

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**GROUP HEALTH INCORPORATED
CLAIMED UNALLOWABLE MEDICARE
PENSION COSTS FOR
PLAN YEARS 2007 AND 2008**

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



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

**March 2016
A-07-16-00475**

Office of Inspector General

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EXECUTIVE SUMMARY

Group Health Incorporated claimed unallowable pension costs of \$1.2 million for Medicare reimbursement during plan years 2007 and 2008.

WHY WE DID THIS REVIEW

Medicare contractors are eligible to be reimbursed a portion of their pension costs, which are funded by the annual contributions that these contractors make to their pension plans. The amount of pension costs that the Centers for Medicare & Medicaid Services (CMS) reimburses to the contractors is determined by the cost reimbursement principles contained in the Federal Acquisition Regulation (FAR), Cost Accounting Standards (CAS), and Medicare contracts. Previous Office of Inspector General reviews found that Medicare contractors have not always complied with Federal requirements when claiming pension costs for Medicare reimbursement.

At CMS's request, the Office of Inspector General, Office of Audit Services, Region VII pension audit team reviews the cost elements related to qualified defined-benefit, nonqualified defined-benefit, postretirement benefit, and any other pension-related cost elements claimed by Medicare fiscal intermediaries and carrier contractors and Medicare administrative contractors through Final Administrative Cost Proposals and/or Incurred Cost Proposals (ICPs).

For this review, we focused on one Medicare contractor, Group Health Incorporated (GHI). In particular, we examined the GHI Medicare segment and Other segment pension costs that GHI claimed for Medicare reimbursement on its ICPs.

The objective of this review was to determine whether the plan years (PYs) 2007 and 2008 pension costs that GHI claimed for Medicare reimbursement, and reported on its ICPs, were allowable and correctly claimed.

BACKGROUND

GHI, an EmblemHealth Company, administered Medicare Part B operations under cost reimbursement contracts with CMS; these contracts terminated on July 18, 2008. As of November 1, 1999, GHI also administers Medicare operations under a Coordination of Benefits contract with CMS. In addition, GHI performs Medicare work as a subcontractor on the Retiree Drug Subsidy contract and the Medicare Secondary Payer Recovery Contract as of February 17, 2005, and August 15, 2006, respectively.

Before January 1, 2007, GHI based its request for Medicare reimbursement on directly claimed costs. Effective January 1, 2007, GHI amended its disclosure statement with CMS to receive Medicare reimbursement based on indirect cost rates submitted on an ICP.

CMS reimburses a portion of the annual contributions that contractors make to their pension plans. The pension costs are included in the computation of the indirect cost rates reported on the ICPs. In turn, CMS uses indirect cost rates in reimbursing costs under cost-reimbursement contracts. In claiming costs, contractors must follow cost reimbursement principles contained in

the FAR, CAS, and Medicare contracts. The cognizant contracting officer will perform a final settlement with the contractor to determine the final indirect cost rates. These rates ultimately determine the final costs of each contract. Contract costs are settled upon the end of the final option period of the contract.

We previously reviewed GHI's allocable pension costs (A-07-12-00381, issued March 13, 2013). That audit report identified the allocable pension costs that GHI should have used when calculating its indirect costs rates for PYs 2007 and 2008.

At the request of CMS, Figliozzi & Company, P.C. (Figliozzi), performed an audit of the ICPs that GHI submitted for PYs 2007 and 2008. At CMS's direction, Figliozzi excluded defined-benefit plan pension costs from its review. CMS will use this allowable pension cost report and Figliozzi's audit report to determine the final indirect cost rates and the total allowable contract costs for GHI for PYs 2007 and 2008.

We reviewed \$4,272,186 of pension costs that GHI reported on its ICPs for PYs 2007 and 2008.

WHAT WE FOUND

GHI claimed Medicare pension costs of \$4,272,186 for Medicare reimbursement, through its ICPs, for PYs 2007 and 2008; however, we determined that the allowable CAS-based pension costs during this period were \$3,056,573. The difference, \$1,215,613, represented unallowable Medicare pension costs that GHI claimed on its ICPs for PYs 2007 and 2008. GHI claimed these unallowable Medicare pension costs primarily because it based its claim for Medicare reimbursement on incorrectly calculated allocable CAS pension costs.

WHAT WE RECOMMEND

We recommend that GHI work with CMS to ensure that its final settlement of contract costs reflects a decrease in Medicare pension costs of \$1,215,613 for PYs 2007 and 2008.

AUDITEE COMMENTS

In written comments on our draft report, GHI agreed with our finding. GHI stated that it would work with CMS to ensure that the final settlement of contract costs reflects an offset in Medicare pension costs for the amounts cited in PYs 2007 and 2008.

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INTRODUCTION

WHY WE DID THIS REVIEW

Medicare contractors are eligible to be reimbursed a portion of their pension costs, which are funded by the annual contributions that these contractors make to their pension plans. The amount of pension costs that the Centers for Medicare & Medicaid Services (CMS) reimburses to the contractors is determined by the cost reimbursement principles contained in the Federal Acquisition Regulation (FAR), Cost Accounting Standards (CAS), and Medicare contracts. Previous Office of Inspector General reviews found that Medicare contractors have not always complied with Federal requirements when claiming pension costs¹ for Medicare reimbursement.

At CMS's request, the Office of Inspector General, Office of Audit Services, Region VII pension audit team reviews the cost elements related to qualified defined-benefit, nonqualified defined-benefit, postretirement benefit, and any other pension-related cost elements claimed by Medicare fiscal intermediaries and carrier contractors and Medicare administrative contractors through Final Administrative Cost Proposals and/or Incurred Cost Proposals (ICPs).

For this review, we focused on one Medicare contractor, Group Health Incorporated (GHI). In particular, we examined the GHI Medicare segment and Other segment pension costs that GHI claimed for Medicare reimbursement and reported on its ICPs.

OBJECTIVE

Our objective was to determine whether the plan years (PYs)² 2007 and 2008 pension costs that GHI claimed for Medicare reimbursement, and reported on its ICPs, were allowable and correctly claimed.

BACKGROUND

Group Health Incorporated

GHI, an EmblemHealth Company, administered Medicare Part B operations under cost reimbursement contracts with CMS; these contracts terminated on July 18, 2008.³ As of

¹ Unless otherwise noted, all subsequent references to Medicare pension costs and reimbursement in the body of this report relate to the Coordination of Benefits (COB), Retiree Drug Subsidy (RDS), and Medicare Secondary Payer Recovery Contract (MSPRC)—all of which are explained below—Medicare pension costs.

² GHI's plan year is January 1 to December 31.

³ We reviewed the allowability of the Part B pension costs that GHI claimed for Medicare reimbursement in a separate audit (A-07-12-00379, issued Apr. 4, 2012).

November 1, 1999, GHI also administers Medicare operations under a COB contract with CMS.⁴ In addition, GHI performs Medicare work as a subcontractor on the RDS⁵ and the MSPRC⁶ as of February 17, 2005, and August 15, 2006, respectively.

During our 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, LLC, Employees' Retirement Plan. Medicare segment employees of GHI participated in all three of these pension plans.

Before January 1, 2007, GHI based its request for Medicare reimbursement on directly claimed costs.⁷ Effective January 1, 2007, GHI amended its disclosure statement with CMS to receive reimbursement based on indirect cost rates submitted on an ICP.⁸

Medicare Reimbursement of Pension Costs

CMS reimburses a portion of the annual contributions that contractors make to their pension plans. The pension costs are included in the computation of the indirect cost rates reported on the ICPs. In turn, CMS uses indirect cost rates in reimbursing costs under cost-reimbursement contracts. 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. In claiming costs, contractors must follow cost reimbursement principles contained in the FAR, the CAS, and the Medicare contracts. The cognizant contracting officer

⁴ The COB contract was issued in accordance with Section 1893 of the Social Security Act (the Act), (added by the Health Insurance Portability and Accountability Act of 1996, P.L. No. 104-191, § 202(a)) to carry out the Medicare Integrity Program activities established by the Act. The primary function of the COB contract is to consolidate activities that support the collection, management, and reporting of all health insurance coverage of Medicare beneficiaries.

⁵ The RDS helps employers and unions assist Medicare-eligible retirees in obtaining prescription drug coverage. The RDS contract was awarded to ViPS, Incorporated. GHI entered into an agreement with ViPS to perform work as a subcontractor on the RDS program.

⁶ The MSPRC protects the Medicare Trust Fund by ensuring that Medicare does not pay for items and services when other health insurance coverage is primarily responsible for paying. The MSPRC was awarded to Chickasaw Nation Industries Administration Services, LLC (CNIAS). GHI entered into an agreement with CNAIS to perform work as a subcontractor on the MSPRC contract.

⁷ We reviewed the allowability of the COB, RDS, and MSPRC pension costs that GHI claimed for Medicare reimbursements during PYs 1999 through 2006 in a separate audit (A-07-12-00380, issued Apr. 4, 2012).

⁸ At the end of each calendar year, each Medicare contractor submits to CMS an ICP which reports the Medicare direct and indirect costs that the contractor incurred during that year. The ICP and supporting data provide the basis for the CMS Contracting Officer and the Medicare contractor to determine the final billing rates for allowable Medicare costs.

will perform a final settlement with the contractor to determine the final indirect cost rates. The final indirect cost rates ultimately determine the final costs of each contract.⁹

Previous Audit of Allocable Pension Costs

We previously reviewed GHI's allocable pension costs (A-07-12-00381, issued March 13, 2013; see also Appendix A). That audit report identified the allocable pension costs that GHI should have used when calculating its indirect costs rates for PYs 2007 and 2008. We recommended that GHI:

- decrease the allocable pension costs in its fringe cost pool (and used to calculate its indirect fringe cost rate) by \$1,411,051, and recognize \$3,258,532 as the allocable pension costs for the fringe cost pool and its indirect fringe rate calculation in its ICPs for PYs 2007 and 2008; and
- decrease the allocable pension costs in its general and administrative (G&A) cost pool by \$10,382,279 and recognize \$540,853 as the pension costs included in the indirect G&A cost rate calculation in its ICPs for PYs 2007 and 2008.

Based on these recommendations, after allocations, the pension costs that GHI included in the G&A cost pools for PYs 2007 and 2008 should have been decreased by \$376,093.

Incurred Cost Proposal Audit

At CMS's request, Figliozzi & Company, P.C. (Figliozzi), performed an audit of the ICPs that GHI submitted for PYs 2007 and 2008. The objective of the Figliozzi audit was to examine GHI's ICP and render an opinion on whether the incurred costs claimed by GHI were reasonable, allocable to the contract, and allowable under the provisions of the contract, part 31 of the FAR, and the U.S. Department of Health and Human Services Acquisition Regulation (HHSAR). Figliozzi also reviewed the adequacy of GHI's accounting system.

At CMS's direction, Figliozzi excluded defined-benefit plan pension costs from its review. CMS will use this allowable pension cost report and the Figliozzi audit report to determine the final indirect cost rates and the total allowable contract costs for GHI for PYs 2007 and 2008.

HOW WE CONDUCTED THIS REVIEW

We reviewed \$4,272,186 of pension costs that GHI reported on its ICPs for PYs 2007 and 2008.

Achieving our objective did not require that we review GHI's overall internal control structure. We limited our review to the internal controls related to the pension costs that were included in

⁹ In accordance with FAR 42.705-1(5)(ii) and FAR 42.705-1(5)(iii)(B), the cognizant contracting officer shall "[p]repare a written indirect cost rate agreement conforming to the requirements of the contracts" and perform a "...[r]econciliation of all costs questioned, with identification of items and amounts allowed or disallowed in the final settlement," respectively.

GHI's ICPs and ultimately used as the basis for Medicare reimbursement, to ensure that the pension costs were allowable in accordance with the FAR.

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.

Appendix A contains details of our audit scope and methodology.

FINDING

GHI claimed Medicare pension costs of \$4,272,186 for Medicare reimbursement, through its ICPs, for PYs 2007 and 2008; however, we determined that the allowable CAS-based pension costs during this period were \$3,056,573. The difference, \$1,215,613, represented unallowable Medicare pension costs that GHI claimed on its ICPs for PYs 2007 and 2008. GHI claimed these unallowable Medicare pension costs primarily because it based its claim for Medicare reimbursement on incorrectly calculated allocable CAS pension costs.

Claimed Medicare Pension Costs

GHI claimed pension costs of \$4,272,186 for PYs 2007 and 2008. We calculated the allowable Medicare pension costs based on separately computed CAS-based pension costs for the Medicare segment and the Other segment in accordance with CAS 412 and 413.

Unallowable Medicare Pension Costs Claimed

After incorporating the results from both Figliozzi's ICP audit and our previous allocable pension costs audit report, we determined that the allowable Medicare pension costs for PYs 2007 and 2008 were \$3,056,573. Thus, GHI overstated the allowable pension costs for these PYs by \$1,215,613. This overclaim occurred because GHI based its allowable pension costs on calculations that did not comply with CAS 412 and 413. In addition, according to Figliozzi's audit report, GHI's ICP submissions for PYs 2007 and 2008 did not comply with part 31 of the FAR or the HHSAR. Figliozzi also reviewed the adequacy of GHI's accounting system as it related to the costs claimed on its ICPs.

As mentioned above, our previous audit found that GHI overstated the pension cost used in the calculation of the fringe cost pool for PYs 2007 and 2008 by \$1,411,051. Our previous audit also found that GHI overstated the pension costs in its G&A indirect costs rate for PYs 2007 and 2008 by \$376,093.

Our computations of the audited indirect cost rates for the current audit included the adjustments mentioned above. Table 1 on the following page shows the allocable CAS-based pension costs that our previous audit of GHI's PYs 2007 and 2008 pension costs identified for both the fringe

cost pool and the G&A cost pool, and compares those amounts with the amounts that GHI proposed in its ICPs.

Table 1: Previous Audit Findings			
Plan Year	Allocable Per Previous Audit	Per GHI	Difference
Fringe Cost Pool			
2007	\$ 1,411,656	\$ 2,521,135	\$ (1,109,479)
2008	1,846,876	2,148,448	(301,572)
Total	\$ 3,258,532	\$ 4,669,583	\$ (1,411,051)
G&A Indirect Cost Rate			
2007	\$ 293,246	\$ 406,349	\$ (113,103)
2008	247,607	510,597	(262,990)
Total	\$ 540,853	\$ 916,946	\$ (376,093)

We then used this information to adjust the fringe and G&A rates and, in turn, to calculate the information below. We are not showing our calculations in this report because the rate calculations that GHI used are proprietary information. Table 2 below compares, for each of the three contracts, the Medicare segment pension costs that we calculated (using our adjusted fringe and G&A rates) and the pension costs that GHI claimed for Medicare reimbursement for PYs 2007 and 2008.

Table 2: Medicare Pension Costs¹⁰			
	Per Audit	Per GHI	Difference
PY 2007			
COB Contract	\$1,074,368	\$1,853,609	(\$779,241)
MSPRC	160,164	276,147	(115,983)
RDS Contract	99,309	169,629	(70,320)
Total PY 2007 Overclaim	\$1,333,841	\$2,299,385	\$ (965,544)
PY 2008			
COB Contract	1,340,661	1,535,515	(194,854)
MSPRC	215,242	247,266	(32,024)
RDS Contract	166,829	190,020	(23,191)
Total PY 2008 Overclaim	\$1,722,732	\$1,972,801	\$ (250,069)
Total Overclaim of Pension Costs	\$3,056,573	\$4,272,186	(\$1,215,613)

¹⁰ Our calculations incorporated the rate ceiling associated with the COB contract. We applied the indirect costs rates associated with the COB contract when computing the allowable pension costs for the MSPRC and RDS contracts.

RECOMMENDATION

We recommend that GHI work with CMS to ensure that its final settlement of contract costs reflects a decrease in Medicare pension costs of \$1,215,613 for PYs 2007 and 2008.

AUDITEE COMMENTS

In written comments on our draft report, GHI agreed with our finding. GHI stated that it would work with CMS to ensure that the final settlement of contract costs reflects an offset in Medicare pension costs for the amounts cited in PYs 2007 and 2008.

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

APPENDIX A: AUDIT SCOPE AND METHODOLOGY

SCOPE

We reviewed \$4,272,186 of Medicare pension costs that GHI reported on its ICPs for PYs 2007 and 2008.

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

We performed our fieldwork at GHI's office in New York, New York.

METHODOLOGY

To accomplish our objective, we:

- reviewed the portions of the FAR, CAS, and Medicare contracts applicable to this audit;
- reviewed information provided by GHI to identify the amount of pension costs used in GHI's calculation of its indirect costs rates for PYs 2007 and 2008;
- reviewed the results of Figliozzi's ICP audit and incorporated the results into our calculations of allowable pension costs; and
- incorporated the information from our previous audit report (A-07-12-00381, issued March 13, 2013) into our work for this audit.

We performed this review in conjunction with the following audit and used the information obtained during that audit for this review: *Group Health Incorporated Overstated Allocable Pension Costs for Plan Years 2007 and 2008* (A-07-12-00381, issued March 13, 2013).

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 objectives.

APPENDIX B: FEDERAL REQUIREMENTS RELATED TO REIMBURSEMENT OF PENSION COSTS

FEDERAL REGULATIONS

Federal regulations (FAR 31.205-6(j)) address the allowability of pension costs and require that contractors fund the pension costs assigned to contract periods by making contributions to the pension plan.

Federal regulations (CAS 412) (as amended) address the determination and measurement of pension cost components. This regulation also addresses the assignment of pension costs to appropriate accounting periods.

Federal regulations (CAS 413) (as amended) address 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.

MEDICARE CONTRACTS

The Medicare contracts require GHI to submit invoices in accordance with FAR 52.216-7, “Allowable Cost & Payment.” Furthermore, FAR 52.216-7(a)(1) addresses the invoicing requirements and the allowability of payments as determined by the Contracting Officer in accordance with FAR subpart 31.2.

APPENDIX C: AUDITEE COMMENTS



February 25, 2016

Mr. 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

Subject: Report Number A-07-16-00475

Dear Mr. Cogley:

Thank you for affording Group Health Incorporated (“GHI”) this opportunity to comment on the U.S. Department of Health and Human Services, Office of Inspector General (“OIG”), final audit report entitled *Group Health Incorporated Claimed Unallowable Medicare Pension Costs for Plan Years 2007 and 2008*.

GHI has carefully reviewed the Draft Audit Report. The report reflected work that was performed by the OIG and a subcontracted audit firm regarding pensions at GHI billed to CMS for Plan Years 2007 and 2008. GHI has no issue with the findings that were identified in this Draft report.

We agree to work with CMS to ensure that the final settlement of contract costs reflects an offset in Medicare pension costs for the amounts cited in Plan Years 2007 and 2008. The final settlement will be a global settlement for the relevant contracts. This final global settlement also needs to include allowable but unclaimed costs that GHI incurred to support the contracts. We will be working with CMS to incorporate these costs into the final settlement amounts.

Sincerely,

A handwritten signature in black ink that reads "Peter S. Moore". The signature is written in a cursive style.

Peter S. Moore
Vice President

Cc: Matt Rubin, Asst. Controller, External Reporting, EmblemHealth
Eric Shipley, CMS Chief Actuary
Theresa Schultz, CMS Contracting Officer
Kathy Markman, CMS Contracting Officer
Greg Rosenthal, Mercer

Group Health Incorporated
441 9th Ave, New York, NY 10001