

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**BLUE CROSS BLUE SHIELD OF
TENNESSEE OVERCLAIMED
SUPPLEMENTAL EXECUTIVE
RETIREMENT PLAN COSTS
FOR FISCAL YEARS
2005 THROUGH 2009**

*Inquiries about this report may be addressed to the Office of Public Affairs at
Public.Affairs@oig.hhs.gov.*



Gloria L. Jarmon
Deputy Inspector General

September 2012
A-07-12-00391

Office of Inspector General

<http://oig.hhs.gov>

The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health and Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

Office of Audit Services

The Office of Audit Services (OAS) provides auditing services for HHS, either by conducting audits with its own audit resources or by overseeing audit work done by others. Audits examine the performance of HHS programs and/or its grantees and contractors in carrying out their respective responsibilities and are intended to provide independent assessments of HHS programs and operations. These assessments help reduce waste, abuse, and mismanagement and promote economy and efficiency throughout HHS.

Office of Evaluation and Inspections

The Office of Evaluation and Inspections (OEI) conducts national evaluations to provide HHS, Congress, and the public with timely, useful, and reliable information on significant issues. These evaluations focus on preventing fraud, waste, or abuse and promoting economy, efficiency, and effectiveness of departmental programs. To promote impact, OEI reports also present practical recommendations for improving program operations.

Office of Investigations

The Office of Investigations (OI) conducts criminal, civil, and administrative investigations of fraud and misconduct related to HHS programs, operations, and beneficiaries. With investigators working in all 50 States and the District of Columbia, OI utilizes its resources by actively coordinating with the Department of Justice and other Federal, State, and local law enforcement authorities. The investigative efforts of OI often lead to criminal convictions, administrative sanctions, and/or civil monetary penalties.

Office of Counsel to the Inspector General

The Office of Counsel to the Inspector General (OCIG) provides general legal services to OIG, rendering advice and opinions on HHS programs and operations and providing all legal support for OIG's internal operations. OCIG represents OIG in all civil and administrative fraud and abuse cases involving HHS programs, including False Claims Act, program exclusion, and civil monetary penalty cases. In connection with these cases, OCIG also negotiates and monitors corporate integrity agreements. OCIG renders advisory opinions, issues compliance program guidance, publishes fraud alerts, and provides other guidance to the health care industry concerning the anti-kickback statute and other OIG enforcement authorities.

Notices

THIS REPORT IS AVAILABLE TO THE PUBLIC
at <http://oig.hhs.gov>

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 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.

BCBS Tennessee sponsors a supplemental executive retirement plan (SERP) whose primary purpose is to provide deferred compensation to a select group of management or highly compensated employees. The SERP is a nonqualified defined-benefit pension plan designed to restore benefits lost because of the Internal Revenue Code limits applicable to the regular qualified pension plan.

CMS reimburses a portion of its contractors' SERP costs. In claiming SERP costs, contractors must follow cost reimbursement principles contained in the Federal Acquisition Regulation, Cost Accounting Standards (CAS), and the Medicare contracts.

OBJECTIVE

Our objective was to determine whether the following costs were allowable for Medicare reimbursement:

- SERP costs claimed by BCBS Tennessee for Medicare reimbursement for fiscal years (FY) 2005 through 2009 and
- BCBS Tennessee's termination claim, dated November 24, 2009, for SERP costs associated with the Medicare Part A contracts.

SUMMARY OF FINDINGS

BCBS Tennessee claimed \$1,365,259 in SERP costs; however, we determined that allowable SERP costs for FYs 2005 through 2009 were \$359,578. The difference, \$1,005,681, was unallowable for Medicare reimbursement. BCBS Tennessee claimed unallowable SERP costs because it did not calculate them in accordance with Federal regulations and the Medicare contracts' requirements.

In addition, BCBS Tennessee's termination claim for SERP costs was unallowable for Medicare reimbursement. BCBS Tennessee submitted a termination claim of \$365,285 for Medicare reimbursement of SERP costs that it said it would incur subsequent to the termination of the Medicare contracts. Pursuant to CAS 412, BCBS Tennessee's entire termination claim of \$365,285 for SERP costs was unallowable for Medicare reimbursement.

RECOMMENDATIONS

We recommend that BCBS Tennessee:

- revise its Final Administrative Cost Proposals for FYs 2005 through 2009 to reduce its claimed SERP costs by \$1,005,681 and
- withdraw its termination claim of \$365,285 for SERP costs associated with the Medicare Part A contracts.

AUDITEE COMMENTS

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

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

TABLE OF CONTENTS

	<u>Page</u>
INTRODUCTION	1
BACKGROUND	1
Blue Cross Blue Shield of Tennessee and Medicare	1
Supplemental Executive Retirement Plan.....	1
OBJECTIVE, SCOPE, AND METHODOLOGY	1
Objective.....	1
Scope.....	1
Methodology.....	2
FINDINGS AND RECOMMENDATIONS	2
FEDERAL REQUIREMENTS FOR SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN	3
UNALLOWABLE SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN COSTS CLAIMED	3
UNALLOWABLE SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN TERMINATION CLAIM	4
RECOMMENDATIONS	5
AUDITEE COMMENTS	5
OTHER MATTER	5
 APPENDIXES	
A: BLUE CROSS BLUE SHIELD OF TENNESSEE STATEMENT OF ALLOWABLE SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN COSTS FOR FISCAL YEARS 2005 THROUGH 2009	
B: AUDITEE COMMENTS	

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 August 1, 2009.

Supplemental Executive Retirement Plan

BCBS Tennessee sponsors a supplemental executive retirement plan (SERP) whose primary purpose is to provide deferred compensation to a select group of management or highly compensated employees.¹ The SERP is a nonqualified defined-benefit pension plan designed to restore benefits lost because of the Internal Revenue Code limits applicable to the regular qualified pension plan.

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

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to determine whether the following costs were allowable for Medicare reimbursement:

- SERP costs claimed by BCBS Tennessee for Medicare reimbursement for fiscal years (FY) 2005 through 2009 and
- BCBS Tennessee's termination claim, dated November 24, 2009, for SERP costs associated with the Medicare Part A contracts.

Scope

We reviewed BCBS Tennessee's SERP costs claimed on its Final Administrative Cost Proposals (FACP) for FYs 2005 through 2009. Additionally, at the request of CMS, we audited the SERP termination claim of \$365,285 that BCBS Tennessee submitted for the Medicare Part A contracts' SERP costs.

¹ BCBS Tennessee's plan document refers to its nonqualified defined-benefit plan as the "Supplemental Retirement Program for Certain Employees of BCBS Tennessee" (emphasis added). However, for this report we follow the more widely used convention and refer to such plans as supplemental executive retirement *plans*.

Achieving our objective did not require that we review BCBS Tennessee's internal control structure. We reviewed the controls related to the SERP costs that BCBS Tennessee claimed for Medicare reimbursement to ensure that those costs were allowable in accordance with the FAR and the CAS.

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

Methodology

We obtained information from BCBS Tennessee regarding costs associated with the SERP for FYs 2005 through 2009² and the termination invoice submitted to CMS. We identified the SERP costs for the Total Company including the Medicare segment. BCBS Tennessee provided us with information on its SERP benefit payments and Medicare line-of-business percentages. In accordance with the FAR and the CAS, we calculated the allowable amortizable benefit for participants who received a lump-sum benefit payment.

We performed this review in conjunction with our audits of pension segmentation requirements (A-07-12-00389) and of pension costs claimed for Medicare reimbursement (A-07-12-00390) for BCBS Tennessee. We used the information obtained and reviewed during these audits in performing 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 claimed \$1,365,259 in SERP costs; however, we determined that allowable SERP costs for FYs 2005 through 2009 were \$359,578. The difference, \$1,005,681, was unallowable for Medicare reimbursement. BCBS Tennessee claimed unallowable SERP costs because it did not calculate them in accordance with Federal regulations and the Medicare contracts' requirements.

In addition, BCBS Tennessee's termination claim for SERP costs was unallowable for Medicare reimbursement. BCBS Tennessee submitted a termination claim of \$365,285 for Medicare reimbursement of SERP costs that it said it would incur subsequent to the termination of the Medicare contracts. Pursuant to CAS 412, BCBS Tennessee's entire termination claim of \$365,285 for SERP costs was unallowable for Medicare reimbursement.

² Through the August 1, 2009, contract termination date.

FEDERAL REQUIREMENTS FOR SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN

The determination and allocation of pension costs are addressed by the Medicare contract, which states: “The calculation of and accounting for pension costs charged to this agreement/contract are governed by the Federal Acquisition Regulation and Cost Accounting Standards 412 and 413.” To be allowable for Medicare reimbursement, pension costs must be (1) measured, assigned, and allocated in accordance with CAS 412 and 413 and (2) funded as specified by part 31 of the FAR.

According to CAS 412.50(c)(3), the cost of nonqualified defined-benefit pension plans shall be assigned to cost accounting periods in the same manner as qualified plans under the following conditions:

- the contractor, in disclosing or establishing cost accounting practices, elects to have a plan so accounted for;
- the plan is funded through the use of a funding agency; and
- the right to a pension benefit is nonforfeitable and is communicated to the participants.

CAS 412.50(c)(4) states that the costs must be assigned using the pay-as-you-go method if a plan does not meet all of the above requirements. The amount of pension costs assignable to a cost accounting period for pay-as-you-go plans is specified in CAS 412.50(b)(3) and consists of:

- the net amount for any periodic benefits paid for that period and
- the level annual installment required to amortize over 15 years any lump-sum benefit payments.

FAR 31.201-2(a) further states, in part, that a cost must be reasonable to be allowable. In addition, FAR 31.205-6(b)(2) provides that comparable market data be used to evaluate the reasonableness of compensation. Furthermore, FAR 31.201-6(a) states: “When an unallowable cost is incurred, its directly associated costs are also unallowable.” SERP pension benefits are directly associated with compensation because the benefit is based on the salary history of the recipient.

Additionally, FAR 31.205-6(p) states: “Costs incurred ... for compensation of a senior executive in excess of the benchmark compensation amount determined applicable for the contractor fiscal year ... are unallowable.”

UNALLOWABLE SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN COSTS CLAIMED

BCBS Tennessee claimed \$1,365,259 in SERP costs; however, we determined that allowable SERP costs for FYs 2005 through 2009 were \$359,578. The difference, \$1,005,681, was

unallowable for Medicare reimbursement. BCBS Tennessee claimed unallowable SERP costs because it did not calculate them in accordance with Federal regulations and the Medicare contracts' requirements.

The Medicare contracts require BCBS Tennessee to calculate SERP costs in accordance with the FAR and CAS 412 and 413. BCBS Tennessee did not meet the conditions for assigning the cost of its nonqualified defined-benefit pension plan in the same manner as qualified plans. Therefore, it should have assigned SERP costs to cost accounting periods using the pay-as-you-go method. However, BCBS Tennessee incorrectly assigned SERP costs on an accrual basis.

We calculated the allowable SERP costs based on periodic payments made to SERP recipients, plus a 15-year amortization of lump-sum SERP payments, in accordance with CAS 412-50(b)(3). Accordingly, we determined that the allowable pay-as-you-go SERP costs for FYs 2005 through 2009 totaled \$359,578.

The table below compares allowable SERP costs with the SERP costs claimed on BCBS Tennessee's FACPs. Appendix A contains additional details on the allowable SERP costs.

<u>Medicare SERP Costs</u>			
Fiscal Year	Allowable Per Audit	Claimed by BCBS Tennessee	Difference
2005	\$74,869	\$354,696	(\$279,827)
2006	66,848	342,207	(275,359)
2007	82,956	368,442	(285,486)
2008	88,114	207,738	(119,624)
2009	46,791	92,176	(45,385)
Total	\$359,578	\$1,365,259	(\$1,005,681)

UNALLOWABLE SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN TERMINATION CLAIM

BCBS Tennessee's entire termination claim of \$365,285 in SERP costs for the Medicare Part A contracts was unallowable for Medicare reimbursement. BCBS Tennessee submitted a termination claim for costs that it said it would incur subsequent to the termination of the Medicare contracts.

According to CAS 412.50(c)(3) and (c)(4), BCBS Tennessee's SERP should have assigned SERP costs to cost accounting periods using the pay-as-you-go cost method. The allocable costs of BCBS Tennessee's SERP therefore consisted of (1) the net amount for any periodic benefits paid for that period and (2) the level annual installment required to amortize, over 15 years, any lump-sum benefit payments.

BCBS Tennessee's contractual relationship with CMS terminated on August 1, 2009. On November 24, 2009, BCBS Tennessee submitted a termination claim of \$365,285 to seek reimbursement for unamortized SERP costs that it said it had not incurred prior to the

termination of the Medicare contracts but would incur subsequent to the termination of those contracts. BCBS Tennessee based its termination claim on a 2003 settlement loss.

The termination claim represented a claim for reimbursement of unfunded costs, which did not comply with all the requirements of CAS 412.50(c)(3). In addition, the SERP termination claim was based on an amount that did not comply with the CAS. Pursuant to CAS 412, these costs were unallowable for Medicare reimbursement.

RECOMMENDATIONS

We recommend that BCBS Tennessee:

- revise its FACPs for FYs 2005 through 2009 to reduce its claimed SERP costs by \$1,005,681 and
- withdraw its termination claim of \$365,285 for SERP costs associated with the Medicare Part A contracts.

AUDITEE COMMENTS

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

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

OTHER MATTER

BCBS Tennessee's Medicare contract was terminated on August 1, 2009. BCBS Tennessee claimed SERP costs on its FACPs through July 31, 2009. However, as of August 1, 2009, BCBS Tennessee had a remaining balance of unamortized SERP payments of \$8,449,576 prior to being allocated to Medicare on the basis of the Medicare-to-Total-Company ratio.

APPENDIXES

**APPENDIX A: BLUE CROSS BLUE SHIELD OF TENNESSEE STATEMENT
OF ALLOWABLE SUPPLEMENTAL EXECUTIVE RETIREMENT
PROGRAM COSTS FOR FISCAL YEARS 2005 THROUGH 2009**

Year	Amortized Lump-Sum Benefit Payments	Annuity Benefit Payments	Allocable Total Benefit Payments	Medicare Salary Ratio	Medicare Allowable SERP Costs
	1/	2/	3/	4/	5/
2005	578,444	230,077	808,521	9.26%	74,869
2006	588,274	220,046	808,320	8.27%	66,848
2007	903,503	201,102	1,104,605	7.51%	82,956
2008	1,143,224	195,901	1,339,125	6.58%	88,114
2009	1,061,637	163,250	1,224,887	3.82%	46,791
Total	\$4,275,082	\$1,010,376	\$5,285,458		\$359,578

ENDNOTES

- 1/ Blue Cross Blue Shield of Tennessee (BCBS Tennessee) provided a schedule of lump-sum benefit payments. In accordance with Cost Accounting Standard 412.50(b)(3), we amortized the lump-sum benefit payments, including an interest equivalent, over a 15-year period. In computing the interest component for the amortized lump-sum benefit payments, we used the valuation interest rate identified in the qualified defined benefit plan actuarial valuation reports.
- 2/ BCBS Tennessee provided a schedule of annuity payments for each calendar year. We converted the calendar annuity payments to a fiscal year basis (October 1 through September 30). We calculated the fiscal-year annuity payments as 1/4 of the prior year's annuity payments plus 3/4 of the current year's annuity payments.
- 3/ Allocable total benefit payments are the sum of the (i) amortized allocable lump-sum benefit payments and (ii) allocable annuity benefit payments. Allocable total benefit payments differ from the total benefit payments provided to us by BCBS Tennessee because of the amortization of lump-sum benefit payments.
- 4/ BCBS Tennessee provided the Total Company Medicare salary ratio for each fiscal year. We verified the percentages and determined that they were reasonable.
- 5/ Medicare allowable Supplemental Executive Retirement Plan costs are total benefit payments multiplied by the Medicare salary ratio.

APPENDIX B: AUDITEE COMMENTS



of Tennessee
plans for better health. plans for a better life.™

1 Cameron Hill Circle
Chattanooga, TN 37402

bcbst.com

August 10, 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 12th Street, Room 0429
Kansas City, MO 64016

Re: Report Number: A-07-12-00391

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 Overclaimed Supplemental Executive Retirement Plan Costs for Fiscal Years 2005 Through 2009*. 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.

Recommendation: Reduce claimed SERP costs by \$1,005,681

We concur with this recommendation and will work directly with CMS to resolve this issue as we no longer have access to the CAFM system to revise FACP's.

Recommendation: Withdraw termination claim of \$365,285

We concur with this recommendation and will work with CMS to resolve this issue. In addition, we will request payment from CMS for the allowable portion of unamortized SERP payments.

If you have questions or comments regarding this response or require anything further, please contact me by e-mail at Ralph.Woodard@BCBST.com or by phone at 423-535-5192.

Sincerely,

A handwritten signature in black ink that reads "T. Ralph Woodard, Jr." with a stylized flourish at the end.

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