

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**FIRST COAST SERVICE OPTIONS,
INC.'S, POSTRETIREMENT
BENEFIT COSTS
WERE REASONABLE
AND ALLOWABLE**

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Office of Inspector General

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represent the findings and opinions of OAS. Authorized officials of the
HHS operating divisions will make final determination on these matters.

Report in Brief

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U.S. DEPARTMENT OF HEALTH & HUMAN SERVICES
OFFICE OF INSPECTOR GENERAL



Why **OIG** Did This Review

The Centers for Medicare & Medicaid Services (CMS) reimburses a portion of Medicare contractors' costs for postretirement benefit (PRB) plans. At CMS's request, the **OIG**, Office of Audit Services, Region VII pension audit team reviews the cost elements related to PRB costs claimed by Medicare contractors through Incurred Cost Proposals (ICPs).

Previous **OIG** reviews found that Medicare contractors have not always complied with Federal requirements when claiming PRB costs for Medicare reimbursement.

Our objective was to determine whether the calendar years (CYs) 2008 through 2010 PRB costs that First Coast Service Option, Inc. (FCSO), claimed for Medicare reimbursement, and reported on its ICPs, were allowable and correctly claimed.

How **OIG** Did This Review

We reviewed \$2.7 million of Medicare PRB costs that FCSO reported on its ICPs for CYs 2008 through 2010.

First Coast Service Options, Inc.'s, Postretirement Benefit Costs Were Reasonable and Allowable

What **OIG** Found

The PRB costs that FCSO claimed for Medicare reimbursement on its ICPs for CYs 2008 through 2010 were allowable and reasonable, and thus were correctly claimed.

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INTRODUCTION

WHY WE DID THIS REVIEW

Medicare contractors are eligible to be reimbursed a portion of their postretirement benefit (PRB) costs, which are funded by direct payments to beneficiaries or contributions to a dedicated trust fund. The amount of PRB 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) as required by the Medicare contracts. Previous Office of Inspector General reviews found that Medicare contractors have not always complied with Federal requirements when claiming PRB costs for Medicare reimbursement.

At CMS's request, the U.S. Department of Health and Human Services (HHS), 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, PRB, and any other pension-related cost elements claimed by Medicare fiscal intermediaries and carrier contractors and Medicare administrative contractors (MACs) through Final Administrative Cost Proposals and/or Incurred Cost Proposals (ICPs).

For this review, we focused on one Medicare contractor, First Coast Service Options, Inc. (FCSO). In particular, we examined the FCSO Medicare segment and Other segment PRB costs (herein referred to as "PRB costs") that FCSO claimed for Medicare reimbursement and reported on its ICPs.

OBJECTIVE

Our objective was to determine whether the calendar years (CYs) 2008 through 2010 PRB costs that FCSO claimed for Medicare reimbursement, and reported on its ICPs, were allowable and correctly claimed.

BACKGROUND

First Coast Service Options, Inc., and Medicare

During our audit period, FCSO and C2C Innovative Solutions, Inc. (C2C), were wholly owned subsidiaries of Diversified Service Options, Inc., a holding company created and owned by Blue Cross and Blue Shield of Florida, Inc. (BCBS Florida), whose office is located in Jacksonville, Florida. FCSO administered Medicare Part A fiscal intermediary and Part B carrier contract operations under cost reimbursement contracts with CMS until its contractual relationships ended on February 13, 2009, and February 1, 2009, respectively. With the implementation of

Medicare contracting reform,¹ FCSO continued to perform Medicare work after being awarded the MAC contract for Medicare Parts A and B Jurisdiction 9² effective September 12, 2008.

On April 2, 2007, C2C was created to perform additional Medicare work under the Qualified Independent Contractors (QIC) contract for the Medicare Part A West jurisdiction and the Medicare Part B North jurisdiction; these contracts had originally been awarded to FCSO in CYs 2004 and 2006, respectively.³ On July 9, 2010, the QIC contract was formally novated from FCSO to C2C. Although C2C was created as a separate segment, its participants were included in the FCSO Medicare segment; however, C2C filed separate ICPs when claiming costs for Medicare reimbursement for the QIC contract. Therefore, FCSO calculated the PRB costs in total for its Medicare segment and then allocated those costs to both the FCSO and C2C ICPs. Subsequently, on August 5, 2011, C2C was sold to TMF Health Quality Institute.

FCSO and C2C employees participated in a PRB plan called the Blue Cross and Blue Shield of Florida, Inc., Retiree Group Benefit Plan. FCSO participates in a voluntary employee benefit association (VEBA) trust for funding annual accruals.⁴ Furthermore, FCSO's accounting practice, approved by CMS, uses segmented accrual accounting for PRBs. This report addresses the Medicare allowable PRB costs that FCSO claimed under the provisions of its MAC-related contracts.

The disclosure statement that FCSO submits to CMS states that FCSO uses pooled cost accounting. Medicare contractors use pooled costing to calculate the indirect cost rates that they submit on their ICPs. The PRB costs are included in the computations of the indirect cost

¹ Section 911 of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003, P.L. No. 108-173, required CMS to transfer the functions of fiscal intermediaries and carriers to MACs between October 2005 and October 2011. Most, but not all, of the MACs are fully operational; for jurisdictions where the MACs are not fully operational, the fiscal intermediaries and carriers continue to process claims. For purposes of this report, the term "Medicare contractor" means the fiscal intermediary, carrier, or MAC, whichever is applicable.

² Medicare Parts A and B Jurisdiction 9 consists of the State of Florida and the territories of Puerto Rico and the U.S. Virgin Islands.

³ The QIC Part A West jurisdiction includes 24 U.S. States and 3 U.S. territories. The QIC Part B North jurisdiction includes 35 northern States, the District of Columbia, and 3 U.S. territories.

⁴ FCSO participates in employee benefit plans, such as the VEBA trust, of its parent company, BCBS Florida. Costs associated with this VEBA trust are self-insurance charges as defined by the FAR.

rates reported on the ICPs. CMS uses these indirect cost rates when reimbursing costs for cost-plus-award-fee type contracts.^{5, 6}

Medicare Reimbursement of Postretirement Benefit Costs

CMS reimburses a portion of the Medicare contractors' annual PRB costs, which are funded by contributions that contractors make to their PRB plans. The PRB 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. FAR 31.205-6(o) requires that to be allowable for Medicare reimbursement, PRB costs must be (1) measured, assigned, and allocated in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 715-60 (formerly Statement of Financial Accounting Standards (SFAS) 106) 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 Cost Accounting Standards (CAS), and the 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.⁷ FCSO claimed PRB costs using segmented accrual basis of accounting.

Previous Audit of Allocable Postretirement Benefit Costs

We previously reviewed FCSO's allocable PRB costs (A-07-17-00502, Jul. 10, 2017). This report identified the allocable PRB costs that FCSO should have used when calculating its indirect cost rates for CYs 2008 through 2012. We recommended that FCSO:

- increase the Medicare segment PRB costs used to calculate its indirect cost rates by \$50,387 for CYs 2008 through 2012 and

⁵ A cost-plus-award-fee contract is a cost reimbursement contract that provides a fee consisting of (a) a base amount fixed at inception of the contract and (b) an award amount, based on a judgmental evaluation by the Federal Government.

⁶ At the end of each CY, each MAC submits to CMS an ICP that 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.

⁷ In accordance with FAR 42.705-1(b)(5)(ii) and FAR 42.705-1(b)(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.

- decrease the Other segment PRB costs used to calculate its indirect cost rates by \$3,357,884 for CYs 2008 through 2012.⁸

Incurred Cost Proposal Audits

At CMS's request, the Defense Contracting Audit Agency (DCAA), Mayer Hoffman McCann P.C. (MHM), and CliftonLarsenAllen LLP (CLA) performed audits of the ICPs that FCSO and C2C⁹ submitted for CYs 2008 through 2010. The objectives of the DCAA, MHM, and CLA reviews were to determine whether the costs were allowable in accordance with the FAR and the HHS Acquisition Regulations.

For this audit, we relied on the DCAA, MHM, and CLA audits' findings and recommendations when computing the allowable PRB costs discussed in this report.

We incorporated the results of the DCAA, MHM, and CLA audits into our computations of the audited indirect cost rates, and ultimately the PRB costs claimed, for the contracts subject to the FAR. We also incorporated our audited allocable pension, PRB, and supplemental executive retirement plan costs into our review of FCSO's ICPs to determine the allowable PRB costs. CMS will use our report on allowable PRB costs, as well as the DCAA, MHM, and CLA audit reports, to determine the final indirect cost rates and the total allowable contract costs for FCSO for CYs 2008 through 2010.

HOW WE CONDUCTED THIS REVIEW

We reviewed \$2,722,443 of PRB costs that FCSO reported on its ICPs for CYs 2008 through 2010.

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.

The Appendix contains details of our audit scope and methodology.

⁸ Because BCBS Florida curtailed its qualified pension plan as of December 31, 2010, we will use only the allocable PRB costs, as determined in our previous review, that relate to CYs 2008 through 2010. We will compute the allowable PRB costs for CYs 2011 and 2012 in a separate review. The allocable PRB variance used in this report to calculate the allowable PRB cost for CYs 2008 through 2010 resulted in an increase of \$56,200 for the Medicare segment and a decrease of \$968,884 for the Other segment's allocable PRB costs.

⁹ C2C's ICP audit for CYs 2008 and 2009 determined that the ICP submissions were inadequate. We received resubmitted ICPs from C2C and used those resubmissions in our calculation of the PRB costs claimed for C2C. The resubmitted ICPs have not been reviewed or audited to determine whether the costs were allowable in accordance with the FAR and the HHS Acquisition Regulations.

RESULTS OF REVIEW

The PRB costs that FCSO claimed for Medicare reimbursement for CYs 2008 through 2010 were allowable and reasonable, and thus were correctly claimed. Federal regulations (FAR 31.205-6(o)) require that, to be allowable for Medicare reimbursement, PRB accrual costs be (1) determined in accordance with ASC 715-60 and (2) funded by payments to an insurer or into a dedicated trust fund, such as a VEBA trust. After reviewing FCSO's methodology for claiming PRB costs, we determined that the PRB costs that FCSO reported on its ICPs for CYs 2008 through 2010 materially complied with Federal requirements. This report therefore makes no recommendations.

APPENDIX: AUDIT SCOPE AND METHODOLOGY

SCOPE

We reviewed \$2,722,443 of Medicare PRB costs that FCSO reported on its ICPs for CYs 2008 through 2010.

Achieving our objective did not require that we review FCSO's overall internal control structure. We limited our review to the internal controls related to the PRB costs that were included in FCSO's ICPs and ultimately used as the basis for Medicare reimbursement, to ensure that the PRB costs were allocable in accordance with the CAS and allowable in accordance with the FAR.

We performed our fieldwork at FCSO in Jacksonville, Florida.

METHODOLOGY

To accomplish our objective, we:

- reviewed the portions of the FAR, CAS, and Medicare contracts applicable to this audit;
- reviewed information provided by FCSO to identify the amount of PRB costs used in FCSO's calculations of its indirect cost rates for CYs 2008 through 2010;
- reviewed the results of the DCAA, MHM, and CLA ICP audits and incorporated those results into our calculations of allowable PRB costs;
- incorporated information from our previous audit report (A-07-17-00502, Jul. 10, 2017); and
- provided the results of our review to FCSO officials on April 5, 2018.

We performed this review in conjunction with the following audit and used the information obtained during that audit for this review: *First Coast Service Options, Inc., Understated Its Medicare Segment and Overstated Its Other Segment Allocable Postretirement Benefit Costs (A-07-17-00502)*.

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.