Department of Health and Human Services

OFFICE OF INSPECTOR GENERAL

REVIEW OF MEDICARE CONTRACTOR'S PENSION SEGMENTATION BLUE CROSS AND BLUE SHIELD OF NEBRASKA

JUNE GIBBS BROWN
Inspector General

JANUARY 1996
CIN: A-07-95-01159

DEPARTRIENT OF HEALTH & HUMAN SERVICES

Office of Inspector General
Office of Audit Services

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

CIN: A-07-95-01 159

January 29, 1996

Mr. Duane Wilson, Controller
Blue Cross and Blue Shield of Nebraska
P.O. Box 3248
Main Post Office Station
Omaha, NE 68180-0001

Dear Mr. Wilson:

This report provides the results of an Office of Inspector General (OIG), Office of Audit Services (OAS) review titled *Review of Medicare Contractor's Pension Segmentation, Blue Cross and Blue Shield of Nebraska.* The purpose of our review was to evaluate Blue Cross and Blue Shield of Nebraska's (Nebraska) compliance with the pension segmentation requirements of its Medicare contract.

Our review showed that Nebraska understated Medicare segment pension assets as of 1986 by $59,406. The understatement occurred because Nebraska incorrectly identified Medicare segment cost centers in determining Medicare's initial assets. However, Nebraska's update of the Medicare segment assets from Plan Year 1986 to Plan Year 1994 overstated segment assets by $21,857. The overstatement primarily occurred because Nebraska used incorrect participant data and benefit payment data.

We recommend that Nebraska increase the January 1, 1994 assets of the Medicare segment by $37,549 ($59,406 less $21,857). Nebraska accepted our recommendations and its response is included in its entirety as Appendix B.

INTRODUCTION

BACKGROUND

Nebraska has administered Medicare Part A under a cost reimbursement contract since the start of the Medicare program. The contract, the Federal Acquisition Regulations (FAR), which superseded the Federal Procurement Regulations (FPR), and the Cost Accounting Standards (CAS) contain reimbursement principles for cost reimbursement contracts.

Since its inception, Medicare has paid a portion of the annual contributions made by contractors to their pension plans. These payments represented allowable pension costs under the FPR and/or the FAR. In 1980, both the FPR and Medicare contracts incorporated CAS 412 and 413.

The CAS 412 regulates the determination and measurement of the components of pension costs. It also regulates the assignment of pension costs to appropriate accounting periods. The CAS 413 regulates 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.

The Health Care Financing Administration (HCFA) incorporated segmentation requirements into Medicare contracts starting with Fiscal Year 1988. The contractual language specifies segmentation requirements and also provides for the separate identification of the pension assets for a Medicare segment.

Nebraska's contract required (1) computing the Medicare segment's actuarial liability, (2) determining the ratio of the Medicare segment's actuarial liability to the total plan actuarial liability (asset fraction), (3) allocating a portion of total pension assets as of 1986 based on the above ratio, (4) updating Medicare pension assets annually, and (5) assessing if Medicare's pension costs should be separately calculated.

The Medicare contracts identify a Medicare segment as:

> ... *any organizational component of the contractor, such as a division, department, or other similar subdivision, having a significant degree of responsibility and accountability for the Medicare contract/agreement, in which:*
>
> 1. *The majority of the salary dollars is allocated to the Medicare agreement/contract; or*
>
> 2. *Less than a majority of the salary dollars 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 provide for separate identification of the pension assets of the Medicare segment. The identification involves the allocation of assets to the Medicare segment as of the first pension plan year after December 3 1, 1985 in which the salary criterion was met. The allocation was to use the ratio of the actuarial liabilities of the Medicare segment to the actuarial liabilities of the total plan, as of the later of the first day of the first plan year starting after December 31, 1980, or the first day of the first pension plan year following the date such Medicare segment first existed.

To ensure that contractors developed and maintained the data necessary for segmentation calculations, HCFA distributed a pension cost questionnaire to contractors in 1989. Nebraska's questionnaire response of April 24, 1989 identified total pension assets of $8,887,735 and Medicare segment assets of $399,521 as of January 1, 1986. Nebraska also concluded that separate valuations for the Medicare segment were required.

Nebraska participates in 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 Nebraska's questionnaire response.

SCOPE

We made our examination in accordance with generally accepted government auditing standards. Our objective was to determine Nebraska's compliance with pension segmentation requirements of its Medicare contract. Achieving the objective did not require a review of Nebraska's internal control structure. The audit addressed Nebraska's initial determination of pension assets for its Medicare segment and later updates. Our review covered January 1, 1981 to January 1, 1994.

We performed this review in conjunction with our audits of unfunded pension costs (CIN: A-07-95-01166) and pension costs claimed for Medicare reimbursement (CIN: A-07-95-01167). The information obtained and reviewed during those audits was also used in performing this review.

We reviewed Nebraska's identification of the Medicare segment as of January 1, 1986 and traced the segment's organizational lineage back to 1981. We also reviewed Nebraska's computation of the asset fraction and its update of Medicare assets from January 1, 1986 to January 1, 1994.

In performing the review, we used information provided by NEBA and NEBA's pension actuary. The information included liabilities, normal costs, contributions, expenses, and earnings. We reviewed Nebraska's accounting records, pension plan documents, annual actuarial valuation reports, and the Department of Labor/Internal Revenue Service Form 5500s. Using these documents, we calculated the asset fraction, determined the 1986 Medicare segment assets, and updated the Medicare segment assets to January 1, 1994. The HCFA pension actuarial staff reviewed our methodology and calculations.

We performed site work at Nebraska's corporate offices in Omaha, Nebraska during June 1995. Subsequently, we performed audit work in our Kansas City, Missouri office.

FINDINGS AND RECOMMENDATIONS

MEDICARE ASSETS AS OF JANUARY 1, 1986

We determined that Nebraska's asset fraction was understated by .6684 percent. Nebraska incorrectly identified Medicare segment cost centers in determining Medicare's initial assets. The appropriate identification of **cost** centers increased the asset fraction from 4.4952 percent to 5.1636, which also increased the Medicare segment assets by $59,406 to $458,927. The following schedule shows the details of Nebraska's and our calculations.

	Total Actuarial Liability (A)	Medicare Actuarial Liability (B)	Rounded Asset Fraction (C) (B)/(A)	1986 Total Company Assets (D)	1986 Medicare Segment Assets (E) (C)x(D)
OIG	$4,992,576	$257,796	.051636	$8,887,735	$458,927
Nebraska	4,992,576	224,424	.044952	8,887,735	399,521
Difference			.006684	$ 0	$ 59,406

Recommendation:

We recommend that Nebraska:

- Increase the 1986 pension assets of the Medicare segment by $59,406.

Auditee Response

Nebraska accepted our recommendation.

MEDICARE'S ASSET BASE AS OF JANUARY 1, 1986 UPDATED TO JANUARY 1, 1994

Nebraska's methodology in updating the Medicare segment assets from January 1, 1986 to January 1, 1994 overstated the segment assets by $21,857. The overstatement resulted primarily from Nebraska misclassifying participants as to segment and non-segment, which decreased the segment by $35,992. Other factors included correcting payments to retirees ($106,338 decrease), adjusting the assignment of pension contributions ($24,877 increase) and revising earnings and expenses ($95,596 increase). When considered with the 1986 adjustment, Nebraska understated Medicare's pension assets by $37,549 as of January 1, 1994.

Participants and Transfers

In the update, Nebraska omitted certain cost centers that met the contractual specifications for inclusion in the segment. Additionally, Nebraska included participants in cost centers that did not meet the specifications for a segment.

Since the identification of the segment participants was incorrect, transfers (representing the movement into and out of the segment each year) in the updates were incorrect. The following table compares Nebraska's and our computations of transfer amounts:

Transfer Adjustments to the Medicare Segment

Year	Nebraska	OIG
1986	$ (65,918)	$ (43,651)
1987	(918)	(54,204)
1988	(18,588)	(20,377)
1989	8,996	13,793
1990	(3,796)	(3,501)
1991	24,647	(9,477)
1992	(22,521)	1,247
1993	(3,655)	(1,575)
Total	$ (81,753)	$(117,745)

The corrected identification of the segment participants and transfer amounts was used in updating the Medicare segment assets. See Appendix A. The computation resulted in a net decrease of $35,992 ($117,745 less $81,753) in the Medicare segment assets.

Payments to Retirees

Due to incorrect identification of the Medicare segment, Nebraska's update of segment assets did not include a lump sum benefit payment to a retiree that was a segment participant. We matched benefit payments to individual retirees and included them in our update of segment assets. A comparison of computed benefit amounts is shown on the following schedule.

Benefit Payments to Medicare Segment Retirees

Year	Nebraska	OIG	Variance
1986	$ 0	106,338	$(106,338)
1987	0	0	0
1988	40,517	40,517	0
1989	42,255	42,255	0
1990	0	0	0
1991	25,000	25,000	0
1992	0	0	0
1993	0	0	0
Total	$107,772	$214,110	$(106,338)

Corrected benefit payment amounts were used in updating the Medicare segment assets shown in Appendix A. This resulted in a net decrease of $106,338 in the Medicare segment assets.

Assignment of Pension Contributions

Nebraska's update methodology did not equitably assign pension contributions to the Medicare segment. As a result, Nebraska understated Medicare segment assets by $24,877. The understatement primarily occurred because Nebraska did not adequately assign contributions to the segment for 1986 and 1993.

Nebraska's consulting actuary incorrectly calculated 1986 pension costs for the Medicare segment. As a result, Nebraska's 1986 contribution to the Medicare segment exceeded the CAS allowable contribution by $545.

For year 1993 Nebraska's consulting actuary calculated pension costs separately for the total company and the Medicare segment. For 1993, Nebraska's actual contribution to the pension trust fund exceeded the total company pension costs calculated by its actuary. However, Nebraska did not assign any portion of the excess contributions to the Medicare segment. Instead all the excess contributions were assigned to the "other segment".

Using the pension costs as calculated by the HCFA Office of the Actuary (CIN: A-07-95-01166), we assigned an additional $25,422 of the 1993 total company contribution to the Medicare segment, based on the ratio of the Medicare segment CAS funding target to the total company CAS funding target. Combined with the 1986 adjustment we increased Medicare segment assets by $24,877 ($25,422 less $545). See Appendix A.

Allocation of Earnings and Expenses

Nebraska's update methodology allocated investment earnings and administrative expenses to the Medicare segment based on a ratio of segment assets to total company assets. Because Nebraska's asset amounts were incorrect, it understated the segment's earnings and expenses for each year of the update. Except for correcting asset amounts, as previously described, we used Nebraska's allocation methodology in our update and increased the Medicare segment assets by $95,596.

Medicare Assets as of January 1, 1994

The pension assets of the Medicare segment from January 1, 1986 to January 1, 1994 were updated. See Appendix A. The update shows an increase of the Medicare segment assets of $37,549 as of January 1, 1994. This increase resulted from revising the asset fraction ($59,406 increase), correcting the transfer adjustments ($35,992 decrease), adjusting for

benefit payments ($106,338 decrease), correcting the allocation of contributions ($24,877 increase), and calculating the update with corrected asset amounts ($95,596 increase).

Recommendation:

We recommend that Nebraska:

❷ Increase the pension assets of the Medicare segment by $37,549 as of January 1, 1994.

Auditee Response

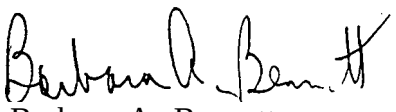
Nebraska accepted our recommendation.

INSTRUCTIONS FOR AUDITEE RESPONSE

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

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.)

Sincerely,



Barbara A. Bennett
Regional Inspector General
for Audit Services

Enclosures

HHS Action Official:

Mr. Joe L. Tilghman
Regional Administrator, Region VII
Health Care Financing Administration
601 East 12th Street, Room 235
Kansas City, Missouri 64106

BLUE CROSS AND BLUE SHIELD OF NEBRASKA
Omaha, Nebraska
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STATEMENT OF MEDICARE PENSION ASSETS
JANUARY 1, 1986 TO JANUARY 1, 1994

Description		Total Plan	Other Segment	Medicare Segment
Assets January 1, 1986	1/	**$8,887,735**	**$8,428,808**	$458,927
Contributions	2/	119,026	117,559	1,467
Asset Adjustment		0	0	0
Investment Return	3/	1,406,853	1,334,209	72,644
Benefit Payments	4/	(246,334)	(139,996)	(106,338)
Expenses	5/	(53,452)	(50,692)	(2,760)
Transfers	6/		43,651	(43,651)
Assets January 1, 1987		**$10,113,828**	**$9,733,539**	**$380,289**
Contributions		0	0	0
Asset Adjustment	7/	0	(7,433)	7,433
Investment Return		486,907	468,599	18,308
Benefit Payments		(290,560)	(290,560)	0
Expenses		(66,547)	(64,045)	(2,502)
Transfers			54,204	(54,204)
Assets January 1, 1988		**$10,243,628**	**$9,894,304**	**$349,324**
Contributions		0	0	0
Asset Adjustment		0	0	0
Investment Return		1,394,313	1,346,765	47,548
Benefit Payments		(469,548)	(429,031)	(40,517)
Expenses		(65,905)	(63,658)	(2,247)
Transfers			20,377	(20.377)
Assets January 1, 1989		**$11,102,488**	**$10,768,757**	**$333.731**
Contributions		0	0	0
Asset Adjustment		0	0	0
Investment Return		2,500,006	2,424,858	75,148
Benefit Payments		(505,334)	(463,079)	(42,255)
Expenses		(73,981)	(71,757)	(2,224)
Transfers			(13,793)	13.793
Assets January 1, 1990		**$13,023,179**	**$12,644,986**	**$378,193**

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STATEMENT OF MEDICARE PENSION ASSETS
JANUARY 1, 1986 TO JANUARY 1, 1994

Description	Total Plan	Other Segment	Medicare Segment
Assets January 1, 1990	**$13,023,179**	**$12,644,986**	**$378,193**
Contributions	0	0	0
Asset Adjustment	0	0	0
Investment Return	(333,496)	(323,811)	(9,685)
Benefit Payments	(423,872)	(423,872)	0
Expenses	(75,261)	(73,075)	(2,186)
Transfers		3,501	(3,501)
Assets January 1, 1991	**$12,190,550**	**$11,827,729**	**$362,821**
Contributions	0	0	0
Asset Adjustment	0	0	0
Investment Return	2,517,734	2,442,800	74,934
Benefit Payments	(1,628,849)	(1,603,849)	(25,000)
Expenses	(64,899)	(62,967)	(1,932)
Transfers		9,477	(9,477)
Assets January 1, 1992	**$13,014,536**	**$12,613,190**	**$401,346**
Contributions	0	0	0
Asset Adjustment	0	0	0
Investment Return	482,872	467,981	14,891
Benefit Payments	(943,536)	(943,536)	0
Expenses	(63,360)	(61,406)	(1,954)
Transfers		1,247	(1,247)
Assets January 1, 1993	**$12,490,512**	**$12,077,476**	**$413,036**
Contributions	1,111,293	1,05 1,521	59,772
Asset Adjustment	0	0	0
Investment Return	1,257,721	1,216,131	41,590
Benefit Payments	(566,794)	(566,794)	0
Expenses	(87,614)	(84,717)	(2,897)
Transfers		1,575	(1,575)
Assets January 1, 1994	**$14,205,118**	**$13,695,192**	**$509,926**
Assets Per Nebraska 8/	14,205,118	13,732,741	472,377
Variance 9/	$ 0	$(37,549)	$ 37,549

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STATEMENT OF MEDICARE PENSION ASSETS
JANUARY 1, 1986 TO JANUARY 1, 1994

FOOTNOTES TO STATEMENT OF MEDICARE PENSION ASSETS

1/ We calculated the Medicare segment assets based on our identification of the Medicare segment and our computed asset fraction (5.1636%). We computed the asset fraction as explained in our finding section of the report narrative. The amounts shown for the other segment represent the difference between the total company and the Medicare segment.

2/ We obtained total contribution amounts from IRS Form 5500 reports. We allocated the 1986 contribution to the Medicare segment based on the ratio of segment participants' normal costs and accrued liability to total company normal costs and accrued liability. Nebraska did not make contributions to the pension trust fund for years 1987 through 1992. For years 1993 and after, we allocated contributions to the Medicare segment based on the ratio of the segment's CAS funding target to the total company CAS funding target.

3/ Nebraska provided earnings amounts and we verified them to IRS Form 5500 reports. We allocated earnings to the Medicare segment based on the ratio of beginning of year market value of Medicare assets to the beginning of year market value of total assets. Nebraska used this same methodology.

4/ Nebraska provided benefit payment amounts and we verified them to IRS Form 5500 reports. We used actual benefit payments for Medicare segment retirees.

5/ Nebraska provided administrative expense amounts and we verified them to IRS Form 5500 reports. We allocated administrative expenses to the Medicare segment on the ratio of beginning of year market value of Medicare assets to the beginning of year market value of total assets. Nebraska used this same methodology.

6/ We identified participant transfers between segments by comparing annual participant valuation listings provided by Nebraska. The listings contained the actuarial liability of each participant at year-end. Our transfer adjustment considered each participant's actuarial liability and the funding level of the segment from which the participant transferred. We calculated the funding level as the assets divided by the liabilities. If the funding level ratio was greater than one, we transferred assets equal to the participant's liability. Nebraska used this same methodology.

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STATEMENT OF MEDICARE PENSION ASSETS
JANUARY 1, 1986 TO JANUARY 1, 1994

7/ Our separate computation of pension costs showed a negative CAS pension cost for the other segment in 1986. Additional details on the development and computation of pension costs are contained in our reported titled "Review of Unfunded Pension Costs of Blue Cross and Blue Shield of Nebraska" (CIN: A-07-95-01166). A negative CAS pension cost represents a release of assets previously applied to a portion of the actuarial liability. Assets released result in unassigned assets, our consideration of the unassigned assets in our computations result in an asset adjustment from the other segment to fund the CAS pension cost of the Medicare segment.

8/ We obtained the total asset amounts as of January 1, 1994 from Nebraska's update of assets provided by its actuary.

9/ The asset variance represents the difference between the OIG calculation of assets as of January 1, 1994 and the assets calculated by Nebraska's actuary.

BlueCross BlueShield
of Nebraska

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December 7, 1995

Ms. Barbara A. Bennett
Regional Inspector General for Audit Services
Region VII Office of Inspector General
Department of Health and Human Services
601 East 12th Street, Room 284A
Kansas City, MO 64106

Re: CIN: A-07-95-01167
A-07-95-01159
A-07-95-01166

Dear Ms. Bennett:

We have reviewed the findings included in the above drafts of the Office of Inspector (OIG) Medicare Pension Audit. We will accept the recommendations in each of the drafts and will move forward to carry out the requested actions.

In the course of our review we had questions about the Medicare segment salary component used in the computations and requested some additional information. Additional material was received for FY 1987, 1988, 1993, and 1994 for review.

The review of this additional information determined that the Medicare segment definition used in the computations was different from our understanding of the composition of the segment. The difference was our Medicare "allocation only" cost centers. These "allocation only" cost centers are used solely by Medicare personnel. These represent a situation where a given Medicare staff person may charge time to several different cost centers in the payroll system even though their function is totally Medicare oriented. The purpose of this process relates to the derivation of certain information for proper recording and reporting on Medicare Interim Expenditure Reports (IER). Specifically, these cost centers are 484, 485, 486, 487, 489, 490, and 491. In fiscal year 1987 cost centers 488, 493 (also FY88), 494, and 495 were also of this nature.

This difference in segment definition has subsequently been discussed with your office and there doesn't seem to be a problem with either definition of the segment. The identified cost centers were included in the indirect Medicare allocation for audit purposes. As stated earlier we will accept the draft audit findings and implement the suggested recomendations but we also want to make sure the correct segment is identified and used prospectively.

If I can be of any further assistance in this matter please give me a call. My telephone number is (402) 398-3701.

Sincerely,

Duane Wilson

Duane Wilson
Controller

cc: Robert Rhodes, BCBSA
Carol Navin, BCBSA
Eric Shipley, HCFA, Office of Actuary, Baltimore