

Department of Health and Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**BLUE CROSS BLUE SHIELD OF  
TENNESSEE OVERSTATED THE  
MEDICARE SEGMENT PENSION ASSETS  
AND MEDICARE'S SHARE OF THE EXCESS  
PENSION LIABILITIES DUE TO THE  
SEGMENT CLOSING**

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# *Office of Inspector General*

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## **EXECUTIVE SUMMARY**

### **BACKGROUND**

Blue Cross Blue Shield of Tennessee (BCBS Tennessee), doing business as Riverbend Government Benefits Administrator, administered Medicare Part A operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS) until the contractual relationship was terminated effective August 1, 2009.

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. Furthermore, in situations such as contract terminations, the Medicare contracts require contractors to identify excess Medicare pension assets/liabilities, in accordance with CAS 413.

#### **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.

Upon the termination of its Medicare contracts, BCBS Tennessee identified Medicare's share of the Medicare segment excess pension liabilities to be \$2,195,355.

#### **Prior Pension Segmentation Audit Report**

We performed a prior pension segmentation audit at BCBS Tennessee (A-07-03-03043, issued October 4, 2004), which brought the Medicare segment pension assets to January 1, 2002. We recommended that BCBS Tennessee decrease its Medicare segment pension assets by \$610,201 and, as a result, recognize \$3,348,862 as the Medicare segment pension assets as of January 1, 2002.

### **OBJECTIVE**

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

- implementing the prior audit recommendation,
- updating the Medicare segment's pension assets from January 1, 2002, to August 1, 2009, and
- determining Medicare's share of the Medicare segment excess pension liabilities as a result of the termination of the Medicare contracts.

## **SUMMARY OF FINDINGS**

BCBS Tennessee implemented the prior audit recommendation to recognize \$3,348,862 as the Medicare segment pension assets as of January 1, 2002. BCBS Tennessee identified Medicare segment pension assets of \$2,315,658; however, we determined that the Medicare segment pension assets were \$2,139,292 as of August 1, 2009. The difference, \$176,366, was an overstatement of Medicare segment pension assets. BCBS Tennessee overstated the Medicare segment pension assets because it did not calculate them in accordance with Federal requirements and the Medicare contract's pension segmentation language when updating the Medicare segment pension assets from January 1, 2002, to August 1, 2009.

In addition, BCBS Tennessee computed Medicare's share of the Medicare segment excess pension liabilities to be \$2,195,355; however, we determined that Medicare's share of the Medicare segment excess pension liabilities was \$2,016,746 as of August 1, 2009. The difference, \$178,609, was unallowable for Medicare reimbursement. BCBS Tennessee overstated Medicare's share of excess pension liabilities because it did not calculate them in accordance with Federal requirements.

## **RECOMMENDATIONS**

We recommend that BCBS Tennessee:

- decrease Medicare segment pension assets as of August 1, 2009, by \$176,366 and
- decrease Medicare's share of the excess pension liabilities by \$178,609 and submit for reimbursement \$2,016,746 as Medicare's share of the excess pension liabilities due to the segment closing calculation.

## **AUDITEE COMMENTS**

In written comments on our draft report, BCBS Tennessee concurred with our recommendations and stated that it would work directly with CMS to resolve these issues.

BCBS Tennessee's comments are included in their entirety as Appendix C.

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## **Glossary of Abbreviations and Acronyms**

BCBS Tennessee	Blue Cross Blue Shield of Tennessee
CAS	Cost Accounting Standards
CMS	Centers for Medicare & Medicaid Services
FAR	Federal Acquisition Regulation
WAV	weighted average value

## **INTRODUCTION**

### **BACKGROUND**

#### **Blue Cross Blue Shield of Tennessee and Medicare**

Blue Cross Blue Shield of Tennessee (BCBS Tennessee), doing business as Riverbend Government Benefits Administrator, administered Medicare Part A operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS) until the contractual relationship was terminated effective August 1, 2009.

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. Furthermore, in situations such as contract terminations, the Medicare contracts require contractors to identify excess Medicare pension assets/liabilities, in accordance with CAS 413.

#### **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. CAS 413 also addresses the determination of segment assets and liabilities in the event of contract terminations, segment closings, or pension plan terminations.

#### **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. 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.

Upon the termination of its Medicare contracts, BCBS Tennessee identified Medicare's share of the Medicare segment excess pension liabilities to be \$2,195,355.

#### **Prior Pension Segmentation Audit Report**

We performed a prior pension segmentation audit at BCBS Tennessee (A-07-03-03043, issued October 4, 2004), which brought the Medicare segment pension assets to January 1, 2002. We recommended that BCBS Tennessee decrease its Medicare segment pension assets by \$610,201

and, as a result, recognize \$3,348,862 as the Medicare segment pension assets as of January 1, 2002.

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

### **Objective**

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

- implementing the prior audit recommendation,
- updating the Medicare segment's pension assets from January 1, 2002, to August 1, 2009, and
- determining Medicare's share of the Medicare segment excess pension liabilities as a result of the termination of the Medicare contracts.

### **Scope**

We reviewed BCBS Tennessee's identification of its Medicare segment; update of Medicare segment assets from January 1, 2002, to August 1, 2009; and the Medicare segment's closing calculation as of August 1, 2009.

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

We performed fieldwork at BCBS Tennessee's office in Chattanooga, Tennessee, during November and December 2011.

### **Methodology**

To accomplish our objectives, we took the following steps:

- We reviewed the portions of the FAR, CAS, and the Medicare contracts applicable to this audit.
- We reviewed the annual actuarial valuation reports prepared by BCBS Tennessee'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 reviewed the Medicare segment closing calculation prepared by BCBS Tennessee's staff and its actuarial consulting firms.

- 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 BCBS Tennessee staff responsible for identifying the Medicare segment to determine whether the segment was properly identified in accordance with the Medicare contracts.
- We reviewed BCBS Tennessee's accounting records to verify the segment identification and benefit payments made to the Medicare segment.
- We reviewed the prior segmentation audit performed at BCBS Tennessee (A-07-03-03043) to determine the beginning market value of assets.
- We provided the CMS Office of the Actuary with the actuarial information necessary for it to calculate the Medicare segment pension assets from January 1, 2002, to August 1, 2009, and the Medicare segment's excess pension liabilities as of August 1, 2009.
- We reviewed the CMS actuaries' methodology and calculations.

We performed this review in conjunction with our audit of BCBS Tennessee's pension costs claimed for Medicare reimbursement (A-07-12-00390) 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**

BCBS Tennessee implemented the prior audit recommendation to recognize \$3,348,862 as the Medicare segment pension assets as of January 1, 2002. BCBS Tennessee identified Medicare segment pension assets of \$2,315,658; however, we determined that the Medicare segment pension assets were \$2,139,292 as of August 1, 2009. The difference, \$176,366, was an overstatement of Medicare segment pension assets. BCBS Tennessee overstated the Medicare segment pension assets because it did not calculate them in accordance with Federal requirements and the Medicare contract's pension segmentation language when updating the Medicare segment pension assets from January 1, 2002, to August 1, 2009.

Appendix A presents details of the Medicare segment's pension assets from January 1, 2002, to August 1, 2009, as determined during our audit. Table 1 below 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 Audit</b>	<b>Per BCBS Tennessee</b>	<b>Difference</b>
<b>Prior Audit Recommendation</b>	\$3,348,862	\$3,348,862	\$0
<b>Update of Medicare Segment Assets</b>			
Contributions and Transferred Prepayment Credits	\$6,015,874	\$6,066,099	(\$50,225)
Benefit Payments	(4,594,436)	(4,564,305)	(30,131)
Net Transfers	(4,241,307)	(4,241,574)	267
Earnings, Net Expenses	1,610,299	1,706,576	(96,277)
<b>Overstatement of Medicare Segment Assets</b>			<b>(\$176,366)</b>

In addition, CAS 413 requires a segment closing adjustment to be made in order to recognize Medicare's share of the Medicare segment excess pension liabilities as a result of the termination of the Medicare contracts. BCBS Tennessee computed Medicare's share of the Medicare segment excess pension liabilities to be \$2,195,355; however, we determined that Medicare's share of the Medicare segment excess pension liabilities was \$2,016,746 as of August 1, 2009. The difference, \$178,609, was unallowable for Medicare reimbursement. BCBS Tennessee overstated Medicare's share of excess pension liabilities because it did not calculate them in accordance with Federal requirements.

## **PRIOR AUDIT RECOMMENDATION**

BCBS Tennessee implemented the prior audit recommendation (A-07-03-03043) which recommended that BCBS Tennessee decrease Medicare segment pension assets by \$610,201 and recognize \$3,348,862 of Medicare segment pension assets as of January 1, 2002.

## **UPDATE OF MEDICARE SEGMENT PENSION ASSETS**

### **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. 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.

Finally, 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 Transferred Prepayment Credits Overstated**

BCBS Tennessee overstated contributions and transferred prepayment credits by \$50,225 for the Medicare segment. The overstatement occurred primarily because BCBS Tennessee did not correctly calculate the assignable pension cost upon which the contributions and transferred prepayment credits were based. As a result, BCBS Tennessee overstated the Medicare segment pension assets by \$50,225.

The audited contributions and transferred prepayment credits are based on the assignable pension costs. In compliance with the CAS, we applied prepayment credits first to current-year assignable pension costs (because the credits were available at the beginning of the year) and then updated any remaining credits with interest to the next measurement (valuation) date. We then allocated contributions to assigned pension costs, as needed, as of the date of deposit.

Table 2 on the following page provides information on our calculations of contributions and prepayment credits, BCBS Tennessee's calculations, and the difference between the two on a year-by-year basis.

<b>Table 2: Contributions and Prepayment Credits for the Medicare Segment</b>			
	<b>Per Audit</b>	<b>Per BCBS Tennessee</b>	<b>Difference</b>
2002	\$668,557	\$668,557	\$0
2003	776,702	838,172	(61,470)
2004	889,287	929,448	(40,161)
2005	1,085,165	1,099,958	(14,793)
2006	1,076,502	1,026,789	49,713
2007	932,594	919,849	12,745
2008	332,756	324,830	7,926
2009	254,311	258,496	(4,185)
<b>Total</b>	<b>\$6,015,874</b>	<b>\$6,066,099</b>	<b>(\$50,225)</b>

### **Benefit Payments Understated**

BCBS Tennessee understated benefit payments by \$30,131 because of differences in the identification of the Medicare segment participants for 2006. Therefore, the Medicare segment pension assets were overstated by \$30,131.

### **Net Transfers Overstated**

BCBS Tennessee overstated net transfers out of the Medicare segment by \$267. The overstatement occurred primarily because BCBS Tennessee incorrectly identified participants who transferred in and out of the Medicare segment. This overstatement of the net transfer adjustment resulted in an understatement of the Medicare segment assets by \$267.

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

BCBS Tennessee overstated investment earnings, less administrative expenses, by \$96,277 for the Medicare segment, because it used incorrect contributions and transferred prepayment credits, benefit payments, and net transfers (all discussed above), to develop the Medicare segment pension asset base. In our audited update, we allocated earnings, net expenses based on the applicable CAS requirements.

Table 3 on the following page provides information on our calculations of earnings, net expenses, BCBS Tennessee's calculations, and the difference between the two on a year-by-year basis.

<b>Table 3: Earnings, Net Expenses for the Medicare Segment</b>			
	<b>Per Audit</b>	<b>Per BCBS Tennessee</b>	<b>Difference</b>
2002	(\$353,735)	(\$382,748)	\$29,013
2003	779,115	839,115	(60,000)
2004	550,447	559,466	(9,019)
2005	540,697	550,882	(10,185)
2006	816,291	827,490	(11,199)
2007	334,695	343,712	(9,017)
2008	(1,231,421)	(1,271,172)	39,751
2009	174,210	239,831	(65,621)
<b>Total</b>	<b>\$1,610,299</b>	<b>\$1,706,576</b>	<b>(\$96,277)</b>

## **MEDICARE SEGMENT EXCESS PENSION LIABILITIES**

### **Federal Requirements**

#### *Medicare Contracts*

In the event of a contract termination, the Medicare contracts require contractors to follow the segment closing provision of the CAS. Furthermore, in situations such as contract terminations, the Medicare contracts require contractors to identify excess Medicare pension assets/liabilities in accordance with CAS 413.

#### *Cost Accounting Standards*

Contract terminations and segment closings are addressed by CAS 413.50(c)(12), which states:

If a segment is closed, if there is a pension plan termination, or if there is a curtailment of benefits, the contractor shall determine the difference between the actuarial liability for the segment and the market value of the assets allocated to the segment, irrespective of whether or not the pension plan is terminated. The difference between the market value of the assets and the actuarial accrued liability for the segment represents an adjustment of previously-determined pension costs.

(i) The determination of the actuarial accrued liability shall be made using the accrued benefit cost method. The actuarial assumptions employed shall be consistent with the current and prior long term assumptions used in the measurement of pension costs....

(ii) ... The market value of the assets shall be reduced by the accumulated value of prepayment credits, if any. Conversely, the market value of assets shall be increased by the current value of any unfunded actuarial liability separately identified and maintained in accordance with 9904.412-50(a)(2).

(iii) The calculation of the difference between the market value of the assets and the actuarial accrued liability shall be made as of the date of the event (e.g., contract termination, plan amendment, plant closure) that caused the closing of the segment, pension plan termination, or curtailment of benefits. If such a date is not readily determinable, or if its use can result in an inequitable calculation, the contracting parties shall agree on an appropriate date.

(iv) Pension plan improvements adopted within 60 months of the date of the event which increase the actuarial accrued liability shall be recognized on a prorata basis using the number of months the date of adoption preceded the event date. Plan improvements mandated by law or collective bargaining agreement are not subject to this phase-in.

### **Medicare Segment Excess Pension Liabilities as of August 1, 2009**

BCBS Tennessee identified \$2,287,164 in excess Medicare segment pension liabilities as of August 1, 2009. However, we calculated the excess Medicare segment pension liabilities to be \$2,132,994 as of that date. Therefore, BCBS Tennessee overstated the excess pension liabilities by \$154,170. The overstatement occurred because BCBS Tennessee did not fully comply with Federal regulations in its calculation of the Medicare segment's excess pension liabilities. Specifically, BCBS Tennessee overstated the excess pension liabilities because it (a) overstated the Medicare segment's final market value of pension assets as of August 1, 2009, (b) did not adjust the Medicare segment's final market value of assets by the accumulated unfunded actuarial liability, (c) did not recognize a prorated portion of the 2006 pension plan amendment when calculating its final accrued actuarial liabilities, and (d) incorrectly identified the final Medicare segment participants as of August 1, 2009. The development of excess liabilities was used to identify Medicare's share of Medicare segment's excess pension liabilities.

### **Medicare's Share of Excess Pension Liabilities as of August 1, 2009**

#### *Federal Requirements*

The methodology for determining the Federal Government's share of excess pension liabilities is addressed by CAS 413.50(c)(12)(vi), which states:

The Government's share of the adjustment amount determined for a segment shall be the product of the adjustment amount and a fraction. The adjustment amount shall be reduced for any excise tax imposed upon assets withdrawn from the funding agency of a qualified pension plan. The numerator of such fraction shall be the **sum of the pension plan costs** allocated to all contracts and subcontracts (including Foreign Military Sales) subject to this Standard during a period of years representative of the Government's participation in the pension plan. The denominator of such fraction shall be the **total pension costs** assigned to cost accounting periods during those same years. This amount shall represent an adjustment of contract prices or cost allowance as appropriate. The adjustment

may be recognized by modifying a single contract, several but not all contracts, or all contracts, or by use of any other suitable technique. [Emphasis added.]

*Medicare’s Share of the Excess Pension Liabilities Overstated*

BCBS Tennessee calculated \$2,195,355 as Medicare’s share of the excess pension liabilities as of August 1, 2009; however, we determined that Medicare’s share of the excess pension liabilities was \$2,016,746 as of August 1, 2009. The difference, \$178,609, was unallowable for Medicare reimbursement. BCBS Tennessee overstated Medicare’s share of excess pension liabilities because it did not calculate them in accordance with Federal requirements. More specifically, the overstatement occurred primarily because BCBS Tennessee (1) overstated the Medicare segment’s excess pension liabilities (as discussed above) and (2) did not correctly compute the aggregate Medicare percentage in accordance with the CAS.

In accordance with CAS 413.50(c)(12)(vi), we calculated the aggregate Medicare percentage using the Medicare segment pension costs developed during the prior pension costs claimed reports (A-07-04-03054 and A-07-94-00815) and current pension costs claimed (A-07-12-00390) audits. Appendix B shows our calculation of the Medicare segment’s aggregate Medicare percentage; Table 4 below shows our calculation of Medicare’s share of the excess pension liabilities.

<b>Table 4: Medicare’s Share of Excess Pension Liabilities</b>			
	<b>Excess Medicare Segment Liabilities (A)</b>	<b>Aggregate Medicare Percentage (B)</b>	<b>Excess Liabilities Attributable to Medicare (A x B)</b>
Per Audit	\$2,132,994	94.55%	\$2,016,746
Per BCBS Tennessee	2,287,164	95.99%	2,195,355
<b>Difference</b>			<b>(\$178,609)</b>

**RECOMMENDATIONS**

We recommend that BCBS Tennessee:

- decrease Medicare segment pension assets as of August 1, 2009, by \$176,366 and
- decrease Medicare’s share of the excess pension liabilities by \$178,609 and submit for reimbursement \$2,016,746 as Medicare’s share of the excess pension liabilities due to the segment closing calculation.

**AUDITEE COMMENTS**

In written comments on our draft report, BCBS Tennessee concurred with our recommendations and stated that it would work directly with CMS to resolve these issues.

BCBS Tennessee’s comments are included in their entirety as Appendix C.

## **OTHER MATTER**

BCBS Tennessee did not correctly identify the Total Company pension assets as of August 1, 2009, in its proposed asset update. BCBS Tennessee did not include the 2008 contributions, which totaled \$46,500,000, in its Total Company pension assets as of August 1, 2009. We included these contributions in our update and identified \$202,264,169 as the Total Company pension assets as of August 1, 2009.

# **APPENDIXES**

**APPENDIX A: STATEMENT OF MARKET VALUE OF PENSION ASSETS  
FOR BLUE CROSS BLUE SHIELD OF TENNESSEE  
FOR THE PERIOD JANUARY 1, 2002, TO AUGUST 1, 2009**

Description		Total Company	“Other” Segment	Medicare Segment
Assets January 1, 2002	<u>1/</u>	\$122,002,507	\$118,653,645	\$3,348,862
Transferred Prepayment Credits	<u>2/</u>	0	(668,557)	668,557
Contributions	<u>3/</u>	58,400,000	58,400,000	0
Earnings	<u>4/</u>	(9,944,663)	(9,606,195)	(338,468)
Benefit Payments	<u>5/</u>	(14,443,923)	(14,230,190)	(213,733)
Expenses	<u>6/</u>	(448,578)	(433,311)	(15,267)
Transfers	<u>7/</u>	0	179,823	(179,823)
Assets January 1, 2003		\$155,565,343	\$152,295,215	\$3,270,128
Transferred Prepayment Credits		0	(776,702)	776,702
Contributions		15,000,000	15,000,000	0
Earnings		28,991,250	28,193,136	798,114
Benefit Payments		(27,335,404)	(27,058,853)	(276,551)
Expenses		(690,136)	(671,137)	(18,999)
Transfers		0	(11,768)	11,768
Assets January 1, 2004		\$171,531,053	\$166,969,891	\$4,561,162
Transferred Prepayment Credits		0	(889,287)	889,287
Contributions		12,500,000	12,500,000	0
Earnings		17,722,676	17,147,614	575,062
Benefit Payments		(12,499,156)	(12,330,702)	(168,454)
Expenses		(758,592)	(733,977)	(24,615)
Transfers		0	(46,305)	46,305
Assets January 1, 2005		\$188,495,981	\$182,617,234	\$5,878,747
Transferred Prepayment Credits		0	(1,085,165)	1,085,165
Contributions		25,500,000	25,500,000	0
Earnings		14,741,370	14,171,880	569,490
Benefit Payments		(18,231,295)	(18,199,986)	(31,309)
Expenses		(745,325)	(716,532)	(28,793)
Transfers		0	821,764	(821,764)
Assets January 1, 2006		\$209,760,731	\$203,109,195	\$6,651,536

Description		Total Company	“Other” Segment	Medicare Segment
Assets January 1, 2006		\$209,760,731	\$203,109,195	\$6,651,536
Transferred Prepayment Credits		0	(1,076,502)	1,076,502
Contributions		14,500,000	14,500,000	0
Earnings		25,159,874	24,318,438	841,436
Benefit Payments		(17,916,581)	(15,891,602)	(2,024,979)
Expenses		(751,859)	(726,714)	(25,145)
Transfers		0	1,906,666	(1,906,666)
Assets January 1, 2007		\$230,752,165	\$226,139,481	\$4,612,684
Transferred Prepayment Credits		0	(932,594)	932,594
Contributions		11,800,000	11,800,000	0
Earnings		16,257,839	15,902,750	355,089
Benefit Payments		(24,356,428)	(22,813,668)	(1,542,760)
Expenses		(933,738)	(913,344)	(20,394)
Transfers		0	(206,607)	206,607
Assets January 1, 2008		\$233,519,838	228,976,018	\$4,543,820
Transferred Prepayment Credits		0	(332,756)	332,756
Contributions		46,500,000	46,500,000	0
Earnings		(56,768,493)	(55,554,500)	(1,213,993)
Benefit Payments		(24,741,528)	(24,446,912)	(294,616)
Expenses		(814,950)	(797,522)	(17,428)
Transfers		0	1,077,251	(1,077,251)
Assets January 1, 2009		\$197,694,867	\$195,421,579	\$2,273,288
Transferred Prepayment Credits		0	(254,311)	254,311
Contributions		0	0	0
Earnings		13,733,148	13,555,032	178,116
Benefit Payments		(8,862,719)	(8,820,685)	(42,034)
Expenses		(301,127)	(297,221)	(3,906)
Transfers		0	520,483	(520,483)
Assets August 1, 2009		\$202,264,169	\$200,124,877	\$2,139,292
Per BCBS Tennessee	8/	\$155,764,169	153,448,511	\$2,315,658
Asset Variance	9/	\$46,500,000	\$46,676,366	(\$176,366)

**ENDNOTES**

- 1/ We determined the Medicare segment pension assets as of January 1, 2002, based upon our prior segmentation audit of Blue Cross Blue Shield of Tennessee (BCBS Tennessee) (A-07-03-03043). 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 avoid incurring unallowable interest. 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 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 investment earnings from the actuarial valuation reports. 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).
- 5/ We based the Medicare segment’s benefit payments on actual payments to Medicare retirees. We obtained the benefit payments from documents provided by BCBS Tennessee.
- 6/ We allocated administrative expenses to the Medicare segment in proportion to investment earnings.
- 7/ We identified participant transfers between segments by comparing valuation data files provided by BCBS Tennessee. 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 August 1, 2009, from documents prepared by BCBS Tennessee’s actuarial consulting firms.
- 9/ The asset variance represents the difference between our calculation of Medicare segment pension assets and BCBS Tennessee’s calculation of the Medicare segment pension assets.

**APPENDIX B: CALCULATION OF AGGREGATE MEDICARE PERCENTAGE**

<b>Year</b>	<b>Medicare Segment Pension Costs Charged to Medicare</b>	<b>Total Medicare Segment Pension Costs</b>	<b>Medicare's Aggregate %</b>
1/	(A)	(B)	(A/B) 2/
1987	\$97,683	\$103,286	
1988	\$26,896	\$28,503	
1989	\$0	\$0	
1990	\$0	\$0	
1991	\$0	\$0	
1992	\$0	\$0	
1993	\$54,844	\$57,164	
1994	\$89,417	\$101,265	
1995	\$74,111	\$89,907	
1996	\$169,818	\$179,247	
1997	\$160,780	\$165,208	
1998	\$196,581	\$200,880	
1999	\$264,620	\$266,943	
2000	\$267,253	\$269,246	
2001	\$362,514	\$364,153	
2002	\$597,996	\$600,759	
2003	\$712,033	\$749,666	
2004	\$806,631	\$861,141	
2005	\$959,517	\$1,036,195	
2006	\$1,021,822	\$1,078,668	
2007	\$896,316	\$968,571	
2008	\$435,748	\$482,716	
2009	\$313,335	\$337,500	
<b>Total</b>	<b>\$7,507,915</b>	<b>\$7,941,018</b>	<b>94.55%</b>

**ENDNOTES**

1/ The aggregate percentage was based on the audited pension costs as determined during the pension audits related to the Tennessee Medicare segment. The information for fiscal years 1987 - 1993 was obtained during our prior audit (A-07-94-00815). The information for fiscal years 1994 - 2002 was obtained from the prior audit (A-07-04-03054). The information for fiscal years 2003 - 2009 was obtained during the current review (A-07-12-00390).

2/ We calculated the aggregate Medicare percentage by dividing the Medicare Segment Pension Costs Claimed for Medicare Reimbursement (numerator) by the Total Medicare Segment Pension Costs (denominator) pursuant to Cost Accounting Standard 413.

## APPENDIX C: AUDITEE COMMENTS



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July 13, 2012

Patrick J. Cogley  
Regional Inspector General for Audit Services  
Department of Health & Human Services  
Office of Inspector General  
Office of Audit Services, Region VII  
601 East 12<sup>th</sup> Street, Room 0429  
Kansas City, MO 64016

Re: Report Number: A-07-12-00389

Mr. Cogley:

This letter is in response to your letter dated June 22, 2012, and the attached draft report entitled *Blue Cross Blue Shield of Tennessee Overstated the Medicare Segment Pension Assets and Medicare's Share of Excess Pension Liabilities Due to the Segment Closing*. As requested, following are our comments on the two summary recommendations set forth in the report including a statement of concurrence as well as a statement describing the nature of the corrective action taken or planned to be taken.

**Recommendation:** Decrease Medicare segment pension assets by \$176,366

We concur with this recommendation and will work directly with CMS to resolve this issue because we no longer have access to the CAFM system.

**Recommendation:** Decrease Medicare's share of excess pension liabilities by \$178,609 and submit for reimbursement of \$2,016,746

We concur with this recommendation and will work with CMS to resolve this issue.

If you have questions or comments regarding this response or require anything further from us please contact me by e-mail at [Ralph.Woodard@BCBST.com](mailto:Ralph.Woodard@BCBST.com) or by phone at 423-535-5192.

Sincerely,

T. Ralph Woodard, Jr.  
Chief Financial Officer, Riverbend Government Benefits Administrator, Inc.