



May 17, 2011

TO: Donald M. Berwick, M.D.
Administrator
Centers for Medicare & Medicaid Services

FROM: /Diann M. Saltman/ for
George M. Reeb
Acting Deputy Inspector General for Audit Services

SUBJECT: Review of Termination Claim for Postretirement Benefits Made by Blue Cross
Blue Shield of Mississippi (A-07-11-00359)

Attached, for your information, is an advance copy of our final report on the termination claim for postretirement benefit costs made by Blue Cross Blue Shield of Mississippi (BCBS Mississippi). We will issue this report to BCBS Mississippi within 5 business days.

If you have any questions or comments about this report, please do not hesitate to contact me at (410) 786-7104 or through email at George.Reeb@oig.hhs.gov or Patrick J. Cogley, Regional Inspector General for Audit Services, Region VII, at (816) 426-3591 or through email at Patrick.Cogley@oig.hhs.gov. Please refer to report number A-07-11-00359.

Attachment



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

May 23, 2011

Report Number: A-07-11-00359

Mr. Jeff Leber
Chief Financial Officer
Blue Cross Blue Shield of Mississippi
3545 Lakeland Drive
Flowood, MS 39232-9799

Dear Mr. Leber:

Enclosed is the U.S. Department of Health & Human Services (HHS), Office of Inspector General (OIG), final report entitled *Review of Termination Claim for Postretirement Benefits Made by Blue Cross Blue Shield of Mississippi*. 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-07-11-00359 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 and Chief Financial Officer
Office of Financial Management
Centers for Medicare & Medicaid Services
Mail Stop C3-01-24
7500 Security Boulevard
Baltimore, MD 21244-1850

Department of Health & Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF TERMINATION CLAIM
FOR POSTRETIREMENT BENEFITS
MADE BY BLUE CROSS
BLUE SHIELD OF MISSISSIPPI**



Daniel R. Levinson
Inspector General

May 2011
A-07-11-00359

Office of Inspector General

<http://oig.hhs.gov>

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Notices

THIS REPORT IS AVAILABLE TO THE PUBLIC

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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.

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

Blue Cross Blue Shield of Mississippi (BCBS Mississippi), through its wholly owned subsidiary TriSpan Health Services, Inc., administered Medicare Part A operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS) until the contractual relationship was terminated effective September 30, 2009. Throughout the period of its Medicare contracts, BCBS Mississippi accounted for postretirement benefit (PRB) costs using the pay-as-you-go method.

CMS reimburses a portion of its contractors' PRB costs. In claiming PRB costs, contractors must follow cost reimbursement principles contained in the Federal Acquisition Regulation and applicable Cost Accounting Standards as required by their Medicare contracts. On December 2, 2009, BCBS Mississippi submitted a termination claim of \$4,198,848 to seek reimbursement for future PRB costs that it had not incurred prior to the termination of the Medicare contracts.

OBJECTIVE

Our objective was to determine whether BCBS Mississippi's termination claim for PRB costs associated with Medicare Part A contracts was allowable for Medicare reimbursement.

SUMMARY OF FINDING

BCBS Mississippi's entire termination claim of \$4,198,848 in PRB costs for the Medicare Part A contracts was unallowable for Medicare reimbursement. The termination claim was calculated based on a retroactive change in accounting practice without CMS approval. Therefore, and pursuant to BCBS Mississippi's Medicare contracts, none of the costs claimed were allowable.

RECOMMENDATION

We recommend that BCBS Mississippi withdraw its termination claim of \$4,198,848 for PRB costs associated with Medicare Part A contracts.

AUDITEE COMMENTS

In written comments on our draft report, BCBS Mississippi did not concur with our recommendation. BCBS Mississippi stated that it had not changed its accounting practice. BCBS Mississippi stated that it will continue to pay PRB benefits past termination on a pay-as-you-go basis, but its "... current cost accounting practice does not recover these ongoing costs in the future...." Citing FAR 49.201, BCBS Mississippi stated that the CMS Contracting Officer should exercise business judgment to "assure that the contractor is made whole, which in this case means, consistent with the statutorily-imposed requirements of contract which states that the Intermediary *not incur a loss*" (emphasis in original). BCBS Mississippi's comments are included in their entirety as the Appendix.

OFFICE OF INSPECTOR GENERAL RESPONSE

BCBS Mississippi did not provide any additional information that would cause us to revise our finding or recommendation. With respect to BCBS Mississippi's statement regarding FAR 49.201, we acknowledge that both the FAR and relevant statutes support the general principle that the CMS contracting officer has the authority to use business judgment in addressing and compromising contract claims. However, this authority, in our view, cannot be read to override provisions of the contract, CMS's *Budget and Performance Requirements* guidance, and the FAR regarding allocating and accounting for PRB costs. We held to these provisions when determining that BCBS Mississippi's unallowable PRB claim represented a request for reimbursement of unallowable costs. Accordingly, we maintain that BCBS Mississippi should withdraw the full termination claim amount.

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INTRODUCTION

BACKGROUND

Blue Cross Blue Shield of Mississippi (BCBS Mississippi), through its wholly owned subsidiary TriSpan Health Services, Inc., administered Medicare Part A operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS) until the contractual relationship was terminated and operations ceased effective September 30, 2009. Throughout the period of its Medicare contracts, BCBS Mississippi accounted for the postretirement benefit (PRB) costs associated with Medicare Part A contracts using the pay-as-you-go method.

CMS reimburses a portion of its contractors' PRB costs. In claiming PRB costs, contractors must follow cost reimbursement principles contained in the Federal Acquisition Regulation (FAR) and applicable Cost Accounting Standards as required by their Medicare contracts.

The Medicare contracts require that costs be estimated (budgeted), accumulated, and reported on a consistent basis and that any change in accounting practice be submitted to CMS in advance for approval. Furthermore, the FAR sets forth the allowability requirements and the three methods of accounting for PRB costs that are permitted under a Government contract.

On December 2, 2010, BCBS Mississippi submitted a termination claim of \$4,198,848 to seek reimbursement for future PRB costs that it had not incurred prior to the termination of the Medicare contracts.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to determine whether BCBS Mississippi's termination claim for PRB costs associated with Medicare Part A contracts was allowable for Medicare reimbursement.

Scope

At the request of CMS, we audited the PRB termination claim of \$4,198,848 that BCBS Mississippi submitted for the Medicare Part A contracts' PRB costs. Achieving our objective did not require that we review BCBS Mississippi's overall internal control structure. However, we reviewed the internal controls related to the PRB termination claim to determine whether the claim was allowable in accordance with the FAR and the Medicare contracts.

Methodology

We examined BCBS Mississippi's PRB claim in relation to applicable laws, regulations, and other Federal requirements. We also reviewed information presented in BCBS Mississippi's termination claim, which included support provided by BCBS Mississippi.

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 RECOMMENDATION

BCBS Mississippi's entire termination claim of \$4,198,848 in PRB costs for the Medicare Part A contracts was unallowable for Medicare reimbursement. The termination claim was calculated based on a retroactive change in accounting practice without CMS approval. Therefore, and pursuant to BCBS Mississippi's Medicare contracts, none of the costs claimed were allowable.

FEDERAL REQUIREMENTS

FAR 31.205-6(o) sets forth the requirements and applicable methods of accounting for PRB costs under a Government contract. PRB costs may include, but are not limited to, postretirement health care; life insurance provided outside a pension plan; and other welfare benefits, such as tuition assistance, daycare, legal services, and housing subsidies provided after retirement. PRB costs do not include retirement income and ancillary benefits, such as life insurance, that pension plans pay following employees' retirement.

FAR 31.205-6(o)(2) requires contractors to use one of three methods for measuring and assigning PRB costs to accounting periods:

- The cash basis (or pay-as-you-go) method recognizes PRB costs when they are paid.
- The terminal funding method recognizes the entire PRB liability as a lump-sum payment upon termination of employees. The lump-sum payment must be remitted to an insurer or trustee for the purpose of providing PRBs to retirees and is allowable if amortized over 15 years.
- The accrual method measures and assigns costs according to generally accepted accounting principles and pays costs to an insurer or trustee to establish and maintain a fund or reserve for the sole purpose of providing PRBs to retirees. The accrual must be calculated in accordance with generally accepted actuarial principles and practices as promulgated by the Actuarial Standards Board.

The Medicare contract, Appendix B, section II(A), requires that costs be estimated (budgeted), accumulated, and reported on a consistent basis. In addition, CMS issued to Medicare contractors the *Budget and Performance Requirements* (BPR), section VI(B), which states that "as regards the allocation of such costs to the Medicare contract/agreement ... [a]ny change in accounting practice for such pension and/or post-retirement benefit costs must be submitted to CMS in advance for approval" [emphasis in original]. The BPR further defines a change in accounting practice to include "a change from cash (pay-as-you-go) accounting to accrual accounting...." In response to our prior reviews of PRB termination claims, CMS agreed that

the Medicare contracts do not permit retroactive changes in accounting practices without advance CMS approval; accordingly, CMS issued cost disallowances on that basis.

UNALLOWABLE TERMINATION CLAIM

BCBS Mississippi's contractual relationship with CMS was terminated on September 30, 2009. On December 2, 2010, BCBS Mississippi submitted a termination claim of \$4,198,848 to seek reimbursement for future PRB costs that BCBS Mississippi had not recognized prior to the termination of the Medicare contracts.

Throughout the entire period of its Medicare contracts, BCBS Mississippi claimed PRB costs for the Medicare Part A contracts using the pay-as-you-go method. By selecting this method, BCBS Mississippi signified that, pursuant to the FAR and its Medicare contracts, it would be reimbursed only for actual paid claims during each year.

BCBS Mississippi based its termination claim for PRB costs on a retroactive change in its contract cost accounting practice from the pay-as-you-go method to the accrual method. BCBS Mississippi did not obtain CMS approval before making this change, as required by the BPR. Therefore, BCBS Mississippi's claimed reimbursement for \$4,198,848 in PRB costs was unallowable.

RECOMMENDATION

We recommend that BCBS Mississippi withdraw its termination claim of \$4,198,848 for PRB costs associated with Medicare Part A contracts.

AUDITEE COMMENTS

In written comments on our draft report, BCBS Mississippi did not concur with our recommendation. BCBS Mississippi stated that it had not changed its accounting practice. BCBS Mississippi stated that it will continue to pay PRB benefits past termination on a pay-as-you-go basis, but its "... current cost accounting practice does not recover these ongoing costs in the future...." Citing FAR 49.201, BCBS Mississippi stated that the CMS Contracting Officer should exercise business judgment to "assure that the contractor is made whole, which in this case means, consistent with the statutorily-imposed requirements of contract which states that the Intermediary *not incur a loss*" (emphasis in original). BCBS Mississippi's comments are included in their entirety as the Appendix.

OFFICE OF INSPECTOR GENERAL RESPONSE

BCBS Mississippi did not provide any additional information that would cause us to revise our finding or recommendation. With respect to BCBS Mississippi's statement regarding FAR 49.201, we acknowledge that both the FAR and relevant statutes support the general principle that the CMS contracting officer has the authority to use business judgment in addressing and compromising contract claims. However, this authority, in our view, cannot be read to override provisions of the contract, CMS's BPR guidance, and the FAR regarding

allocating and accounting for PRB costs. We held to these provisions when determining that BCBS Mississippi's unallowable PRB claim represented a request for reimbursement of unallowable costs. Accordingly, we maintain that BCBS Mississippi should withdraw the full termination claim amount.

APPENDIX

APPENDIX: AUDITEE COMMENTS



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March 31, 2011

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

Re: TriSpan Postretirement Welfare Benefits

Blue Cross & Blue Shield of Mississippi (“BCBSMS”) submits this letter in response to the Department of Health & Human Services (“HHS”), Office of Inspector General (“OIG”), draft report entitled *Review of Termination Claim for Postretirement Benefits Made by Blue Cross Blue Shield of Mississippi* (“Draft PRB Report”).

The Draft PRB Report concludes that BCBSMS’s claim for Postretirement Benefit (“PRB”) reimbursement in the amount of \$4,198,848 related to BCBSMS’s Title XVIII Medicare contract is “unallowable for Medicare reimbursement... based on a retroactive change in accounting practice without CMS approval.” BCBSMS is not in concurrence with this recommendation and believes our PRB obligations should be considered by the contracting officer as part of the final settlement.

As stated in our original letter dated December 2, 2010, BCBSMS has and will continue to pay for these benefits past termination. BCBSMS’s current cost accounting practice does not recover these ongoing costs in the future because BCBSMS will no longer hold a Medicare contract with CMS against which to charge these costs. FAR 49.201 specifically provides that business judgment, not rigid accounting principles, are to govern the settlement of terminations:

A settlement should compensate the contractor fairly for the work done and the preparations made for the terminated portions of the contract, including a reasonable allowance for profit. Fair compensation is a matter of judgment and cannot be measured exactly. In a given case, various methods may be equally appropriate for arriving at fair compensation. The use of business judgment, as distinguished from strict accounting principles, is the heart of a settlement.

(b) The primary objective is to negotiate a settlement by agreement. The parties may agree upon a total *amount* to be paid the contractor without agreeing on or segregating the particular elements of costs or profit comprising this amount.

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(c) Costs and accounting data may provide guides, but are not rigid measures, for ascertaining fair compensation. In appropriate cases, costs may be estimated, differences compromised, and doubtful questions settled by agreement. Other types of data, criteria, or standards may furnish equally reliable guides to fair compensation. The amount of recordkeeping, reporting, and accounting related to the settlement of terminated contracts should be kept to a minimum compatible with the reasonable protection of the public interests.

As noted above, a concept central to termination proceedings is that the Contracting Officer is to exercise business judgment to assure equitable treatment of the contractor. Such treatment necessarily includes actions which assure that the contractor is made whole, which in this case means, consistent with the statutorily-imposed requirements of contract which states that the Intermediary *not incur a loss*. BCBSMS has provided the documentation for the Medicare segment PRB liabilities and requests OIG and CMS give consideration for the liability generated by BCBSMS's long service to the Medicare program.

We continue to incur post retirement expenses on a pay as you go basis since the termination of the contract. We will be accumulating these expenses and submitting them for reimbursement periodically as termination expenses until we reach a final settlement. Since these are expenses that are a direct result of BCBSMS Medicare contract, they should be fully reimbursable as a termination expense and do not represent a change in accounting practice. At the time of final settlement, we would like to discuss BCBSMS future PRB obligations as we believe we are entitled to equitable treatment as allowed under the FAR.

Sincerely,

Marc H. Ransier, CPA
Blue Cross Blue Shield of Mississippi
Vice President, Finance and R&D

