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U.S. OFFICE OF PERSONNEL MANAGEMENT  
OFFICE OF THE INSPECTOR GENERAL  
OFFICE OF AUDITS

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# Final Audit Report

Subject:

**HORIZON BLUECROSS BLUESHIELD OF  
NEW JERSEY  
NEWARK, NEW JERSEY**

Report No. 1A-10-49-09-025

Date: February 12, 2010

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UNITED STATES OFFICE OF PERSONNEL MANAGEMENT  
Washington, DC 20415

Office of the  
Inspector General

**AUDIT REPORT**

Federal Employees Health Benefits Program  
Service Benefit Plan      Contract CS 1039  
BlueCross BlueShield Association  
Plan Code 10

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Horizon BlueCross BlueShield of New Jersey  
Plan Codes 280/780  
Newark, New Jersey

REPORT NO. 1A-10-49-09-025

DATE: February 12, 2010

A handwritten signature in black ink, appearing to read "Michael R. Esser".

Michael R. Esser  
Assistant Inspector General  
for Audits



UNITED STATES OFFICE OF PERSONNEL MANAGEMENT

Washington, DC 20415

Office of the  
Inspector General

**EXECUTIVE SUMMARY**

Federal Employees Health Benefits Program  
Service Benefit Plan Contract CS 1039  
BlueCross BlueShield Association  
Plan Code 10

Horizon BlueCross BlueShield of New Jersey  
Plan Codes 280/780  
Newark, New Jersey

REPORT NO. 1A-10-49-09-025      DATE: February 12, 2010

This final audit report on the Federal Employees Health Benefits Program (FEHBP) operations at Horizon BlueCross BlueShield of New Jersey (Plan) in Newark, New Jersey questions \$2,277,467 in health benefit charges and \$1,290,130 in administrative expenses. The BlueCross BlueShield Association (Association) agreed (**A**) with \$1,639,848 and disagreed (**D**) with \$1,927,749 of the questioned costs. Lost investment income (LII) on the questioned costs amounts to \$231,737.

Our audit was conducted in accordance with Government Auditing Standards. The audit covered claim payments from January 1, 2005 through October 31, 2008, as well as miscellaneous payments and credits and administrative expenses from 2003 through 2007 as reported in the Annual Accounting Statements. In addition, we reviewed the Plan's cash management practices related to FEHBP funds for contract years 2003 through 2007.

Questioned items are summarized as follows:

## HEALTH BENEFIT CHARGES

### Claim Payments

- **Omnibus Budget Reconciliation Act of 1990 Review** **\$352,093**

The Plan incorrectly paid 36 claims that were priced or should have been priced under the Omnibus Budget Reconciliation Act of 1990 pricing guidelines, resulting in net overcharges of \$352,093 to the FEHBP. Specifically, the Plan overpaid 29 claims by \$393,826 and underpaid 7 claims by \$41,733. The Association agreed with \$50,430 (*A*) and disagreed with \$301,663 (*D*) of the questioned charges.

- **Claim Payment Errors (A)** **\$16,074**

The Plan incorrectly paid 39 claims, resulting in net overcharges of \$16,074 to the FEHBP. Specifically, the Plan overpaid 38 claims by \$39,534 and underpaid 1 claim by \$23,460.

### Miscellaneous Payments and Credits

- **Subrogation Recoveries** **\$1,237,935**

The Plan had not returned subrogation recoveries of \$1,219,668 to the FEHBP as of December 31, 2007. Subsequent to this date, the Plan returned \$1,201,907 of these questioned recoveries to the FEHBP. As a result, the FEHBP is still due \$30,947, consisting of \$17,761 for the remaining questioned recoveries and \$13,186 for LII on recoveries deposited untimely or not deposited into the Federal Employee Program (FEP) investment account. The Association agreed with \$36,028 (*A*) and disagreed with \$1,201,907 (*D*) of the questioned amount.

- **Health Benefit Refunds** **\$544,050**

The Plan had not returned refunds of \$530,864 to the FEHBP as of December 31, 2007. Subsequent to this date, the Plan returned \$424,179 of these questioned refunds to the FEHBP. As a result, the FEHBP is still due \$119,871, consisting of \$106,685 for the remaining questioned refunds and \$13,186 for LII on refunds deposited untimely or not deposited into the FEP investment account. The Association agreed with \$119,871 (*A*) and disagreed with \$424,179 (*D*) of the questioned amount.

- **Fraud Recoveries (A)** **\$79,046**

The Plan did not deposit into the FEP investment account and/or return to the FEHBP letter of credit account 21 fraud recoveries totaling \$70,320. Also, the Plan deposited 30 fraud recoveries untimely into the FEP investment account. As a result, the FEHBP is due \$79,046, consisting of \$70,320 for fraud recoveries not returned to the FEHBP and \$8,726 for LII on recoveries deposited untimely or not deposited into the FEP investment account.

- **Special Plan Invoices (A)** **\$48,269**

The Plan did not deposit \$39,529 into the FEP investment account for six miscellaneous credits that were reported on special plan invoices (SPI) in 2004 and 2005. Also, the Plan deposited five miscellaneous credits untimely into the FEP investment account that were reported on SPI's in 2006. As a result, the FEHBP is due \$48,269, consisting of \$39,529 for miscellaneous credits and \$8,740 for LII on miscellaneous credits deposited untimely or not deposited into the FEP investment account.

### **ADMINISTRATIVE EXPENSES**

- **Directors Liability and Fidelity & Bond Insurance (A)** **\$731,676**

The Plan overcharged the FEHBP for Directors Liability and Fidelity & Bond Insurance expenses from 2003 through 2007.

- **Post-Retirement Benefit Costs (A)** **\$251,682**

The Plan overcharged the FEHBP for post-retirement benefit costs from 2003 through 2007.

- **Pension Costs (A)** **\$251,241**

The Plan overcharged the FEHBP for pension costs from 2003 through 2007.

- **Administrative Expense Overcharges (A)** **\$70,491**

The Plan overcharged the FEHBP for information technology-related expenses in 2007.

- **Unallowable and/or Unallocable Expenses (A)** **\$52,442**

The Plan charged unallowable and/or unallocable expenses to the FEHBP from 2003 through 2007.

- **Inter-Company Profit Adjustment (A)** **(\$67,402)**

The Plan overstated the adjustment to remove inter-company profits from its subsidiary, National Account Service Company, in 2005.

### **CASH MANAGEMENT**

Overall, we concluded that the Plan handled FEHBP funds in accordance with Contract CS 1039 and applicable laws and regulations, except for the findings pertaining to cash management noted in the "Miscellaneous Payments and Credits" section.

## **LOST INVESTMENT INCOME ON AUDIT FINDINGS**

As a result of our audit findings presented in this audit report, the FEHBP is due LII of **\$231,737**, calculated through June 30, 2009.

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## **I. INTRODUCTION AND BACKGROUND**

### **INTRODUCTION**

This final audit report details the findings, conclusions, and recommendations resulting from our audit of the Federal Employees Health Benefits Program (FEHBP) operations at Horizon BlueCross BlueShield of New Jersey (Plan). The Plan is located in Newark, New Jersey.

The audit was performed by the Office of Personnel Management's (OPM) Office of the Inspector General (OIG), as established by the Inspector General Act of 1978, as amended.

### **BACKGROUND**

The FEHBP was established by the Federal Employees Health Benefits (FEHB) 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. OPM's Retirement and Benefits Office has overall responsibility for administration of the FEHBP. The provisions of the FEHB Act are implemented by OPM through regulations, which are codified in Title 5, Chapter 1, Part 890 of the Code of Federal Regulations (CFR). Health insurance coverage is made available through contracts with various health insurance carriers.

The BlueCross BlueShield Association (Association), on behalf of participating BlueCross and BlueShield plans, has entered into a Government-wide Service Benefit Plan contract (CS 1039) with OPM to provide a health benefit plan authorized by the FEHB Act. The Association delegates authority to participating local BlueCross and BlueShield plans throughout the United States to process the health benefit claims of its federal subscribers. The Plan is one of approximately 63 local BlueCross and BlueShield plans participating in the FEHBP.

The Association has established a Federal Employee Program (FEP<sup>1</sup>) Director's Office in Washington, D.C. to provide centralized management for the Service Benefit Plan. The FEP Director's Office coordinates the administration of the contract with the Association, member BlueCross and BlueShield plans, and OPM.

The Association has also established an FEP Operations Center. The activities of the FEP Operations Center are performed by CareFirst BlueCross BlueShield, located in Washington, D.C. These activities include acting as fiscal intermediary between the Association and member plans, verifying subscriber eligibility, approving or disapproving the reimbursement of local plan payments of FEHBP claims (using computerized system edits), maintaining a history file of all FEHBP claims, and maintaining an accounting of all program funds.

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<sup>1</sup> Throughout this report, when we refer to "FEP" we are referring to the Service Benefit Plan lines of business at the Plan. When we refer to the "FEHBP" we are referring to the program that provides health benefits to federal employees.



Compliance with laws and regulations applicable to the FEHBP is the responsibility of the Association and Plan management. Also, management of the Plan is responsible for establishing and maintaining a system of internal controls.

All findings from our previous audit of the Plan (Report No. 1A-10- 49-04-072, dated October 5, 2006) for contract years 1999 through 2002 have been satisfactorily resolved.

The results of this audit were provided to the Plan in written audit inquiries; were discussed with Plan and/or Association officials throughout the audit and at an exit conference; and were presented in detail in a draft report, dated July 8, 2009. The Association's comments offered in response to the draft report were considered in preparing our final report and are included as Appendices to this report.

## **II. OBJECTIVES, SCOPE, AND METHODOLOGY**

### **OBJECTIVES**

The objectives of our audit were to determine whether the Plan charged costs to the FEHBP and provided services to FEHBP members in accordance with the terms of the contract. Specifically, our objectives were as follows:

#### **Health Benefit Charges**

- To determine whether the Plan complied with contract provisions relative to benefit payments.
- To determine whether miscellaneous payments charged to the FEHBP were in compliance with the terms of the contract.
- To determine whether credits and miscellaneous income relating to FEHBP benefit payments were returned promptly to the FEHBP.

#### **Administrative Expenses**

- To determine whether administrative expenses charged to the contract were actual, allowable, necessary, and reasonable expenses incurred in accordance with the terms of the contract and applicable regulations.

#### **Cash Management**

- To determine whether the Plan handled FEHBP funds in accordance with applicable laws and regulations concerning cash management in the FEHBP.

### **SCOPE**

We conducted our performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient and 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.

We reviewed the BlueCross and BlueShield FEHBP Annual Accounting Statements as they pertain to Plan codes 280 and 780 for contract years 2003 through 2007. During the period, the Plan paid approximately \$1.3 billion in health benefit charges and \$104 million in administrative expenses (See Figure 1 and Schedule A).

Specifically, we reviewed approximately \$16 million in claim payments made from January 1, 2005 through October 31, 2008 for proper adjudication. In addition, we reviewed miscellaneous payments and credits, such as refunds and subrogation recoveries, administrative expenses, and cash management for 2003 through 2007.

In planning and conducting our audit, we obtained an understanding of the Plan's internal control structure to help determine the nature, timing, and extent of our auditing procedures. This was determined to be the most effective approach to select areas of audit. For those areas selected, we primarily relied on substantive tests of transactions and not tests of controls. Based on our testing, we did not identify any significant matters involving the Plan's internal control structure and its operation. However, since our audit would not necessarily disclose all significant matters in the internal control structure, we do not express an opinion on the Plan's system of internal controls taken as a whole.

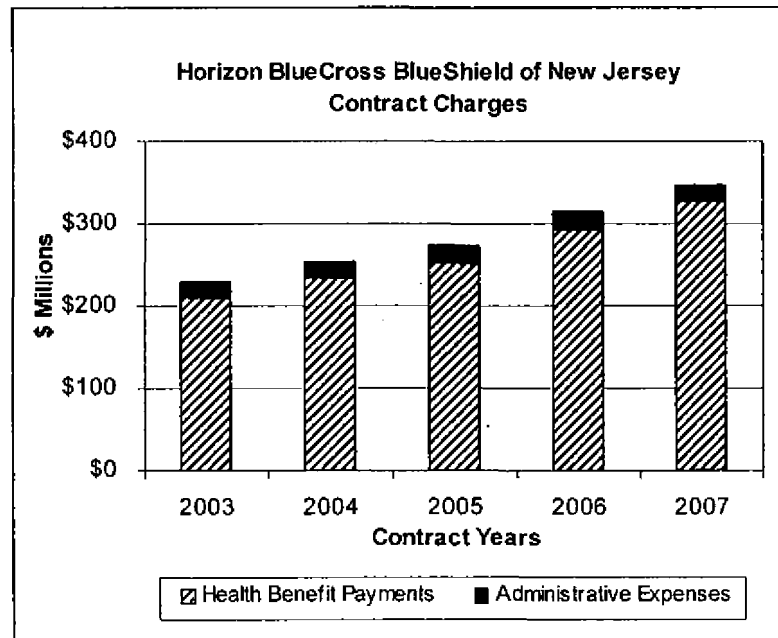


Figure 1 -- Contract Charges

We also conducted tests to determine whether the Plan had complied with the contract, the applicable procurement regulations (i.e., Federal Acquisition Regulations (FAR) and Federal Employees Health Benefits Acquisition Regulations (FEHBAR), as appropriate), and the laws and regulations governing the FEHBP. The results of our tests indicate that, with respect to the items tested, the Plan did not comply with all provisions of the contract and federal procurement regulations. Exceptions noted in the areas reviewed are set forth in detail in the "Audit Findings and Recommendations" section of this audit report. With respect to the items not tested, nothing came to our attention that caused us to believe that the Plan had not complied, in all material respects, with those provisions.

In conducting our audit, we relied to varying degrees on computer-generated data provided by the FEP Director's Office, the FEP Operations Center, the Plan, and the Centers for Medicare and Medicaid Services. Due to time constraints, we did not verify the reliability of the data generated by the various information systems involved. However, while utilizing the computer-generated data during our audit testing, nothing came to our attention to cause us to doubt its reliability. We believe that the data was sufficient to achieve our audit objectives.

The audit was performed at the Plan's office in Newark, New Jersey from March 16 through April 10, 2009 and April 27 through May 8, 2009. Audit fieldwork was also performed at our offices in Washington, D.C. and Jacksonville, Florida.

## **METHODOLOGY**

We obtained an understanding of the internal controls over the Plan's claims processing, financial, and cost accounting systems by inquiry of Plan officials.

To test the Plan's compliance with the FEHBP health benefit provisions, we selected and reviewed samples of 766 claims.<sup>2</sup> We used the FEHBP contract, the Service Benefit Plan brochure, the Plan's provider agreements, and the Association's FEP administrative manual to determine the allowability of benefit payments. The results of these samples were not projected to the universe of claims.

We interviewed Plan personnel and reviewed the Plan's policies, procedures, and accounting records during our audit of miscellaneous payments and credits. We also judgmentally selected and reviewed 209 high dollar health benefit refunds and subrogation recoveries, totaling \$2,889,198 (from a universe of 10,161 refunds and recoveries, totaling \$5,789,816); 42 high dollar hospital and provider audit recoveries, totaling \$846,219 (from a universe of 1,527 recoveries, totaling \$2,493,950); 28 high dollar special plan invoices, totaling \$1,456,194 in net credits (from a universe of 250 special plan invoices, totaling \$4,232,586 in net payments); and 23 fraud cases, totaling \$228,496 in recoveries (from a universe of 36 fraud cases, totaling \$234,118 in recoveries), to determine if refunds and recoveries were promptly returned to the FEHBP and if miscellaneous payments were properly charged to the FEHBP.<sup>3</sup> The results of these samples were not projected to the universe of miscellaneous payments and credits.

We judgmentally reviewed administrative expenses charged to the FEHBP for contract years 2003 through 2007. Specifically, we reviewed administrative expenses relating to cost centers, natural accounts, out-of-system adjustments, prior period adjustments, pension, post-retirement, employee health benefits, executive compensation, subcontracts, non-recurring projects, return on investment, inter-company profits, and Health Insurance Portability and Accountability Act of 1996 compliance. We used the FEHBP contract, the FAR, and the FEHBPBAR to determine the allowability, allocability, and reasonableness of charges.

We also reviewed the Plan's cash management to determine whether the Plan handled FEHBP funds in accordance with Contract CS 1039 and applicable laws and regulations.

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<sup>2</sup> See the audit findings for "Omnibus Budget Reconciliation Act of 1990 Review" (A1.a) and "Claim Payment Errors" (A1.b) on pages 6 through 10 for specific details of our sample selection methodologies.

<sup>3</sup> See the audit findings for "Subrogation Recoveries" (A2.a), "Health Benefit Refunds" (A2.b), "Fraud Recoveries" (A2.c), and "Special Plan Invoices" (A2.d) on pages 11 through 19 for specific details of our sample selection methodologies.

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

#### **A. HEALTH BENEFIT CHARGES**

##### **1. Claim Payments**

###### **a. Omnibus Budget Reconciliation Act of 1990 Review** **\$352,093**

The Plan incorrectly paid 36 claims that were priced or should have been priced under the Omnibus Budget Reconciliation Act of 1990 (OBRA 90) pricing guidelines, resulting in net overcharges of \$352,093 to the FEHBP. Specifically, the Plan overpaid 29 claims by \$393,826 and underpaid 7 claims by \$41,733.

Contract CS 1039, Part III, section 3.2 (b)(1) states, "The Carrier may charge a cost to the contract for a contract term if the cost is actual, allowable, allocable, and reasonable." Part II, section 2.6 states, "(a) The Carrier shall coordinate the payment of benefits under this contract with the payment of benefits under Medicare . . . (b) The Carrier shall not pay benefits under this contract until it has determined whether it is the primary carrier . . . ." Part II, section 2.3(g) states, "If the Carrier or OPM determines that a Member's claim has been paid in error for any reason, the Carrier shall make a diligent effort to recover an overpayment . . . ."

OBRA 90 limits the benefit payments for certain inpatient hospital services provided to annuitants age 65 or older who are not covered under Medicare Part A. The FEHBP fee-for-service plans are required to limit the claim payment to the amount equivalent to the Medicare Part A payment.

Using a program developed by the Centers for Medicare and Medicaid Services (CMS) to price OBRA 90 claims, we recalculated the claim payment amounts for the claims in our samples that were subject to and/or processed as OBRA 90.

The following summarizes the claim payment errors.

###### **OBRA 90 Claim Pricing Errors**

For the period January 1, 2005 through October 31, 2008, we identified 1,823 claims, totaling \$17,105,505 in payments, that were subject to OBRA 90 pricing guidelines. From this universe, we selected and reviewed a judgmental sample of 208 claims, totaling \$6,241,077 in payments, to determine if these claims were correctly priced by the FEP Operations Center and paid by the Plan. Our sample included all OBRA 90 claims with amounts paid of \$15,000 or more.

Based on our review, we determined that 14 claims were paid incorrectly, resulting in net overcharges of \$205,243 to the FEHBP. Specifically, the Plan overpaid 11 claims by \$218,041 and underpaid 3 claims by \$12,798.

These claim payment errors resulted from the following:

- In 12 instances, the claims were not priced in accordance with OBRA 90 pricing, resulting in net overcharges of \$180,772 to the FEHBP. Specifically, the Plan overpaid nine claims by \$193,570 and underpaid three claims by \$12,798.
- The FEP Operations Center priced two claims using incorrect Medicare Diagnostic Related Group (DRG) codes, resulting in overcharges of \$24,471 to the FEHBP.

#### Claims Not Priced Under OBRA 90 (Possible OBRA 90 Claims)

For the period January 1, 2005 through October 31, 2008, we identified 370 claims, totaling \$5,420,031 in payments, that were potentially subject to OBRA 90 pricing guidelines but appeared to be paid under the Plan's standard pricing procedures. From this universe, we selected and reviewed a judgmental sample of 137 claims, totaling \$4,338,974 in payments, to determine if the Plan paid these claims properly. Our sample included all possible OBRA 90 claims with amounts paid of \$10,000 or more.

Based on our review, we determined that 22 claims were paid incorrectly, resulting in net overcharges of \$146,850 to the FEHBP. Specifically, the Plan overpaid 18 claims by \$175,785 and underpaid 4 claims by \$28,935.

These claim payment errors resulted from the following:

- The FEP Operations Center priced six claims using incorrect Medicare DRG codes, resulting in overcharges of \$98,747 to the FEHBP.
- In 12 instances, the claims were not priced in accordance with OBRA 90 pricing, resulting in net overcharges of \$37,271 to the FEHBP. Specifically, the Plan overpaid eight claims by \$66,206 and underpaid four claims by \$28,935.
- The Plan did not properly coordinate four claims with Medicare, resulting in overcharges of \$10,832 to the FEHBP.

#### Association's Response:

The Association agrees with \$50,430 and disagrees with \$301,663 of the questioned charges. The Association states that the Plan has initiated refund requests to recover the uncontested overpayments. To the extent that errors did occur, the Association states that these payments were good faith erroneous benefit payments and fall within the context of CS 1039, Part II, section 2.3(g). Any payments the Plan is unable to recover are allowable charges to the FEHBP. As good faith erroneous payments, lost investment income does not apply to the claim payment errors identified in this finding.

For the contested amount, the Association states that when the claims were re-priced using the most current version of the FEP Operations Center's OBRA 90 Pricer, the re-priced amounts differed from the CMS Pricer amounts. The Association also states that the FEP Operations Center's OBRA 90 Pricer is the official OPM approved source for FEP OBRA 90 pricing.

In addition, the Association states, "To reduce these types of pricing errors in the future, the Plan has implemented and updated its Policy & Procedure for OBRA '90 claim processing. . . . Also, the FEP Director's Office includes potential OBRA '90 priced claims in its periodic System-Wide Claims Review to facilitate early identification and recovery of OBRA '90 claim payment errors."

### **OIG Comments:**

Based on our review of the Association's response and additional documentation provided by the Plan, we revised the questioned costs from the draft report to \$352,093.

For \$123,218 of the contested amount, the overpayments are being questioned because incorrect DRG codes were used to price these claims. The Plan did not provide documentation to support that these claims were priced using the correct DRG's. Based on the diagnosis and procedure codes on each of these claims, the CMS DRG grouper is calculating a different DRG code than what was originally used by the FEP Operations Center to price the claim. Our re-pricing of these claims recognizes the correct DRG codes that should have been used to price them.

For the remaining contested amount of \$178,445, the FEP Operations Center's OBRA 90 pricing amounts differed from the CMS Pricer amounts. Based on our experience with auditing BlueCross and BlueShield plans, we have found that these pricing differences occur because the mainframe pricing software used by the FEP Operations Center is not always up-to-date. Therefore, we will continue to use the latest version of the CMS Pricer program, which includes up-to-date pricing, to determine if claims paid under OBRA 90 were correctly priced by the FEP Operations Center and paid by the Plan.

### **Recommendation 1**

We recommend that the contracting officer disallow \$393,826 for claim overcharges, and verify that the Plan returns all amounts recovered to the FEHBP.

### **Recommendation 2**

We recommend that the contracting officer allow the Plan to charge the FEHBP \$41,733 if additional payments are made to the providers to correct the underpayment errors.

### **Recommendation 3**

Although the Plan has developed a corrective action plan to reduce OBRA 90 findings, we recommend that the contracting officer instruct the Association to ensure that the Plan is following the corrective action plan.

#### **b. Claim Payment Errors \$16,074**

The Plan incorrectly paid 39 claims, resulting in net overcharges of \$16,074 to the FEHBP. Specifically, the Plan overpaid 38 claims by \$39,534 and underpaid 1 claim by \$23,460.

As previously cited from CS 1039, costs charged to the FEHBP must be actual, allowable, allocable, and reasonable. If errors are identified, the Plan is required to make a prompt and diligent effort to recover the overpayments.

The following summarizes the claim payment errors:

#### **Assistant Surgeon Claims**

For claims reimbursed from January 1, 2005 through October 31, 2008, we identified 1,171 assistant surgeon claim groups, totaling \$190,308 in potential overpayments that may not have been paid in accordance with the Plan's assistant surgeon pricing procedures. From this universe, we selected and reviewed a judgmental sample of 163 assistant surgeon claim groups, totaling \$83,379 in potential overpayments, to determine if the Plan paid these claims properly. Our sample included all assistant surgeon claim groups with potential overpayments of \$250 or more.

Based on our review, we determined that 33 claims were paid incorrectly, resulting in overcharges of \$29,479 to the FEHBP. The claim payment errors resulted from the following:

- The Plan incorrectly paid nine assistant surgeon claims, resulting in overcharges of \$14,259 to the FEHBP. These overcharges were due to errors in the calculation of the assistant surgeon fee, which should have been priced at 20 percent of the procedure allowance.
- The Plan incorrectly paid 24 assistant surgeon claims that were subject to Omnibus Budget Reconciliation Act of 1993 (OBRA 93) pricing guidelines. These errors were due to Palmetto (an OBRA 93 pricing vendor) not recognizing the assistant surgeon pricing modifier and erroneously calculating the assistant surgeon fee. As a result, the Plan overpaid these claims by \$15,220.



## System Review

For claims reimbursed from January 1 through October 31, 2008, we identified 2,649,818 claim lines, totaling \$252,570,234 in payments, using a standard criteria based on our experience. From this universe, we selected and reviewed a judgmental sample of 126 claims (representing 1,406 claim lines), totaling \$3,488,898 in payments, to determine if the Plan adjudicated these claims properly.<sup>4</sup>

Our review identified two claim payment errors, resulting in overcharges of \$100 to the FEHBP. In each instance, the Plan did not apply the correct subscriber liability amount when paying the claim.

## Amounts Paid Greater than Covered Charges

For the period January 1, 2005 through October 31, 2008, we identified 6,507 claims where the amounts paid were greater than the covered charges by a total of \$2,247,808. From this universe, we selected and reviewed a judgmental sample of 132 claims with a total variance of \$1,514,671, and determined if the Plan paid these claims properly. Our sample included all claims where the amounts paid exceeded covered charges by \$1,000 or more.

Based on our review, we determined that four claims were paid incorrectly, resulting in net undercharges of \$13,505 to the FEHBP. Specifically, the Plan overpaid three claims by \$9,955 and underpaid one claim by \$23,460. These four claim payment errors resulted from processor errors.

## Association's Response:

The Association agrees with this finding. The Association states that the Plan has initiated recovery of the overpayments. The Association also states that these payments were good faith erroneous benefit payments and fall within the context of CS 1039, Part II, section 2.3(g). Any payments the Plan is unable to recover are allowable charges to the FEHBP. As good faith erroneous payments, lost investment income (LII) does not apply to the claim payment errors identified in this finding.

In addition, the Association states, "The Plan has several methods in place to identify overpayments. These methods include, but are not limited to, the System Wide Claims Reports (which includes a listing of Assistant Surgeon Claims, Amounts Paid Greater than Charges Claims, OBRA '90, OBRA '93, High Dollar and Termination Claims), . . . provided by the FEP Director's Office along with routine claims quality assurance audits performed by the Plan's Internal Auditors. These are all tools that are used to promote claims accuracy. While these measures are not absolute, they

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<sup>4</sup> We selected our sample from an OIG-generated "Place of Service Report" (SAS application) that stratified the claims by place of service (POS), such as provider's office, and payment category, such as \$50 to \$99.99. We judgmentally determined the number of sample items to select from each POS stratum based on the stratum's total claim dollars paid.

provide reasonable assurances that such items will be identified. Efforts will be made to periodically examine existing procedures and add additional controls where necessary.”

**Recommendation 4**

We recommend that the contracting officer disallow \$39,534 for claim overcharges and verify that the Plan returns all amounts recovered to the FEHBP.

**Recommendation 5**

We recommend that the contracting officer allow the Plan to charge the FEHBP \$23,460 if an additional payment is made to the provider to correct the underpayment error.

**2. Miscellaneous Payments and Credits**

**a. Subrogation Recoveries**

**\$1,237,935**

The Plan had not returned subrogation recoveries of \$1,219,668 to the FEHBP as of December 31, 2007. Subsequent to this date, the Plan returned \$1,201,907 of these questioned recoveries to the FEHBP. As a result, the FEHBP is still due \$30,947, consisting of \$17,761 for the remaining questioned recoveries and \$13,186 for LII on recoveries deposited untimely or not deposited into the FEP investment account.

48 CFR 31.201-5 states, “The applicable portion of any income, rebate, allowance, or other credit relating to any allowable cost and received by or accruing to the contractor shall be credited to the Government either as a cost reduction or by cash refund.”

Contract CS 1039, Part II, Section 2.3 (i) states, “All health benefit refunds and recoveries, including erroneous payment recoveries, must be deposited into the working capital or investment account within 30 days and returned to or accounted for in the FEHBP letter of credit account within 60 days after receipt by the Carrier.” Also, based on an agreement between OPM and the Association, dated March 26, 1999, BlueCross and BlueShield plans have 30 days to return health benefit refunds and recoveries to the FEHBP before LII will commence to be assessed.

FAR 52.232-17(a) states, “all amounts that become payable by the Contractor . . . shall bear simple interest from the date due . . . The interest rate shall be the interest rate established by the Secretary of the Treasury as provided in Section 611 of the Contract Disputes Act of 1978 (Public Law 95-563), which is applicable to the period in which the amount becomes due, as provided in paragraph (e) of this clause, and then at the rate applicable for each six-month period as fixed by the Secretary until the amount is paid.”

For the period 2003 through 2007, there were 800 subrogation recoveries totaling \$2,833,541. From this universe, we selected and reviewed a sample of 100 subrogation recoveries, totaling \$1,843,283, for the purpose of determining if the Plan promptly returned these recoveries to the FEHBP. Our sample included high dollar subrogation recoveries and at least 50 percent of each year's recovery dollars.

The following summarizes the exceptions noted:

- The Plan did not return 14 subrogation recoveries, totaling \$11,239, to the FEHBP letter of credit (LOC) account.
- The Plan did not deposit eight subrogation recoveries, totaling \$6,522, into the FEP investment account. Since these recoveries were not deposited into the FEP investment account, the FEHBP is also due \$1,045 for LII (calculated through June 30, 2009) on these funds.
- The Plan deposited numerous subrogation recoveries, totaling \$674,704, into the FEP investment account in an untimely manner. Specifically, the Plan deposited these funds into the FEP investment account between 31 and 1,086 days after being received. As a result, the FEHBP is due \$2,544 for LII on these funds.

Our sample also included numerous subrogation recoveries that were previously reviewed during a "Control and Performance Review" (CPR) of this Plan conducted by the Association in 2007. During the CPR, the Association identified 556 subrogation recoveries, totaling \$1,201,907, that were deposited into the FEP investment account but not returned to the LOC account. These subrogation recoveries were received by the Plan during 2003 through 2007. Since these recoveries were deposited into the FEP investment account, the Association did not assess LII on these funds. As part of our review, we verified that the Plan returned these subrogation recoveries to the FEHBP by reducing the LOC drawdown by \$1,201,907 on June 13, 2008. Although these recoveries were returned to the FEHBP before the start of our audit, we are continuing to question this amount as a monetary finding since the Plan returned these recoveries to the LOC account more than 60 days after receipt (i.e., from 169 to 1,032 days after receipt) and after receiving our audit notification letter and standard audit request (dated August 27, 2007). In addition, we reviewed the processing dates of these recoveries and noted the following additional exceptions:

- Numerous recoveries were deposited untimely or not deposited into the FEP investment account. Specifically, 67 recoveries, totaling \$151,377, were not deposited into the FEP investment account. Since these recoveries were not deposited into the FEP investment account, the FEHBP is due \$13,524 for LII (calculated through May 11, 2009) on these funds. (Note: As part of our review, we verified that the Plan deposited \$151,377 into the FEP investment account on May 11, 2009. This amount is already included as part of the questioned amount of \$1,201,907.)

- 90 recoveries, totaling \$460,727, were deposited untimely into the FEP investment account. As a result, the FEHBP is due \$1,154 for LII on these funds.

In total, we are questioning \$1,237,935, consisting of \$1,219,668 (\$11,239 + \$6,522 + \$1,201,907) for subrogation recoveries and \$18,267 (\$1,045 + \$2,544 + \$13,524 + \$1,154) for LII on recoveries deposited untimely or not deposited into the FEP investment account.

**Association's Response:**

The Association agrees with \$36,028 of the questioned amount, consisting of \$17,761 for recoveries and \$18,267 for LII. The Association states, "Special Plan Invoices to credit the Program for the \$31,245 (\$11,239 principle and \$20,006 LII) were submitted to FEP on August 18, 2009. These funds were wired to BCBSA FEP on August 19, 2009. An additional \$4,783 was deposited into the FEP Investment Account on August 19, 2009. This amount will be included in the final wire of funds to close out this audit."

The Association disagrees with \$1,201,907 of the questioned amount. The Association states, "This amount was identified as a result of the 2007 BCBSA Control Performance Review (CPR) Plan Audit. The Plan received the final CPR Audit report on May 23, 2008. The amount of the finding was agreed upon by the CPR Audit Team and the Plan and funds were returned to the Program on June 13, 2008, which was prior to the 2009 OPM Audit."

In addition, the Association states that the Plan has enhanced procedures and developed additional monitoring tools to ensure that funds are deposited into the investment account within 30 days of receipt.

**OIG Comments:**

Since the Plan returned the contested recoveries of \$1,201,907 to the FEHBP more than 60 days after receipt and after receiving our audit notification letter and standard audit request, we will continue to question this amount as a monetary finding.

**Recommendation 6**

Since we verified that the contested subrogation recoveries of \$1,201,907 were returned to the FEHBP on June 13, 2008 and May 11, 2009, no further action is required for this questioned amount.

**Recommendation 7**

We recommend that the contracting officer verify that the Plan credits the FEHBP \$17,761 for subrogation recoveries.

### **Recommendation 8**

We recommend that the contracting officer verify that the Plan credits the FEHBP \$18,267 (plus interest accruing after June 30, 2009) for LII on subrogation recoveries that were deposited untimely or not deposited into the FEP investment account.

### **Recommendation 9**

We recommend that the contracting officer have the Association verify that the Plan implemented procedures and developed additional monitoring tools to ensure that subrogation recoveries are returned to the FEHBP in a timely manner.

#### **b. Health Benefit Refunds**

**\$544,050**

The Plan had not returned health benefit refunds of \$530,864 to the FEHBP as of December 31, 2007. Subsequent to this date, the Plan returned \$424,179 of these questioned refunds to the FEHBP. As a result, the FEHBP is still due \$119,871, consisting of \$106,685 for the remaining questioned refunds and \$13,186 for LII on refunds deposited untimely or not deposited into the FEP investment account.

As previously stated under audit finding A2.a, the Plan is required to promptly return health benefit refunds to the FEHBP with applicable LII.

For the period 2003 through 2007, there were 9,361 health benefit refunds totaling \$2,956,275. From this universe, we selected and reviewed a judgmental sample of 109 refunds, totaling \$1,045,915, for the purpose of determining if the Plan promptly returned these funds to the FEHBP. Our sample included all provider refunds of \$3,000 or more and all member refunds of \$1,500 or more.

The following summarizes the exceptions noted:

- In seven instances, the Plan deposited refunds of \$79,268 into the FEP investment account, but did not return these funds to the LOC account. The Plan also deposited \$71,490 of these refunds untimely into the FEP investment account. As a result, the FEHBP is due \$79,375, consisting of \$79,268 for refunds not returned to the LOC account and \$107 for LII on refunds deposited untimely into the FEP investment account.
- In three instances, the Plan did not deposit refunds of \$22,804 into the FEP investment account. Since these refunds were not deposited into the FEP investment account, the FEHBP is due \$26,442, consisting of \$22,804 for refunds and \$3,638 for LII (calculated through June 30, 2009) on these funds.

- In one instance, the Plan did not deposit a refund of \$4,613 into the FEP investment account, nor did the Plan return these funds to the LOC account. Since these funds were not deposited into the FEP investment account and returned to the LOC account, the FEHBP is due \$4,954, consisting of \$4,613 for this refund and \$341 for LII (calculated through June 30, 2009).
- In 22 instances, the Plan returned refunds of \$94,109 to the LOC account, but deposited these funds untimely into the FEP investment account. Specifically, we found that the Plan deposited these funds into the FEP investment account from 33 to 100 days after being received. As a result, the FEHBP is due \$230 for LII on these funds.

Our sample also included numerous health benefit refunds that were previously reviewed during a CPR of this Plan conducted by the Association in 2007. During the CPR, the Association identified 1,378 refunds, totaling \$424,179, that were deposited into the FEP investment but not returned to the LOC account. These refunds were received by the Plan from 2003 through 2007. Since these refunds were deposited into the FEP investment account, the Association did not assess LII on these funds. As part of our review, we verified that these refunds were returned to the FEHBP on August 8, 2008. Although these refunds were returned to the FEHBP before the start of our audit, we are continuing to question this amount as a monetary finding since the Plan returned these refunds to the LOC account more than 60 days after receipt (i.e., from 225 to 2,004 days after receipt) and after receiving our audit notification letter and standard audit request (dated August 27, 2007). In addition, we reviewed the processing dates of these refunds and noted the following additional exceptions:

- Numerous refunds were deposited untimely or not deposited into the FEP investment account. Specifically, 73 refunds, totaling \$80,447, were not deposited into the FEP investment account. Since these refunds were not deposited into the FEP investment account, the FEHBP is due \$5,958 for LII (calculated through August 8, 2008) on these funds.
- 16 refunds, totaling \$134,358, were deposited untimely into the FEP investment account. As a result, the FEHBP is due \$2,912 for LII on these funds.

In total, we are questioning \$544,050, consisting of \$530,864 (\$79,268 + \$22,804 + \$4,613 + \$424,179) for refunds and \$13,186 (\$107 + \$3,638 + \$341 + \$230 + \$5,958 + \$2,912) for LII on refunds deposited untimely or not deposited into the FEP investment account.

**Association's Response:**

The Association agrees with \$119,871 of the questioned amount, consisting of \$106,685 for refunds and \$13,186 for LII. The Association states, "Special Plan Invoices to credit the Program for \$97,550 (\$83,881 principle and \$13,669 LII) were submitted and wired to BCBSA FEP on August 19, 2009. An additional \$22,321 was deposited into the FEP Investment Account on August 19, 2009. This amount will be included in the final wire of funds to close out this audit."

The Association disagrees with \$424,179 of the questioned amount. The Association states that "this amount was identified as a result of the 2007 BCBSA CPR Plan Audit prior to the start of the 2009 OPM Audit. Funds were returned to the Program on July 15, 2008, prior to the start of the 2009 OPM Audit."

In addition, the Association states that the Plan has enhanced procedures and developed additional monitoring tools to ensure that refunds are deposited into the investment account within 30 days of receipt.

**OIG Comments:**

Since the Plan returned the contested refunds of \$424,179 to the FEHBP more than 60 days after receipt and after receiving our audit notification letter and standard audit request, we will continue to question this amount as a monetary finding.

**Recommendation 10**

Since we verified that the contested refunds of \$424,179 were returned to the FEHBP on August 8, 2008, no further action is required for this questioned amount.

**Recommendation 11**

We recommend that the contracting officer verify that the Plan credits the FEHBP \$106,685 for refunds.

**Recommendation 12**

We recommend that the contracting officer verify that the Plan credits the FEHBP \$13,186 (plus interest accruing after June 30, 2009) for LII on refunds that were deposited untimely or not deposited into the FEP investment account.

**Recommendation 13**

We recommend that the contracting officer have the Association verify that the Plan implemented procedures and developed additional monitoring tools to ensure that health benefit refunds are returned to the FEHBP in a timely manner.

c. **Fraud Recoveries**

**\$79,046**

The Plan did not deposit into the FEP investment account and/or return to the LOC account 21 fraud recoveries totaling \$70,320. Also, the Plan deposited 30 fraud recoveries untimely into the FEP investment account. As a result, the FEHBP is due \$79,046, consisting of \$70,320 for fraud recoveries not returned to the FEHBP and \$8,726 for LII on recoveries deposited untimely or not deposited into the FEP investment account.

As previously stated under audit finding A2.a, the Plan is required to promptly return fraud recoveries to the FEHBP with applicable LII.

For the period 2003 through 2007, there were 36 FEP fraud cases with recoveries totaling \$234,118. From this universe, we selected and reviewed a judgmental sample of 23 fraud cases (representing 63 recoveries), totaling \$228,496 in recoveries, for the purpose of determining if the Plan promptly returned these recoveries to the FEHBP. Our sample included all fraud cases with cumulative recoveries of \$1,000 or more. Most of the fraud cases included multiple recoveries that were received on various dates.

The following summarizes the exceptions noted for the 63 recoveries in our sample:

- In 11 instances, the Plan did not deposit fraud recoveries of \$30,620 into the FEP investment account. Since these funds were not deposited into the FEP investment account, the FEHBP is also due \$6,056 for LII on these funds.
- In 10 instances, the Plan did not return fraud recoveries of \$39,700 to the LOC account. Since \$1,595 of these funds were not deposited into the FEP investment account, the FEHBP is also due \$312 for LII.
- In 30 instances, the Plan deposited fraud recoveries of \$82,856 into the FEP investment account in an untimely manner. Specifically, we found that the Plan deposited these funds into the FEP investment account from 42 to 1,785 days after being received. As a result, the FEHBP is due \$2,358 for LII on these funds.

In total, the Plan owes the FEHBP \$79,046, consisting of \$70,320 (\$30,620 + \$39,700) for fraud recoveries not returned to the FEHBP and \$8,726 (\$6,056 + \$312 + \$2,358) for LII on recoveries deposited untimely or not deposited into the FEP investment account.

**Association's Response:**

The Association agrees with this finding. The Association states, "Special Plan Invoices to credit the Program for the \$48,498 (\$39,700 principle and \$8,798 LII) were submitted to FEP on August 19, 2009. An additional \$30,548 was deposited into the FEP Investment Account on August 19, 2009. This amount will be included in the final



wire of funds to close out this audit. In addition, procedures have been enhanced and additional monitoring tools developed to promote the deposit of refunds into the FEP investment account funds within 30 days of receipt.”

**Recommendation 14**

We recommend that the contracting officer verify that the Plan credits the FEHBP \$70,320 for fraud recoveries.

**Recommendation 15**

We recommend that the contracting officer verify that the Plan credits the FEHBP \$8,726 for LII on fraud recoveries that were deposited untimely or not deposited into the FEP investment account.

**d. Special Plan Invoices**

**\$48,269**

The Plan did not deposit \$39,529 into the FEP investment account for six miscellaneous credits that were reported on special plan invoices (SPI) in 2004 and 2005. Also, the Plan deposited five miscellaneous credits untimely into the FEP investment account that were reported on SPI's in 2006. As a result, the FEHBP is due \$48,269, consisting of \$39,529 for miscellaneous credits and \$8,740 for LII on miscellaneous credits deposited untimely or not deposited into the FEP investment account.

As previously stated under audit finding A2.a, the Plan is required to promptly return health benefit refunds and recoveries to the FEHBP with applicable LII.

For the period 2003 through 2007, there were 250 SPI's with miscellaneous payments and credits totaling \$4,232,586 in net payments. From this universe, we selected and reviewed a judgmental sample of 28 high dollar SPI's, totaling \$1,456,194 in net credits, for the purpose of determining if the Plan properly credited or charged the FEHBP for these invoices.

The following summarizes the exceptions noted:

- The Plan did not deposit \$39,529 into the FEP investment account for six miscellaneous credits reported on SPI's in 2004 and 2005. These SPI's were for claim overpayment refunds and fraud recoveries. Since the funds were not deposited into the FEP investment account, the FEHBP is also due \$7,905 for LII on these funds.

- The Plan deposited five miscellaneous credits, totaling \$74,355, into the FEP investment account in an untimely manner. These credits were for claim overpayment refunds and fraud recoveries that were reported on SPI's in 2006. Specifically, we found that the Plan deposited these funds into the FEP investment account from 71 to 172 days after being received. As a result, the FEHBP is due \$835 for LII on these funds.

In total, the Plan owes the FEHBP \$48,269, consisting of \$39,529 for miscellaneous credits and \$8,740 (\$7,905 + \$835) for LII on miscellaneous credits deposited untimely or not deposited into the FEP investment account.

**Association's Response:**

The Association agrees with this finding. The Association states that the Plan wire transferred \$31,787 and \$7,742 (\$31,787 + \$7,742 = \$39,529) into the FEP investment account on April 2, 2009 and May 12, 2009, respectively. The Plan also transferred an additional \$8,740 into the FEP investment account on August 19, 2009 for LII. In addition, the Association states that the Plan's internal procedures have been revised to ensure that this type of exception does not occur in the future.

**Recommendation 16**

We recommend that the contracting officer verify that the Plan credited the FEHBP \$39,529 for miscellaneous credits.

**Recommendation 17**

We recommend that the contracting officer verify that the Plan credited the FEHBP \$8,740 for LII on miscellaneous credits that were deposited untimely or not deposited into the FEP investment account.

## **B. ADMINISTRATIVE EXPENSES**

### **1. Directors Liability and Fidelity & Bond Insurance** **\$731,676**

The Plan overcharged the FEHBP \$731,676 for Directors Liability and Fidelity & Bond Insurance expenses from 2003 through 2007.

Contract CS 1039, Part III, section 3.2 (b)(1) states, "The Carrier may charge a cost to the contract for a contract term if the cost is actual, allowable, allocable, and reasonable."

48 CFR 31.201-4 states, "A cost is allocable if it is assignable or chargeable to one or more cost objectives on the basis of relative benefits received or other equitable relationship. Subject to the foregoing, a cost is allocable to a Government contract if it --

- (a) Is incurred specifically for the contract;
- (b) Benefits both the contract and other work and can be distributed . . . in reasonable proportion to the benefits received; or
- (c) Is necessary to the overall operation of the business . . . ."

From 2003 through 2007, the Plan allocated Directors Liability and Fidelity & Bond Insurance expenses to the FEHBP using a revenue ratio methodology. The Directors Liability Insurance includes professional liability coverage for the Plan's senior management and board of directors. This insurance also includes employment practice liability, which covers employee lawsuits for wrongful termination and/or discrimination, and employee errors and/or omissions occurring during normal work activities. The Fidelity & Bond Insurance covers an employer against losses due to fraudulent or dishonest employees, electronic crime, and travel accidents.

On average, the Plan allocated 10.46 percent of these expenses to FEP from 2003 through 2007 using a revenue ratio methodology. In the draft audit report, we questioned the reasonableness of the FEP allocation percentage. Since these insurance policies benefit the company as a whole, our position is that the Plan should allocate these expenses to FEP based on a company expense ratio. Company cost centers, which benefit all lines of business, were allocated to FEP by the Plan using the company expense ratio methodology.

As a result, the Plan re-evaluated how the revenue was allocated and determined that insured revenue was inadvertently used instead of gross revenue in the allocation methodology. The Plan then recalculated the 2003 through 2007 allocations using the gross revenue ratio methodology and determined that the FEHBP was overcharged \$731,676 for these years. We accepted the Plan's revised allocations since the Plan's allocation percentages using the gross revenue ratio methodology are now comparable to the percentages using the company expense ratio methodology.

#### **Association's Response:**

The Association agrees with the questioned overcharges.

**Recommendation 18**

We recommend that the contracting officer disallow \$731,676 for insurance overcharges from 2003 through 2007.

**2. Post-Retirement Benefit Costs \$251,682**

The Plan overcharged the FEHBP \$251,682 (net) for post-retirement benefit costs (PRB) from 2003 through 2007.

As previously cited from CS 1039, costs charged to the FEHBP must be actual, allowable, allocable, and reasonable.

48 CFR 31.205-6(o)(2) states: "To be allowable, PRB costs must be reasonable and incurred pursuant to law, employer-employee agreement, or an established policy of the contractor. In addition, to be allowable, PRB costs must also be calculated in accordance with paragraphs (o)(2)(i), (ii), or (iii) of this section."

For 2003 through 2007, we reviewed the Plan's calculations of PRB costs chargeable to the FEHBP. We found that for the FEP dedicated cost centers the Plan properly limited FEP's PRB costs to the actual payments for the current year benefits. However, the Plan transposed a number in the 2006 year-end PRB adjustment calculation. As a result, the FEHBP was undercharged \$4,705 for PRB costs from the FEP dedicated cost centers in 2006.

For the indirect cost centers, we found that the Plan did not limit FEP's PRB costs to the actual payments for the current year benefits. Therefore, we requested that the Plan provide the amounts charged to FEP for PRB costs from the indirect cost centers. We then limited those charges to the actual payments for the current year benefits. As a result, we determined that the FEHBP was overcharged \$256,387 (\$108,691 in 2003, \$82,949 in 2004, \$33,656 in 2005, \$29,937 in 2006, and \$1,154 in 2007) for PRB costs from the indirect cost centers in 2003 through 2007.

In total, the FEHBP was overcharged \$251,682 (net) for PRB costs from 2003 through 2007.

**Association's Response:**

The Association agrees with this finding. The Association states that the Plan submitted prior period adjustments for the overcharges on June 15, 2009, and transferred applicable LII assessed on these funds to the Association's FEP account on August 19, 2009.

### **OIG Comments:**

Since the Association did not provide support for the Plan's LII assessed on these questioned charges, we did not include LII as part of this finding. Instead, we calculated LII on these questioned charges in Schedule C of this report.

### **Recommendation 19**

We recommend that the contracting officer disallow \$251,682 (net) for PRB cost overcharges from 2003 through 2007, and verify that these overcharges were returned to the FEHBP.

### **3. Pension Costs**

**\$251,241**

The Plan overcharged the FEHBP \$251,241 for pension costs from 2003 through 2007.

As previously cited from CS 1039, costs charged to the FEHBP must be actual, allowable, allocable, and reasonable.

48 CFR 31.205-6(j)(2) states, "The cost of all defined-benefit pension plans shall be measured, allocated, and accounted for in compliance with the provisions of 48 CFR 9904.412, Cost accounting standard for composition and measurement of pension cost, and 48 CFR 9904.413, Adjustment and allocation of pension cost. The costs of all defined-contribution pension plans shall be measured, allocated, and accounted for in accordance with the provisions of 48 CFR 9904.412 and 48 CFR 9904.413. Pension costs are allowable subject to the referenced standards and the cost limitations and exclusions set forth in paragraph (j)(2)(i) and in paragraphs (j)(3) through (8) of this subsection."

The Federal Acquisition Regulations (FAR) limit the amount of pension costs that may be charged to a government contract to the amount of any cash contribution to the pension fund trustee, or the amount of expense calculated in accordance with Cost Accounting Standard (CAS) 412 and 413, whichever is lower.

For 2003 through 2007, we reviewed the Plan's calculations of pension costs chargeable to the FEHBP. We found that for FEP dedicated employees the Plan properly limited FEHBP's pension costs to the lower of CAS or funded amounts, except in 2004 where the Plan did not limit FEHBP's pension costs to the lower amount. This resulted in an overcharge of \$43,350 to the FEHBP. However, since we verified that the Plan returned this overcharge to the FEHBP on February 27, 2007 (during the audit scope), we did not question this amount in the finding. In addition, we noted that in 2004 and 2006, the Plan elected to apply a portion of its prepaid credit to make the funded amount equal to the CAS amount.

In determining FEHBP's portion of pension costs for indirect employees, we found that the Plan did not limit FEHBP's pension costs to the lower of CAS or funded amounts. Therefore, we requested that the Plan provide the FEP pension charges from the indirect cost centers. We then limited those charges to the lower of CAS or funded. As a result, we determined that the FEHBP was overcharged \$251,241 (\$52,111 in 2003, \$100,004 in 2004, \$13,857 in 2005, \$30,723 in 2006, and \$54,546 in 2007) for pension costs from 2003 through 2007.

**Association's Response:**

The Association agrees with this finding. The Association states that the Plan submitted prior period adjustments for the overcharges on June 1, 2009, and transferred applicable LII assessed on these funds to the Association's FEP account on August 19, 2009.

**OIG Comments:**

Since the Association did not provide support for the Plan's LII assessed on these questioned charges, we did not include LII as part of this finding. Instead, we calculated LII on these questioned charges in Schedule C of this report.

**Recommendation 20**

We recommend that the contracting officer disallow \$251,241 for pension cost overcharges from 2003 through 2007, and verify that these overcharges were returned to the FEHBP.

**4. Administrative Expense Overcharges \$70,491**

The Plan overcharged the FEHBP \$70,491 for information technology-related expenses in 2007.

As previously cited from CS 1039, costs charged to the FEHBP must be actual, allowable, allocable, and reasonable.

During our review of FEP's system chargeback expenses and electronic media claim expenses, we identified overcharges of \$27,435 to the FEHBP in 2007. Also, although the Plan's support for the system chargeback expenses only totaled \$936,315, the Plan charged the FEHBP \$979,371 for these expenses, resulting in an additional overcharge of \$43,056. In total, the FEHBP was overcharged \$70,491 for these information technology-related expenses in 2007.

**Association's Response:**

The Association agrees with this finding. The Association states that the Plan wire transferred the questioned amount into the FEP investment account.

**OIG Comments:**

We reviewed additional documentation provided by the Plan and revised our questioned costs from the draft report to \$70,491.

**Recommendation 21**

We recommend that the contracting officer disallow \$70,491 for administrative expense overcharges in 2007 and verify that these overcharges are returned to the FEHBP.

**5. Unallowable and/or Unallocable Expenses \$52,442**

The Plan charged unallowable and/or unallocable expenses of \$52,442 to the FEHBP from 2003 through 2007.

As previously cited from CS 1039, costs charged to the FEHBP must be actual, allowable, allocable, and reasonable.

48 CFR 31.201-4 states, "A cost is allocable if it is assignable or chargeable to one or more cost objectives on the basis of relative benefits received or other equitable relationship. Subject to the foregoing, a cost is allocable to a Government contract if it –

- (a) Is incurred specifically for the contract;
- (b) Benefits both the contract and other work, and can be distributed to them in reasonable proportion to the benefits received; or
- (c) Is necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown."

For the period 2003 through 2007, the Plan allocated administrative expenses of \$105,065,829 to the FEHBP from 173 natural accounts and 140 cost centers. From this universe, we selected a judgmental sample of 30 natural accounts to review, which totaled \$23,271,725 in expenses allocated to the FEHBP. We also selected a judgmental sample of 23 cost centers to review, which totaled \$10,569,924 in expenses allocated to the FEHBP. We selected the natural accounts and cost centers based on high dollar amounts, our nomenclature review, and significant dollar amount fluctuations from year to year. We reviewed the expenses from these natural accounts and cost centers for allowability, allocability, and reasonableness.

Based on our review, we determined that the Plan charged the following expenses to the FEHBP that were expressly unallowable and/or did not benefit the FEHBP or only minimally benefited the FEHBP:

Natural Account Number	Natural Account Name	Reason for Questioning	Amount Questioned
66596	Consignment Expenses	Unallowable	\$2,818
66420	Outside Agency Fees	Unallocable	12,870
65010	Legal Charges	Unallocable	10,920
64110	Advertising -- Other	Unallowable	5,928
60190	Settlements/Separation Payments	Unallocable	5,882
66840	AT&T NASCO Fees	Unallocable	5,193
66423	Outside Agency Fee AAI-Insured	Unallocable	3,306
66598	Administrative Penalties	Unallowable	1,864
64210	Promotional Expenses	Unallowable	1,382
60040	Personal Car Allowance	Unallowable	1,359
60130	Commissions	Unallowable	920
<b>Total</b>			<b>\$52,442</b>

For advertising, marketing and promotional expenses charged to the FEHBP, 48 CFR 31.205-1 and 48 CFR 1631.205-70 provide specific criteria on the extent to which such costs are chargeable. Generally, these regulations state that such costs are unallowable.

Regarding consignment and commission expenses charged to the FEHBP, 48 CFR 31.205-1 through 205-52 specifically addresses certain costs and state that entertainment and commissions are unallowable.

Regarding fines and penalties charged to the FEHBP, 48 CFR 31.205-15 provides specific criteria on the extent to which such costs are chargeable. Generally, this regulation states that such costs are unallowable.

**Association's Response:**

In the draft report response (dated September 18, 2009), the Association agreed with \$47,760 of the questioned costs.

**OIG Comments:**

We reviewed additional documentation provided by the Plan and revised our questioned costs from the draft report to \$52,442. Subsequent to the draft report response, the Association agreed with the revised questioned costs of \$52,442.

**Recommendation 22**

We recommend that the contracting officer disallow \$52,442 for unallowable and/or unallocable costs from 2003 through 2007.



**6. Inter-Company Profit Adjustment**

**(\$67,402)**

The Plan overstated the adjustment to remove inter-company profits from its subsidiary, National Account Service Company (NASCO), by \$67,402 in 2005.

As previously cited from CS 1039, costs charged to the FEHBP must be actual, allowable, allocable, and reasonable.

48 CFR 31.205-26(e) states, "Allowance for all materials, supplies, and services that are sold or transferred between any divisions, subdivisions, subsidiaries, or affiliates of the contractor under a common control shall be on the basis of cost incurred . . . ."

From 2003 through 2007, the Plan made out-of-system adjustments to remove inter-company profits from the NASCO subsidiary expenses. In 2005, the Plan miscalculated the adjustment to remove NASCO profits by using the net income for the month of November instead of the December year-to-date net income. Therefore, we recalculated the inter-company profit adjustment by using the December 2005 year-to-date net income. We determined that the Plan overstated the adjustment, resulting in an undercharge of \$67,402 to the FEHBP in 2005.

**Association's Response:**

The Association agrees with this finding. The Association states that the Plan submitted a prior period adjustment on August 5, 2009 to credit the Plan for the undercharge.

**Recommendation 23**

We recommend that the contracting officer allow the Plan to charge the FEHBP \$67,402 for an undercharge in 2005.

**C. CASH MANAGEMENT**

Overall, we concluded that the Plan handled FEHBP funds in accordance with Contract CS 1039 and applicable laws and regulations, except for the audit findings pertaining to cash management noted in the "Miscellaneous Payments and Credits" section.

**D. LOST INVESTMENT INCOME ON AUDIT FINDINGS**

**\$231,737**

As a result of the audit findings presented in this report, the FEHBP is due LII of \$231,737 from January 1, 2004 through June 30, 2009.

FAR 52.232-17(a) states, "all amounts that become payable by the Contractor . . . shall bear simple interest from the date due . . . The interest rate shall be the interest rate established by the Secretary of the Treasury as provided in Section 611 of the Contract Disputes Act of 1978 (Public Law 95-563), which is applicable to the period in which the amount becomes due, as provided in paragraph (e) of this clause, and then at the rate applicable for each six-month period as fixed by the Secretary until the amount is paid."

We computed investment income that would have been earned using the semiannual rates specified by the Secretary of the Treasury. Our computations show that the FEHBP is due LII of \$231,737 from January 1, 2004 through June 30, 2009 on questioned costs for contract years 2003 through 2007 (see Schedule C).

**Association's Response:**

The draft audit report did not include an audit finding for LII. Therefore, the Association did not address this item in its reply.

**OIG Comments:**

According to the Association's draft report response (Appendix A), the Plan submitted prior period adjustments to the Association and/or wire transferred funds into the FEP investment account during June and August 2009 for the administrative expense audit findings that are subject to LII. The Plan also calculated LII on the audit findings for "Post-Retirement Benefit Costs" (B2) and "Pension Costs" (B3) and wire transferred these LII funds to the Association's FEP account on August 19, 2009.

**Recommendation 24**

We recommend that the contracting officer direct the Plan to credit \$231,737 (plus interest accruing after June 30, 2009) to the Special Reserve for LII on audit findings.

#### IV. MAJOR CONTRIBUTORS TO THIS REPORT

##### Experience-Rated Audits Group

██████████ Lead Auditor

██████████ Auditor

██████████ Auditor

██████████ Auditor

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██████████ Chief ██████████

██████████ Senior Team Leader

## V. SCHEDULES

HORIZON BLUECROSS BLUESHIELD OF NEW JERSEY  
NEWARK, NEW JERSEY

## CONTRACT CHARGES

CONTRACT CHARGES	2003	2004	2005	2006	2007	TOTAL
<b>A. HEALTH BENEFIT CHARGES</b>						
PLAN CODE 280	\$101,122,882	\$115,299,117	\$123,513,995	\$144,141,400	\$154,009,873	\$638,087,267
MISCELLANEOUS PAYMENTS AND CREDITS	1,514,547	765,390	(102,115)	350,750	481,715	3,010,287
PLAN CODE 780	107,031,349	118,358,418	128,942,209	148,695,449	171,592,572	674,619,996
MISCELLANEOUS PAYMENTS AND CREDITS	0	0	0	0	0	0
<b>TOTAL</b>	<b>\$209,668,778</b>	<b>\$234,422,925</b>	<b>\$252,354,088</b>	<b>\$293,187,600</b>	<b>\$326,084,160</b>	<b>\$1,315,717,551</b>
<b>B. ADMINISTRATIVE EXPENSES</b>						
PLAN CODE 280	\$20,036,346	\$20,345,524	\$22,007,772	\$22,157,899	\$20,518,288	\$105,065,829
PRIOR PERIOD ADJUSTMENTS	(304,288)	(211,528)	(193,049)	(4,542)	(41,540)	(754,947)
<b>TOTAL</b>	<b>\$19,732,058</b>	<b>\$20,133,996</b>	<b>\$21,814,723</b>	<b>\$22,153,357</b>	<b>\$20,476,748</b>	<b>\$104,310,882</b>
<b>TOTAL CONTRACT CHARGES</b>	<b>\$229,400,836</b>	<b>\$254,556,921</b>	<b>\$274,168,811</b>	<b>\$315,340,957</b>	<b>\$346,560,908</b>	<b>\$1,420,028,433</b>

HORIZON BLUECROSS BLUESHIELD OF NEW JERSEY  
NEWARK, NEW JERSEY

QUESTIONED CHARGES

AUDIT FINDINGS	2003	2004	2005	2006	2007	2008	2009	TOTAL
<b>A. HEALTH BENEFIT CHARGES</b>								
<b>1. Claim Payments*</b>								
a. Omnibus Budget Reconciliation Act of 1990 Review	\$0	\$0	\$94,535	\$6,382	\$82,542	\$168,634	\$0	\$352,093
b. Claim Payment Errors	0	0	6,414	(5,004)	12,110	2,554	0	16,074
<b>Total Claim Payments</b>	<b>\$0</b>	<b>\$0</b>	<b>\$100,949</b>	<b>\$1,378</b>	<b>\$94,652</b>	<b>\$171,188</b>	<b>\$0</b>	<b>\$368,167</b>
<b>2. Miscellaneous Payments and Credits**</b>								
a. Subrogation Recoveries	\$174	\$1,764	\$12,835	\$71,382	\$1,140,005	\$7,807	\$3,968	\$1,237,935
b. Health Benefit Refunds	9,163	49,483	88,717	220,975	171,286	3,665	761	544,050
c. Fraud Recoveries	22	4,845	65,737	3,576	2,365	1,811	690	79,046
d. Special Plan Invoices	0	7,801	32,781	2,659	2,480	1,946	602	48,269
<b>Total Miscellaneous Payments and Credits</b>	<b>\$9,359</b>	<b>\$63,893</b>	<b>\$200,070</b>	<b>\$298,592</b>	<b>\$1,316,136</b>	<b>\$15,229</b>	<b>\$6,021</b>	<b>\$1,909,300</b>
<b>TOTAL HEALTH BENEFIT CHARGES</b>	<b>\$9,359</b>	<b>\$63,893</b>	<b>\$301,019</b>	<b>\$299,970</b>	<b>\$1,410,788</b>	<b>\$186,417</b>	<b>\$6,021</b>	<b>\$2,277,467</b>
<b>B. ADMINISTRATIVE EXPENSES***</b>								
1. Directors Liability and Fidelity & Bond Insurance	\$107,179	\$123,268	\$168,382	\$159,892	\$172,955	\$0	\$0	\$731,676
2. Post-Retirement Benefit Costs	108,691	82,949	33,656	25,232	1,154	0	0	251,682
3. Pension Costs	52,111	100,004	13,857	30,723	54,546	0	0	251,241
4. Administrative Expense Overcharges	0	0	0	0	70,491	0	0	70,491
5. Unallowable and/or Unallocable Expenses	1,807	11,038	20,845		18,752	0	0	52,442
6. Inter-Company Profit Adjustment	0	0	(67,402)	0	0	0	0	(67,402)
<b>TOTAL ADMINISTRATIVE EXPENSES</b>	<b>\$269,788</b>	<b>\$317,259</b>	<b>\$169,338</b>	<b>\$215,847</b>	<b>\$317,898</b>	<b>\$0</b>	<b>\$0</b>	<b>\$1,290,130</b>
<b>C. CASH MANAGEMENT</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>
<b>D. LOST INVESTMENT INCOME ON AUDIT FINDINGS</b>	<b>0</b>	<b>11,466</b>	<b>25,684</b>	<b>41,128</b>	<b>53,473</b>	<b>63,701</b>	<b>36,285</b>	<b>\$231,737</b>
<b>TOTAL QUESTIONED CHARGES</b>	<b>\$279,147</b>	<b>\$392,618</b>	<b>\$496,041</b>	<b>\$556,945</b>	<b>\$1,782,159</b>	<b>\$250,118</b>	<b>\$42,306</b>	<b>\$3,799,334</b>

\* We did not review claim payments for contract years 2003 and 2004.

\*\* The audit findings for miscellaneous payments and credits include lost investment income.

\*\*\* The audit findings for administrative expenses are subject to lost investment income.

HORIZON BLUECROSS BLUESHIELD OF NEW JERSEY  
NEWARK, NEW JERSEY

LOST INVESTMENT INCOME CALCULATION

LOST INVESTMENT INCOME	2003	2004	2005	2006	2007	2008	2009	TOTAL
<b>A. QUESTIONED CHARGES (Subject to Lost Investment Income)</b>								
ADMINISTRATIVE EXPENSES	\$269,788	\$317,259	\$169,338	\$215,847	\$317,898	\$0	\$0	\$1,290,130
<b>B. LOST INVESTMENT INCOME CALCULATION</b>								
a. Prior Years Total Questioned (Principal)	\$0	\$269,788	\$317,259	\$169,338	\$215,847	\$317,898	\$0	
b. Cumulative Total	<u>0</u>	<u>0</u>	<u>269,788</u>	<u>587,047</u>	<u>756,385</u>	<u>972,232</u>	<u>1,290,130</u>	
c. Total	\$0	\$269,788	\$587,047	\$756,385	\$972,232	\$1,290,130	\$1,290,130	
d. Treasury Rate: January 1 - June 30	4.250%	4.000%	4.250%	5.125%	5.250%	4.750%	5.625%	
e. Interest (d * c)	\$0	\$5,396	\$12,475	\$19,382	\$25,521	\$30,641	\$36,285	\$129,700
f. Treasury Rate: July 1 - December 31	3.125%	4.500%	4.500%	5.750%	5.750%	5.125%		
g. Interest (f * c)	\$0	\$6,070	\$13,209	\$21,746	\$27,952	\$33,060		\$102,037
Total Interest By Year (e + g)	\$0	\$11,466	\$25,684	\$41,128	\$53,473	\$63,701	\$36,285	\$231,737



**BlueCross BlueShield  
Association**

An Association of Independent  
Blue Cross and Blue Shield Plans

September 18, 2009

██████████ Group Chief  
Experience-Rated Audits Group  
Office of the Inspector General  
U.S. Office of Personnel Management  
1900 E Street, Room 6400  
Washington, DC 20415-1100

Federal Employee Program  
1310 G Street, N.W.  
Washington, D.C. 20005  
202.942.1000

**Reference: OPM DRAFT AUDIT REPORT  
Horizon Blue Cross Blue Shield of New Jersey  
Audit Report Number 1A-10-49-09-025  
(Dated July 8, 2009 and Received July 8, 2009)**

Dear ██████████

This is our response to the above referenced U.S. Office of Personnel Management (OPM) Draft Audit Report covering the Federal Employees' Health Benefits Program (FEHBP) concerning the Horizon BlueCross BlueShield Plan of New Jersey. Our comments concerning the findings in the report are as follows:

## **A. HEALTH BENEFIT CHARGES**

### **1. Claim Payments**

#### **a. Omnibus Budget Reconciliation Act 1990 Review **\$787,068****

The Plan disagrees with \$736,638 of this finding. The amount includes a \$434,975 claim where the payment was issued via an off-system check because of a local system issue. The claim was processed accurately on FEP Direct, but not posted to history on the Plan's local system (NASCO). Supporting documentation regarding the off-system check was sent to OPM on July 23, 2009 reflecting that the claim posted on the local system. Based on the documentation provided by the Plan, OPM agreed to remove the \$434,975 from the audit finding. In addition, the Plan disagrees that \$301,663 was paid incorrectly due to the OBRA '90 Pricer and CMS Pricer pricing differences. When the claims were re-priced with the most current version of the FEP Operations Center OBRA '90 Pricer, the priced obtained was different from the price obtained using the CMS Pricer. Documentation was provided to support the \$301,663 payment based on the FEP Operations Center OBRA '90 Pricer which is the official OPM approved source for FEP OBRA '90 pricing.

Of the remaining amount, the Plan agrees that \$50,430 represents OBRA '90 claim overpayments. To reduce these types of pricing errors in the future, the Plan has implemented and updated its Policy & Procedure for OBRA '90 claim processing. Request for refunds have been initiated to recover payment errors and any amounts recovered will be returned to the Program. Also, the FEP Director's Office includes potential OBRA '90 priced claims in its periodic System-Wide Claims Review to facilitate early identification and recovery of OBRA '90 claim payment errors. Completion of these periodic reports assists in timely the timely identification and recovery of OBRA '90 claim payment errors.

Accordingly, to the extent that errors did occur, the payments are good faith erroneous benefits payments and fall within the context of CS 1039, Section 2.3(g). Any benefit payments the Plan is unable to recover are allowable charges to the Program. In addition, as good faith payments, the Plan continues to initiate recovery in a timely manner for confirmed overpayments. Because these are good faith erroneous payments, they are not subject to lost investment income.

**b. Claims Payment Errors** **\$16,074**

**Assistant Surgeon Review** **\$29,479**

The Plan does not contest this finding. Recovery activities have been initiated for these overpayments. The Plan has reviewed the identified errors and determined that they were the result of examiner manual interventions. Additional training has been provided to the examiners re-emphasizing the proper procedures for handling these claims. Also, the FEP Director's Office generates periodic listings of Assistant Surgeon Claims as a part of its System-wide Claims Review Process to ensure that these claim payment errors are identified and recovered in a timely manner.

For the Assistant Surgeon claim errors noted that related to the OBRA '93 pricing of claims with the "AS Modifier, the FEPDO implemented the following:

- Modified its contract with Palmetto to include the pricing of AS modifier claims.
- Issued a final comprehensive listing of unadjusted OBRA '93 Assistant Surgeon claims with the AS Modifier to all Plans in the Phase IV of the System-wide Claims Review Process that was sent during January 2009 so that claims can be adjusted as necessary.

Accordingly, to the extent that errors did occur, the payments are good faith erroneous benefits payments and fall within the context of CS 1039,



Section 2.3(g). Any benefit payments the Plan is unable to recover are allowable charges to the Program. In addition, as good faith payments, the Plan continues to initiate recovery in a timely manner for confirmed overpayments. Because these are good faith erroneous payments, they are not subject to lost investment income.

**System Review**

**\$100**

The Plan does not contest this audit finding. Recovery activities have been initiated for the two overpayments identified. Claims were manually priced with the incorrect provider allowance, which resulted in incorrect payments. The Plan will review processing procedures and documentation to ensure training materials are up to date as well as provide refresher training to claim processors to reduce these types of payment errors in the future.

The Plan has several methods in place to identify overpayments. These methods include, but are not limited to, the System Wide Claims Reports (which includes a listing of Assistant Surgeon Claims, Amount Paid Greater than Charges Claims, OBRA '90, OBRA '93, High Dollar and Termination Claims), COB claims reports and Duplicate claims reports provided by the FEP Director's Office along with routine claims quality assurance audits performed by the Plan's Internal Auditors. These are all tools that are used to promote claims accuracy. While these measures are not absolute, they provide reasonable assurances that such items will be identified. Efforts will be made to periodically examine existing procedures and add additional controls where necessary.

Accordingly, to the extent that errors did occur, the payments are good faith erroneous benefits payments and fall within the context of CS 1039, Section 2.3(g). Any benefit payments the Plan is unable to recover are allowable charges to the Program. In addition, as good faith efforts, the Plan continues to initiate recovery in a timely manner for confirmed overpayments. Because these are good faith erroneous payments, they are not subject to lost investment income.

**Amounts Paid Greater than Covered Charge**

**\$(13,505)**

The Plan does not contest this audit finding. Recovery efforts have been initiated the identified overpayments totaling \$9,955. The one claim that was underpaid by \$23,460 has been processed to issue an additional payment to the provider. The four errors (three overpayments and one underpayment) that occurred in this area were the result of manual intervention. To ensure these types of errors do not occur in the future, the Plan has reviewed its processing procedures and its training materials to ensure they are current. In addition, the FEP Director's Office System Wide Claims Review process includes Amounts Paid Greater than Covered Charges Claims for Plan review and identification of potential

September 18, 2009

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overpayments. This review process should continue to reduce these types of findings in the future.

Accordingly, to the extent that errors did occur, the payments are good faith erroneous benefits payments and fall within the context of CS 1039, Section 2.3(g). Any benefit payments the Plan is unable to recover are allowable charges to the Program. In addition, as good faith efforts, the Plan continues to initiate recovery in a timely manner for confirmed overpayments. Because these are good faith erroneous payments, they are not subject to lost investment income.

## **2. Miscellaneous Payment and Credits**

**Response for "Subrogation Recoveries" (A2.a), "Health Benefit Refunds" (A2.b), and "Fraud Recoveries" (A2.c) – Superseded by the November 11, 2009 Response (Appendix B).**

**d. Special Plan Invoices \$48,269**

The Plan agrees that the funds were not deposited in the Investment Account but when the Special Plan Invoice was approved by FEP, the funds were reduced from the amount payable to the Plan in the daily draws for 2004 and 2005 transactions. Therefore, only LII is due the Program starting 31 days after the funds were received until the Special Plan Invoices were processed.

The Plan has calculated the values for the two Special Plan Invoices at \$39,529. On April 2, 2009 and May 12, 2009 the Plan wired \$31,787.36 and \$7,741.73 respectively to the FEP Investment Account. An additional \$8,740 of LII was wired on August 19, 2009. Internal procedures have been revised to ensure that this type of exception does not occur in the future.

**B. ADMINISTRATIVE EXPENSES**

**1. Directors and Liability and Fidelity & Bond Insurance \$922,118**

The Plan does not agree with OPM that using Revenue as the methodology was inappropriate. However, the Plan has re-evaluated how the Revenue was allocated and determined that Insured Revenue was used instead of Gross Revenue. The Plan has subsequently recalculated the overcharge as follows:

Horizon Healthcare Services, Inc. (HHSI) (Horizon Blue Cross Blue Shield of New Jersey) incurs significant expenses for Directors' Liability Insurance coverage and Fidelity & Bond Insurance coverage. These policies are written on a consolidated basis, and cover HHSI as well as all of its subsidiaries and affiliates. The total expense is first allocated to each legal entity, based upon gross revenues (which include premium equivalents for self-funded groups). The costs allocated to HHSI are coded to the Executive department, which is then allocated to Market Segments as part of the Plan expense allocations.

Since HHSI has made the decision not to charge the FEP Program with any Executive department salary or benefit costs, the original Plan expense allocations to the FEP Market Segment for Executive costs, including the liability insurance expenses, were backed out, in total, from the FEP cost submissions. However, since these insurance costs are valid charges to FEP, an alternative allocation methodology was then utilized to calculate the amount of insurance expenses properly allocable to FEP. For the years under audit, the insurance expenses in HHSI were allocated to FEP using Insured Revenues. FEP revenues were divided by total Insured revenues to get the FEP percentage, and this was applied against the total Directors' Liability and Fidelity & Bond insurance costs charged to HHSI. The OPM auditors have questioned the use of revenues as a basis for allocating these insurance costs, and have proposed that total expenses should be used as the basis for allocating these insurance costs, not revenues. (See Audit Inquiry #11)

The Plan's initial response was that there was nothing in the CAS regulations that would prohibit the use of revenues as an allocation basis, and since the insurance expenses in question were originally allocated to the legal entities using revenues, the use of revenues to allocate to Market Segments would be appropriate.

Upon further review, the Plan now believes that the use of Insured premiums, as opposed to gross revenues, was inconsistent with the original allocation of the insurance expenses to the legal entities, and that the expenses allocated to the FEP Market Segment should have been calculated under that methodology. By using Insured premiums, the Plan was not allocating any of the Liability insurance costs to self-funded business, which would be incorrect. We still disagree with the OPM proposal to use total expenses, but we do agree that the original expense allocations have been overstated.

Attachment 1 shows the Plan's revised allocations, by year, of the costs of the Directors' Liability and Fidelity & Bond insurance costs to the FEP Program, based upon gross revenues by Market Segment. This results in overcharges to the FEP Program of \$731,676, as opposed to the \$922,118 calculated by OPM. We hereby submit that this revised amount should be returned to the FEP Program.

Although the Plan does not agree with the full amount questioned, on August 19, 2009, \$922,118 was wired into the FEP Investment Account pending a final resolution to this issue. The applicable Lost Investment Income will be assessed.

Supporting Documentation

Attachments 2a and 2b show the total insurance expense allocated by legal entity, to prove that the HHSI amount has already been reduced for amounts applicable to other legal entities under the Horizon corporate structure.

See Attachment 3 (pages 1-5) that shows the total consolidated insurance expenses to support the previous two attachments.

In summary since the charges were consistently allocated based on a percentage of revenue to all reporting entities and internal market segments, the allocation to FEP should also be based on gross revenues.

**2. Post-Retirement Benefit Costs \$251,682**

The Plan does not contest this audit finding. On June 15, 2009 the Plan submitted Prior Period Adjustment (PPAs) forms for the overcharges from 2003-2007.

To prevent this error from occurring in the future, the Plan has revised its accounting for Post Retirements Benefits. The accounting for Post Retirement Benefits for non FEP cost centers will be calculated in the same format as is used for Direct FEP cost centers.

Applicable Lost Investment Income was assessed on these funds and wired to BCBSA FEP on August 19, 2009.

**3. Pension Costs \$251,241**

The Plan does not contest this audit finding. On June 1, 2009, the Plan submitted Prior Period Adjustment forms for the overcharges from 2003-2007.

To prevent this error from occurring in the future, the Plan has revised the accounting for Pension Costs. The accounting for Pension costs for non FEP cost centers will be calculated using the CAS pension expense instead of the GAAP pension expense.

Applicable Lost Investment Income was assessed on these funds and wired to BCBSA FEP on August 19, 2009.

**4. Administrative Expense Overcharges \$185,077**

The Plan agrees with only \$70,491 of the audit finding. The FEP Program appears to have been overcharged for \$43,056 related to systems charge-backs. In addition, the Plan agrees that \$27,435 of the \$142,021 related to EMC Charges were improperly charged to the Program.

However, the Plan disagrees with \$114,586 of the finding. The OPM auditors did not take into consideration the realignment of our IT department in 2007 when determining the allowable charges to the Program. In completing our review of this Audit Inquiry, Plan staff has identified additional charges that were part of the cost center that handled electronic media claims (EMC) (cost center 9677) in 2006 but were transferred to various cost centers in 2007 and are allowable/allocable to FEP. See Attachment 4 for further analysis of the charges to FEP.

Although the Plan does not agree with the full amount questioned, on August 19, 2009 \$185,077 was wired into the FEP Investment Account, pending a final resolution of this issue. As applicable, Lost Investment Income will be assessed once the audit finding is resolved.

**5. Unallowable and/or Unallocable Expenses \$136,159**

The Plan agrees with \$47,760 of this finding. However, it disagrees with \$88,399 of this finding. Specifically, the Plan disagrees with the disallowance of the Managed Medicare and Sales and Reporting cost centers, and natural accounts 61040 (Print Promotional), 66596 (Consignment Expense) and 66598 (Admin Penalties) and feel that these are allowable expenses, totaling \$88,399. The following are the Plan's responses for those items where there is disagreement with the amount questioned by OPM.

**Managed Medicare cc 9452** – During the on-site portion of the audit, additional information was provided for this cost center. A document was provided that stated that the correct name of this cost center in 2003 was "HCM Compliance/Gov't Programs". There were seven FTEs in the cost center of which 3 FTEs "cover all products for compliance/mandates". Since FEP is one of Horizon's products, an allocation to FEP is warranted and justifiable. An Excel file was also produced that showed the monthly allocation of \$2,034 to FEP which on an annual basis is \$24,408 or only \$269 less than the actual allocation of \$24,677. Of the total expense in the cost center, 2.35% was allocated and charged to FEP. Disallowing expenses because of the cost center name is inappropriate.

**Sales & Reporting cc 4083** - During the on-site portion of the audit, additional information was provided for this cost center. An e-mail from the manager of the cost center dated July 2, 2004, stated that the cost center performed a number of functions including "prepared monthly enrollment and

financial reports that include the entire enterprise". Since FEP enrollment is included in Horizon produced enrollment reports and would be included in many financial reports that include the entire enterprise, the allocation of these costs to FEP are both warranted and justified. For the three years in question, the percentage allocation of this cost center to FEP was never more than 1.0%.

**Print Promotional – Account 61040** - The expenses in the Print Promotional account for 2005 represents payments made to a vendor who published our "Focus" member magazine in 2005 as well as our Health and Wellness calendar. Since this publication was distributed to our members, this would include our members and FEP staff, the allocation of this expense to FEP would be both warranted and justified. This print information was intended to educate, inform and advise our members so while this expense was charged to a print promotional account the Plan believes that this should not be treated as either a disallowed or non-chargeable account.

**Consignment Expenses – Account 66596.** This expense represents the costs of entertainment tickets, monthly bus and train passes, and water that are sold out of Horizon's fitness center. These expenses are fully offset by revenues that are coded to account 75140 – Credits Other in that same cost center. FEP is allocated a portion of the Fitness Center cost center, since it serves all employees, including the FEP staff. As part of that allocation, these credits were allocated back to FEP for each year of the audit. Since the credit was allocated back to FEP the expense should also be chargeable. The credits were included in the amount reported in Information Request #25 on line 262 (Credits Other).

**Admin Penalties – Account 66598.** If the expense from this account in 2004 of \$1,864 is to be classified as a disallowed account, then the credit of \$2,924 from 2005 should also be disallowed. This credit was not included by the auditors as a disallowed account in 2005; only the amount from 2004 was included in the draft report.

Of the remaining Natural Accounts the Plan agrees that these should not have been charged to FEP. The agreed upon amount is \$29,008

**Transaction Expenses** - The Plan agrees that these two transactions should not have been charged to FEP. The agreed upon amount is \$18,752.

Procedures have been enhanced to ensure that errors of this nature do not occur in the future.

Although the Plan does not agree with the total amount of this finding, on August 19, 2009 \$136,159 was wired into the FEP Investment Account,

pending final resolution of this issue. Applicable Lost Investment Income will be assessed after final resolution.

**6. Inter-Company Profit Adjustment (\$67,402)**

The Plan does not contest this finding. A Prior Period Adjustment form was submitted on August 5, 2009 to credit the Plan for this overpayment.

We appreciate the opportunity to provide our response to each of the findings and request that our comments be included in their entirety as part of the Final Audit Report.

[REDACTED]  
Executive Director  
Program Integrity

[REDACTED]  
cc: [REDACTED]





**BlueCross BlueShield  
Association**

An Association of Independent  
Blue Cross and Blue Shield Plans

November 11, 2009

██████████ Group Chief  
Experience-Rated Audits Group  
Office of the Inspector General  
U.S. Office of Personnel Management  
1900 E Street, Room 6400  
Washington, DC 20415-1100

Federal Employee Program  
1310 G Street, N.W.  
Washington, D.C. 20005  
202.942.1000  
Fax 202.942.1125

**Reference: OPM DRAFT AUDIT REPORT  
Horizon Blue Cross Blue Shield of New Jersey  
Audit Report Number 1A-10-49-09-025  
(Dated July 8, 2009 and Received July 8, 2009)**

Dear ██████████

This is our revised response findings 2a, 2b and 2c to the above referenced U.S. Office of Personnel Management (OPM) Draft Audit Report covering the Federal Employees' Health Benefits Program (FEHBP) concerning the Horizon BlueCross BlueShield Plan of New Jersey.

## **2. Miscellaneous Payment and Credits**

### **a. Subrogation Recoveries**

**\$1,237,935**

The Plan disagrees with \$1,201,907 of this audit finding. This amount was identified as a result of the 2007 BCBSA Control Performance Review (CPR) Plan Audit. The Plan received the final CPR Audit report on May 23, 2008. The amount of the finding was agreed upon by the CPR Audit Team and the Plan and funds were returned to the Program on June 13, 2008, which was prior to the 2009 OPM Audit. Documentation to support the position that the Plan was selected for the 2007 CPR audit prior to OPM Audit notification was forwarded by the FEP Director's Office to the OPM audit team on June 9, 2009.

The Plan does agree that \$36,028, which is comprised of \$18,265 in LII and \$17,761 in refunds, was not credited to the Program. Special Plan Invoices to credit the Program for the \$31,245 (\$11,239 principle and \$20,006 LII) were submitted to FEP on August 18, 2009. These funds were wired to BCBSA FEP on August 19, 2009. An additional \$4,783 was deposited into the FEP Investment Account on August 19, 2009. This amount will be included in the final wire of funds to close out this audit.

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In addition, procedures have been enhanced and additional monitoring tools developed to ensure the deposits in the investment account within 30 days of receipt.

**b. Health Benefit Refunds \$544,050**

The Plan disagrees with \$424,179 of the audit finding because this amount was identified as a result of the 2007 BCBSA CPR Plan Audit prior to the start of the 2009 OPM Audit. Funds were returned to the Program on July 15, 2008, prior to the start of the 2009 OPM Audit. Documentation to support the position that the Plan was selected for the 2007 CPR audit prior to OPM Audit notification was forwarded by the FEP Director's Office to the OPM audit team on June 9, 2009.

The Plan agrees that \$119,871, which is comprised of \$13,186 in LII and \$106,685 in refunds, was not credited to the Program. Special Plan Invoices to credit the Program for \$97,550 (\$83,881 principle and \$13,669 LII) were submitted and wired to BCBSA FEP on August 19, 2009. An additional \$22,321 was deposited into the FEP Investment Account on August 19, 2009. This amount will be included in the final wire of funds to close out this audit. In addition, procedures have been enhanced and additional monitoring tools developed to ensure the deposits in the investment account within 30 days of receipt.

**c. Fraud Recoveries \$79,046**

The Plan agrees with this finding. Special Plan Invoices to credit the Program for the \$48,498 (\$39,700 principle and \$8,798 LII) were submitted to FEP on August 19, 2009. An additional \$30,548 was deposited into the FEP Investment Account on August 19, 2009. This amount will be included in the final wire of funds to close out this audit. In addition, procedures have been enhanced and additional monitoring tools developed to promote the deposit of refunds into the FEP investment account funds within 30 days of receipt.

If you have any other questions or concerns, please feel free to call either [REDACTED] or myself at [REDACTED]

Sincerely,

[REDACTED]  
Director, Program Assurance, FEP