for the segment if such calculation (as opposed to an allocation) materially affected the amount of pension costs charged to the contracts.

In accordance with the Medicare contracts, we computed both an allocated and a separately calculated pension cost. We determined that, beginning with plan year 1988, the use of an allocated pension cost was materially different when compared to a separately calculated pension cost. The Medicare contracts require that, in cases of material difference, a separately calculated pension cost be used. Therefore, in our calculations we based the audited contributions and prepayment credits for plan years 1988 through 2008 upon a separately calculated pension cost, pursuant to the Medicare contracts.

For ease of understanding, Table 2, on the following page, includes only the years in which there was a variance between GHI's and our calculations of allocated pension contributions and prepayment credits.

Table 2: Comparison of Allocated Pension Contributions			
Year	Per Audit	Per GHI	Variance
1987	\$0	\$105,660	(\$105,660)
1988	0	(52,830)	52,830
1995	175,169	34,121	141,048
1997	0	14,311	(14,311)
1998	0	16,287	(16,287)
1999	0	43,563	(43,563)
2000	0	46,672	(46,672)
2001	0	41,622	(41,622)
2001	0	70,200	(70,200)
2003	0	83,943	(83,943)
2004	402,012	70,643	331,369
2005	508,823	149,131	359,692
2006	907,417	368,262	539,155
2007	1,004,099	14,591	989,508
2008	126,151	286,539	(160,388)
Total	\$3,123,671	\$1,292,715	\$1,830,956

Benefit Payments Overstated

GHI overstated benefit payments by \$551,153 because it incorrectly included benefit payments from its terminated Florida Medicare operations during 1989 through 2008. As a result, GHI understated the Medicare segment pension assets by \$551,153.

A comparison of GHI's and our calculations of benefit payments from the Medicare segment appears in Table 3.

Year	Per Audit	Per GHI	Variance
1987	\$72,769	\$72,769	\$0
1988	71,080	71,080	0
1989	137,433	164,634	27,201
1990	158,850	186,051	27,201
1991	182,499	113,139	(69,360)
1992	235,137	262,338	27,201
1993	245,362	272,563	27,201
1994	246,564	271,492	24,928
1995	248,777	273,705	24,928
1996	249,493	273,363	23,870
1997	295,434	319,304	23,870
1998	327,271	357,850	30,579
1999	355,357	392,424	37,067
2000	359,032	396,099	37,067
2001	378,081	415,148	37,067
2001	378,081	415,148	37,067
2003	449,557	486,624	37,067
2004	466,457	500,947	34,490
2005	489,986	523,833	33,847
2006	501,130	534,977	33,847
2007	568,197	602,044	33,847
2008	509,923	572,091	62,168
Total	\$6,926,470	\$7,477,623	\$551,153

Net Transfers Understated

GHI understated net transfers into the Medicare segment by \$822,966 because it did not adjust the Medicare segment pension assets for participant transfers. The CAS requires an adjustment to be made for transfers if the transfers materially affect the segment's ratio of pension plan assets to actuarial accrued liabilities. We determined that, beginning in plan year 2005, participant transfers materially affected the segment's ratio of pension plan assets to actuarial accrued liabilities. Our audited update therefore included an adjustment to the Medicare segment pension assets, beginning in plan year 2005, for participant transfers and for identified net transfers into the Medicare segment, of \$822,966. This understatement of the net transfer adjustment resulted in an understatement of the Medicare segment pension assets of \$822,966.

Earnings, Net Expenses Overstated

GHI overstated investment earnings, less administrative expenses, by \$13,033,223 for the Medicare segment because it (a) did not allocate earnings, net expenses using the WAV of assets as required by the CAS for plan years starting in 1996, (b) incorrectly computed the initial Medicare segment asset base (discussed above), and (c) used incorrect contribution and prepayment credit amounts, benefit payment amounts, and transfer amounts (all discussed

above) to develop the Medicare segment pension asset base as of January 1, 2009. In our audited update, we allocated earnings and expenses based on the applicable CAS requirements.

A comparison of GHI's and our calculations of earnings, net expenses allocated to the Medicare segment appears in Table 4.

Year	Per Audit	Per GHI	Variance
1987	\$55,632	\$95,134	(\$39,502)
1988	286,916	502,219	(215,303)
1989	776,083	1,358,553	(582,470)
1990	(127,841)	(225,832)	97,991
1991	1,036,490	1,852,903	(816,413)
1992	432,392	790,292	(357,900)
1993	702,355	1,305,022	(602,667)
1994	(167,636)	(316,623)	148,987
1995	1,497,043	2,879,818	(1,382,775)
1996	812,664	1,554,028	(741,364)
1997	1,390,516	2,699,020	(1,308,504)
1998	1,353,138	2,669,031	(1,315,893)
1999	553,834	1,113,214	(559,380)
2000	638,622	1,305,933	(667,311)
2001	(295,977)	(621,792)	325,815
2001	(597,136)	(1,286,650)	689,514
2003	1,153,561	2,569,298	(1,415,737)
2004	732,432	1,551,127	(818,695)
2005	536,145	1,127,326	(591,181)
2006	1,070,922	1,896,351	(825,429)
2007	1,576,034	2,687,287	(1,111,253)
2008	1,401,374	2,345,127	(943,753)
Total	\$14,817,563	\$27,850,786	(\$13,033,223)

RECOMMENDATIONS

We recommend that GHI:

- decrease Medicare segment pension assets as of January 1, 2009, by \$12,608,823 and recognize \$15,753,896 as the Medicare segment pension assets;
- allocate contributions and prepayment credits to the Medicare segment based on separately calculated pension costs; and
- establish controls to ensure compliance with Federal regulations and the Medicare contracts' pension segmentation requirements when allocating contributions and prepayment credits, benefit payments, participant transfers, and investment earnings and expenses.

AUDITEE COMMENTS

In written comments on our draft report, GHI agreed with our findings and recommendations for our first and third recommendations. GHI did not specifically address our second recommendation.

Specifically, GHI agreed to adjust the segmented assets as of January 1, 2009, as recommended in our draft report. GHI also agreed to establish controls to ensure compliance with applicable Federal regulations including the FAR, CAS, and the Medicare contract requirements.

GHI's comments are included in their entirety as Appendix B.

OFFICE OF INSPECTOR GENERAL RESPONSE

Although GHI did not specifically address our second recommendation, its agreement with our third recommendation meant that GHI had also effectively agreed to allocate contributions and prepayment credits to the Medicare segment based on separately calculated pension costs, as stated in our second recommendation. Accordingly, we maintain that all of our findings and recommendations remain valid.

APPENDIXES

APPENDIX A: GROUP HEALTH INCORPORATED
STATEMENT OF MARKET VALUE OF THE LOCAL 153 PENSION PLAN ASSETS
FOR THE PERIOD APRIL 1, 1987, TO JANUARY 1, 2009

Description		Total Company	"Other" Segment	Medicare Segment
Assets April 1, 1987	1/	\$31,642,971	\$27,726,805	\$3,916,166
Prepayment Transfer		0	0	0
Contributions	2/	88,331	88,331	0
Earnings	3/	603,391	528,715	74,676
Benefit Payments	4/	(872,846)	(800,077)	(72,769)
Expenses	5/	(153,879)	(134,835)	(19,044)
Assets January 1, 1988		\$31,307,968	\$27,408,939	\$3,899,029
Prepayment Transfer		0	0	0
Contributions		0	0	0
Earnings		2,434,908	2,131,670	303,238
Benefit Payments		(703,302)	(632,222)	(71,080)
Expenses		(131,060)	(114,738)	(16,322)
Assets January 1, 1989		\$32,908,514	\$28,793,649	\$4,114,865
Prepayment Transfer		0	0	0
Contributions		0	0	0
Earnings		6,375,965	5,578,717	797,248
Benefit Payments		(1,021,986)	(884,553)	(137,433)
Expenses		(169,266)	(148,101)	(21,165)
Assets January 1, 1990		\$38,093,227	\$33,339,712	\$4,753,515
Prepayment Transfer		0	0	0
Contributions		0	0	0
Earnings		(831,929)	(728,116)	(103,813)
Benefit Payments		(1,129,751)	(970,901)	(158,850)
Expenses		(192,551)	(168,523)	(24,028)
Assets January 1, 1991		\$35,938,996	\$31,472,172	\$4,466,824
Prepayment Transfer		0	0	0
Contributions		0	0	0
Earnings		8,452,753	7,402,168	1,050,585
Benefit Payments		(1,208,087)	(1,025,588)	(182,499)
Expenses		(113,404)	(99,309)	(14,095)
Assets January 1, 1992		\$43,070,258	\$37,749,443	\$5,320,815
Prepayment Transfer		0	0	0
Contributions		0	0	0
Earnings		3,621,909	3,174,465	447,444
Benefit Payments		(1,396,899)	(1,161,762)	(235,137)
Expenses		(121,839)	(106,787)	(15,052)
Assets January 1, 1993		\$45,173,429	\$39,655,359	\$5,518,070

Description	Total Company	"Other" Segment	Medicare Segment
Assets January 1, 1993	\$45,173,429	\$39,655,359	\$5,518,070
Prepayment Transfer	0	0	0
Contributions	0	0	0
Earnings	5,871,705	5,154,459	717,246
Benefit Payments	(1,501,560)	(1,256,198)	(245,362)
Expenses	(121,904)	(107,013)	(14,891)
Assets January 1, 1994	\$49,421,670	\$43,446,607	\$5,975,063
Prepayment Transfer	0	0	0
Contributions	0	0	0
Earnings	(945,878)	(831,522)	(114,356)
Benefit Payments	(1,646,183)	(1,399,619)	(246,564)
Expenses	(440,697)	(387,417)	(53,280)
Assets January 1, 1995	\$46,388,912	\$40,828,049	\$5,560,863
Prepayment Transfer	0	0	0
Contributions	2,408,626	2,233,457	175,169
Earnings	12,951,454	11,398,901	1,552,553
Benefit Payments	(1,814,644)	(1,565,867)	(248,777)
Expenses	(463,070)	(407,560)	(55,510)
Assets January 1, 1996	\$59,471,278	\$52,486,980	\$6,984,298
Prepayment Transfer	0	0	0
Contributions	0	0	0
Earnings	7,452,673	6,578,632	874,041
Benefit Payments	(1,964,130)	(1,714,637)	(249,493)
Expenses	(523,342)	(461,965)	(61,377)
Assets January 1, 1997	\$64,436,479	\$56,889,010	\$7,547,469
Prepayment Transfer	0	0	0
Contributions	900,032	900,032	0
Earnings	12,442,558	10,988,302	1,454,256
Benefit Payments	(2,248,949)	(1,953,515)	(295,434)
Expenses	(545,356)	(481,616)	(63,740)
Assets January 1, 1998	\$74,984,764	\$66,342,213	\$8,642,551
Prepayment Transfer	0	0	0
Contributions	1,024,332	1,024,332	0
Earnings	12,385,083	10,960,974	1,424,109
Benefit Payments	(2,497,169)	(2,169,898)	(327,271)
Expenses	(617,218)	(546,247)	(70,971)
Assets January 1, 1999	\$85,279,792	\$75,611,374	\$9,668,418

Description	Total Company	"Other" Segment	Medicare Segment
Assets January 1, 1999	\$85,279,792	\$75,611,374	\$9,668,418
Prepayment Transfer	0	0	0
Contributions	2,741,584	2,741,584	0
Earnings	5,570,105	4,941,660	628,445
Benefit Payments	(2,744,658)	(2,389,301)	(355,357)
Expenses	(661,300)	(586,689)	(74,611)
Assets January 1, 2000	\$90,185,523	\$80,318,628	\$9,866,895
Prepayment Transfer	0	0	0
Contributions	3,361,467	3,361,467	0
Earnings	6,557,672	5,842,816	714,856
Benefit Payments	(3,047,685)	(2,688,653)	(359,032)
Expenses	(699,328)	(623,094)	(76,234)
Assets January 1, 2001	\$96,357,649	\$86,211,164	\$10,146,485
Prepayment Transfer	0	0	0
Contributions	4,461,143	4,461,143	0
Earnings	(1,807,446)	(1,619,401)	(188,045)
Benefit Payments	(3,263,564)	(2,885,483)	(378,081)
Expenses	(1,037,421)	(929,489)	(107,932)
Assets January 1, 2002	\$94,710,361	\$85,237,934	\$9,472,427
Prepayment Transfer	0	0	0
Contributions	5,859,236	5,859,236	0
Earnings	(5,141,584)	(4,636,044)	(505,540)
Benefit Payments	(3,623,865)	(3,245,784)	(378,081)
Expenses	(931,571)	(839,975)	(91,596)
Assets January 1, 2003	\$90,872,577	\$82,375,367	\$8,497,210
Prepayment Transfer	0	0	0
Contributions	7,664,540	7,664,540	0
Earnings	13,891,610	12,626,419	1,265,191
Benefit Payments	(4,162,610)	(3,713,053)	(449,557)
Expenses	(1,225,685)	(1,114,055)	(111,630)
Assets January 1, 2004	\$107,040,432	\$97,839,218	\$9,201,214
Prepayment Transfer	0	0	0
Contributions	26,765,678	26,363,666	402,012
Earnings	9,348,668	8,560,926	787,742
Benefit Payments	(5,434,094)	(4,967,637)	(466,457)
Expenses	(656,397)	(601,087)	(55,310)
Assets January 1, 2005	\$137,064,287	\$127,195,086	\$9,869,201

Description	Total Company	"Other" Segment	Medicare Segment
Assets January 1, 2005	\$137,064,287	\$127,195,086	\$9,869,201
Prepayment Transfer	6/ 0	(508,823)	508,823
Contributions	6,000,000	6,000,000	0
Earnings	8,451,028	7,814,426	636,602
Benefit Payments	(5,091,327)	(4,601,341)	(489,986)
Expenses	(1,333,596)	(1,233,139)	(100,457)
Transfers	7/ 0	(1,353,742)	1,353,742
Assets January 1, 2006	\$145,090,392	\$133,312,467	\$11,777,925
Prepayment Transfer	0	(907,417)	907,417
Contributions	4,174,556	4,174,556	0
Earnings	13,727,983	12,527,154	1,200,829
Benefit Payments	(5,869,905)	(5,368,775)	(501,130)
Expenses	(1,485,109)	(1,355,202)	(129,907)
Transfers	0	(344,312)	344,312
Assets January 1, 2007	\$155,637,917	\$142,038,471	\$13,599,446
Prepayment Transfer	0	(1,004,099)	1,004,099
Contributions	13,488,137	13,488,137	0
Earnings	18,615,840	16,911,953	1,703,887
Benefit Payments	(6,536,124)	(5,967,927)	(568,197)
Expenses	(1,396,855)	(1,269,002)	(127,853)
Transfers	0	(187,101)	187,101
Assets January 1, 2008	\$179,808,915	\$164,010,432	\$15,798,483
Prepayment Transfer	0	(126,151)	126,151
Contributions	11,000,000	11,000,000	0
Earnings	17,111,953	15,622,336	1,489,617
Benefit Payments	(7,001,856)	(6,491,933)	(509,923)
Expenses	(1,013,691)	(925,448)	(88,243)
Transfers	0	1,062,189	(1,062,189)
Assets January 1, 2009	\$199,905,321	\$184,151,425	\$15,753,896
Per GHI	8/ \$199,905,321	\$171,542,602	\$28,362,719
Asset Variance	9/ \$0	\$12,608,823	(\$12,608,823)

FOOTNOTES

- 1/ We calculated the Medicare segment pension assets initial allocation based upon our computed asset fraction (12.3761 percent). The amounts shown for the "Other" segment represent the difference between the Total Company and the Medicare segments. All pension assets in this appendix are shown at market value.
- 2/ We obtained Total Company contribution amounts from the Department of Labor/Internal Revenue Service Forms 5500 (DOL/IRS 5500). 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.
- 3/ We obtained investment earnings from DOL/IRS 5500s. We allocated investment earnings based on the market value of Medicare assets at the beginning of the plan year after adjustments for prepayment credits and participant transfers. For years starting with 1996, we allocated 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).

- 4/ We based the Medicare segment's benefit payments on actual payments to Medicare retirees. We obtained the benefit payments from documents provided by Group Health Incorporated (GHI).
- 5/ We allocated administrative expenses to the Medicare segment in proportion to investment earnings as required by the CAS.
- 6/ Prepayment credits represent funds available to satisfy future funding requirements and are applied to future funding requirements before current year contributions in order to avoid incurring unallowable interest costs. Prepayment credits are maintained in the "Other" segment and transferred to the Medicare segment as needed to cover funding requirements.
- 7/ We identified participant transfers between segments starting in plan year 2005 by comparing valuation data files provided by GHI. The CAS requires an adjustment to be made for transfers only if the transfers materially affect the segment's ratio of pension plan assets to actuarial accrued liabilities. Asset transfers were equal to the actuarial liability determined under the accrued benefit cost method in accordance with the CAS.
- 8/ We obtained total asset amounts as of January 1, 2009, from documents prepared by GHI's actuarial consulting firms.
- 9/ The asset variance represents the difference between our calculation of Medicare segment pension assets and GHI's calculation of the Medicare segment pension assets.

APPENDIX B: AUDITEE COMMENTS



June 24, 2011

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

Re: OIG Report March 2011, A-07-11-00358

Dear Mr. Cogley:

This response is in regard to the subject report.

GHI agrees to make the adjustment to segmented assets as of the January 1, 2009 plan year as recommended in the draft audit report. It is our understanding that the additional plans from the audit periods are currently being audited and those results will be ready in the next 6 months. Once all plans have been audited we would like to address the process to settle all of these periods.

GHI agrees to establish controls to ensure compliance with applicable Federal regulations including the Federal Acquisition Regulation (FAR), Cost Accounting Standards (CAS) and Medicare contract requirements concerning segmentation of pension activity including contributions, prepayment credits, benefit payments, participant transfers, investment earnings and administrative expenses.

Please let me know if you have any questions regarding this letter.

Sincerely,

A handwritten signature in black ink that reads 'Peter S. Moore'. The signature is written in a cursive style with a large initial 'P'.

Peter S. Moore
Vice President

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