



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

Final Audit Report

Subject:

**AUDIT OF THE
GOVERNMENT EMPLOYEES HOSPITAL
ASSOCIATION'S
PHARMACY OPERATIONS
AS ADMINISTERED BY
MEDCO HEALTH SOLUTIONS
2003 - 2006**

Report No. 1H-02-00-08-004

Date: August 14, 2009

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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
Pharmacy Operations
Contract CS 1063
Government Employees Hospital Association
Plan Code 31

Medco Health Solutions
Franklin Lakes, New Jersey

REPORT NO. 1H-02-00-08-004

DATE: August 14, 2009

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

Michael R. Esser
Assistant Inspector General
for Audits



Office of the
Inspector General

UNITED STATES OFFICE OF PERSONNEL MANAGEMENT
Washington, DC 20415

EXECUTIVE SUMMARY

Federal Employees Health Benefits Program
Pharmacy Operations
Contract CS 1063
Government Employees Hospital Association
Plan Code 31

Medco Health Solutions
Franklin Lakes, New Jersey

REPORT NO. 1H-02-00-08-004

DATE: August 14, 2009

The Office of the Inspector General has completed a performance audit of the 2003 through 2006 Government Employees Hospital Association's (GEHA) pharmacy operations as administered by Medco Health Solutions (Medco). The primary objective of the audit was to determine if Medco complied with the regulations and requirements contained within its contract with GEHA and Contract 1063 (between GEHA and the Office of Personnel Management). The audit was conducted in Franklin Lakes, New Jersey from September 24 through September 28, 2007, and from October 15 through November 16, 2007.

The audit showed that the 2003 through 2006 GEHA pharmacy operations were in compliance with the contracts.

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I. INTRODUCTION AND BACKGROUND

INTRODUCTION

As authorized by the Inspector General Act of 1978, as amended, we conducted an audit of the 2003 through 2006 Government Employees Hospital Association (GEHA) pharmacy operations as administered by Medco Health Solutions (Medco). The audit field work was conducted at Medco's offices in Franklin Lakes, New Jersey, from September 24 through September 28, 2007, and from October 15 through November 16, 2007. Additional audit work was completed at our Washington D.C. office.

BACKGROUND

The Federal Employees Health Benefits Program (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. The Office of Personnel Management's (OPM) 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 that provide service benefits, indemnity benefits, or comprehensive medical services.

GEHA has entered into a government-wide contract (CS 1063) with OPM to provide a health benefit plan authorized by the FEHB Act. GEHA has contracted directly with Medco to manage the delivery and financing of prescription drug benefits for GEHA health benefit purchasers.

This is our first audit of the GEHA pharmacy benefit operations as administered by Medco.

II. OBJECTIVES, SCOPE, AND METHODOLOGY

OBJECTIVES

The objectives of our audit were to determine whether Medco's charges to the FEHBP and services provided to FEHBP members were in accordance with the terms of the contracts. Specifically, our objectives were as follows:

Rebates

- To determine whether pharmaceutical manufacturer rebates were correctly calculated and returned to the FEHBP in accordance with the Medco and GEHA contracts.

Payment Reconciliation

- To determine whether GEHA paid for only those items billed/charged by Medco.

Processing and Administrative Fees

- To determine whether processing and administrative fees charged to the FEHBP were in compliance with the terms of the contract between Medco and GEHA.
- To identify areas of the contract between Medco and GEHA requiring improvement.

Drug Interchange Program

- To determine whether costs charged to the FEHBP for Drug Interchange Programs were charged in accordance with the GEHA/Medco contracts.
- To determine if savings amounts reported by Medco were properly calculated.

SCOPE

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on the audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on the audit objectives.

We reviewed the GEHA Annual Accounting Statements for contract years 2003 through 2006. During this period, Medco paid approximately \$1.8 billion in retail pharmacy drug charges (See Schedule A).

In planning and conducting the audit, we obtained an understanding of Medco'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 Medco'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 Medco's system of internal controls taken as a whole.

In conducting the audit we relied to varying degrees on computer-generated data provided by Medco. 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 audit testing, nothing came to our attention to doubt its reliability. We believe that the data was sufficient to achieve the audit objectives.

We also conducted tests to determine whether Medco had complied with the contract, the applicable procurement regulations (i.e., Federal Acquisition Regulations and Federal Employees Health Benefits Acquisition Regulations, as appropriate), and the laws and regulations governing the FEHBP. The results of our tests indicate that, with respect to the items tested, Medco complied with all provisions of the contract and federal procurement regulations.

METHODOLOGY

To test Medco's compliance with the contracts we reviewed the following areas:

- For our review of rebates, we judgementally selected the top 6 out of 117 drug manufacturers by claim dollar for 2003 through 2006 and reviewed the entire universe of rebates paid to Medco by the manufacturers. We then compared this amount to the amount paid by Medco to GEHA for 2003 through 2006, to determine whether rebates were correctly calculated and returned to the FEHBP.
- For our payment reconciliation review, we judgementally selected five invoices (totaling \$61,966,505) from Medco to GEHA (one invoice per year for 2003 through 2005 and two invoices in 2006) to verify the correct amount was paid. This universe included 154 invoices with payments totaling \$1,743,811,253.
- For our processing and administrative fees review we judgementally selected certain charges from Medco invoices to determine whether the fees charged were in compliance with the Medco/GEHA contract. Specifically, we selected six invoices (two 2005 invoices and four 2006 invoices) paid to GEHA totaling \$428,631. We also reviewed the allowability and reasonableness of the Medicare flat fees charged to the sampled 2005 invoices, and credits for excess copays that occurred in 2006. Our sample review consisted of:
 - Prior Authorization and Smart Rules 2 reviews related to invoice dates of March 29 and December 6 of 2005; and
 - Prior Authorization and Smart Rules 2 reviews related to invoice dates of January 31, March 28, June 20, and September 12 of 2006.

- Finally, for our drug interchange review, we judgementally selected interchange samples to determine whether the costs charged were in accordance with the Medco/GEHA contract and whether the savings amounts reported by Medco were properly calculated. While no standardized selection process was utilized to select the interchanges reviewed, we did select a total sample size of 100 interchanges totaling \$13,396. The universe included 53,756 interchange samples totaling \$6,922,579.

The above samples that were selected and reviewed in performing the audit were not statistically based. Consequently, the results could not be projected to the universe since it is unlikely that the results are representative of the universe taken as a whole. We used the Contract CS 1063 and the contract between Medco and GEHA to determine if processing and administrative fees charged to the FEHBP were in compliance with the terms of the contract.

III. AUDIT RESULTS

Based on our review of rebate payments, processing and administrative fees, drug interchanges, and payment reconciliations, we found that the GEHA pharmacy operations for 2003 through 2006, as administered by Medco, were administered in accordance with the contracts.

IV. MAJOR CONTRIBUTORS TO THIS REPORT

Special Audits Group

██████████ Auditor

██████████ Auditor

██████████ Auditor

██████████ Senior Team Leader

██████████ Chief, Special Audits Group ██████████

Jill S. Henderson, Deputy Assistant Inspector General for Management

AUDIT OF THE
 GOVERNMENT EMPLOYEE HOSPITAL ASSOCIATION
 PHARMACY OPERATIONS
 AS ADMINISTERED BY MEDCO HEALTH SOLUTIONS
 FRANKLIN LAKES, NEW JERSEY

CONTRACT CHARGES
 REPORT NUMBER: 1H-02-00-08-004

CONTRACT CHARGES	2003	2004	2005	2006	TOTAL
A. PHARMACY BENEFIT CHARGES	\$428,457,343	\$435,370,596	\$462,369,339	\$424,487,769	\$1,750,685,047