DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Memorandum

Date NOV 20 1992

From Bryan B. Mitchell Bryan Mitchell
Principal Deputy Inspector General

Subject Audit of Medicare Contractor's Segmented Pension Cost, Blue Cross and Blue Shield of Florida, Inc. (A-07-91-00473)

To William Toby, Jr.
Acting Administrator
Health Care Financing Administration

This is to alert you to the issuance on November 23, 1992, of our final audit report. A copy is attached. Our review showed that Blue Cross and Blue Shield of Florida, Inc. (Florida) had, as of January 1, 1990, overstated Medicare pension assets by $1.2 million and accumulated $2.4 million in pension costs which are unallowable for Medicare reimbursement.

Under title XVIII of the Social Security Act, intermediaries (Part A) and carriers (Part B) contractually perform Medicare administrative operations. Florida is both an intermediary and carrier for Medicare and has performed Medicare administrative operations since the inception of the program.

Contractually, Florida is required to separately identify, calculate, and report pension assets, and when appropriate, costs for the Medicare segment. Compliance requires (i) computing an actuarial liability for the segment and establishing a ratio (asset fraction) using the 1981 actuarial liabilities of the segment and the total plan, (ii) applying the ratio to total pension assets as of 1986, and (iii) updating the Medicare segment's 1986 pension assets to subsequent years.

In carrying out its contractual pension responsibility, Florida misidentified the Medicare segment cost centers and the inactive plan participants for 1981. This understated the 1981 asset fraction which, when applied to the 1986 pension assets, understated Medicare's asset share. Medicare's share of the actuarial value of pension assets on January 1, 1986, was understated by $1,206,991. We are recommending that the assets of the Medicare segment be increased by this amount as of January 1, 1986. Florida agreed with the recommendation.

Even considering the $1,206,991 understatement as of January 1, 1986, our review showed that Florida's computation of assets as of January 1, 1990, overstated the Medicare segment assets by $1,170,376. The overstatement was the net result of Florida's using contributions to the pension plan that had not been funded, identifying segment participants incorrectly, and including benefit payments in incorrect years in updating the assets from 1986 to 1990. We are recommending that the Medicare segment assets as of January 1, 1990, be reduced by $1,170,376. Florida agreed with the recommendation.

In addition, we found that, as of January 1, 1990, Florida has accumulated $2,378,198 in direct pension costs of the Medicare segment which are unallowable for future Medicare reimbursement. These pension costs are unallowable because they were not funded within a specific time period set by regulation. Imputed interest on the unfunded costs is also not allowable. The $2,378,198 represents unfunded costs and imputed interest for the period 1986 through 1989.

We are recommending that Florida separately identify $2,378,198 as being unallowable components of direct pension costs of the Medicare segment as of January 1, 1990. We are also recommending that Florida continue updating unallowable components of pension costs for subsequent years relating to the unfunded costs for 1986 through 1990 and provide similar treatment to any subsequent years' unfunded pension costs. Florida agreed with the recommendations except for the dollar amount. Florida stated the dollar amount should be either $2,172,313 or $2,346,929.

Regional Health Care Financing Administration officials did not provide comments on the draft report.

Attachment

For further information contact:
Vincent R. Imbriani
Regional Inspector General
for Audit Services, Region VII
816-426-3591

Department of Health and Human Services

OFFICE OF INSPECTOR GENERAL

AUDIT OF MEDICARE CONTRACTOR'S SEGMENTED PENSION COST, BLUE CROSS AND BLUE SHIELD OF FLORIDA, INC.

NOVEMBER 1992 A-07-91-00473

DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General
Office of Audit Services

Region VII
601 East 12th Street
Room 284A
Kansas City, Missouri 64106

NOV 23 1992

CIN: A-07-91-00473

Mr. Rick Kibler
Director of Internal Audits
Blue Cross and Blue Shield of Florida, Inc.
P.O. Box 1798
Jacksonville, Florida 32231

Dear Mr. Kibler:

Enclosed for your information are two copies of an Office of Inspector General (OIG), Office of Audit Services (OAS) report identified by the above Common Identification Number (CIN) and titled "Audit of Medicare Contractor's Segmented Pension Cost, Blue Cross and Blue Shield of Florida, Inc." Your attention is invited to the findings and recommendations contained in the report. The below named official will be communicating with you in the near future regarding implementation of necessary actions.

Final determination as to actions to be taken on all matters reported will be made by the Department of Health and Human Services (HHS) official named below. We request that you respond to the recommendations in this report within 30 days from the date of this letter to the HHS official named below, presenting any comments or additional information that you believe may have a bearing on his final decision.

In accordance with the principles of the Freedom of Information Act (Public Law 90-23), OIG, OAS' reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act which the Department chooses to exercise. (See 45 CFR Part 5.)

To facilitate identification, please refer to the above CIN in all correspondence relating to this report.

Sincerely,

Vincent R. Imbriani
Regional Inspector General for
Audit Services, Region VII

Enclosures

Direct Reply To:

Mr. George Holland
Regional Administrator, Region IV
Health Care Financing Administration
101 Marietta Tower, Suite 701
Atlanta, Georgia 30323

SUMMARY

Under title XVIII of the Social Security Act, intermediaries (Part A) and carriers (Part B) contractually perform Medicare administrative operations. Blue Cross and Blue Shield of Florida, Inc. (Florida) is both an intermediary and carrier for Medicare and has performed Medicare administrative operations since the inception of the program.

Contractually, Florida is required to separately identify, calculate, and report pension assets, and when appropriate, costs for the Medicare segment. Compliance requires (i) computing an actuarial liability for the segment and establishing a ratio (asset fraction) using the 1981 actuarial liabilities of the segment and the total plan, (ii) applying the ratio to total pension assets as of 1986, and (iii) updating the Medicare segment's 1986 pension assets to subsequent years.

In carrying out its contractual pension responsibility, Florida misidentified the Medicare segment cost centers and the inactive plan participants for 1981. This understated the 1981 asset fraction which, when applied to the 1986 pension assets, understated Medicare's asset share. Medicare's share of the actuarial value of pension assets on January 1, 1986 was understated by $1,206,991. We are recommending that the assets of the Medicare segment be increased by this amount as of January 1, 1986. Florida agreed with the recommendation.

Even considering the $1,206,991 understatement as of January 1, 1986, our review showed that Florida's computation of assets as of January 1, 1990, overstated the Medicare segment assets by $1,170,376. The overstatement was the net result of Florida using contributions to the pension plan that had not been funded, identifying segment participants incorrectly, and including benefit payments in incorrect years in updating the assets from 1986 to 1990. We are recommending that the Medicare segment assets as of January 1, 1990, be reduced by $1,170,376. Florida agreed with the recommendation.

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We are recommending that Florida separately identify $2,378,198 as being unallowable components of direct pension costs of the Medicare segment as of January 1, 1990. We are also recommending that Florida continue updating unallowable components of pension

costs for subsequent years relating to the unfunded costs for 1986 through 1990 and provide similar treatment to any subsequent years' unfunded pension costs. Florida agreed with the recommendations except for the dollar amount. Florida stated the dollar amount should be either $2,172,313 or $2,346,929.

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INTRODUCTION

BACKGROUND

Title XVIII of the Social Security Act, Health Insurance Program for the Aged and Disabled (Medicare), provides that organizations may assist in administering Medicare under contracts with the Secretary, HHS. Most Medicare contractors, intermediaries (Part A) and carriers (Part B), perform under cost reimbursement contracts which are renewed annually. Florida has administered Medicare Part A and Part B operations under cost reimbursement contracts since the inception of the Medicare program.

Contractors are to follow cost reimbursement principles contained in their contracts, the Federal Acquisition Regulations (FAR), which superseded the Federal Procurement Regulations (FPR), and the Cost Accounting Standards (CAS). A fundamental reimbursement principle in the contracts is that the contractor "...shall be paid its costs of administration under the principle of neither profit nor loss...."

To ensure that a no profit, no loss principle was followed concerning pension costs, we issued an audit report to the Health Care Financing Administration (HCFA) in 1985. The report was titled "Medicare Intermediaries and Carriers Should Be Required To Use Segment Accounting For Claiming Pension Costs" (ACN: 07-52013). The report showed that pension contributions charged to Medicare exceeded the amounts required to meet Medicare's pension liabilities. The report recommended that HCFA amend Medicare contracts to require treatment of Medicare as a separate segment for calculating and charging pension costs.

The HCFA incorporated segmenting requirements into Medicare contracts starting with Fiscal Year (FY) 1988 and distributed a pension cost questionnaire to contractors in 1989. The purpose of the questionnaire was to ensure that contractors had, and would maintain, data necessary to make and document the segmentation calculations.

Florida was a member of the National Retirement Program administered by the Blue Cross/Blue Shield National Employee Benefits Administration (NEBA). The Wyatt Company, NEBA's actuarial firm, played a major role in the preparation of Florida's questionnaire response.

CRITERIA GOVERNING SEGMENTED PENSION COSTS

Since its inception, Medicare has reimbursed a portion of annual contributions paid into contractors' pension plans. The Medicare reimbursements represented allowable pension costs in accordance with the FPR and/or the FAR. In 1980, CAS 412 and 413 were incorporated into both the FPR and the Medicare contracts.

The CAS 412 provides guidance for determining and measuring the components of pension costs. It also specifies how pension costs are to be assigned to appropriate accounting periods. The CAS 413 provides guidance for valuing pension assets, allocating pension costs to segments of an organization, adjusting pension costs for actuarial gains and losses, and assigning gains and losses to cost accounting periods.

In addition to the CAS requirements, HCFA, starting with FY 1988, incorporated specific segmenting language into Medicare contracts. The contracts specified segmentation requirements and also provided that pension assets of a Medicare segment were to be separately identified regardless of whether pension costs were allocated or separately calculated. Florida's contract generally required (1) computing the Medicare segment's actuarial liability as of 1981, (2) determining the ratio of Medicare's actuarial liability to the total actuarial liability as of 1981, (3) allocating a portion of total pension assets as of 1986 based on the 1981 ratio, (4) updating the 1986 Medicare assets to subsequent years, and (5) assessing whether Medicare's pension costs should be separately calculated.

SCOPE OF AUDIT

Our examination was made in accordance with generally accepted government auditing standards. Our objective was to determine Florida's compliance with requirements involving pension segmentation. Achieving our objective did not require that we review the internal control structure of Florida. The audit addressed Florida's initial determination, and subsequent year updates, of pension assets for a Medicare segment. Our review covered January 1, 1981 through January 1, 1990.

We reviewed Florida's identification of the Medicare segment as of January 1, 1988, and traced the segment's organizational lineage back to 1981. Utilizing Florida's organizational matrix of cost centers by operation and function and the contractual definition of a Medicare segment, we identified individual cost centers, or groupings of cost centers, that should have been included in the 1981 Medicare segment. Individual employees working in the cost centers were identified and their pension liabilities were determined using The Wyatt Company's 1981 Retirement Cost Listing (The Wyatt Company). We compared the results of our identification of cost centers, cost center employees, and employee liabilities to Florida's identifications in determining the liabilities of the 1981 Medicare segment.

The HCFA's pension actuarial staff reviewed Florida's calculations of pension assets and pension costs for 1986 through 1990. We reviewed pension assets (actuarial value) allocated to the Medicare segment as of January 1, 1986, and the asset updates made from January 1, 1986 to January 1, 1990.

We reviewed documents from Florida's accounting, personnel, and Medicare departments. We also reviewed actuarial records, benefit payments, and settlement records at NEBA and at The Wyatt Company.

In establishing pension assets and actuarial liabilities, we reviewed pension plan documents, annual actuarial valuation reports, and Department of Labor/Internal Revenue Service Forms 5500. The forms were filed annually and provided information on pension plan assets, plan participants, and annual contributions.

Field work was performed from February 1991 to December 1991. Our field work included on site efforts at Florida's corporate offices in Jacksonville, Florida and at NEBA and The Wyatt Company, both located in Chicago, Illinois.

FINDINGS AND RECOMMENDATIONS

INITIAL DETERMINATION OF THE MEDICARE SEGMENT ASSETS

Florida understated the 1986 Medicare segment pension assets by $1,206,991. Florida was required to allocate 1986 pension assets to the Medicare segment using a ratio of the 1981 actuarial liabilities of the Medicare segment to the total plan. Florida incorrectly identified plan participants and participant liabilities in determining the actuarial liability of the Medicare segment. The incorrect identifications understated the 1981 ratio and 1986 transfers for inactive participants. As a result, assets of the 1986 Medicare segment were understated.

Segmentation Requirements

The Medicare contracts specify that:

> "The term 'Medicare Segment' shall mean 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 is allocated to the Medicare agreement/contract, and these salary dollars represent 40 percent or more of the total salary dollars allocated to the Medicare agreement/contract."

The contracts also provided that, beginning with FY 1988, pension assets of the Medicare segment were to be separately identified. Assets were to be allocated to the Medicare segment as of the first pension plan year after December 31, 1985, during which the salary criteria was met. The allocation was to be based on the ratio of the actuarial liabilities of the Medicare segment to the total plan as of the first day of the first plan year starting after December 31, 1980.

Pension costs for a segment could consider all participants or just active participants (CAS, section 413.50(c)(9)). Adjustments are required for transfers in and out of a segment if the ratio of assets to liabilities would otherwise be distorted (CAS, section 413.50(c)(8)).

Computation of Assets

Florida's pension plan years began on January 1 and its asset allocation and ratio used to make the allocation are representative of conditions as of January 1, 1981 and January 1, 1986. (References in this report to segment years reflect conditions as of January 1 of the stated year.) The following schedule summarizes Florida's and our computation of the pension assets for the 1986 Medicare segment.

Description	Computations	
	Florida	OIG
1981 ASSET FRACTION		
1. 1981 Total Plan Liabilities	$25,898,039	$25,898,039
2. 1981 Medicare Segment Liabilities	$ 4,898,633	$ 5,669,559
3. 1981 Segmentation Fraction 1/	.189151	.218918
1986 MEDICARE SEGMENT ASSETS ACTIVE AND INACTIVE PARTICIPANTS		
4. 1986 Total Pension Plan Assets	$42,635,141	$42,635,141
5. 1986 Medicare Segment Assets 2/ (Includes All Plan Participants)	$ 8,064,480	$ 9,333,600
INACTIVE PARTICIPANT ADJUSTMENT		
6. 1986 Inactive Transfer Adjustment	$ (573,797)	$ (635,926)
1986 MEDICARE SEGMENT ASSETS CONSIDERING ONLY ACTIVE PARTICIPANTS		
7. 1986 Medicare Segment Assets 3/	$ 7,490,683	$ 8,697,674

1/ (1981 Medicare Segment Liabilities / 1981 Total Plan Liabilities)

2/ (1981 Segmentation Fraction x 1986 Total Pension Plan Assets)

3/ (1986 Medicare Segment Assets - 1986 Inactive Transfer Adjustment)

Our computation reflects adjustments to Florida's computation for the participant liability of the 1981 Medicare segment and for the 1986 inactive transfer adjustment. Additional details regarding our adjustments are provided in the following paragraphs.

Participant Liability of the 1981 Medicare Segment

Florida understated the actuarial liability of the 1981 Medicare segment by $770,926 due to an incorrect identification of participants and participant liabilities. Florida's determination of $4,898,633 incorrectly excluded $810,502 and included $39,576 involving 86 plan participants. We adjusted Florida's determination of the actuarial liability of the 1981 Medicare segment to reflect:

- addition of $692,575 for 65 active plan participants. We added 65 plan participants who were in cost centers, or cost center groupings, which met the contractual specifications for a segment. Florida excluded these participants.

- addition of $34,554 for five active plan participants. We included five additional participants who were in cost centers used by Florida in determining the 1981 Medicare segment.

- addition of $73,763 for six inactive plan participants. We added six additional participants who were terminated from the Medicare cost centers used by Florida.

- addition of $9,610 for six active plan participants. We corrected errors in Florida's computation of the liabilities for these participants.

- reduction of $39,576 for four active plan participants. We excluded these four participants because they were not previously assigned to Medicare cost centers or they were ineligible plan participants.

The net $770,926 increase in the actuarial liability of the 1981 Medicare segment increased the 1981 asset fraction from .189151 to .218918. When applied to total plan assets as of 1986, the higher asset fraction resulted in additional pension assets of $1,269,120 (before an inactive transfer adjustment) being allocated to the Medicare segment.

Transfer Adjustment
1986 Medicare Inactives

After establishing the assets of the 1986 Medicare segment, Florida transferred assets and liabilities of $573,797 for inactive plan participants to the nonsegment. Transferring the $573,797 reduced the assets of the 1986 Medicare segment to $7,490,683 ($8,064,480 - $573,797).

We identified 10 additional inactive plan participants, based on our identification of segment participants, who should have been included in the transfer adjustment. The 10 additional inactive participants represented assets and liabilities of $62,129. Adjusting the transfer amount for the $62,129 reduced our calculated pension assets for the 1986 Medicare segment to $8,697,674 ($9,333,600 - $635,926).

Summary

Our computation of pension assets for the 1986 Medicare segment reflects a $770,926 increase to Item 2 (1981 Medicare Segment Liabilities) and a $62,129 increase to Item 6 (1986 Inactive Transfer Adjustment). The adjustments increase the pension assets of the 1986 Medicare segment by $1,206,991 ($8,697,674 - $7,490,683). Florida's and our calculations and our adjustments are summarized in greater detail on Appendix A.

Recommendation

We recommend that Florida increase the Medicare segment's pension assets by $1,206,991 as of January 1, 1986.

Auditee Comment

"The Plan Agrees."

MEDICARE'S ASSET BASE AS OF 1986 UPDATED TO 1990

Florida's update of assets from 1986 to 1990 overstated the Medicare segment assets by $1,170,376. The change from understated assets as of 1986 to overstated assets as of 1990 was the net result of Florida's using contributions to the pension plan that had not been funded, identifying segment participants incorrectly, and including benefit payments in incorrect years.

Unfunded Contributions in Asset Update

Pension costs must be measured, assigned, and allocated in accordance with CAS 412 and 413 for Medicare reimbursement. The CAS pension costs must also meet CAS and FAR funding requirements to be allowable under Medicare. Section 412.30(a)(8) and (9) of CAS 412 defines funding as:

> "Funded pension cost. The portion of pension costs for a current or prior cost accounting period that has been paid to a funding agency...."

> "Funding agency. An organization or individual which provides facilities to receive and accumulate assets to be used either for the payment of benefits under a pension plan, or for the purchase of such benefits."

The FAR 48 CFR 31.205-6(j)(2)(i) states:

> "To be allowable in the current year, pension costs must be funded by the time set for filing the Federal income tax return or any extension thereof. Pension costs assigned to the current year, but not funded by the tax return time, shall not be allowable in any subsequent year."

Florida included $2,130,362 as pension plan contributions for the Medicare segment in updating the pension assets of the segment from 1986 to 1990. Contribution amounts included by year were:

Year	Contributions
1986	$ 30,021
1987	486,930
1988	673,550
1989	939,861

Our review of the contributions showed that, on a yearly basis, all or part of them were not funded by deposits to the trust fund. The portion of the contributions that had not been funded should not have been included in Florida's update of assets from 1986 to 1990.

The $30,021 included for 1986 represented Medicare's share of a directly paid pension administrative cost and did not represent funding of a pension plan cost. It should not have been included as a contribution in the update of the pension assets of the Medicare segment.

For its pension plan for 1987, Florida funded $1,633,003, of which $486,930 was included in the update of the pension assets for the Medicare segment. Considering the segment's ratio of computed CAS costs to total CAS costs, the proportionate amount of funded contributions for the segment should have been $309,629.

Contributions used by Florida for 1988 and 1989 represented transfers of pension assets from the nonsegment (other lines-of-business) to the Medicare segment. Although the transferred amounts were computed in accordance with CAS, the transfers of assets did not meet the definition of funding as established by CAS and the transferred amounts should not have been considered in Florida's update.

Our computation of the Medicare segment assets on Appendix C includes contributions of $309,629 for 1987 and does not include any contributions for 1986, 1988, and 1989. Our computation also considered an increase of $1,206,991 in pension assets for the Medicare segment as of January 1, 1986. (See Recommendation on page 7.)

Transfers

Florida's update of the Medicare segment included transfers of participant liabilities and assets. The transfers represented the movement of participants into and out of the Medicare segment from year to year. We updated the Medicare segment using Florida's methodology and our adjustments explained on pages 5 and 6. Amounts transferred out of each segment according to Florida's and our updates are shown in the following schedules and summarized on Appendix B and Appendix C.

Florida Transfers

Year	Segment	NonSegment	Net
1986	$883,223	$1,369,318	($486,095)
1987	417,119	461,014	(43,895)
1988	269,457	509,553	(240,096)
1989	561,823	392,144	169,679

OIG Transfers

Year	Segment	NonSegment	Net
1986	$586,261	$ 310,993	$275,268
1987	364,564	209,176	155,388
1988	330,520	395,632	(65,112)
1989	349,613	374,283	(24,670)

Benefit Payments

Florida's update included 1986 and 1987 lump sum payments with 1988 benefit payments. We included payments in the proper year, as shown below, in our update of the pension assets on Appendix C. (Difference in totals is due to rounding by year.)

	Benefit Payments	
Year	Florida	OIG
1986	$ 7,494	$ 469,858
1987	-0-	133,046
1988	860,451	265,042
1989	535,546	535,546
	$1,403,491	$1,403,492

Recommendation

We recommend that Florida:

- Transfer pension assets of $1,170,376 from the Medicare segment to the nonsegment as of January 1, 1990. This recommendation considers the increase of $1,206,991 to the Medicare segment's assets as of January 1, 1986. (See Recommendation on page 7.)

Auditee Comment

"The Plan Agrees."

UNFUNDED CAS COSTS

We found that, as of January 1, 1990, Florida had accumulated $2,378,198 in unallowable direct pension costs related to the Medicare segment. These pension costs were unallowable because they were not funded within specific time periods set by regulation. Imputed interest on the unfunded costs was also unallowable. The $2,378,198 represents unfunded costs and imputed interest for the period 1986 through 1989.

The FAR 48 CFR 31.205-6(j)(3)(i) and (iii) state:

> "...costs of pension plans not funded in the year incurred, and all other components of pension costs...assignable to the current accounting period but not funded during it, shall not be allowable in subsequent years...."

> "Increased pension costs caused by delay in funding beyond 30 days after each quarter of the year to which they are assignable are unallowable."

Furthermore, the CAS within 48 CFR 30.412-50(a)(7) states:

> "If any portion of the pension costs computed for a cost accounting period is not funded in that period, no amount for interest on the portion not funded in that period shall be a component of pension cost of any future cost accounting period."

We compared CAS pension costs for the segment, computed by HCFA's Office of the Actuary, to Florida's actual contributions to the Medicare segment for 1986 through 1989 and found:

Year	CAS Computed Costs	Actual Funding	Difference
1986	$ 200,734	$ -0-	$ 200,734
1987	445,086	309,629	135,457
1988	741,838	-0-	741,838
1989	925,581	-0-	925,581
	$2,313,239	$309,629	$2,003,610

Since the difference of $2,003,610 had not been funded within specified time periods, the pension costs are unallowable as a component of pension costs for any future years. Interest related to these unfunded costs is also unallowable as a component of future years' pension costs.

The following table shows both the unfunded amounts plus interest which are unallowable on a cumulative basis. Our computation of the unfunded amounts considered those costs which should have been funded for the applicable years. In other words, if the costs had been funded, the assets of the Medicare segment would have been greater at the specified time periods.

	Unfunded Pension Costs and Interest				
Date	1986	1987	1988	1989	Total
1/1/87	$218,800	$ -0-	$ -0-	$ -0-	$ 218,800
1/1/88	237,398	173,289	-0-	-0-	410,687
1/1/89	258,764	188,885	808,603	-0-	1,256,252
1/1/90	282,053	205,885	881,377	1,008,883	2,378,198

Recommendations

We recommend that Florida:

- separately identify $2,378,198 as unallowable components of direct pension costs as of 1990 due to unfunded CAS costs for 1986 through 1989.
- continue a yearly update of unallowable pension cost components related to the unfunded CAS costs for 1986 through 1990.
- identify and track unallowable components of pension costs for any subsequent years for which CAS costs of the pension plan are not funded.

Auditee Comments

Florida agreed with our second and third recommendations. However, Florida disagreed with our first recommendation. Details of Florida's disagreement are contained on Appendix D which is Florida's response in its entirety to the draft report.

Florida's disagreement centers on 1987 and involves two different issues. The first issue involves the allocation of funded CAS costs for 1987 and the second issue involves the computation of interest on the amount of unfunded CAS costs for 1987. To put the issues in perspective, we have included in the following paragraphs the methodologies used by OIG and the alternate methodologies advocated by Florida in its response.

OIG Methodologies Florida funded $1,633,003 of 1987 total CAS costs of $2,347,410. Since Florida only partially funded the CAS costs, we allocated the funds between the other segments and the

Medicare segment based on the ratio of Medicare CAS costs to total CAS costs. Our computation is summarized as follows:

	Total Plan	Other Segments	Medicare Segment
CAS Pension Costs	$2,347,410	$1,902,324	$445,086
Funded Pension Cost	1,633,003	1,323,374	309,629
Percent of CAS Costs Funded	69.57%	69.57%	69.57%

In determining the unfunded CAS costs for 1987, we determined interest from the first of the year and then deducted Florida's funded contribution of $309,629 made in 1988 for 1987. Our methodology is illustrated in the following table.

	1986	1987	1988	1989
CAS Pension Cost	$200,734	$445,086	$741,838	$925,581
Interest to Yearend	18,066	37,832	66,765	83,302
Interest Rate	9%	8.5%	9%	9%
Actual Contribution		(309,629)		
Interest to Yearend	0	0	0	0
	$218,800	$173,289	$808,603	$1,008,883

Florida Methodologies. Florida, first of all, disagreed with our allocation of costs between the other segments and the Medicare segment saying "that there is no provision in the Medicare contract or the CAS rules and regulations that requires the proration...." Florida advocated first considering the Medicare segment's CAS costs as being fully funded and then applying the remaining funds to the other segments. Florida's methodology results in:

	Total Plan	Other Segments	Medicare Segment
CAS Pension Costs	$2,347,410	$1,902,324	$445,086
Funded Pension Cost	1,633,003	1,187,917	445,086
Percent of CAS Costs Funded	69.57%	62.45%	100%

Florida's approach would show no 1987 unfunded pension costs for the Medicare segment and would reduce the OIG's computation of the total unallowable component (costs plus interest) from $2,378,198 to $2,172,313.

Florida also advocated that, even if a change was not made in identifying funded costs to segments for 1987, a change should be made in calculating unfunded costs plus interest for 1987. The effect of Florida's calculation is shown in the following table:

	1987
CAS Pension Cost	$445,086
Interest to Yearend	37,832
Interest Rate	8.5%
Actual Contribution	(309,629)
Interest to Yearend	(26,318)
	$146,971

This approach for 1987 would reduce the OIG's computation of the total unallowable component (costs plus interest) from $2,378,198 to $2,346,929.

OIG Response

With regard to Florida's statement on proration, we would agree that there are no specific provisions in the contract or CAS dealing with the given situation. However, both the contract and CAS provide, as a major premise, for the consistent treatment of costs among different cost objectives. For example, Paragraph B, Section II, Appendix B of the Medicare contract states "...the criteria for determining the allocation of costs...should be the same for all similar objectives." The CAS 413.50(c)(1) and (10) state "...the base to be used for allocating such costs shall be representative of the factors [on] which the pension benefits are based." and "...where pension cost is separately calculated for one or more segments, the actuarial cost method shall be the same for all segments...."

Florida made a single deposit into the pension trust fund and we found no evidence showing that any of the deposit was dedicated to a particular cost objective or group of employees. We therefore believe that proration of the funded costs is appropriate as it provides consistent and equitable treatment of the funded costs among the segments. It should also be noted that the asset update in the previous finding considers only the actual funding of $309,629 (page 10) and any change in the amount involving unfunded costs would necessitate a corresponding change in the asset update.

As to the interest question, the OIG calculation reflects the addition of interest from January 1987 for CAS costs determined as of that date and the deduction of the $309,629 contribution. Florida's calculation considers interest on both the CAS costs and the actual contribution from January 1987. Since the contribution was not made until 1988, there should be no interest considered for 1987 on the contribution.

INSTRUCTIONS FOR AUDITEE RESPONSE

Final determination as to actions to be taken on all matters reported will be made by the HHS official named below. We request that you respond to the recommendations in this report within 30 days from the date of this letter to the HHS official named below, presenting any comments or additional information that you believe may have a bearing on his final decision.

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In accordance with the principles of the Freedom of Information Act (Public Law 90-23), OIG, OAS' reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act which the Department chooses to exercise. (See 45 CFR Part 5.)

APPENDICES

BLUE CROSS AND BLUE SHIELD OF FLORIDA, INC.
JACKSONVILLE, FLORIDA

CALCULATION OF MEDICARE SEGMENT ASSETS
AS OF JANUARY 1, 1986

Description	Florida's Calculation	OIG Adjustments	OIG Calculation
1981 ASSET FRACTION			
1. 1981 Total Plan Liabilities	$25,898,039	$ 0	$25,898,039
2. 1981 Medicare Segment Liabilities	$ 4,898,633	$ 692,575	
		73,763	
		34,554	
		9,610	
		(39,576)	
		$ 770,926	$ 5,669,559
3. 1981 Segmentation Fraction 1/	.189151	.029767	.218918
1986 MEDICARE SEGMENT ASSETS ACTIVE AND INACTIVE PARTICIPANTS			
4. 1986 Total Pension Plan Assets	$42,635,141	$ 0	$42,635,141
5. 1986 Medicare Segment Assets 2/ (Includes All Plan Participants)	$ 8,064,480	$ 1,269,120	$ 9,333,600
INACTIVE PARTICIPANT ADJUSTMENT			
6. 1986 Inactive Transfer Adjustment	$ (573,797)	$ (62,129)	$ (635,926)
1986 MEDICARE SEGMENT ASSETS CONSIDERING ONLY ACTIVE PARTICIPANTS			
7. 1986 Medicare Segment Assets 3/	$ 7,490,683	$ 1,206,991	$ 8,697,674

1/ (1981 Medicare Segment Liabilities / 1981 Total Plan Liabilities)

2/ (1981 Segmentation Fraction x 1986 Total Pension Plan Assets)

3/ (1986 Medicare Segment Assets - 1986 Inactive Transfer Adjustment)

BLUE CROSS AND BLUE SHIELD OF FLORIDA, INC.
JACKSONVILLE, FLORIDA

STATEMENT OF MEDICARE PENSION ASSETS
AS PROPOSED

FOR THE PERIOD
JANUARY 1, 1986 THROUGH JANUARY 1, 1990

		Florida Actuarial Values		
Date	Description	Total	NonMedicare Segment	Medicare Segment
01-Jan-86	Assets @ Actuarial	$42,635,141	$35,144,458	$7,490,683
	Contributions	0	(30,021)	30,021
	Benefits Paid	(1,765,717)	(1,758,223)	(7,494)
	Expenses	(302,011)	(248,543)	(53,468)
	Exp. Earnings	3,744,115	3,071,346	672,769
31-Dec-86	Expected Value	$44,311,528	$36,179,017	$8,132,511
	Gain or (Loss)	1,694,464	1,384,986	309,478
	Corridor Adj.	1,499,473	1,229,551	269,922
31-Dec-86	Actuarial Value	$47,505,465	$38,793,554	$8,711,911
	Transfers	0	486,095	(486,095)
01-Jan-87	Assets @ Actuarial	$47,505,465	$38,307,459	$9,198,006
	Contributions	1,633,003	1,146,073	486,930
	Benefits Paid	(1,136,968)	(1,136,968)	0
	Expenses	(358,932)	(290,123)	(68,809)
	Exp. Earnings	3,974,389	3,127,753	846,636
31-Dec-87	Expected Value	$51,616,957	$41,154,194	$10,462,763
	Gain or (Loss)	942,891	794,291	148,600
	Corridor Adj.	0	0	0
31-Dec-87	Actuarial Value	$52,559,848	$41,948,485	$10,611,363
	Transfers	0	43,895	(43,895)
01-Jan-88	Assets @ Actuarial	$52,559,848	$41,904,590	$10,655,258

BLUE CROSS AND BLUE SHIELD OF FLORIDA, INC.
JACKSONVILLE, FLORIDA

STATEMENT OF MEDICARE PENSION ASSETS
AS PROPOSED

FOR THE PERIOD
JANUARY 1, 1986 THROUGH JANUARY 1, 1990

		Florida Actuarial Values		
Date	Description	Total	NonMedicare Segment	Medicare Segment
01-Jan-88	Assets @ Actuarial	$52,559,848	$41,904,590	$10,655,258
	Contributions	0	(673,550)	673,550
	Benefits Paid	(1,452,291)	(591,840)	(860,451)
	Expenses	(376,458)	(301,278)	(75,180)
	Exp. Earnings	4,648,093	3,670,604	977,489
31-Dec-88	Expected Value	$55,379,192	$44,008,526	$11,370,666
	Gain or (Loss)	1,509,480	1,270,811	238,669
	Corridor Adj.	0	0	0
31-Dec-88	Actuarial Value	$56,888,672	$45,279,337	$11,609,335
	Transfers	0	240,096	(240,096)
01-Jan-89	Assets @ Actuarial	$56,888,672	$45,039,241	$11,849,431
	Contributions	0	(939,861)	939,861
	Benefits Paid	(2,826,020)	(2,290,474)	(535,546)
	Expenses	(428,250)	(340,156)	(88,094)
	Exp. Earnings	4,973,538	3,850,566	1,122,972
31-Dec-89	Expected Value	$58,607,940	$45,319,316	$13,288,624
	Gain or (Loss)	3,256,260	2,670,161	586,099
	Corridor Adj.	2,480,378	2,231,881	248,497
31-Dec-89	Actuarial Value	$64,344,578	$50,221,358	$14,123,220
	Transfers	0	(169,679)	169,679
01-Jan-90	Assets @ Actuarial	$64,344,578	$50,391,037	$13,953,541
Assets Per Florida Actuarial Valuation Report		64,344,578	50,391,037	13,953,541
Asset Variance @ Actuarial		$ 0	$ 0	$ 0

BLUE CROSS AND BLUE SHIELD OF FLORIDA, INC.
JACKSONVILLE, FLORIDA

OIG STATEMENT OF MEDICARE PENSION ASSETS

FOR THE PERIOD
JANUARY 1, 1986 THROUGH JANUARY 1, 1990

		Audited Actuarial Values		
Date	Description	Total	NonMedicare Segment	Medicare Segment
01-Jan-86	Assets @ Actuarial	$42,635,141	$33,937,467	$8,697,674
	Contributions	0	0	0
	Benefits Paid	(1,765,717)	(1,295,859)	(469,858)
	Expenses	(302,211)	(240,108)	(62,103)
	Exp. Earnings	3,744,106	2,985,254	758,852
31-Dec-86	Expected Value	$44,311,319	$35,386,754	$8,924,565
	Gain or (Loss)	1,931,369	1,516,478	414,891
	Corridor Adj.	1,262,777	936,457	326,320
31-Dec-86	Actuarial Value	$47,505,465	$37,839,689	$9,665,776
	Transfers	0	(275,268)	275,268
01-Jan-87	Assets @ Actuarial	$47,505,465	$38,114,957	$9,390,508
	Contributions	1,633,003	1,323,374	309,629
	Benefits Paid	(1,136,968)	(1,003,922)	(133,046)
	Expenses	(358,932)	(287,877)	(71,055)
	Exp. Earnings	3,974,389	3,184,870	789,519
31-Dec-87	Expected Value	$51,616,957	$41,331,402	$10,285,555
	Gain or (Loss)	1,209,079	966,234	242,845
	Corridor Adj.	0	0	0
31-Dec-87	Actuarial Value	$52,826,036	$42,297,636	$10,528,400
	Transfers	0	(155,388)	155,388
01-Jan-88	Assets @ Actuarial	$52,826,036	$42,453,024	$10,373,012

BLUE CROSS AND BLUE SHIELD OF FLORIDA, INC.
JACKSONVILLE, FLORIDA

OIG STATEMENT OF MEDICARE PENSION ASSETS

FOR THE PERIOD
JANUARY 1, 1986 THROUGH JANUARY 1, 1990

		Audited Actuarial Values		
Date	Description	Total	NonMedicare Segment	Medicare Segment
01-Jan-88	Assets @ Actuarial	$52,826,036	$42,453,024	$10,373,012
	Contributions	0	0	0
	Benefits Paid	(1,452,291)	(1,187,249)	(265,042)
	Expenses	(376,458)	(302,490)	(73,968)
	Exp. Earnings	4,672,050	3,753,734	918,316
31-Dec-88	Expected Value	$55,669,337	$44,717,019	$10,952,318
	Gain or (Loss)	1,770,876	1,418,675	352,201
	Corridor Adj.	0	0	0
31-Dec-88	Actuarial Value	$57,440,213	$46,135,694	$11,304,519
	Transfers	0	65,112	(65,112)
01-Jan-89	Assets @ Actuarial	$57,440,213	$46,070,582	$11,369,631
	Contributions	0	0	0
	Benefits Paid	(2,826,020)	(2,290,474)	(535,546)
	Expenses	(428,250)	(343,478)	(84,772)
	Exp. Earnings	5,023,177	4,027,825	995,352
31-Dec-89	Expected Value	$59,209,120	$47,464,455	$11,744,665
	Gain or (Loss)	3,507,727	2,811,107	696,620
	Corridor Adj.	1,627,731	1,310,521	317,210
31-Dec-89	Actuarial Value	$64,344,578	$51,586,083	$12,758,495
	Transfers	0	24,670	(24,670)
01-Jan-90	Assets @ Actuarial	$64,344,578	$51,561,413	$12,783,165
Florida's Update (Appendix B)		64,344,578	50,391,037	13,953,541
Asset Variance @ Actuarial		$ 0	$1,170,376	($1,170,376)

Blue Cross Blue Shield of Florida

532 Riverside Avenue
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Jacksonville, Florida 32231-0014
Claims and Membership Assistance: (904) 354-3331
All Other Departments: (904) 791-6111

July 31, 1992

Mr. Vincent R. Imbriani
Regional Inspector General
Office of Inspector General/Office of Audit Services
601 East 12th Street
Kansas City, Missouri 64106

**Re: MEDICARE SEGMENTED PENSION COST AUDIT - PLAN RESPONSES
CIN A-07-91-00473**

Dear Mr. Imbriani:

We have reviewed the draft audit report for the review referenced above. This letter will serve to document Blue Cross and Blue Shield of Florida's responses to the audit. Due to the technical nature of the review, we have relied heavily on our consultants from the National Employee Benefits Administration (NEBA) and our actuary from The Wyatt Company. The page numbers below correspond to the page numbers in the draft report.

- (Recommendation - page 7) We recommend that Florida increase the Medicare segment's pension assets by $1,206,991 as of January 1, 1986.

  Response: The Plan agrees.

- (Recommendation - page 9) We recommend that Florida transfer pension assets of $1,170,376 from the Medicare segment to the nonsegment as of January 1, 1990. This recommendation considers the increase of $1,206,991 to the Medicare segment's assets as of January 1, 1986 in the recommendation on page 7.

  Response: The Plan agrees.

- (Recommendations - page 11)

  Bullet #1.

  We recommend that Florida separately identify $2,378,198 as unallowable components of direct pension costs as of 1990 due to unfunded CAS costs for 1986 through 1990.

OIG AUDIT REPORT NO. CIN A-07-91-00473
BCBSF'S RESPONSES - CONTINUED

Response: The Plan disagrees. There is no provision in the Medicare contract or the CAS rules and regulations that requires the proration of the non-reimbursable cost. Section 412.30 of CAS only specifies that only the "funded pension cost" will be reimbursed. Since the Plan funded $1,633,003 in 1987, which was more than the 1987 Medicare Segment pension cost, we think the entire $486,930 of the Medicare Segment pension cost should be reimbursed. According to our calculations, we believe accumulated unfunded cost should be $2,172,313 instead of $2,378,198 as shown in the schedule below:

Date	1986	1987	1988	1989	Total
1/1/87	218,800	0	0	0	218,800
1/1/88	237,398	0	0	0	237,398
1/1/89	258,764	0	808,603	0	1,067,367
1/1/90	282,053	0	881,377	1,008,883	2,172,313

Also, there appears to be several calculation errors in the table at the bottom of page 10 of the audit report that should be corrected regardless of whether a portion of the Medicare Segment amount is disallowed or not. Based on our calculations, the 1987 and total columns on page 10 should be:

Date	1987	Total
1/1/87	0	218,800
1/1/88	146,971	384,369
1/1/89	160,198	1,227,565
1/1/90	174,616	2,346,929

Therefore, the unfunded cost should be $2,346,929.

OIG AUDIT REPORT NO. CIN A-07-91-00473
BCBSF'S RESPONSES - CONTINUED

Bullet #2.

We recommend that Florida continue a yearly update of unallowable pension cost components related to the unfunded CAS costs for 1986 through 1990.

Response: The Plan agrees.

Bullet #3.

We recommend that Florida identify and track unallowable components of pension costs for any subsequent years for which CAS costs of the pension plan are not funded.

Response: The Plan agrees.

If you have any questions, please contact me at (904) 363-4661 or Joe Rice at (904) 363-4659.

Sincerely,

Rick Kibler
Audit Director
Internal Audit Division

RK:jmr
(JMR07238)

cc: B. A. Davidson
A. J. Favino
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D. Williams
T. Riggs