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US OFFICE OF PERSONNEL MANAGEMENT  
OFFICE OF THE INSPECTOR GENERAL  
OFFICE OF AUDITS

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# Final Audit Report

Subject:

**Audit of the Federal Employees Health Benefits  
Program Operations of Health Plan of Nevada**

Report No. 1C-NM-00-08-049

Date: February 5, 2009

--CAUTION--

This audit report has been distributed to Federal officials who are responsible for the administration of the audited program. This audit report may contain proprietary data which is protected by Federal law (18 U.S.C. 1905); therefore, while this audit report is available under the Freedom of Information Act, caution needs to be exercised before releasing the report to the general public.



Office of the  
Inspector General

UNITED STATES OFFICE OF PERSONNEL MANAGEMENT

Washington, DC 20415

**AUDIT REPORT**

**Federal Employees Health Benefits Program  
Community-Rated Health Maintenance Organization  
Health Plan of Nevada  
Contract Number CS 1942 - Plan Code NM  
Las Vegas, Nevada**

Report No. 1C-NM-00-08-049

Date: February 5, 2009

A handwritten signature in black ink, appearing to read "Michael R. Esser", written over a horizontal line.

**Michael R. Esser**  
**Assistant Inspector General**  
**for Audits**



UNITED STATES OFFICE OF PERSONNEL MANAGEMENT

Washington, DC 20415

Office of the  
Inspector General

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**EXECUTIVE SUMMARY**

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**Federal Employees Health Benefits Program  
Community-Rated Health Maintenance Organization  
Health Plan of Nevada  
Contract Number CS 1942 - Plan Code NM  
Las Vegas, Nevada**

**Report No. 1C-NM-00-08-049**

**Date: February 5, 2009**

The Office of the Inspector General performed an audit of the Federal Employees Health Benefits Program (FEHBP) operations at Health Plan of Nevada (Plan). The audit covered contract years 2003 through 2008 and was conducted at the Plan's office in Las Vegas, Nevada. This report questions \$2,158,941 for inappropriate charges to the FEHBP in 2004, 2007, and 2008, including \$94,261 for lost investment income. We found that the FEHBP rates were developed in accordance with the applicable laws, regulations, and OPM's rating instructions in contract years 2003, 2005, and 2006.

The questioned costs are a result of the Plan applying an incorrect discount to the FEHBP rates in 2004 because of an error in its calculation of a discount for [REDACTED]; the Plan giving [REDACTED] a 2 year contract starting in 2006, which resulted in a discount of [REDACTED] percent; and the Plan giving [REDACTED] a 2 year contract starting in 2007, which resulted in a [REDACTED] percent discount. We applied these discounts to the FEHBP's rates and determined that the FEHBP was overcharged \$2,064,680.

Consistent with the FEHBP regulations and contract, the FEHBP is due \$94,261 for lost investment income, calculated through January 31, 2009, on the defective pricing findings in 2004, 2007, and 2008. In addition, the contracting officer should recover lost investment income on amounts due for the period beginning February 1, 2009, until all defective pricing amounts have been returned to the FEHBP.

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# I. INTRODUCTION AND BACKGROUND

## Introduction

We completed an audit of the Federal Employees Health Benefits Program (FEHBP) operations at Health Plan of Nevada (Plan) in Las Vegas, Nevada. The audit covered contract years 2003 through 2008. The audit was conducted pursuant to the provisions of Contract CS 1942; 5 U.S.C. Chapter 89; and 5 Code of Federal Regulations (CFR) Chapter 1, Part 890. The audit was performed by the Office of Personnel Management's (OPM) Office of the Inspector General, as established by the Inspector General Act of 1978, as amended.

## Background

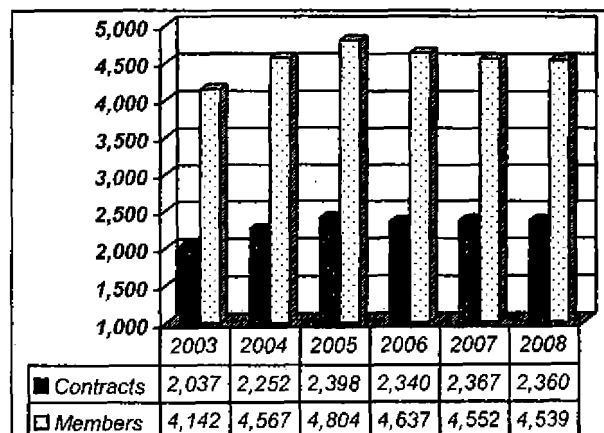
The FEHBP was established by the Federal Employees Health Benefits Act (Public Law 86-382), enacted on September 28, 1959. The FEHBP was created to provide health insurance benefits for federal employees, annuitants, and dependents. The FEHBP is administered by OPM's Center for Retirement and Insurance Services. The provisions of the Federal Employees Health Benefits Act are implemented by OPM through regulations codified in Chapter 1, Part 890 of Title 5, CFR. Health insurance coverage is provided through contracts with various health insurance carriers that provide service benefits, indemnity benefits, or comprehensive medical services.

Community-rated carriers participating in the FEHBP are subject to various federal, state and local laws, regulations, and ordinances. While most carriers are subject to state jurisdiction, many are further subject to the Health Maintenance Organization Act of 1973 (Public Law 93-222), as amended (i.e., many community-rated carriers are federally qualified). In addition, participation in the FEHBP subjects the carriers to the Federal Employees Health Benefits Act and implementing regulations promulgated by OPM.

The FEHBP should pay a market price rate, which is defined as the best rate offered to either of the two groups closest in size to the FEHBP. In contracting with community-rated carriers, OPM relies on carrier compliance with appropriate laws and regulations and, consequently, does not negotiate base rates. OPM negotiations relate primarily to the level of coverage and other unique features of the FEHBP.

The chart to the right shows the number of FEHBP contracts and members reported by the Plan for March 31 of each contract year audited.

**FEHBP Contracts/Members  
March 31**



The Plan began participating in the FEHBP in 1984 and provides health benefits to FEHBP members throughout Las Vegas, Nevada. The last audit of the Plan conducted by our office was a full scope audit of contract years 2000 through 2002. As a result of that audit, we found that the Plan's rating of the FEHBP was in accordance with the applicable laws, regulations, and OPM rating instructions for the years audited.

The preliminary results of this audit were discussed with Plan officials at an exit conference and through subsequent correspondence. A draft report was also provided to the Plan for review and comment. The Plan's comments were considered in the preparation of this final report and are included, as appropriate, as the Appendix.

## II. OBJECTIVES, SCOPE, AND METHODOLOGY

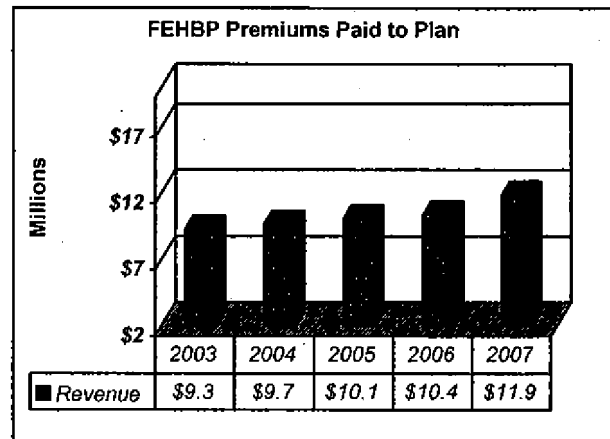
### Objectives

The primary objectives of the audit were to verify that the Plan offered market price rates to the FEHBP and to verify that the loadings to the FEHBP rates were reasonable and equitable. Additional tests were performed to determine whether the Plan was in compliance with the provisions of the laws and regulations governing the FEHBP.

### Scope

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 objectives.

This performance audit covered contract years 2003 through 2008<sup>1</sup>. For contract years 2003 through 2007, the FEHBP paid approximately \$51 million in premiums to the Plan. The premiums paid for each contract year audited are shown on the chart to the right.



OIG audits of community-rated carriers are designed to test carrier compliance with the FEHBP contract, applicable laws and regulations, and OPM rate instructions. These audits are also designed to provide reasonable assurance of detecting errors, irregularities, and illegal acts.

We obtained an understanding of the Plan's internal control structure, but we did not use this information to determine the nature, timing, and extent of our audit procedures. However, the audit included such tests of the Plan's rating systems and such other auditing procedures as we considered necessary under the circumstances. Our review of internal controls was limited to the procedures the Plan has in place to ensure that:

- The appropriate similarly sized subscriber groups (SSSG) were selected;
- the rates charged to the FEHBP were the market price rates (i.e., equivalent to the best rate offered to an SSSG); and
- the loadings to the FEHBP rates were reasonable and equitable.

<sup>1</sup> The Subscription Income Report for 2008 was not available at the time this report was completed.

In conducting the audit, we relied to varying degrees on computer-generated billing, enrollment, and claims data provided by the Plan. We did not verify the reliability of the data generated by the various information systems involved. However, nothing came to our attention during our audit testing utilizing the computer generated data to cause us to doubt its reliability. We believe that the available data was sufficient to achieve our audit objectives. Except as noted above, the audit was performed in accordance with generally accepted government auditing standards, issued by the Comptroller General of the United States.

The audit fieldwork was conducted at the Plan's office in Las Vegas, Nevada, during June and July 2008. Additional audit work was completed at our office in Jacksonville, Florida.

### **Methodology**

We examined the Plan's federal rate submissions and related documents as a basis for validating the market price rates. In addition, we examined the rate development documentation and billings to other groups, such as SSSGs, to determine if the market price was actually charged to the FEHBP. Finally, we used the contract, the Federal Employees Health Benefits Acquisition Regulations (FEHBAR), and OPM's Rate Instructions to Community-Rated Carriers to determine the propriety of the FEHBP premiums and the reasonableness and acceptability of the Plan's rating system.

To gain an understanding of the internal controls in the Plan's rating system, we reviewed the Plan's rating system's policies and procedures, interviewed appropriate Plan officials, and performed other auditing procedures necessary to meet our audit objectives.



### **III. AUDIT FINDINGS AND RECOMMENDATIONS**

#### **Premium Rates**

##### **1. Defective Pricing**

**\$2,064,680**

The Certificates of Accurate Pricing the Plan signed for contract years 2004, 2007, and 2008 were defective. In accordance with federal regulations, the FEHBP is therefore due a price adjustment for each year. We applied the defective pricing remedies for the years in question and determined that the FEHBP is entitled to premium adjustments totaling \$2,064,680 (see Exhibit A). We found that the FEHBP rates were developed in accordance with the applicable laws, regulations, and OPM rating instructions in contract years 2003, 2005, and 2006.

Carriers proposing rates to OPM are required to submit a Certificate of Accurate Pricing certifying that the proposed subscription rates, subject to adjustments recognized by OPM, are market price rates. OPM regulations refer to a market price rate in conjunction with the rates offered to an SSSG. If it is found that the FEHBP was charged rates that exceeded the market price (i.e., the best rate offered to an SSSG), a condition of defective pricing exists, requiring a downward adjustment of the FEHBP premiums to the equivalent market price.

#### **2004**

The Plan selected [REDACTED] as SSSGs for contract year 2004. We agree with these selections. [REDACTED] started the contract year with three subgroups - [REDACTED] and [REDACTED]. All three groups had different billed rates. Starting in July, the group decided to include both [REDACTED] into the [REDACTED] plan. However, the billed rates for all enrollees remained at the [REDACTED] rates. The Plan calculated a [REDACTED] percent discount as a result of the combination of the three groups and applied this discount to the FEHBP rates. However, we calculated a [REDACTED] percent discount. Accordingly, we redeveloped the FEHBP rates by applying the [REDACTED] percent SSSG discount. A comparison of the audited rates to the reconciled rates shows that the FEHBP was overcharged \$52,414 in 2004 (see Exhibit B).

#### **Plan's Comments (See Appendix):**

The Plan states that the [REDACTED] was not included in the calculation of the average premium ratio in the [REDACTED] worksheet for the [REDACTED] group. The original ratio of [REDACTED] should be [REDACTED]. This correction reduces the discount to [REDACTED] percent and results in \$52,090 due the FEHBP.

#### **OIG's Response to the Plan's Comments:**

We reviewed the [REDACTED] worksheet submitted by the Plan and agree that the [REDACTED] category was not included in the calculation of the average premium ratio.

We also agree with the revised discount of [REDACTED] percent given to the [REDACTED] group and that this discount should be applied to the FEHBP rates. However, our calculation shows that the FEHBP is due \$52,414 for 2004, not \$52,090.

## **2007**

The Plan selected [REDACTED] as SSSGs for contract year 2007. We agree with these selections. Our analysis of the SSSG rates shows that [REDACTED] had a two year contract starting in 2006. However, in calculating any potential discount as a result of the two year contract, the Plan used the same enrollment data from the calculation of the 2006 [REDACTED] adjustment factor instead of using enrollment data that would be available at the time the 2007 rates were developed.

Accordingly, we recalculated [REDACTED] rates using current enrollment data for the calculation of the [REDACTED] adjustment factor. As a result, [REDACTED] received a [REDACTED] percent discount, instead of the [REDACTED] percent discount calculated by the Plan and applied to the FEHBP rates. Therefore, we redeveloped the FEHBP rates by applying the [REDACTED] percent SSSG discount. A comparison of the audited rates to the reconciled rates shows that the FEHBP was overcharged \$444,115 in contract year 2007 (see Exhibit B).

### **Plan's Response (See Appendix):**

The Plan disagrees with updating the enrollment data in the middle of a two year contract. The Plan states that using updated enrollment to evaluate the rates charged to an SSSG introduces "hindsight" into the process which the Plan says is contrary to the principles of community rating. The Plan further states that there is no basis in OPM's regulations or rating instructions for this approach. The Plan states that the only instruction relating to rates that extend beyond 12 months requires that premium adjustments be made or the rate extensions will be considered as a discount. The Plan states that it complied with this requirement at the time of the 2007 rate reconciliation when it gave the FEHBP a [REDACTED] percent discount in connection with the rates charged to [REDACTED].

### **OIG's Response to the Plan's Comments:**

OPM's 2007 Rate Reconciliation Instructions state that, "If an SSSG's rate is extended beyond twelve months...a premium adjustment that reflects the entire value of the extension must be made for the SSSG in the following year, or the rate extension will be considered a discount." In determining the discount, the Plan used the same enrollment data from the calculation of the 2006 [REDACTED] adjustment factor. To be consistent with the methodology used to develop the FEHBP's and the other SSSG's rates, enrollment data that was available at the time the 2007 rates were developed should have been used for the calculation of the [REDACTED] adjustment factor. Therefore, we recalculated [REDACTED] rates using current enrollment data for the calculation of the [REDACTED] adjustment factor. As a result, [REDACTED] received a [REDACTED] percent discount, which we applied to the FEHBP rates.

## 2008

The Plan selected [REDACTED] as the SSSGs for contract year 2008. We agree with these selections. Our analysis of the SSSG rates shows that [REDACTED] had a two year contract starting in 2007. However, in calculating any potential discount as a result of the two year contract, the Plan used the same enrollment data from the calculation of the 2007 [REDACTED] adjustment factor instead of using enrollment data that was available at the time the 2008 rates were developed. Accordingly, we recalculated [REDACTED] rates using the current enrollment data for the calculation of the [REDACTED] adjustment factor. As a result, we determined that a [REDACTED] percent discount was given to [REDACTED]. Therefore, we applied this discount to the FEHBP rates. A comparison of the audited rates to the reconciled rates shows that the FEHBP was overcharged \$1,568,151 in contract year 2008 (see Exhibit B).

### Plan's Comments (See Appendix):

The Plan states that OPM's instructions regarding multi-year rate agreements require a plan to use the current year's rating methodology when determining any discount in the second and subsequent years of the rate agreement. The Plan states that its evaluation of [REDACTED] rates was consistent with OPM's instructions. Further, the Plan states that according to OPM's rate reconciliation instructions, a plan may not update the FEHBP enrollment data to reflect the impact of open season. Therefore, to be consistent with the established rating methodology, the Plan used the enrollment data it used in developing [REDACTED] 2007 [REDACTED] factor.

### OIG's Response to the Plan's Comments:

The Plan states that it followed OPM's instructions by using the current year's methodology to determine any discount in the second year of [REDACTED] two year contract. We disagree. The methodology used to develop [REDACTED] current rates (i.e., the 2007 rates) was based on rating factors, including enrollment, that were available at the time the rates were developed. Therefore, to evaluate the 2008 rates, the Plan should use the rating factors, including enrollment, that were available at the time the 2008 rates were developed. This is the methodology we used in calculating the [REDACTED] percent discount given to [REDACTED].

Further, the Plan states that OPM does not allow plans to update the FEHBP's enrollment to reflect open season changes; therefore, the Plan applied the same approach when developing [REDACTED] rates. We agree that OPM does not allow plans to update the FEHBP's enrollment between the proposal and reconciliation to reflect the impact of open season changes. However, that limitation applies within the same year. For example, the Plan cannot use one set of enrollment statistics to develop the proposed 2008 rates and then use a different set of enrollment statistics to develop the reconciled 2008 rates. The issue with [REDACTED] is not the same. The Plan used the same set of enrollment statistics to develop both the 2007 and potential 2008 rates. Using the enrollment data that

was available at the time 2008 rates were developed is not inconsistent with OPM's instructions.

In conclusion, we developed [REDACTED] 2008 rates as the Plan would have done had the group not had a two year contract and determined that the group received a [REDACTED] percent discount in 2008 that was not applied to the FEHBP rates.

### **Recommendation 1**

We recommend that the contracting officer require the Plan to return \$2,064,680 to the FEHBP for defective pricing in 2004, 2007, and 2008.

## **2. Lost Investment Income**

**\$94,261**

In accordance with FEHBP regulations and the contract between OPM and the Plan, the FEHBP is entitled to recover lost investment income on the defective pricing findings in contract years 2004, 2007, and 2008. We determined that the FEHBP is due \$94,261 for lost investment income, calculated through January 31, 2009. In addition, the FEHBP is entitled to lost investment income for the period beginning February 1, 2009, until all defective pricing amounts have been returned to the FEHBP.

FEHBAR 1652.215-70 provides that, if any rate established in connection with the FEHBP contract was increased because the carrier furnished cost or pricing data that was not complete, accurate, or current as certified in its Certificate of Accurate Pricing, the rate shall be reduced by the amount of the overcharge caused by the defective data. In addition, when the rates are reduced due to defective pricing, the regulation states that the government is entitled to a refund and simple interest on the amount of the overcharge from the date the overcharge was paid to the carrier until the overcharge is liquidated.

Our calculation of lost investment income is based on the United States Department of the Treasury's semiannual cost of capital rates.

### **Plan's Response (See Appendix):**

The Plan did not provide any comments regarding the lost investment income finding.

### **Recommendation 2**

We recommend that the contracting officer require the Plan to return \$94,261 to the FEHBP for lost investment income, calculated through January 31, 2009. In addition, we recommend that the contracting officer recover lost investment income on amounts due for the period beginning February 1, 2009, until all defective pricing amounts have been returned to the FEHBP.

## IV. MAJOR CONTRIBUTORS TO THIS REPORT

### Community-Rated Audits Group

██████████ Auditor-in-Charge

██████████ Staff Auditor

██████████ Staff Auditor

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██████████ Chief

██████████ Senior Team Leader

**Health Plan of Nevada  
Summary of Questioned Costs**

Defective Pricing Questioned Costs:

Contract Year 2004	\$52,414
Contract Year 2007	\$444,115
Contract Year 2008	<u>\$1,568,151</u>

Total Defective Pricing Questioned Costs \$2,064,680

Lost Investment Income \$94,261

***Total Questioned Costs*** **\$2,158,941**

Exhibit B

Health Plan of Nevada  
Defective Pricing Questioned Costs

2004

	<u>Self</u>	<u>Family</u>	
FEHBP Line 5 - Reconciled Rate			
FEHBP Line 5 - Audited Rate			
Overcharge			
To Annualize Overcharge:			
3/31/04 enrollment			
Pay Periods	26	26	
Subtotal	\$12,243	\$40,171	
Total 2004 Defective Pricing Questioned Costs			<u>\$52,414</u>

2007

	<u>Self</u>	<u>Family</u>	
FEHBP Line 5 - Reconciled Rate			
FEHBP Line 5 - Audited Rate			
Overcharge			
To Annualize Overcharge:			
3/31/07 enrollment			
Pay Periods	26	26	
Subtotal	\$117,066	\$327,049	
Total 2007 Defective Pricing Questioned Costs			<u>\$444,115</u>

2008

	<u>Self</u>	<u>Family</u>	
FEHBP Line 5 - Reconciled Rate			
FEHBP Line 5 - Audited Rate			
Overcharge			
To Annualize Overcharge:			
3/31/08 enrollment			
Pay Periods	26	26	
Subtotal	\$414,800	\$1,153,351	
Total 2008 Defective Pricing Questioned Costs			<u>\$1,568,151</u>

**Total Defective Pricing Questioned Costs** \$2,064,680

**Health Plan of Nevada  
Lost Investment Income**

<b>Year</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>Total</b>
<b>Audit Findings:</b>							
1. Defective Pricing	\$52,414	\$0	\$0	\$444,115	\$1,568,151	\$0	\$2,064,680
Totals (per year):	\$52,414	\$0	\$0	\$444,115	\$1,568,151	\$0	\$2,064,680
Cumulative Totals:	\$52,414	\$52,414	\$52,414	\$496,529	\$2,064,680	\$2,064,680	\$2,064,680
Avg. Interest Rate (per year):	4.250%	4.375%	5.4375%	5.5000%	4.9375%	5.6250%	
Interest on Prior Years Findings:	\$0	\$2,293	\$2,850	\$2,883	\$24,516	\$9,678	\$42,220
Current Years Interest:	\$1,114	\$0	\$0	\$12,213	\$38,714	\$0	\$52,041
Total Cumulative Interest Calculated Through January 31, 2009:	\$1,114	\$2,293	\$2,850	\$15,096	\$63,230	\$9,678	<b>\$94,261</b>





2008 DEC 23 AM 7:11 HEALTH PLAN OF NEVADA  
A UnitedHealthcare Company

December 17, 2008

VIA UPS OVERNIGHT

[REDACTED]  
Chief, Community-Rated Audits Group  
U.S. Office of Personnel Management  
Office of the Inspector General  
1900 E Street, NW  
Room 6400  
Washington, DC 20415

Re: Health Plan of Nevada, Inc.  
Draft Audit Report No. IC-NM-00-08-049

Dear [REDACTED]

This letter and accompanying exhibit respond to the above-referenced draft audit report (the "Draft Report") on the Federal Employees Health Benefits Program ("FEHBP") operations at Health Plan of Nevada, Inc. (the "Plan") for contract years 2003 through 2008. A CD containing this response is enclosed.

The Draft Report contains preliminary findings that the Plan engaged in defective pricing in contract years 2004, 2007 and 2008, and questions \$2,444,266 for inappropriate health benefit charges to the FEHBP excluding lost investment income. The Draft Report found that the Plan's rates to the FEHBP for contract years 2003, 2005 and 2006 were developed in accordance with Office of Personnel Management ("OPM") rules and regulations.

As discussed below, the Plan disagrees that it engaged in defective pricing in 2004, 2007 and 2008. Moreover, the only adjustment due the FEHBP in connection with these three years is a slight additional discount for 2004.

**I. Contract Year 2004**

For contract year 2004, the Draft Report agrees with the Plan's similarly sized subscriber group ("SSSG") selections of [REDACTED]. The [REDACTED] had three separate subgroups - [REDACTED] - each with separate billed rates. In mid 2004, the [REDACTED] were combined into the [REDACTED]. The billed rates for all enrollees remained at the [REDACTED] rates. In the 2004 reconciliation, the Plan determined that the [REDACTED]

Good health takes a good plan.<sup>SM</sup>

received a [REDACTED] discount as a result of combining the three subgroups, and therefore gave the FEHBP the same discount. However, the Draft Report calculated a [REDACTED] discount for the SSSG. Based on that calculation, the Draft Report recommends that the Plan overcharged the FEHBP by \$385,674.

The Plan disagrees with the Draft Report's calculation of the additional discount for the [REDACTED] group and the resulting overcharge amount for the FEHBP. Upon further review of the group's rating, the Plan identified an error in the calculation of the average Premium Ratio [REDACTED] in the [REDACTED] worksheet originally prepared by the Plan and in the audited [REDACTED] worksheets for the period 6/1/04-12/31/04. Specifically, the [REDACTED] category was excluded from the calculation. (See Excel file A, [REDACTED].xls, tab [REDACTED]). The premium ratio is also used in the derivation of the step up factor, which is used to convert the adjusted per member per month premium rate into an employee only premium rate. The original step up factor was [REDACTED] and the corrected factor is [REDACTED] (See Excel file B, [REDACTED]4-25-04)7-04Corrected.xls, tab "[REDACTED]"). This correction in step up factor generates a final discount of [REDACTED] % and an additional adjustment to the FEHBP of \$52,090. (See Excel file D, [REDACTED] 2004 Rev.xls.)

## II. Contract Year 2007

For contract year 2007, the Draft Report agrees with the Plan's SSSG selections of [REDACTED]. In 2007, [REDACTED] was in the second year of a two year contract. For purposes of determining whether the SSSG received a discount in 2007 as a result of the two year contract, the Plan, consistent with its established rating practice, compared the pricing factors used in the original rating of the group to updated trend and other pricing factors. Based on that analysis, the Plan determined that the SSSG received a [REDACTED] % discount and reported this discount in the 2007 rate reconciliation.

The Draft Report contains preliminary findings that [REDACTED] received a [REDACTED] discount in 2007 as a result of the two year contract and recommends that the Plan return an additional \$444,115 to the FEHBP. The difference between the Plan's discount calculation and the Draft Report's discount calculation is solely attributable to the Draft Report using updated enrollment data (i.e., the enrollment data that the Plan would have used if the group had a 12 month contract for 2007) to develop the [REDACTED] adjustment factor. In evaluating

the group's 2007 rates for purposes of the 2007 reconciliation, the Plan used the enrollment data that was available at the time of the original rating for the two year contract to develop the [REDACTED] adjustment factor. The Plan disagrees with the Draft Report's use of updated enrollment data in analyzing the second year of a two year contract. Such an approach is not appropriate and is not provided for in OPM's rating instructions.

Specifically, there is no reason to review the enrollment data from the middle of the two year contract period to assess the Plan's rates for the group. That data is relevant for the limited purpose of determining whether the group is in fact an SSSG based on its size. The only enrollment data that is relevant to an evaluation of the rates charged the SSSG is the enrollment data used in the original rating of the group. Were OPM to take the position that updated enrollment data must be used for rate evaluation purposes, such a position would inappropriately shift the focus to whether health plans had, in retrospect, guessed right, rather than focusing, as the OIG always has, on whether the plans rated the SSSGs properly based on information available at the time their rates were set.

Finally, there is no basis in OPM's regulations or rating instructions for the approach taken in the Draft Report. Neither the 2007 Community Rate Instructions nor the Reconciliation Guidelines for 2007 Rates provide for the approach used in the Draft Report. The Instructions and Guidelines do refer to enrollment data as of March 31<sup>st</sup> of the coverage year, but that is in reference to the *identification* of the SSSGs, not the evaluation of the rates charged the SSSGs.<sup>1</sup> Using updated enrollment data to evaluate the rates charged a group introduces "hindsight" into the rating process, which is contrary to principles of community rating. The only instruction relating to rates that extend beyond 12 months requires that premium adjustment be made or the rate extension will be considered as a discount. The Plan complied with this requirement at the time of the 2007 rate reconciliation when it gave the FEHBP a [REDACTED] % discount in connection with the rates charged [REDACTED]

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<sup>1</sup> The 2007 Community Rating Guidelines provide at page 8 that: "All group enrollments including new groups (the Federal group and the SSSG enrollments) should be the latest 2007 enrollment available to the carrier (but no later than March 31, 2007)."

### III. Contract Year 2008

The findings and recommendation for contract year 2008 are similar to those for 2007. The Draft Report agrees with the Plan's SSSG selections of [REDACTED]. For 2008, [REDACTED] was in the second year of a two year rate contract. The Draft Report contains preliminary findings that the SSSG received a [REDACTED] discount by using updated enrollment data to calculate the [REDACTED] adjustment factor for contract year 2008. Consistent with 2007 and the Plan's established rating practice, the Plan used the original enrollment data for purposes of the 2008 rate reconciliation. For the reasons discussed in Section II above, the Plan disagrees with the Draft Report's use of updated enrollment data to calculate the [REDACTED] adjustment factor in evaluating [REDACTED] 2008 rates.<sup>2</sup>

Also, the 2008 Rate Instructions include the following discussion at page 13 regarding multi-year rate agreements:

If a group has negotiated a multi year contract and is determined to be an SSSG, the following rules will apply:

- If the SSSG is in the first year of the multi year contract, the current methodology for determining reasonableness of rate will be applied. For the second and all subsequent years of a multi year contract, SSSG discounts or overcharges will be determined by applying the current year methodology to the current year rate. If a discount is determined to have been applied to the SSSG, the previous years in the multi year contract will be used to determine if the carrier included additional costs due to the multi year rate contract. If this is the case, the discount applied to the SSSG may be offset by these costs.

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<sup>2</sup> The Plan has identified an error in the billed premium rate used by the auditors for members enrolled in the HMO D20 benefit plan. Specifically, the [REDACTED] worksheet prepared by the auditor (Revised SSSG [REDACTED] Audited Rate Development.xls) contains the correct rate of \$ [REDACTED]. However, the 2008 Lead Schedule also prepared by the auditors uses an incorrect rate of \$ [REDACTED] (see tab labeled "Lead Schedule" in workbook named "2008 FEHBP Audited Rate Development Rev.xls"). Using the correct billed rate results in a discount calculation of [REDACTED]%. See tab "Lead Schedule Rev" in same spreadsheet. Copies of the April 2008 Facets invoice and April 2008 premium remittance memo are enclosed. The documents show the billed rate and paid rate of \$ [REDACTED].

In addition the Reconciliation Instructions for 2008 Rates provide at page 6 as follows:

**Multi-Year Rate Agreements**

If a group has negotiated a multi-year contract and is determined to be an SSSG, the following rules will apply:

First year of a multi-year agreement - The process of determining discounts as defined above applies.


Second and all subsequent years of a multi-year agreement – The process of determining discounts as defined above applies. Any additional costs incurred in previous years of the multi-year rate agreement will be considered when determining the discount.


The Plan's rate evaluation of [REDACTED] 2008 rates and of [REDACTED] 2007 rates for purposes of the FEHBP rate reconciliation in each of the two years was consistent with the OPM instructions quoted above.

Finally, the 2008 instructions do not provide for the approach used in the Draft Report. Consistent with its current methodology, the Plan recalculated the SSSGs' rates using the enrollment data used in the original rating of the groups but updated trend and other pricing factors. This is the same approach that the Plan follows and is required by OPM for the FEHBP. That is, in performing the FEHBP rate reconciliation, a plan may use updated rates and pricing factors but may not update the FEHBP enrollment data to reflect the impact of open season. To do so, could artificially increase or decrease the group's rates. Thus, consistent with its established rating methodology and the methodology used for the FEHBP, the Plan used the original enrollment data in its analysis of [REDACTED] 2008 rates and of [REDACTED] 2007 rates.

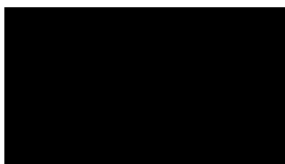
**IV. Conclusion**

Based on the foregoing, no adjustment is due the FEHBP for contract years 2007 or 2008 as the Plan properly accounted for the SSSGs' two year rate contracts. For contract year 2004, the FEHBP is entitled to an additional discount of \$52,090.

  
OPM OIG  
December 17, 2008  
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Please don't hesitate to contact me if you have any questions or require additional information. I can be reached at 

Sincerely,



Chief Operating Officer

Enclosures