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

Final Audit Report

Subject:

AUDIT OF BLUE SHIELD OF CALIFORNIA
ACCESS+ HMO
SAN FRANCISCO, CALIFORNIA

Report No. 1D-SJ-00-09-021

Date: June 9, 2009

--CAUTION--

UNITED STATES OFFICE OF PERSONNEL MANAGEMENT
Washington, DC 20415

Office of the
Inspector General

AUDIT REPORT

Federal Employees Health Benefits Program
Experience-Rated Health Maintenance Organization

Blue Shield of California Access+ HMO
Contract CS 2639 Plan Code SJ
San Francisco, California

REPORT NO. 1D-SJ-00-09-021 DATE: June 9, 2009

Michael R. Esser
Assistant Inspector General
for Audits

UNITED STATES OFFICE OF PERSONNEL MANAGEMENT
Washington, DC 20415

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EXECUTIVE SUMMARY

Federal Employees Health Benefits Program
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Blue Shield of California Access+ HMO
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REPORT NO. 1D-SJ-00-09-021 DATE: June 9, 2009

This final audit report on the Federal Employees Health Benefits Program (FEHBP) operations at Blue Shield of California Access+ HMO (Plan) questions $178,930 in administrative expenses and $402,805 in lost investment income (LII) on excess letter of credit drawdowns. The Plan agreed (*A*) with all questioned charges.

Our limited scope audit was conducted in accordance with Government Auditing Standards. The audit covered miscellaneous health benefit 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:

A. MISCELLANEOUS HEALTH BENEFIT PAYMENTS AND CREDITS

The audit disclosed no findings pertaining to miscellaneous health benefit payments and credits. Overall, we concluded that the Plan returned health benefit refunds and recoveries, including pharmacy drug rebates, to the FEHBP.

B. ADMINISTRATIVE EXPENSES

- **Incorrect Reporting of Administrative Expenses *(A)*** **$121,822**

  The Plan overstated the administrative expenses reported in the 2007 Annual Accounting Statement by $121,822. Since administrative expenses are considered when developing the premium rates, overstating administrative expenses may increase future rates.

- **Unallocable Cost Center Expenses *(A)*** **$57,108**

  The Plan charged the FEHBP $50,484 in expenses from two unallocable cost centers. As a result, the FEHBP is due $57,108, consisting of $50,484 for unallocable cost center expenses and $6,624 for LII on these expenses.

C. CASH MANAGEMENT

- **Lost Investment Income on Excess Letter of Credit Drawdowns *(A)*** **$402,805**

  For the period 2003 through 2007, the Plan included inflow and outflow adjustments, totaling $5,430,761 (net), when calculating and requesting letter of credit (LOC) drawdowns. The inclusion of these adjustments in the LOC drawdown calculations caused the Plan to withdraw funds in excess of actual expenses. The Plan subsequently returned these excess drawdowns to the FEHBP in 2008, but did not return LII of $402,805 on these excess funds.

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I. INTRODUCTION AND BACKGROUND

INTRODUCTION

This final audit report details the findings, conclusions, and recommendations resulting from our limited scope audit of the Federal Employees Health Benefits Program (FEHBP) operations at Blue Shield of California Access+ HMO (Plan). The Plan is located in San Francisco, California.

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 Center for Retirement and Insurance Services 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 Plan is an experience-rated health maintenance organization (HMO) that provides heath benefits to federal enrollees and their families.[1] Enrollment is open to all federal employees and annuitants in the Plan's service area. The Plan's service area includes most of California.

The Plan's contract (CS 2639) with OPM is experience-rated. Thus, the costs of providing benefits in the prior year, including underwritten gains and losses which have been carried forward, are reflected in current and future years' premium rates. In addition, the contract provides that in the event of termination, unexpended program funds revert to the FEHBP Trust Fund. In recognition of these provisions, the contract requires an accounting of program funds be submitted at the end of each contract year. The accounting is made on a statement of operations known as the Annual Accounting Statement.

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

[1] Members of an experience-rated HMO have the option of using a designated network of providers or using non-network providers. A member's choice in selecting one healthcare provider over another has monetary and medical implications. For example, if a member chooses a non-network provider, the member will pay a substantial portion of the charges and benefits available may be less comprehensive.

This is our first audit of the Plan. The results of our audit were provided to the Plan in written audit inquiries; were discussed with Plan officials throughout the audit and at an exit conference; and were presented in detail in a draft report, dated March 27, 2009. The Plan's comments offered in response to the draft report were considered in preparing our final report and are included as an Appendix 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:

Miscellaneous Health Benefit Payments and Credits

- 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 limited scope 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 Plan's FEHBP Annual Accounting Statements for contract years 2003 through 2007. During this period, the Plan paid approximately $419 million in health benefit charges and $19 million in administrative expenses (See Figure 1 and Schedule A). The Plan also paid approximately $3 million in other expenses and retentions (See Schedule A).

Specifically, we reviewed miscellaneous health benefit payments and credits (i.e., refunds, subrogation recoveries, provider audit recoveries, fraud recoveries, uncashed provider and subscriber checks, and pharmacy drug rebates), 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.

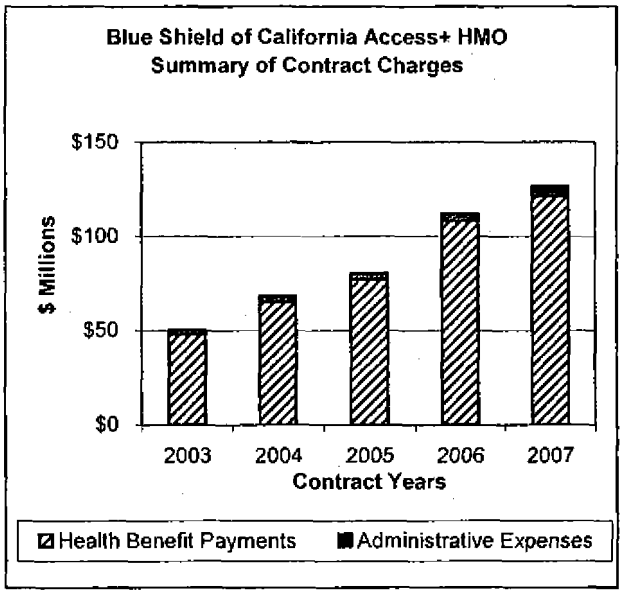

Figure 1 – Contract Charges

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 Plan. 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 San Francisco, California from February 3, 2009 through February 26, 2009. Audit fieldwork was also performed at our offices in Cranberry Township, Pennsylvania and Jacksonville, Florida through March 27, 2009.

METHODOLOGY

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

We interviewed Plan personnel and reviewed the Plan's policies, procedures, and accounting records during our audit of miscellaneous health benefit payments and credits. Using various sampling methodologies, we selected and reviewed 186 health benefit refunds and recoveries, totaling $4,644,328 (from a universe of 4,050 refunds and recoveries, totaling $12,544,799), to determine if refunds and recoveries were promptly returned to the FEHBP. Specifically, our sample included 168 refunds, subrogation recoveries, and provider audit recoveries totaling $2,489,490; 13 uncashed checks totaling $54,583; and 5 pharmacy drug rebates totaling $2,100,255. In addition, prior to the start of our audit, the Plan identified and returned $181,522 in refunds, uncashed checks, provider interest charges, and lost investment income to the FEHBP as part of a corrective action plan. Of this amount, we judgmentally selected and reviewed $57,522 to determine if these funds were properly returned to the FEHBP. The results of these samples were not projected to the universe of miscellaneous health benefit 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, employee health benefits, executive compensation, BlueCross BlueShield Association dues, gains and losses, return on investment, benefit plan brochures, and Health Insurance Portability and Accountability Act of 1996 compliance. We used the FEHBP contract, the FAR, and the FEHBAR 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 2639 and applicable laws and regulations.

III. AUDIT FINDINGS AND RECOMMENDATIONS

A. MISCELLANEOUS HEALTH BENEFIT PAYMENTS AND CREDITS

The audit disclosed no findings pertaining to miscellaneous health benefit payments and credits. Overall, we concluded that the Plan returned health benefit refunds and recoveries, including pharmacy drug rebates, to the FEHBP.

B. ADMINISTRATIVE EXPENSES

1. Incorrect Reporting of Administrative Expenses $121,822

The Plan overstated the administrative expenses reported in the 2007 Annual Accounting Statement (AAS) by $121,822. Since administrative expenses are considered when developing the premium rates, overstating administrative expenses may increase future rates.

Contract CS 2639, Part III, Section 3.2 (a)(3) states, "Based on the results of either the independent audit prescribed by the Guide or a Government audit, OPM may require the carrier to adjust its annual accounting statements (i) by amounts found not to constitute actual, allowable, allocable and reasonable costs; or (ii) to reflect prior overpayments or underpayments."

We reconciled the Plan's cost accounting reports to the administrative expenses reported on the AAS's for contract years 2003 through 2007. Based on our reconciliation, we determined that the Plan overstated the amount of administrative expenses reported on the 2007 AAS. This overstatement was caused by the following items:

- The Plan misclassified the December 2007 service charge accrual of $69,310 as an administrative expense accrual.

- The Plan incorrectly recorded $2,012 in lost investment income (LII) as an increase in administrative expenses, instead of recording this amount as a decrease.

- The Plan incorrectly calculated the amount of disallowed charges to be excluded from the administrative expense amount reported on the AAS, resulting in an overstatement of $50,500.

As a result of these inadvertent errors, the Plan overstated the administrative expenses by $121,822 in the 2007 AAS.

Plan's Response:

The Plan agrees with this finding and has adjusted the 2008 AAS accordingly.

Recommendation 1

We recommend that the contracting officer verify that the Plan made the appropriate prior period adjustment in the 2008 AAS to correct the 2007 administrative expense overstatement of $121,822.

2. Unallocable Cost Center Expenses — $57,108

The Plan charged the FEHBP $50,484 in expenses from two unallocable cost centers. As a result, the FEHBP is due $57,108, consisting of $50,484 for unallocable expenses and $6,624 for LII on these expenses.

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."

48 CFR 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."

From 2003 through 2007, the Plan charged the following expenses to the FEHBP from two cost centers that did not benefit the FEHBP:

Cost Centers	
2503H – Hospital and Provider Liaison	$39,821
6035H – Producer Internet Sales	10,663
	$50,484

Specifically, cost center 2503H (Hospital and Provider Liaison) benefits the preferred provider organization Federal Employee Program product but not the experience-rated HMO product, and cost center 6035H (Producer Internet Sales) does not provide support to the FEHBP. As a result, the FEHBP is due $50,484 for unallocable cost center expenses charged to the FEHBP.

Subsequent to us identifying this audit finding, the Plan returned $50,484 to the FEHBP on March 16, 2009 for these unallocable cost center expenses. Accordingly, we verified the return of these funds to the FEHBP and calculated LII of $6,624 through March 16, 2009 on these questioned expenses.

Plan's Response:

The Plan agrees with this finding. The Plan will return LII of $6,624 to the FEHBP in the next drawdown during the first week of May 2009.

Recommendation 2

We verified that the Plan returned the questioned cost center expenses of $50,484 to the FEHBP on March 16, 2009. Therefore, no further action is required for these questioned expenses.

Recommendation 3

We recommend that the contracting officer verify that the Plan returned $6,624 to the FEHBP for LII on the unallocable cost center expenses that were charged to the FEHBP.

C. CASH MANAGEMENT

1. Lost Investment Income on Excess Letter of Credit Drawdowns $402,805

For the period 2003 through 2007, the Plan included inflow and outflow adjustments, totaling $5,430,761 (net), when calculating and requesting letter of credit (LOC) drawdowns. The inclusion of these adjustments in the LOC drawdown calculations caused the Plan to withdraw funds in excess of actual expenses. The Plan subsequently returned these excess drawdowns to the FEHBP in 2008, but did not return LII of $402,805 on these excess funds.

Contract CS 2639, 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. In addition, the Carrier must: . . . (ii) determine the cost in accordance with: (A) the terms of this contract . . . ."

48 CFR 1652.215-71 requires the carrier to invest and reinvest all excess FEHBP funds on hand, and to credit all investment income earned on those funds to the Special Reserve on behalf of the FEHBP.

48 CFR 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

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."

From 2003 through 2007, the Plan requested $432,760,945 in reimbursements via LOC drawdowns. When requesting these funds, the Plan included inflow and outflow adjustments totaling $5,430,761 (net) in their LOC drawdown calculations. According to the Plan, these adjustments were included primarily to cover estimated capitation expenses incurred a month prior to reimbursement from the FEHBP. For example, the Plan wire transferred the January 2005 provider capitation payments in the beginning of January; however, the Plan was not reimbursed for these expenses until the month-end drawdown was requested in mid-February. In order to have sufficient funds for the January 2005 provider capitation payments, the Plan added an inflow and outflow adjustment to the December 2004 month-end drawdown.

Although these adjustments were added to the LOC drawdowns to cover estimated allowable expenses, the LOC drawdowns were not properly reconciled or adjusted for variances between month-end actual expenses versus funds received for the corresponding month. As a result, as of December 31, 2007, the Plan maintained a balance of $6,555,018 in excess funds.[2]

In 2008, the Plan discontinued the use of inflow and outflow adjustments and adjusted various LOC drawdowns to return the excess funds of $6,555,018 to the FEHBP. Although the Plan returned the principal amount to the FEHBP, the Plan did not return LII on the overdrawn funds. As a result, the FEHBP is due LII of $402,805 on these excess funds.

Plan's Response:

The Plan agrees with this finding and returned LII of $402,805 to the FEHBP on April 16, 2009.

Recommendation 4

We recommend that the contracting officer verify that the Plan returned $402,805 to the FEHBP for LII on the excess LOC drawdowns.

[2] The funds returned to the FEHBP in 2008 were greater than the inflow and outflow adjustments disclosed in our review for the period 2003 though 2007 because the balance of $6,555,018 also included inflow and outflow adjustments accumulated prior to 2003.

IV. MAJOR CONTRIBUTORS TO THIS REPORT

Experience-Rated Audits Group

[redacted] Auditor-In-Charge (AIC)

[redacted] Co-AIC

[redacted] Auditor

[redacted] Auditor

[redacted] Chief [redacted]

[redacted] Senior Team Leader

SCHEDULE A

V. SCHEDULES

BLUE SHIELD OF CALIFORNIA ACCESS+ HMO
SAN FRANCISCO, CALIFORNIA

CONTRACT CHARGES AND AMOUNTS QUESTIONED

CONTRACT CHARGES*	2003	2004	2005	2006	2007	2008	2009	TOTAL
A. HEALTH BENEFIT CHARGES	$47,702,247	$64,806,091	$76,965,557	$108,482,649	$121,352,159			$419,308,703
B. ADMINISTRATIVE EXPENSES	2,487,298	3,431,558	3,462,416	4,275,300	5,477,599			19,134,171
C. OTHER EXPENSES AND RETENTIONS	301,107	417,280	594896	669,267	818,742			2,801,292
TOTAL CONTRACT CHARGES	$50,490,652	$68,654,929	$81,022,869	$113,427,216	$127,648,500			$441,244,166

AMOUNTS QUESTIONED (PER SCHEDULE B)	2003	2004	2005	2006	2007	2008	2009	TOTAL
A. MISCELLANEOUS HEALTH BENEFIT PAYMENTS AND CREDITS	$0	$0	$0	$0	$0	$0	$0	$0
B. ADMINISTRATIVE EXPENSES	6,508	6,990	7,412	10,029	144,907	2,492	592	178,930
C. CASH MANAGEMENT	24,635	83,435	35,818	80,898	98,652	79,367	0	402,805
TOTAL QUESTIONED CHARGES	$31,143	$90,425	$43,230	$90,927	$243,559	$81,859	$592	$581,735

* We did not review claim payments and other expenses and retentions.

SCHEDULE B

BLUE SHIELD OF CALIFORNIA ACCESS+ HMO
SAN FRANCISCO, CALIFORNIA

QUESTIONED CHARGES

AUDIT FINDINGS	2003	2004	2005	2006	2007	2008	2009	TOTAL
A. MISCELLANEOUS HEALTH BENEFIT PAYMENTS AND CREDITS	$0	$0	$0	$0	$0	$0	$0	$0
B. ADMINISTRATIVE EXPENSES								
1. Incorrect Reporting of Administrative Expenses	$0	$0	$0	$0	$121,822	$0	$0	$121,822
2. Unallocable Cost Center Expenses*	6,508	6,990	7,412	10,029	23,085	2,492	592	57,108
TOTAL ADMINISTRATIVE EXPENSES	$6,508	$6,990	$7,412	$10,029	$144,907	$2,492	$592	$178,930
C. CASH MANAGEMENT								
1. Lost Investment Income on Excess Letter of Credit Drawdowns	$24,635	$83,435	$35,818	$80,898	$98,652	$79,367	$0	$402,805
TOTAL CASH MANAGEMENT	$24,635	$83,435	$35,818	$80,898	$98,652	$79,367	$0	$402,805
TOTAL QUESTIONED CHARGES	$31,143	$90,425	$43,230	$90,927	$243,559	$81,859	$592	$581,735

* This audit finding includes lost investment income of $6,624.

blue of california

April 27, 2009

[redacted] Senior Team Lead
Experienced-Rated Audit Group
Office of Inspector General

RE: Report No. 1D-SJ-00-09-021

Dear [redacted]

In response to the April 21, 2009 email from OIG stating that OIG has decided to not change the LII calculation methodology and also agreed to revise the Audit Inquiry #2 overcharge to be $50,484, Blue Shield of California has the following responses to the Draft Audit Report dated March 27, 2009 and revised Audit Inquiry #2:

Audit Inquiry #1 - Incorrect Reporting of 2007 Administrative Expenses ($121,822)

- Blue Shield of California agrees with the finding and has adjusted the 2008 AAS accordingly.

Audit Inquiry #2 - Unallocable Cost Centers ($57,108)

- Blue Shield of California agrees with this finding that cost centers 2503H – Hospital and Provider Liaison and 6035H – Producer Internet Sales were charged in error to the program.

Cost Centers:	
2503H – Hospital and Provider Liaison	$39,821
6035H – Producer Internet Sales	10,663
	$50,484

- Blue Shield of California agrees with the revised LII calculation of $6,624 related to the overcharge to the program and will return the LII to OPM on the next drawdown during the first week of May 2009.

Audit Inquiry #3 - Lost Investment Income on Excess Letter of Credit Drawdowns (402,805)

- Blue Shield of California agrees with the finding. Even though the LII amount wasn't completely finalized, Blue Shield returned the $402,805 to OPM on April 16, 2009 with the assumption that any LII calculation changes would be adjusted during a future drawdown. Since OIG did not revise the LII calculation methodology, no future draw adjustments will be needed.

Sincerely,

[redacted]
Director, Federal Employee Program
Blue Shield of California