



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General
Offices of Audit Services

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

OCT 19 2006

Report Number: A-07-06-00214

Mark Stimpson, Vice President Medicare Northwest
2890 East Cottonwood Parkway
P.O. Box 30270
Salt Lake City, Utah 84130

Dear Mr. Stimpson:

Enclosed are two copies of the U.S. Department of Health and Human Services, Office of Inspector General (OIG) report entitled "Review of Medicare Part A Pension Costs Claimed for Medicare Reimbursement by Blue Cross Blue Shield of Oregon for Fiscal Year 1996." A copy of this report will be forwarded to the HHS action official noted on the next page for his review and any action deemed necessary.

The HHS action official will make final determination regarding actions taken on all matters in the report. We request that you respond to the HHS action 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 contact me at (816) 426-3591, extension 274 or Jenenne Tambke, Audit Manager, at (573) 893-8338, extension 21, or through e-mail at Jenenne.Tambke@oig.hhs.gov. Please refer to report number A-07-06-00214 in all correspondence.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Patrick J. Cogley", written over a large, stylized, circular flourish.

Patrick J. Cogley
Regional Inspector General
for Audit Services

Enclosures

Direct Reply to HHS Action Official:

Mr. RJ Ruff
Regional Administrator, Region X
Centers for Medicare & Medicaid Services
2201 Sixth Avenue, MS-40
Seattle, Washington 98121

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF MEDICARE PART A
PENSION COSTS CLAIMED FOR
MEDICARE REIMBURSEMENT BY
BLUE CROSS BLUE SHIELD OF
OREGON FOR FISCAL YEAR 1996**



Daniel R. Levinson
Inspector General

October 2006
A-07-06-00214

Office of Inspector General

<http://oig.hhs.gov>

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OAS FINDINGS AND OPINIONS

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

EXECUTIVE SUMMARY

BACKGROUND

Blue Cross Blue Shield of Oregon (Oregon) administered Medicare Part A under a cost reimbursement contract with Centers for Medicare & Medicaid Services (CMS) until it merged with King County Medical Blue Shield, Pierce County Medical Bureau, and Medical Service Bureau of Idaho on January 1, 1997 to form The Regence Group (TRG). Each of these four entities maintained a separate qualified defined benefit pension plan. Effective January 1, 1997, TRG merged these four defined-benefit pension plans to form The Regence Group Retirement Plan. Oregon also serves as the Common Working File Host for the Great Western Sector under a separate cost reimbursable contract.

Medicare reimburses a portion of the annual contributions that contractors make to their pension plans. In claiming costs, contractors must follow cost reimbursement principles contained in the Federal Acquisition Regulations, Cost Accounting Standards (CAS), and Medicare contracts.

The Medicare contracts require contractors to allocate or separately calculate pension costs. The separate calculation method must be used if there is a material difference between the results of the two methods.

OBJECTIVE

Our objective was to determine the allowability of Medicare Part A pension costs claimed by Oregon for Medicare reimbursement for fiscal year (FY) 1996.

SUMMARY OF FINDING

Oregon failed to claim \$136,186 of allowable Medicare Part A pension costs due to an adjustment made to pension costs from an administrative cost audit. Oregon claimed \$25,552 of pension costs for Medicare reimbursement; however, we calculated the allowable Medicare pension costs during this period to be \$161,738.

RECOMMENDATION

We recommend that Oregon revise its Final Administrative Cost Proposal to claim the allowable Medicare Part A CAS pension costs of \$136,186 for FY 1996.

AUDITEE'S COMMENTS

Oregon agreed with our recommendation. Oregon's response is included in its entirety as Appendix B.

INTRODUCTION

BACKGROUND

Oregon's Medicare Contract

Blue Cross Blue Shield of Oregon (Oregon) administered Medicare Part A under a cost reimbursement contract with Centers for Medicare & Medicaid Services (CMS) until it merged with King County Medical Blue Shield, Pierce County Medical Bureau, and Medical Service Bureau of Idaho on January 1, 1997 to form The Regence Group (TRG). Each of these four entities maintained a separate defined benefit plan. Effective January 1, 1997, TRG merged these four plans to form The Regence Group Retirement Plan. Oregon also serves as the Common Working File Host (CWFH) for the Great Western Sector under a separate cost reimbursable contract.

Medicare reimburses a portion of the annual contributions that contractors make to their pension plans. To be allowable for Medicare reimbursement, pension costs must be (1) measured, assigned, and allocated in accordance with Cost Accounting Standards (CAS) 412 and 413; and (2) funded as specified by part 31 of the Federal Acquisition Regulations (FAR).

Beginning in fiscal year (FY) 1988, CMS incorporated specific segmentation language into Medicare contracts that requires contractors to use either an allocation method or a separate calculation method to identify and claim pension costs for Medicare reimbursement. Under the allocation method, the contractor determines total plan CAS pension costs and allocates a share to Medicare. Under the separate calculation method, the contractor separately identifies the pension cost components for the Medicare segment. The contractor must use the separate calculation method if its result is materially different from that of the allocation method.

Regulations

The Medicare contract addresses the determination and allocation of pension costs. Appendix B, section XVI, of the contract states: "The calculation of and accounting for pension costs charged to this agreement/contract are governed by the Federal Acquisition Regulation and Cost Accounting Standards 412 and 413."

The FAR 31.205-6(j) addresses allowability of pension costs and requires that plan contributions substantiate pension costs assigned to contract periods.

The CAS 412 regulates the determination and measurement of pension cost components. 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.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to determine the allowability of Medicare Part A pension costs claimed by Oregon for Medicare reimbursement for FY 1996.

Scope

The scope of this review was limited to the pension costs claimed for Medicare reimbursement for FY 1996 Medicare Part A contract. Closing agreements had previously been executed for FY 1995 Medicare Part A pension costs and for FYs 1995 through 1996 CWFH pension costs. We reviewed pension costs that Oregon claimed for Medicare reimbursement on its Final Administrative Cost Proposals (FACPs) for the Medicare Part A contract for FY 1996. Achieving the objective did not require that we review Oregon's overall internal control structure. However, we did review the internal controls related to the pension costs claimed for Medicare reimbursement to ensure that the pension costs were allocable in accordance with the CAS and allowable in accordance with the FAR.

We performed fieldwork at Oregon's office in Portland, Oregon, during November 2005.

Methodology

We identified Oregon's CAS pension costs for the total company and the Medicare segment. We also determined the extent to which Oregon funded CAS pension costs with contributions to the pension trust fund and accumulated prepayment credits. Using this information, we calculated CAS pension costs that were allowable for Medicare reimbursement for FY 1996 Medicare Part A. The calculations were based on separately computed CAS pension costs for the Medicare segment and total company CAS pension costs. The CMS Office of the Actuary calculated the allocable CAS pension costs based on Oregon's historical practices and on the results of our segmentation review ("Review of Medicare Contractor's Pension Segmentation Requirements at Blue Cross Blue Shield of Oregon for the Period January 1, 1994, through January 1, 1997," A-07-06-00197). Appendix A contains details on the pension costs and contributions.

In performing our review, we used information that Oregon's prior and current actuarial consulting firms provided. The information included assets, liabilities, normal costs, contributions, benefit payments, investment earnings, and administrative expenses. Oregon was unable to provide the accrued liabilities and normal costs by participant for 1995; however, after analysis of the data, we were able to accept the Medicare segment accrued liabilities and normal costs as identified by Oregon. We examined Oregon's accounting records, pension plan documents, annual actuarial valuation reports, and Department of Labor/Internal Revenue Service Form 5500s.

We performed our review in accordance with generally accepted government auditing standards.

FINDING AND RECOMMENDATION

Oregon failed to claim \$136,186 of allowable Medicare Part A pension costs for FY 1996.

We calculated the allowable pension costs based on separately computed CAS pension costs for the Medicare segment and total company CAS pension costs. For FY 1996, Oregon claimed pension costs of \$25,552 for Medicare reimbursement; however, allowable CAS pension costs were \$161,738. Therefore, Oregon failed to claim \$136,186 of allowable pension costs. The underclaim occurred primarily because it made an adjustment to pension costs as recommended during an administrative cost audit.

RECOMMENDATION

We recommend that Oregon revise its FACP to claim the allowable Medicare Part A CAS pension costs of \$136,186 for FY 1996.

AUDITEE'S COMMENTS

Oregon agreed with our recommendation. Oregon's response is included in its entirety as Appendix B.

APPENDIXES

BLUE CROSS BLUE SHIELD OF OREGON
STATEMENT OF ALLOWABLE PENSION COSTS
FOR FISCAL YEAR 1996

Date	Description	Total Company	Other Segment	Medicare Segment
1995	Contributions	<u>1/</u> \$4,166,179	\$4,166,179	\$0
8.50%	Discount For Interest	<u>2/</u> (223,801)	(223,801)	0
	Present Value Contributions	<u>3/</u> 3,942,378	3,942,378	0
	Prepayment Credit	<u>4/</u> 2,485,169	2,406,441	78,728
	Present Value Of Funding	<u>5/</u> 6,427,547	6,348,819	78,728
	CAS Funding Target	<u>6/</u> 2,485,169	2,406,441	78,728
	Percentage Funded	<u>7/</u>	100.00%	100.00%
	Funded Pension Cost	<u>8/</u>	2,406,441	78,728
	Allowable Interest	<u>9/</u>	0	0
	Allocable Pension Cost	<u>10/</u>	2,406,441	78,728
	Medicare Part A LOB* Percentage	<u>11/</u>	0.73%	88.85%
	Allowable CY Pension Cost	<u>12/</u>	17,567	69,950
1995	Allowable Part A FY Pension Costs	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>
1996	Contributions	\$3,966,334	\$3,966,334	\$0
8.50%	Discount For Interest	(210,362)	(210,362)	0
	Present Value Contributions	3,755,972	3,755,972	0
	Prepayment Credit	4,069,510	3,923,771	145,739
	Present Value Of Funding	7,825,482	7,679,743	145,739
	CAS Funding Target	4,069,510	3,923,771	145,739
	Percentage Funded		100.00%	100.00%
	Funded Pension Cost		3,923,771	145,739
	Allowable Interest		0	0
	Allocable Pension Cost		3,923,771	145,739
	Medicare Part A LOB Percentage		1.26%	94.03%
	Allowable CY Pension Cost		49,440	137,038
1996	Allowable Part A FY Pension Cost	<u>13/</u> \$161,738	<u>41,472</u>	<u>120,266</u>

* Line of business.

**BLUE CROSS BLUE SHIELD OF OREGON
STATEMENT OF ALLOWABLE PENSION COSTS
FOR FISCAL YEAR 1996**

FOOTNOTES

- 1/ We obtained total company contribution amounts and dates of deposit from Internal Revenue Service Form 5500 reports. The contributions included deposits made during the plan year and accrued contributions deposited after the end of the plan year but within the time allowed for filing tax returns. The contributions allocated to the Medicare segment were determined during the pension segmentation review (A-07-06-00197). The amounts shown for the other segment represent the difference between the total company and the Medicare segment.
- 2/ We subtracted the interest that is included in the contributions deposited after January 1 of each year to discount the contributions back to their beginning of the year value. For purposes of this appendix, we computed the interest as the difference between the present value of contributions at the valuation interest rate and actual contribution amounts.
- 3/ The present value of contributions is the value of the contributions discounted from the date of deposit back to January 1. For purposes of this appendix, we deemed deposits made after the end of the plan year to have been made on the final day of the plan year consistent with the method mandated by ERISA.
- 4/ A prepayment credit represents the accumulated value of premature funding from the previous year(s). A prepayment credit is created when contributions, plus interest, exceed the end-of-year Cost Accounting Standards (CAS) funding target. A prepayment credit may be carried forward, with interest, to the first of each subsequent plan years until needed to fund future CAS pension costs. The accumulated value of prepayment credits is available as of the first day of the plan year and is applied as of the first day of the plan year to cover the cost assigned to the period.
- 5/ The present value of funding represents the present value of contributions plus accumulated prepayment credits. This is the amount of funding that is available to cover the CAS funding target measured at the first day of each plan year.
- 6/ The CAS funding target must be funded by accumulated prepayment credits or current year contributions to satisfy the funding requirement of the Federal Acquisition Regulations (FAR) 31.205-6(j)(2)(i).
- 7/ The percentage of costs funded is a measure of the portion of the CAS funding target that was funded during the plan year. Since any funding in excess of the CAS funding target is considered premature funding in accordance with CAS 412.50(c)(1) (as amended), the funded ratio may not exceed 100 percent. We computed the percentage funded as the present value of funding divided by the CAS funding target. For purposes of illustration, the percentage of funding has been rounded to four decimals.

**BLUE CROSS BLUE SHIELD OF OREGON
STATEMENT OF ALLOWABLE PENSION COSTS
FOR FISCAL YEAR 1996**

- 8/ We computed the funded CAS pension cost as the CAS funding target multiplied by the percent funded.
- 9/ We assumed that interest on the funded CAS pension cost, less the prepayment credit, accrues in the same proportion as the interest on contributions bears to the present value of contributions. However, we limited the interest in accordance with FAR 31.205-6(j)(2)(iii), which does not permit the allowable interest to exceed the interest that would accrue if the CAS funding target, less the prepayment credit, was funded in four equal installments deposited within 30 days of the end of the quarter.
- 10/ The allocable CAS pension cost is the amount of pension cost that may be allocated for contract cost purposes.
- 11/ We calculated allowable pension costs of the Medicare and other segment based on the Medicare Part A line of business percentage of each segment. We obtained the percentages from documents provided by Oregon.
- 12/ We computed the allowable calendar year Medicare pension cost as the allocable pension cost multiplied by the Medicare line of business percentage.
- 13/ We converted the plan year (January 1 through December 31) allowable pension costs to a Federal fiscal year (FY) basis (October 1 through September 30). We calculated the FY pension costs as 1/4 of the prior year's costs plus 3/4 of the current year's costs. Costs charged to the Medicare contract should consist of the Medicare segment's direct pension costs plus pension costs attributable to indirect Medicare operations.



October 11, 2006

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Patrick J. Cogley
Regional Inspector General for Audit Services Region VII
601 East 12th Street
Kansas City, Missouri 64106

Dear Mr. Cogley

RE: Audit Response

We have reviewed the referenced draft audit reports and include the following written comments for your consideration:

Report Number: A-07-06-00197

Summary of Findings:

Oregon did correctly implement the prior audit recommendation; however it did not comply with the Medicare contract's pension segmentation requirements when updating the segment's assets from January 1, 1994, through January 1, 1997. As a result, Oregon overstated the January 1, 1997 Medicare segment assets by \$298,048.

Recommendation:

We recommend that Oregon decrease Medicare segment pension assets by \$298,048 as of January 1, 1997.

Regence Response:

We agree with the recommendation. Regence BlueCross and BlueShield of Oregon terminated its Medicare Part A contract effective November 30, 2005.

Report Number: A-07-06-00214

Summary of Findings:

Oregon failed to claim \$136,186 of allowable Medicare Part A pension cost due to an adjustment made to pension costs from an administrative cost audit. Oregon claimed \$25,552 of pension costs for Medicare reimbursement; however we calculated the allowable Medicare pension costs during this period to be \$161,738.

Patrick J. Cogley
October 11, 2006
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Recommendation:

We recommend that Oregon revise its Final Administrative Cost Proposal to claim the allowable Medicare Part A CAS pension cost of \$136,186 for FY 1996.

Regence Response:

We agree with the recommendation. Regence BlueCross and BlueShield of Oregon terminated its Medicare Part A contract effective November 30, 2005 and will include allowable pension cost of \$136,186 as a part of our global settlement with CMS.

Sincerely,



R Paul Warburton
Director of Finance