DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General
Office of Audit Services

Region VII
601 East 12th Street
Room 0429
Kansas City, Missouri 64106

February 1, 2012

Report Number: A-07-11-00357

Ms. Jared A. Adair
Senior Vice President, Medicare Division
Wisconsin Physicians Service Insurance Corporation
P.O. Box 8190
Madison, WI 53708

Dear Ms. Adair:

Enclosed is the U.S. Department of Health and Human Services (HHS), Office of Inspector General (OIG), final report entitled *Review of the Pension Segmentation Requirements for the Managerial Retirement Program for Michigan, Illinois, and Minnesota Employees of Wisconsin Physicians Service Insurance Corporation for the Period of August 1, 1998, to January 1, 2008*. We will forward a copy of this report to the HHS action official noted on the following page for review and any action deemed necessary.

The HHS action official will make final determination as to actions taken on all matters reported. We request that you respond to this official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

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If you have any questions or comments about this report, please do not hesitate to call me at (816) 426-3591, or contact Jenenne Tambke, Audit Manager, at (573) 893-8338, extension 21, or through email at Jenenne.Tambke@oig.hhs.gov. Please refer to report number A-07-11-00357 in all correspondence.

Sincerely,

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

Enclosure

Direct Reply to HHS Action Official:

Ms. Deborah Taylor
Director & Chief Financial Officer
Office of Financial Management
Centers for Medicare & Medicaid Services
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Baltimore, MD 21244-1850

Department of Health and Human Services

OFFICE OF INSPECTOR GENERAL

REVIEW OF THE PENSION SEGMENTATION REQUIREMENTS FOR THE MANAGERIAL RETIREMENT PROGRAM FOR MICHIGAN, ILLINOIS, AND MINNESOTA EMPLOYEES OF WISCONSIN PHYSICIANS SERVICE INSURANCE CORPORATION FOR THE PERIOD OF AUGUST 1, 1998, TO JANUARY 1, 2008

Daniel R. Levinson
Inspector General

February 2012
A-07-11-00357

Office of Inspector General

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OFFICE OF AUDIT SERVICES FINDINGS AND OPINIONS

The designation of financial or management practices as questionable, a recommendation for the disallowance of costs incurred or claimed, and any other conclusions and recommendations in this report represent the findings and opinions of OAS. Authorized officials of the HHS operating divisions will make final determination on these matters.

EXECUTIVE SUMMARY

BACKGROUND

Wisconsin Physicians Service Insurance Corporation and Medicare

Wisconsin Physicians Service Insurance Corporation (WPS) administered Medicare Part A and Part B operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS). With the award to WPS of the CMS Parts A and B Medicare administrative contractors Jurisdiction 5 contract, WPS acquired Mutual of Omaha's Medicare Part A business segment in November 2007.

During the audit period, WPS maintained four separate defined benefit pension plans. This report will address the pension assets for the Managerial Retirement Program for Michigan, Illinois, and Minnesota Employees of WPS only.

On December 31, 2002, WPS terminated its Medicare Part A contract (prior to acquiring the Medicare Part A business segment from Mutual of Omaha). The closing date for the Medicare Part A segment was December 31, 2002. Upon the termination of its Medicare Part A contract, WPS identified Medicare's share of the Medicare Part A segment excess pension liabilities to be $2,059.

Since its inception, Medicare has paid a portion of contractors' contributions to their pension plans. These contributions are allowable Medicare costs subject to the criteria set forth in the Federal Acquisition Regulation, Cost Accounting Standards (CAS), and Medicare contracts.

Pension Segmentation

Beginning with fiscal year 1988, CMS incorporated segmentation requirements into the Medicare contracts. The Medicare contracts define a segment and specify the methodology for the identification and initial allocation of pension assets to the segment. Additionally, the contracts require Medicare segment assets to be updated for each year after the initial allocation in accordance with CAS 412 and 413.

OBJECTIVE

Our objective was to determine whether WPS complied with Federal requirements and the Medicare contracts' pension segmentation requirements when:

- updating the Medicare Part B segment's pension assets from August 1, 1998, to January 1, 2008,

- updating the Medicare Part A segment's pension assets from August 1, 1998, to December 31, 2002, and

- determining Medicare's share of the Medicare Part A segment excess pension liabilities as a result of the termination of the Medicare contract.

SUMMARY OF FINDINGS

WPS did not always comply with Federal requirements and the Medicare contracts' pension segmentation requirements when updating its Medicare Part B segment pension assets from August 1, 1998, to January 1, 2008, and when updating its Medicare Part A segment pension assets from August 1, 1998, to December 31, 2002. WPS identified Medicare Part B segment pension assets of $23,422,092; however, we determined that the Medicare Part B segment pension assets were $22,879,005 as of January 1, 2008. Thus, WPS overstated the Medicare Part B segment pension assets by $543,087 as of January 1, 2008.

In addition, WPS identified Medicare Part A segment pension assets of $51,787; however, we determined that the Medicare Part A segment pension assets were $41,175 as of December 31, 2002. Thus, WPS overstated Medicare Part A segment pension assets by $10,612 as of December 31, 2002.

Furthermore, WPS did not fully comply with Federal requirements in its calculation of Medicare's share of the Medicare Part A segment excess pension liabilities associated with the termination of the Medicare contract. WPS computed Medicare's share of the Medicare Part A segment excess pension liabilities to be $2,059; however, we determined that Medicare's share of the Medicare Part A segment excess pension liabilities was $13,012 as of December 31, 2002. Thus, WPS understated Medicare's share of excess pension liabilities, due to the termination of the Medicare Part A contract, by $10,953.

RECOMMENDATIONS

We recommend that WPS:

- reduce the Medicare Part B segment pension assets as of January 1, 2008, by $543,087 and recognize $22,879,005 as the Medicare segment's pension assets,

- reduce the Medicare Part A segment pension assets as of December 31, 2002, by $10,612, and recognize $41,175 as the Medicare segment's pension assets, and

- increase Medicare's share of the Medicare segment excess pension liabilities as of December 31, 2002, by $10,953 and submit for reimbursement $13,012 as Medicare's share of the excess pension liabilities due to the segment closing calculation.

AUDITEE COMMENTS

In written comments on our draft report, WPS concurred with, and said that it will implement, our recommendations. However, WPS disagreed with our treatment of certain participants as part of the "Other" segment instead of as part of the "Direct" segment. WPS stated that it agreed with us that the treatment of these participants was immaterial for segmentation purposes, but

added that it would have a material impact on pension costs claimed (which we reviewed separately).

WPS's comments are included in their entirety as Appendix D.

OFFICE OF INSPECTOR GENERAL RESPONSE

After reviewing WPS's comments, we maintain that our findings and recommendations remain valid. WPS was correct in saying that we determined that any changes to those few individuals would be immaterial for the purposes of this review. Furthermore, the Medicare contracts require that the Medicare segment be determined based on the organizational structure of the company, not on the basis of the status of individual participants in the pension plan. We identified the Medicare segment based upon the contract language. We maintain that the identification of the Medicare segment complied with the Medicare contracts and that therefore, no change was necessary.

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Glossary of Abbreviations and Acronyms

CAS	Cost Accounting Standards
CMS	Centers for Medicare & Medicaid Services
FAR	Federal Acquisition Regulation
MAC	Medicare administrative contractor
WAV	weighted average value
WPS	Wisconsin Physicians Service Insurance Corporation

INTRODUCTION

BACKGROUND

Wisconsin Physicians Service Insurance Corporation and Medicare

Wisconsin Physicians Service Insurance Corporation (WPS) administered Medicare Part A and Part B operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS). With the award to WPS of the CMS Parts A and B Medicare administrative contractors (MAC) Jurisdiction 5 contract, WPS acquired Mutual of Omaha's Medicare Part A business segment in November 2007.[1]

During the audit period, WPS had four defined benefit pension plans. The Employees' Pension Plan and the Managerial Pension Plan were ongoing pension plans that we reviewed in prior audits.[2] On August 1, 1998, WPS established two additional defined benefit pension plans: the Represented Employees' Retirement Income Plan (ERIP) and the Managerial Retirement Program for Michigan, Illinois, and Minnesota Employees of WPS. Effective December 31, 2007, WPS merged the ERIP and the Managerial Retirement Program for Michigan, Illinois, and Minnesota Employees of WPS and renamed the plan the WPS Managerial Retirement Program for Selected Locations. This report will address the pension assets for the Managerial Retirement Program for Michigan, Illinois, and Minnesota Employees of WPS.[3]

On December 31, 2002, WPS terminated its Medicare Part A contract (prior to receiving the Medicare Part A business segment from Mutual of Omaha). The closing date for the Medicare Part A segment was December 31, 2002. Upon the termination of its Medicare Part A contract, WPS identified Medicare's share of the Medicare Part A segment excess pension liabilities to be $2,059.

Since its inception, Medicare has paid a portion of contractors' contributions to their pension plans. These contributions are allowable Medicare costs subject to the criteria set forth in the Federal Acquisition Regulation (FAR), Cost Accounting Standards (CAS), and Medicare contracts.

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[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] We performed a prior pension segmentation audit (A-05-92-00048, issued October 1992), which brought the Medicare segment pension assets to December 31, 1989.

[3] We provide the results of our review of the ERIP in a separate report (A-07-11-00356).

Federal Requirements

CAS 412 addresses the determination and measurement of pension cost components. It also addresses the assignment of pension costs to appropriate accounting periods.

CAS 413 addresses 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.

Pension Segmentation

Beginning with fiscal year 1988, CMS incorporated segmentation requirements into the Medicare contracts. The Medicare contracts define a segment and specify the methodology for the identification and initial allocation of pension assets to the segment. Additionally, the contracts require Medicare segment assets to be updated for each year after the initial allocation in accordance with CAS 412 and 413. In claiming costs, contractors must follow cost reimbursement principles contained in the FAR, CAS, and the Medicare contracts.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to determine whether WPS complied with Federal requirements and the Medicare contracts' pension segmentation requirements when:

- updating the Medicare Part B segment's pension assets from August 1, 1998, to January 1, 2008,

- updating the Medicare Part A segment's pension assets from August 1, 1998, to December 31, 2002, and

- determining Medicare's share of the Medicare Part A segment excess pension liabilities as a result of the termination of the Medicare contract.

Scope

We reviewed WPS's identification of its Medicare segments; update of Medicare Part B segment assets from August 1, 1998, to January 1, 2008; update of Medicare Part A segment assets from August 1, 1998, to December 31, 2002; and the Medicare Part A segment closing calculation as of December 31, 2002.

Achieving our objective did not require us to review WPS's overall internal control structure. We reviewed controls relating to the identification of the Medicare segment, the update of the segment's assets, and the calculation of the segment closing to ensure adherence to the Medicare contracts, CAS 412, and CAS 413.

We performed fieldwork at WPS's office in Madison, Wisconsin, during July 2009.

Methodology

To accomplish our objective, we did the following:

- We reviewed the applicable portions of the FAR, CAS, and the Medicare contracts.

- We reviewed the annual actuarial valuation reports prepared by WPS's actuary, which included the pension plan's assets, liabilities, normal costs, contributions, benefit payments, investment earnings, and administrative expenses. We used this information to calculate the Medicare segments' assets.

- We reviewed the Medicare Part A segment closing calculation prepared by WPS's actuary.

- We obtained and reviewed the pension plan documents and Department of Labor/Internal Revenue Service (IRS) Forms 5500 used in calculating the Medicare segments' assets.

- We interviewed WPS staff responsible for identifying the Medicare segments to determine whether the segments were properly identified in accordance with the Medicare contracts.

- We reviewed WPS's accounting records to verify the segment identification and benefit payments made to the Medicare segments.

- We provided the CMS Office of the Actuary with the actuarial information necessary for it to calculate both the Medicare Part A segment pension assets (at market value) from August 1, 1998, to December 31, 2002, and the Medicare segment's excess pension liabilities as of December 31, 2002.

- We provided the CMS Office of the Actuary with the actuarial information necessary for it to calculate the Medicare Part B segment pension assets (at market value) from August 1, 1998, to January 1, 2008.

- We reviewed the CMS actuaries' methodology and calculations.

We performed this review in conjunction with our audit of WPS's pension costs claimed for Medicare reimbursement, to be issued in a subsequent report (A-07-11-00369), and used the information obtained during that audit in this review.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

FINDINGS AND RECOMMENDATIONS

WPS did not always comply with Federal requirements and the Medicare contracts' pension segmentation requirements when updating its Medicare Part B segment pension assets from August 1, 1998, to January 1, 2008, and when updating its Medicare Part A segment pension assets from August 1, 1998, to December 31, 2002. WPS identified Medicare Part B segment pension assets of $23,422,092; however, we determined that the Medicare Part B segment pension assets were $22,879,005 as of January 1, 2008. Thus, WPS overstated the Medicare Part B segment pension assets by $543,087 as of January 1, 2008.

In addition, WPS identified Medicare Part A segment pension assets of $51,787; however, we determined that the Medicare Part A segment pension assets were $41,175 as of December 31, 2002. Thus, WPS overstated Medicare Part A segment pension assets by $10,612 as of December 31, 2002.

Appendix A presents details on both Medicare Part B segment pension assets from August 1, 1998, to January 1, 2008, and Medicare Part A segment pension assets from August 1, 1998, to December 31, 2002, as determined during our audit.

Furthermore, WPS did not fully comply with Federal requirements in its calculation of Medicare's share of the Medicare Part A segment excess pension liabilities associated with the termination of the Medicare contract. WPS computed Medicare's share of the Medicare Part A segment excess pension liabilities to be $2,059; however, we determined that Medicare's share of the Medicare Part A segment excess pension liabilities was $13,012 as of December 31, 2002. Thus, WPS understated Medicare's share of excess pension liabilities, due to the termination of the Medicare Part A contract, by $10,953.

UPDATE OF MEDICARE SEGMENTS' PENSION ASSETS

WPS did not always comply with Federal requirements and the Medicare contracts' pension segmentation requirements when updating the Medicare Part B segment pension assets from August 1, 1998, to January 1, 2008, and when updating its Medicare Part A segment pension assets from August 1, 1998, to December 31, 2002.

Federal Requirements

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 are charged to the Medicare agreement/contract, and these salary dollars represent 40% or more of the total salary dollars charged to the Medicare agreement/contract.

Furthermore, the Medicare contracts state that "… the pension assets allocated to each Medicare Segment shall be adjusted in accordance with CAS 413.50(c)(7)." CAS 413.50(c)(7) requires that the asset base be adjusted by contributions, permitted unfunded accruals, income, benefit payments, and expenses. The CAS requires expenses to be allocated among the segments in proportion to the investment earnings. In addition, CAS 413.50(c)(8) requires an adjustment to be made for transfers (participants who enter or leave the segment) if the transfers materially affect the segment's ratio of pension plan assets to actuarial accrued liabilities.

For plan years beginning after March 30, 1995, the CAS requires investment income and expenses to be allocated among segments based on the ratio of the segment's weighted average value (WAV) of assets to Total Company WAV of assets.

Furthermore, CAS 412.50(a)(4) requires that contributions in excess of the pension cost assigned to the period be recognized as prepayment credits and accumulated at the assumed valuation interest rate until applied to future period costs. Prepayment credits that have not been applied to fund pension costs are excluded from the value of assets used to compute pension costs.

Medicare Part B Segment Pension Assets

WPS overstated Medicare Part B segment pension assets by $543,075 as of January 1, 2008, as a result of the component variances discussed below.

Table 1 summarizes the audit adjustment required to update the Medicare Part B segment pension assets to January 1, 2008, in accordance with Federal requirements.

Table 1: Summary of Medicare Part B Audit Adjustments as of January 1, 2008

	Per Audit	Per WPS	Difference
Contributions and Prepayment Credits	$12,466,949	$12,725,688	($258,739)
Benefit Payments	1,353,939	1,380,203	26,264
Net Transfers Out	47,014	(109,825)	156,839
Earnings, Net Expenses	3,939,865	3,971,443	(31,578)
Other Transaction	7,780,996	8,216,869	(435,873)
Under/(Over)statement of Medicare Pension Segment Assets			**($543,087)**

Contributions and Prepayment Credits Overstated

WPS overstated contributions and prepayment credits by $258,739 for the Medicare Part B segment, primarily because of differences in the assignable pension costs. As a result, WPS overstated the Medicare Part B segment pension assets by $258,739.

The audited contributions and prepayment credits are based on the assignable pension costs. In compliance with the CAS, we applied prepayment credits first to current-year assignable pension costs because the credits were available at the beginning of the year, and then updated any remaining credits with interest to the next measurement (valuation) date. We then allocated contributions as needed to assigned pension costs as of the date of deposit. Table 2 provides information on our calculations of contributions and prepayment credits, WPS's calculations, and the difference between the two on a year-by-year basis.

Table 2: Contributions and Prepayment Credits
Medicare Part B Segment

	Per Audit	Per WPS	Difference
1998	$344,759	$344,759	$0
1999	742,099	821,327	(79,228)
2000	805,078	865,489	(60,411)
2001	1,139,652	1,160,555	(20,903)
2002	1,347,481	1,369,666	(22,185)
2003	1,801,351	1,854,548	(53,197)
2004	1,684,427	1,702,799	(18,372)
2005	1,683,622	1,698,608	(14,986)
2006	1,715,615	1,693,007	22,608
2007	1,202,865	1,214,930	(12,065)
Total	**$12,466,949**	**$12,725,688**	**($258,739)**

Benefit Payments Overstated

WPS overstated benefit payments by $26,264 because of differences in the identification of the Medicare Part B segment participants. As a result, WPS understated the Medicare Part B segment pension assets by $26,264.

Net Transfers Out Overstated

WPS overstated net transfers out of the Medicare Part B segment by $156,839, primarily because of differences in identification of the Medicare Part B segment participants. This overstatement of the net transfer adjustment resulted in an understatement of the Medicare Part B segment assets by $156,839. Table 3 on the following page provides information on our calculations of net transfers, WPS's calculations, and the difference between the two on a year-by-year basis.

Table 3: Net Transfers Out			
Medicare Part B Segment			
	Per Audit	**Per WPS**	**Difference**
1998	($6,211)	$0	($6,211)
1999	(11,118)	(2,921)	(8,197)
2000	69,293	0	69,293
2001	(26,215)	0	(26,215)
2002	133,847	93,420	40,427
2003	0	0	0
2004	(197,971)	(227,045)	29,074
2005	947	1,027	(80)
2006	52,728	52,728	0
2007	31,714	(27,034)	58,748
Total	**$47,014**	**($109,825)**	**$156,839**

Earnings, Net Expenses Overstated

WPS overstated investment earnings, less administrative expenses, by $31,578 for the Medicare Part B segment because it used incorrect contribution, prepayment credit, benefit payment, and net transfer amounts (all discussed above) to develop the Medicare Part B segment pension asset base. In our audited update, we allocated earnings and expenses based on the applicable CAS requirements.

Other Transaction Overstated

Effective December 31, 2007, WPS merged the ERIP into this pension plan. WPS transferred assets totaling $8,216,869 into the Medicare Part B segment from the ERIP. In our separate review of the ERIP (A-07-11-00356), we determined that WPS overstated the Medicare Part B segment assets by $435,873. Therefore, the assets transferred from the ERIP plan were overstated by $435,873.

Medicare Part A Segment Pension Assets

WPS overstated Medicare Part A segment pension assets by $10,612 as of December 31, 2002, as a result of the component variances discussed below.

Table 4 on the following page summarizes the audit adjustment required to update the Medicare Part A segment pension assets to December 31, 2002, in accordance with Federal requirements.

Table 4: Summary of Medicare Part A Audit Adjustments as of December 31, 2007			
	Per Audit	**Per WPS**	**Difference**
Contributions and Prepayment Credits	$159,213	$160,501	($1,288)
Net Transfers Out	(102,849)	(93,420)	(9,429)
Earnings, Net Expenses	(15,189)	(15,294)	105
Under/(Over)statement of Medicare Pension Segment Assets			**($10,612)**

Contributions and Prepayment Credits Overstated

WPS overstated contributions and prepayment credits by $1,288 for the Medicare Part A segment because of differences in the assignable pension costs. As a result, WPS overstated the Medicare Part A segment pension assets by $1,288.

The audited contributions and prepayment credits are based on the assignable pension costs. In compliance with the CAS, we applied prepayment credits first to current-year assignable pension costs because the credits were available at the beginning of the year, and then updated any remaining credits with interest to the next measurement (valuation) date. We then allocated contributions as needed to assigned pension costs as of the date of deposit.

Net Transfers Out Understated

WPS understated net transfers out of the Medicare Part A segment by $9,429, primarily because of differences in identification of the Medicare Part A segment participants. This understatement of the net transfer adjustment resulted in an overstatement of the Medicare Part A segment assets by $9,429.

Earnings, Net Expenses Overstated

WPS overstated investment earnings, less administrative expenses, by $105 for the Medicare Part A segment because it used incorrect contribution, prepayment credit, benefit payment, and net transfer amounts (all discussed above) to develop the Medicare Part A segment pension asset base. In our audited update, we allocated earnings and expenses based on the applicable CAS requirements.

MEDICARE PART A SEGMENT EXCESS PENSION LIABILITIES

WPS did not fully comply with Federal requirements in its calculation of Medicare's share of the Medicare Part A segment excess pension liabilities associated with the termination of the Medicare contract.

Federal Requirements

CAS 413 requires a segment closing adjustment to be made in order to recognize Medicare's share of the Medicare Part A segment excess pension liabilities as a result of the termination of the Medicare Part A contract.

Medicare Contracts

In the event of a contract termination, the Medicare contracts require contractors to follow the segment closing provision of the CAS. Furthermore, in situations such as contract terminations, the Medicare contracts require contractors to identify excess Medicare pension liabilities in accordance with CAS 413.

Cost Accounting Standards

Contract terminations and segment closings are addressed by CAS 413.50(c)(12), which states:

> If a segment is closed, if there is a pension plan termination, or if there is a curtailment of benefits, the contractor shall determine the difference between the actuarial liability for the segment and the market value of the assets allocated to the segment, irrespective of whether or not the pension plan is terminated. The difference between the market value of the assets and the actuarial accrued liability for the segment represents an adjustment of previously-determined pension costs.
>
> (i) The determination of the actuarial accrued liability shall be made using the accrued benefit cost method. The actuarial assumptions employed shall be consistent with the current and prior long term assumptions used in the measurement of pension costs….
>
> (ii) … The market value of the assets shall be reduced by the accumulated value of prepayment credits, if any. Conversely, the market value of assets shall be increased by the current value of any unfunded actuarial liability separately identified and maintained in accordance with 9904.412-50(a)(2).
>
> (iii) The calculation of the difference between the market value of the assets and the actuarial accrued liability shall be made as of the date of the event (e.g., contract termination, plan amendment, plant closure) that caused the closing of the segment, pension plan termination, or curtailment of benefits. If such a date is not readily determinable, or if its use can result in an inequitable calculation, the contracting parties shall agree on an appropriate date.

Determination of Excess Medicare Part A Segment Pension Liabilities as of December 31, 2002

WPS identified $2,059 in excess Medicare Part A segment pension liabilities as of December 31, 2002. However, we calculated the excess Medicare Part A segment pension liabilities to be $13,013 as of that date. Therefore, WPS understated the excess pension liabilities by $10,954. The understatement occurred because WPS overstated the Part A Medicare segment's final market value of assets (as previously discussed) as of December 31, 2002.

Medicare's Share of Excess Medicare Part A Segment Pension Liabilities as of December 31, 2002

Federal Requirements

The methodology for determining the Federal Government's share of excess pension liabilities is addressed by CAS 413.50(c)(12)(vi), which states:

> The Government's share of the adjustment amount determined for a segment shall be the product of the adjustment amount and a fraction. The adjustment amount shall be reduced for any excise tax imposed upon assets withdrawn from the funding agency of a qualified pension plan. The numerator of such fraction shall be the **sum of the pension plan costs** allocated to all contracts and subcontracts (including Foreign Military Sales) subject to this Standard during a period of years representative of the Government's participation in the pension plan. The denominator of such fraction shall be the **total pension costs** assigned to cost accounting periods during those same years. This amount shall represent an adjustment of contract prices or cost allowance as appropriate. The adjustment may be recognized by modifying a single contract, several but not all contracts, or all contracts, or by use of any other suitable technique. [Emphasis added.]

Medicare's Share of the Excess Medicare Part A Segment Pension Liabilities Understated

WPS did not fully comply with the Medicare contracts in determining Medicare's share of the Medicare Part A segment excess pension liabilities associated with the termination of the Medicare contract as of December 31, 2002. WPS calculated $2,059 as Medicare's share of the Medicare Part A segment excess pension liabilities as of December 31, 2002; however, we determined that Medicare's share of the Medicare Part A segment excess pension liabilities was $13,012 as of December 31, 2002. The understatement occurred primarily because of differences in the final market value of the Medicare Part A segment pension assets (as discussed above). Thus, WPS understated Medicare's share of the Medicare Part A segment excess pension liabilities by $10,953.

In accordance with CAS 413.50(c)(12)(vi), we calculated the aggregate Medicare percentage using the Medicare segment pension costs developed during our current pension costs claimed (A-07-11-00369) audit. Appendix C shows our calculation of the Medicare Part A segment's aggregate Medicare percentage; Table 5 on the following page shows our calculation of Medicare's share of the Medicare Part A segment excess liabilities.

Table 5: Calculation of Medicare's Share of the Excess Medicare Part A Segment Pension Liabilities			
	Excess Medicare Segment Liabilities (A)	**Aggregate Medicare Percentage (B)**	**Excess Liabilities Attributable to Medicare (A x B)**
Per OIG	($13,013)	99.99%	($13,012)
Per WPS	(2,059)	100.00%	(2,059)
Difference	**($10,954)**	**0.01%**	**($10,953)**

RECOMMENDATIONS

We recommend that WPS:

- reduce the Medicare Part B segment pension assets as of January 1, 2008, by $543,087 and recognize $22,879,005 as the Medicare segment's pension assets,

- reduce the Medicare Part A segment pension assets as of December 31, 2002, by $10,612, and recognize $41,175 as the Medicare segment's pension assets, and

- increase Medicare's share of the Medicare segment excess pension liabilities as of December 31, 2002, by $10,953 and submit for reimbursement $13,012 as Medicare's share of the excess pension liabilities due to the segment closing calculation.

AUDITEE COMMENTS

In written comments on our draft report, WPS concurred with, and said that it will implement, our recommendations. However, WPS disagreed with our treatment of certain participants as part of the "Other" segment instead of as part of the "Direct" segment.

Specifically, WPS stated that when it shared information with us regarding the treatment of the participants in question, we responded that we had determined that " '… any changes would be immaterial to the segment for any year and also that as the years go by each participant gets transferred back into the Medicare segment before the end of the audit period except for 3.' " WPS stated that it agreed with us that the treatment of these participants was immaterial for segmentation purposes, but added that it would have a material impact on pension costs claimed. Accordingly, WPS indicated that in its written comments on our related draft report on pension costs claimed (A-07-11-00369), it will request that an additional $88,000 be considered allowable pension costs because of the treatment of these participants.

WPS's comments are included in their entirety as Appendix D.

OFFICE OF INSPECTOR GENERAL RESPONSE

After reviewing WPS's comments, we maintain that our findings and recommendations remain valid. WPS was correct in saying that we determined that any changes to those few individuals

would be immaterial for the purposes of this review. Furthermore, the Medicare contracts require that the Medicare segment be determined based on the organizational structure of the company, not on the basis of the status of individual participants in the pension plan. We identified the Medicare segment based upon the contract language. We maintain that the identification of the Medicare segment complied with the Medicare contracts and that therefore, no change was necessary.

With respect to WPS's comment about the allowability of the additional $88,000, we will address that in our response to the pension costs claimed report (A-07-11-00369).

APPENDIXES

APPENDIX A: WISCONSIN PHYSICIANS SERVICE INSURANCE CORPORATION
STATEMENT OF MARKET VALUE OF THE MANAGERIAL RETIREMENT PLAN PENSION ASSETS
FOR THE PERIOD AUGUST 1, 1998, TO JANUARY 1, 2008

Description		Total Company	Other Segment	Medicare Part B	Medicare Part A
Assets August 1, 1998	1/	$0	$0	$0	$0
Prepayment Credits		0	0	0	0
Contributions	2/	344,759	0	344,759	0
Earnings		34,526	0	34,526	0
Benefit Payments	3/	(1,880)	0	(1,880)	0
Expenses		(3,290)	0	(3,290)	0
Transfers		0	6,211	(6,211)	0
Assets January 1, 1999		$374,115	$6,211	$367,904	$0
Prepayment Credits	4/	0	220	(385)	165
Contributions		851,677	79,490	742,484	29,703
Earnings	5/	231,259	12,998	214,088	4,173
Benefit Payments		(7,665)	0	(7,665)	0
Expenses	6/	(57,911)	(3,255)	(53,611)	(1,045)
Transfers		0	11,118	(11,118)	0
Assets January 1, 2000		$1,391,475	$106,782	$1,251,697	$32,996
Prepayment Credits		0	(38,949)	37,086	1,863
Contributions		910,209	103,642	767,992	38,575
Earnings		2,765	179	2,505	81
Benefit Payments		(48,462)	(200)	(48,262)	0
Expenses		(38,490)	(2,491)	(34,871)	(1,128)
Transfers	7/	0	(67,512)	69,293	(1,781)
Assets January 1, 2001		$2,217,497	$101,451	$2,045,440	$70,606
Prepayment Credits		0	(53,969)	52,110	1,859
Contributions		1,216,990	90,652	1,087,542	38,796
Earnings		(173,495)	(5,584)	(162,225)	(5,686)
Benefit Payments		(43,022)	(217)	(42,805)	0
Expenses		(56,453)	(1,817)	(52,786)	(1,850)
Transfers		0	26,215	(26,215)	0
Assets January 1, 2002		$3,161,517	$156,731	$2,901,061	$103,725
Prepayment Credits		0	(77,582)	74,900	2,682
Contributions		1,440,914	122,763	1,272,581	45,570
Earnings		(211,826)	(7,214)	(197,512)	(7,100)
Benefit Payments		(42,560)	(6,657)	(35,903)	0
Expenses		(78,591)	(2,677)	(73,280)	(2,634)
Transfers		0	(32,779)	133,847	(101,068)
Assets December 31, 2002		$4,269,454	$152,585	$4,075,694	$41,175

Description		Total Company	Other Segment	Medicare Part B
Assets January 1, 2003	8/	$4,269,454	$193,760	$4,075,694
Prepayment Credits		0	(106,684)	106,684
Contributions		1,904,619	209,952	1,694,667
Earnings		825,085	33,068	792,017
Benefit Payments		(927,224)	(618)	(926,606)
Expenses		(85,605)	(3,431)	(82,174)
Transfers		0	0	0
Assets January 1, 2004		$5,986,329	$326,047	$5,660,282
Prepayment Credits		0	(163,710)	163,710
Contributions		1,766,580	245,863	1,520,717
Earnings		807,030	32,426	774,604
Benefit Payments		(45,673)	(4,732)	(40,941)
Expenses		(78,369)	(3,149)	(75,220)
Transfers		0	197,971	(197,971)
Assets January 1, 2005		$8,435,897	$630,716	$7,805,181
Prepayment Credits		0	(180,216)	180,216
Contributions		1,853,000	349,594	1,503,406
Earnings		751,090	51,942	699,148
Benefit Payments		(54,573)	(3,059)	(51,514)
Expenses		(96,297)	(6,659)	(89,638)
Transfers		0	(947)	947
Assets January 1, 2006		$10,889,117	$841,371	$10,047,746
Prepayment Credits		0	(222,488)	222,488
Contributions		1,836,000	342,873	1,493,127
Earnings		1,383,278	91,468	1,291,810
Benefit Payments		(64,287)	(2,559)	(61,728)
Expenses		(109,502)	(7,241)	(102,261)
Transfers		0	(52,728)	52,728
Assets January 1, 2007		$13,934,606	$990,696	$12,943,910
Prepayment Credits		0	(211,260)	211,260
Contributions		1,344,257	352,652	991,605
Earnings		1,253,450	81,649	1,171,801
Benefit Payments		(157,346)	(18,831)	(138,515)
Expenses		(121,693)	(7,927)	(113,766)
Transfers		0	(31,714)	31,714
Other Transactions	9/	8,544,232	763,236	7,780,996
Assets January 1, 2008		$24,797,506	$1,918,501	$22,879,005
Per WPS	10/	$24,797,506	$1,375,414	$23,422,092
Asset Variance	11/	$0	$543,087	($543,087)

ENDNOTES

1/ The pension plan was established on August 1, 1998. We obtained the beginning market value of assets from the actuarial valuation reports. At the inception of this plan it was 100% Medicare Part B employees so Total Company and the Medicare Part B segment were the same; however, through the audit period Wisconsin Physicians Service Insurance Corporation (WPS) developed the "Other" segment and the Medicare Part A segment. The amounts shown for the "Other" segment represent the difference between the Total Company and the Medicare segments. All pension assets in this appendix are shown at market value.

2/ We obtained Total Company contribution amounts from the actuarial valuation reports and Department of Labor/Internal Revenue Service Forms 5500. We allocated Total Company contributions to the Medicare segment based on the ratio of the Medicare segment funding target divided by the Total Company funding target. Contributions in excess of the funding targets were treated as prepayment credits and accounted for in the "Other" segment until needed to fund pension costs in the future.

3/ We based the Medicare segment's benefit payments on actual payments to Medicare retirees. We obtained the benefit payments from documents provided by WPS.

4/ Prepayment credits represent funds available to satisfy future funding requirements and are applied to future funding requirements before current year contributions in order to avoid incurring unallowable interest. Prepayment credits are transferred to the Medicare segment as needed to cover funding requirements.

5/ We allocated investment earnings based on the ratio of the segment's weighted average value (WAV) of assets to Total Company WAV of assets as required by the Cost Accounting Standards (CAS).

6/ We allocated administrative expenses to the Medicare segment in proportion to investment earnings.

7/ We identified participant transfers between segments by comparing valuation data files provided by WPS. Asset transfers were equal to the actuarial liability determined under the accrued benefit cost method in accordance with the CAS. Furthermore, the CAS requires an adjustment to be made for transfers only if the transfers materially affect the segment's ratio of pension plan assets to actuarial accrued liabilities.

8/ The Medicare Part A segment closed as of December 31, 2002. The remaining assets were moved to the "Other" segment as of January 1, 2003.

9/ The other transaction represents the merger of the assets from the Represented Employees' Retirement Income Plan as of December 31, 2007.

10/ We obtained total asset amounts as of January 1, 2008, from the actuarial valuation report prepared by WPS's actuary.

11/ The asset variance represents the difference between our calculation of Medicare segment pension assets and WPS's calculation of the Medicare segment pension assets.

APPENDIX B: EXCESS MEDICARE PART A SEGMENT PENSION LIABILITIES

		WPS	OIG	Variance
Final Market Value of Assets As December 31, 2002	1/	$52,129	$41,175	($10,954)
Accrued Actuarial Liabilities	2/	54,188	54,188	0
Excess Medicare Segment Pension Assets/(Liabilities)	3/	($2,059)	($13,013)	($10,954)
		100.00%	99.99%	0.01%
Medicare's Share of Excess Pension Liabilities		**($2,059)**	**($13,012)**	**$10,953**

ENDNOTES:

1/ We obtained the final market value of assets from Appendix A.

2/ The accrued actuarial liabilities included participants that were in the Medicare Part A segment as of December 31, 2002.

3/ We calculated the Medicare segment excess liabilities due to the termination of the Medicare contract based upon the required adjustments. The Medicare segment excess liabilities represent the adjusted final market value of assets less the adjusted accrued actuarial liabilities.

APPENDIX C: CALCULATION OF THE MEDICARE PART A SEGMENT AGGREGATE MEDICARE PERCENTAGE

WPS Medicare Segment Part A Aggregate Medicare Percentage			
Fiscal Year	**Medicare Segment Pension Costs Claimed for Medicare Reimbursement**	**Total Medicare Segment Pension Costs**	**Aggregate Percentage[1]**
1998	$0	$0	
1999	22,401	22,401	
2000	37,796	37,796	
2001	40,589	40,601	
2002	46,353	46,353	
2003	12,063	12,063	[2]
Total	**$159,202**	**$159,214**	**99.99%** [3]

[1]The aggregate percentage was based on the audited pension costs as determined during the pension audits related to the Wisconsin Physicians Service Insurance Corporation (WPS) Medicare Part A segment. The information for 1998 - 2003 was obtained during the current review of pension costs claimed (A-07-11-00369).

[2]The fiscal year 2003 pension costs were computed for October 1, 2002, to December 31, 2002.

[3]We calculated the aggregate Medicare percentage by dividing the Medicare Segment Pension Costs Claimed for Medicare Reimbursement (numerator) by the Total Medicare Segment Pension Costs (denominator) pursuant to Cost Accounting Standard 413.

APPENDIX D: AUDITEE COMMENTS

CMS CENTERS for MEDICARE & MEDICAID SERVICES

Medicare

December 2, 2011

Mr. Patrick J. Cogley
Regional Inspector General for Audit Services
HHS, Office of Audit Services
601 East 12th Street, Room 0429
Kansas City, MO 64106

RE: OIG Draft Report Number A-07-11-00357

Dear Mr. Cogley:

This letter is in response to Report Number A-07-11-00357, the Draft Audit Report Review of the Pension Segmentation Requirements for the Managerial Retirement Program for Michigan, Illinois, and Minnesota Employees of Wisconsin Physicians Service Insurance Corporation for the Period of August 1, 1998, to January 1, 2008.

While WPS concurs with, and will implement the audit recommendations, we disagree with OIG's treatment of certain participants as part of the "Other" segment instead of the "Direct" segment.

When WPS shared information regarding the treatment of the participants in question with the OIG auditors, the auditors responded that they "determined than any changes would be immaterial to the segment for any year and also that as the years go by each participant gets transferred back into the Medicare segment before the end of the audit period except for 3." WPS agrees that the treatment of these individuals is immaterial for segmentation purposes. However, the appropriate treatment of these participants will have a material impact on cost claimed during the audit period. In responding to draft Report Number A-07-11-00369, WPS is requesting that an additional $88,000 be considered allowable pension cost because of this difference.

Based on this Report, WPS will:

- Reduce the Medicare Part B segment pension assets as of January 1, 2008, by $543,087 and recognize $22,879,005 as the Medicare segment's pension assets,
- Reduce the Medicare Part A segment pension assets as of December 31, 2002, by $10,612 and recognize $41,175 as the Medicare segment's pension assets, and
- Increase Medicare's share of the Medicare Part A segment excess pension liabilities as of December 31, 2002, by $10,953 and submit for reimbursement $13,012 as Medicare's share of the excess pension liabilities due to the segment closing calculation.

WPS HEALTH INSURANCE
Wisconsin Physicians Service Insurance Corporation serving as a CMS contractor
P.O. Box 1787 • Madison, WI 53701 • Phone 608-221-4711

Thank you for the opportunity to comment on this report. If you have any questions, please contact me at (608) 301-2639 or by e-mail at Jared.Adair@wpsic.com.

Sincerely,

Jared A. Adair
Senior Vice President
Medicare Division