



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General
Offices of Audit Services

FEB 27 2009

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

Report Number: A-07-07-00244

Mr. Emery Hill
Manager, External Audit Coordination
CareFirst of Maryland, Incorporated
10455 Mill Run Circle
Owings Mills, Maryland 21117

Dear Mr. Hill:

Enclosed is the U.S. Department of Health and Human Services (HHS), Office of Inspector General (OIG), final report entitled "Review of Pension Costs Claimed for Medicare Reimbursement by CareFirst of Maryland, Incorporated, for Fiscal Years 2002 Through 2005." 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.

Pursuant to the Freedom of Information Act, 5 U.S.C. § 552, OIG reports generally are made available to the public to the extent that information in the report is not subject to exemptions in the Act. Accordingly, this report will be posted on the Internet at <http://oig.hhs.gov>.

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 e-mail at Jenenne.Tambke@oig.hhs.gov. Please refer to report number A-07-07-00244 in all correspondence.

Sincerely,

A handwritten signature in black ink, appearing to read "Patrick J. Cogley", written over a white background.

Patrick J. Cogley
Regional Inspector General
for Audit Services

Enclosure

Direct Reply to HHS Action Official:

Ms. Nanette Foster Reilly, Consortium Administrator
Consortium for Financial Management & Fee for Service Operations
Centers for Medicare & Medicaid Services
601 East 12th Street, Room 235
Kansas City, Missouri 64106

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF PENSION COSTS
CLAIMED FOR MEDICARE
REIMBURSEMENT BY CAREFIRST
OF MARYLAND, INCORPORATED
FOR FISCAL YEARS 2002
THROUGH 2005**



Daniel R. Levinson
Inspector General

February 2009
A-07-07-00244

Office of Inspector General

<http://oig.hhs.gov>

The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health and Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

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The Office of Audit Services (OAS) provides auditing services for HHS, either by conducting audits with its own audit resources or by overseeing audit work done by others. Audits examine the performance of HHS programs and/or its grantees and contractors in carrying out their respective responsibilities and are intended to provide independent assessments of HHS programs and operations. These assessments help reduce waste, abuse, and mismanagement and promote economy and efficiency throughout HHS.

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Pursuant to the Freedom of Information Act, 5 U.S.C. § 552, Office of Inspector General reports generally are made available to the public to the extent that information in the report is not subject to exemptions in the Act.

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

CareFirst of Maryland, Incorporated (CareFirst), administered Medicare Part A operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services until the contractual relationship was terminated September 30, 2005.

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 Regulation, Cost Accounting Standards (CAS), and Medicare contracts.

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

OBJECTIVE

Our objective was to determine the allowability of pension costs that CareFirst claimed for Medicare reimbursement for fiscal years (FY) 2002 through 2005.

SUMMARY OF FINDING

CareFirst did not claim some allowable Medicare pension costs for FYs 2002 through 2005. CareFirst claimed \$137,604 of pension costs for Medicare reimbursement; however, allowable Medicare pension costs were \$146,547. CareFirst did not claim \$8,943 of allowable pension costs for FYs 2002 through 2005 because it did not claim pension costs in accordance with the Medicare contracts. Instead, CareFirst based its claim on a pension expense developed for financial reporting purposes.

RECOMMENDATION

We recommend that CareFirst revise its Final Administrative Cost Proposals for FYs 2002 through 2005 to increase claimed pension costs by \$8,943.

AUDITEE COMMENTS

In written comments on our draft report, CareFirst disagreed with our original recommendation to reduce claimed pension costs by \$18,543. Instead, CareFirst stated that its claimed pension costs should be increased by \$8,943.

CareFirst's comments are included in their entirety as the Appendix.

OFFICE OF INSPECTOR GENERAL RESPONSE

After reviewing CareFirst's comments, we revised our calculations and the related recommendation to adjust claimed pension costs.

INTRODUCTION

BACKGROUND

CareFirst

CareFirst of Maryland, Incorporated (CareFirst), administered Medicare Part A operations under cost reimbursement contracts with the Centers for Medicare & Medicaid Services (CMS) until the contractual relationship was terminated September 30, 2005.

Medicare Reimbursement of Pension Costs

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 Regulation (FAR).

Beginning with 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.

Federal Requirements

The Medicare contracts address the determination and allocation of pension costs. Appendix B, section XVI, of the contracts 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.”

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

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

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 pension costs that CareFirst claimed for Medicare reimbursement for FYs 2002 through 2005.

Scope

We reviewed pension costs that CareFirst claimed for Medicare reimbursement on its Final Administrative Cost Proposals (FACP) for FYs 2002 through 2005. Achieving the objective did not require that we review CareFirst'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 CareFirst in Baltimore, Maryland, during October 2005 and May 2007.

Methodology

In performing our review, we used information that CareFirst's actuarial consulting firm provided. We verified CareFirst's actuarial consulting firm's calculation of CAS pension costs for the total company and the Medicare segment. We also verified the extent to which CareFirst funded CAS pension costs with contributions to the pension trust fund and accumulated prepayment credits. 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 reviewed the allocable CAS pension costs based on CareFirst's historical practices and on the results of our segmentation review, "Review of the Qualified Pension Plan at CareFirst of Maryland, Incorporated, a Terminated Medicare Contractor, for the Period January 1, 2002, to December 31, 2005" (A-07-07-00243).

The information provided by CareFirst's actuarial consulting firm included assets, liabilities, normal costs, contributions, benefit payments, investment earnings, and administrative expenses. We examined CareFirst's accounting records, pension plan documents, annual actuarial valuation reports, and Department of Labor/Internal Revenue Service Form 5500s.

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 finding and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objective.

FINDING AND RECOMMENDATION

ALLOWABLE PENSION COSTS NOT CLAIMED

CareFirst did not claim some allowable Medicare pension costs for FYs 2002 through 2005. CareFirst claimed \$137,604 of pension costs for Medicare reimbursement; however, allowable Medicare pension costs were \$146,547. CareFirst did not claim \$8,943 of allowable pension costs for FYs 2002 through 2005 because it did not claim pension costs in accordance with the Medicare contracts. Instead, CareFirst based its claim on a pension expense developed for financial reporting purposes.

On its FACP's for FYs 2002 through 2005, CareFirst claimed pension costs of \$137,604 for Medicare reimbursement. CareFirst based its claim on a pension expense developed for financial reporting purposes. However, this differed from the allowable CAS pension costs. In its written comments on our draft report, CareFirst's determined the allowable pension costs based on separately computed CAS pension costs for the Medicare segment and indirect Medicare operations. We accepted CareFirst's determination

Accordingly, we compared allowable CAS pension costs with the pension costs claimed on CareFirst's FACP's, as shown in the table below.

Pension Cost Claimed Variance			
Fiscal Year	Per Audit	Per CareFirst	Difference
2002	\$39,036	\$34,374	\$4,662
2003	38,598	38,517	\$81
2004	33,862	31,699	\$2,163
2005	35,051	33,014	\$2,037
Total	\$146,547	\$137,604	\$8,943

The allowable CAS pension costs totaled \$146,547. Thus, CareFirst did not claim \$8,943 of allowable pension costs.

RECOMMENDATION

We recommend that CareFirst revise its FACP's for FYs 2002 through 2005 to increase claimed pension costs by \$8,943.

AUDITEE COMMENTS

In written comments on our draft report, CareFirst disagreed with our original recommendation to reduce claimed pension costs by \$18,543. Instead, CareFirst stated that its claimed pension costs should be increased by \$8,943.

CareFirst stated that there were "... several differences between our pension cost figures as reflected in our actuarial reports and those figures used by the OIG [Office of Inspector General],

including the calculation of: the pension cost amount included in the 2005 FACP . . .” In addition, CareFirst said that “. . . it appears that . . . the OIG limited the CAS funding target to the prepayment credit that the OIG calculated.”

CareFirst’s comments are included in their entirety as the Appendix.

OFFICE OF INSPECTOR GENERAL RESPONSE

After reviewing CareFirst’s comments, we revised our calculations and the related recommendation to adjust claimed pension costs.

With respect to the differing cost computations, CareFirst’s written comments were incorrect as to the reason why our original cost computations differed from those computed by CareFirst’s actuarial consulting firm. That is, contrary to CareFirst’s statement, we did not limit the CAS funding target to the prepayment credit that we had calculated. In actuality, we based our original pension cost calculations associated with indirect Medicare operations on the Plan that was formed through the merger, effective December 31, 2002, of the CareFirst of Maryland, Inc., Retirement Plan and the Group Hospitalization and Medical Services, Inc., Pension Trust Plan.¹ However, CareFirst’s Medicare indirect pension costs were based on CareFirst of Maryland, Inc., being treated as a separate segment for computing CAS pension costs. After considering CareFirst’s written comments and supporting information, we agreed with this approach and accepted CareFirst’s computation of indirect pension costs.

With respect to the pension cost claimed on the FY 2005 FACP, the amount shown in our draft report was previously verified by CareFirst personnel. However, as part of its response, CareFirst provided documentation regarding an adjustment to the amount of pension cost claimed.

¹The result of this merger was called the CareFirst, Inc., Retirement Plan.

APPENDIX

William V. Stack
Vice President and
Corporate Controller

CareFirst BlueCross BlueShield
10455 Mill Run Circle
Owings Mills, MD 21117-4208
Tel. 410-998-7011
Fax 410-998-6850
Cellular 410-218-6634
E-mail: Bill.Stack@carefirst.com



November 7, 2008

Office of the Inspector General
Office of Audit Services
Department of Health and Human Services
Region VII
601 East 12th Street
Room 284A
Kansas City, Missouri 64106

Re: Audit Report A-07-07-00244

Dear Mr. Cogley:

CareFirst of Maryland, Inc., d/b/a CareFirst BlueCross BlueShield ("CareFirst") submits this letter as its response to the above referenced draft report entitled "Review of Pension Costs Claimed for Medicare Reimbursement by CareFirst of Maryland, Incorporated for Fiscal Years 2002 Through 2005" (the "Draft Pension Costs Report").

Recommendation

The Draft Pension Costs Report found that CareFirst "claimed \$18,543 of unallowable pension costs for FYs 2002 through 2005 because it based its claim on incorrectly computed CAS pension costs." The Draft Pension Costs Report recommends that CareFirst revise its Final Administrative Cost Proposals (FACPs) for FYs 2002 through 2005 to reduce claimed pension costs by \$18,543.

Plan Response

CareFirst disagrees with this recommendation. In preparing its response to the Draft Pension Costs Report, CareFirst reviewed the final funded CAS pension cost amounts for FYs 2002 through 2005 as reflected in its actuarial reports. As a result of this review, CareFirst determined that pension costs were undercharged in the amount of \$8,943 for FYs 2002 through 2005. Our calculations are reflected in the attached Schedule A.

Our review of the schedules provided by the OIG in the Appendix to the Draft Pension Costs Report revealed several differences between our pension cost figures as reflected in our actuarial reports and those figures used by the OIG, including the calculation of: the pension cost amount included in the 2005 FACP (see attached Schedule B), contribution amounts, the conversion of the calendar year allowable costs to the fiscal year allowable costs, and the CAS funding target. OIG's basis for most of these differing calculations is not clear from the Draft Pension Costs Report. With respect to the CAS funding targets, it appears that for at least two years, the OIG limited the CAS funding target to the prepayment credit that the OIG calculated. We do not believe that this limitation is supported by CAS 412 or CAS 413, the Medicare contract, or the regulations. Carefirst believes the CAS amounts as determined in its actuarial reports to be correct.

CareFirst will make appropriate adjustments to correct the claimed pension costs undercharge in CareFirst's final settlement proposal that will be submitted in connection with the termination of CareFirst's Medicare A contract.

If you have any questions regarding this response, please contact me at (410) 998-7011. We appreciate your consideration of the issues raised in our response.

Sincerely,

A handwritten signature in blue ink, appearing to read "William V. Stack".

William V. Stack
Vice President and
Corporate Controller