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

Final Audit Report

Subject:

Audit of the Federal Employees Health Benefits Program Operations at Preferred Care

Report No. 1C-GV-00-10-004

Date: July 27, 2010

-- CAUTION --

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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
Community-Rated Health Maintenance Organization
Preferred Care
Contract Number CS 2371 - Plan Code GV
Rochester, New York

Report No. 1C-GV-00-10-004 **Date:** July 27, 2010

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
Community-Rated Health Maintenance Organization
Preferred Care
Contract Number CS 2371 - Plan Code GV
Rochester, New York

Report No. <u>**1C-GV-00-10-004**</u> **Date:** July 27, 2010

The Office of the Inspector General performed an audit of the Federal Employees Health Benefits Program (FEHBP) operations at Preferred Care (Plan). The audit covered contract years 2006 through 2009 and was conducted at the Plan's office in Rochester, New York.

This report questions $746,845 for inappropriate health benefit charges to the FEHBP in contract years 2006 through 2009. The questioned amount includes $685,407 for defective pricing and $61,438 due the FEHBP for lost investment income, calculated through July 31, 2010.

For contract year 2006, we determined that the FEHBP's rates were overstated by $30,306 because the Plan charged broker commissions to the FEHBP. Broker commissions have been identified as an unallowable cost under 48 Code of Federal Regulations (CFR) 1631.205-75 Selling Costs part (a).

For contract year 2007, we determined that the FEHBP's rates were overstated by $64,093 because the Plan charged the FEHBP both broker commissions and a state assessed market stabilization fee. Broker commissions have been identified as an unallowable cost under 48 CFR 1631.205-75. New York's market stabilization fee is an unallowable cost under Carrier Letter

2003-16, the Federal Employees Health Benefits Act, and the Omnibus Budget Reconciliation Act of 1990 at United States Code (U.S.C.) sub code 8909(f).

For contract year 2008, we determined that the FEHBP's rates were overstated by $374,167 because the Plan charged broker commissions to the FEHBP. Broker commissions have been identified as an unallowable cost under 48 CFR 1631.205-75 Selling Costs part (a).

For contract year 2009, we determined that the FEHBP's rates were overstated by $216,841 because the Plan charged the FEHBP a state assessed market stabilization fee. New York's market stabilization fee is an unallowable cost under Carrier Letter 2003-16, the Federal Employees Health Benefits Act, and the Omnibus Budget Reconciliation Act of 1990 at U.S.C. sub code 8909(f).

Consistent with the FEHBP regulations and contract, the FEHBP is due $61,438 for lost investment income, calculated through July 31, 2010, on the defective pricing findings. In addition, we recommend that the contracting officer recover lost investment income starting August 1, 2010, until all defective pricing amounts have been returned to the FEHBP.

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I. INTRODUCTION AND BACKGROUND

Introduction

We completed an audit of the Federal Employees Health Benefits Program (FEHBP) operations at Preferred Care (Plan). The audit covered contract years 2006 through 2009 and was conducted at the Plan's office in Rochester, New York. The audit was conducted pursuant to the provisions of Contract CS 2371; 5 U.S.C. Chapter 89; and 5 Code of Federal Regulations (CFR) Chapter 1, Part 890. The audit was performed by the Office of Personnel Management's (OPM) Office of the Inspector General (OIG), as established by the Inspector General Act of 1978, as amended.

Background

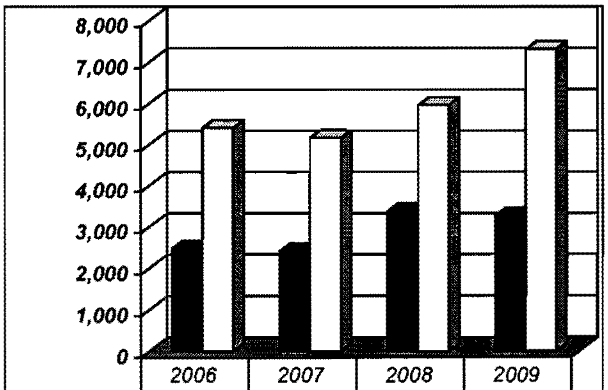
The FEHBP was established by the Federal Employees Health Benefits Act (Public Law 86-382), enacted on September 28, 1959. The FEHBP was created to provide health insurance benefits for federal employees, annuitants, and dependents. The FEHBP is administered by OPM's Retirement and Benefits Office. The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

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

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

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

FEHBP Contracts/Members
March 31



	2006	2007	2008	2009
■ Contracts	2,482	2,411	3,386	3,284
□ Members	5,411	5,164	5,959	7,314

The Plan has participated in the FEHBP since 1988 and provides health benefits to FEHBP members throughout the Rochester area. The last full-scope audit of the Plan covered contract years 2001 through 2005. All issues related to that audit have been resolved.

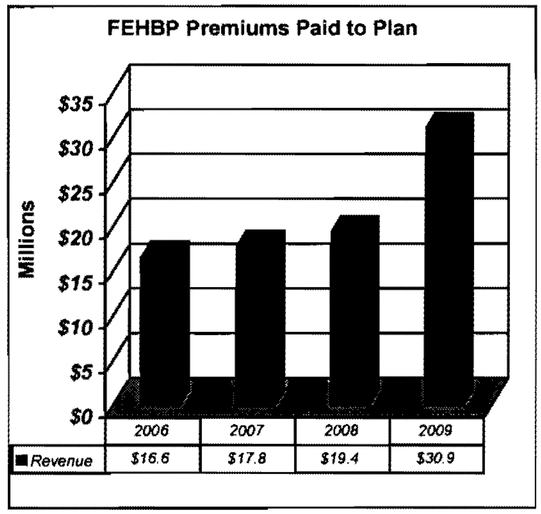
The preliminary results of this audit were discussed with Plan officials at an exit conference and through subsequent correspondence. A draft report was also provided to the Plan for review and comment. The Plan's comments were considered in the preparation of this final report and are included, as appropriate,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

II. OBJECTIVES, SCOPE, AND METHODOLOGY

Objectives

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

Scope



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

This performance audit covered contract years 2006 through 2009. For these years, the FEHBP paid approximately $84.7 million in premiums to the Plan. The premiums paid for each contract year audited are shown on the chart to the right.

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

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

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

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

The audit fieldwork was performed at the Plan's office in Rochester, New York during October 2009. Additional audit work was completed at our offices in Jacksonville, Florida, and Cranberry Township, Pennsylvania.

Methodology

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

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

III. AUDIT FINDINGS AND RECOMMENDATIONS

Premium Rates

1. Defective Pricing $685,407

The Certificates of Accurate Pricing the Plan signed for contract years 2006 through 2009 were defective. In accordance with federal regulations, the FEHBP is therefore due a rate reduction for these years. Application of the defective pricing remedies shows that the FEHBP is entitled to premium adjustments totaling $685,407 (see Exhibit A).

FEHBAR 1652.215-70 provides that carriers proposing rates to OPM are required to submit a Certificate of Accurate Pricing certifying that the proposed subscription rates, subject to adjustments recognized by OPM, are market price rates. OPM regulations refer to a market price rate in conjunction with the rates offered to an SSSG. If it is found that the FEHBP was charged higher than a market price (i.e., the best rate offered to an SSSG), a condition of defective pricing exists, requiring a downward adjustment of the FEHBP premiums to the equivalent market price.

2006

We reviewed the FEHBP's rates and found that the Plan charged broker commissions to the FEHBP. The broker commission was built into the community rate. Broker commissions are unallowable costs identified by United States Code of Federal Regulation Title 48 – Federal Acquisition Regulations System Chapter 16 – Office of Personnel Management Federal Employees Health Benefits Acquisition Regulation Part 1631 – Contract Cost Principles and Procedures 1631.205-75 Selling Costs part (a).

We re-developed the FEHBP's rates by applying a credit to offset the broker commission. A comparison of the reconciled line 5 rates to our audited line 5 rates shows that the FEHBP was overcharged $30,306 in 2006 (see Exhibit B).

2007

We reviewed the FEHBP's rates and found that the Plan charged both broker commissions and a market stabilization fee to the FEHBP. The broker commission and market stabilization fee were built into the community rate. The market stabilization fee is an assessment imposed by the state of New York to fund a pool used to pay high cost claims for individual and small group insurance policies.

Broker commissions are unallowable costs identified by United States Code of Federal Regulation Title 48 – Federal Acquisition Regulations System Chapter 16 – Office of Personnel Management Federal Employees Health Benefits Acquisition Regulation Part 1631 – Contract Cost Principles and Procedures 1631.205-75 Selling Costs part (a).

The market stabilization fee is an unallowable cost associated with Carrier Letter 2003-16, the Federal Employees Health Benefits Act, and the Omnibus Budget Reconciliation Act of 1990 at U.S.C. sub code 8909(f). The regulation states, "No tax, fee, or other monetary payment may be imposed, directly or indirectly, on a carrier or an underwriting or plan administration subcontractor of an approved health benefits plan by any State...with respect to any payment made from the Employees Health Benefits Fund." This regulation excludes the FEHBP from surcharges that subsidize indigent care and other health care initiatives through pooled funds.

We re-developed the FEHBP's rates by applying a credit to offset both the broker commission and the market stabilization fee. A comparison of the reconciled line 5 rates to our audited line 5 rates shows that the FEHBP was overcharged $64,093 in 2007 (see Exhibit B).

2008

We reviewed the FEHBP's rates and found that the Plan charged broker commissions to the FEHBP. The broker commission was built into the community rate. Broker commissions are unallowable costs identified by United States Code of Federal Regulation Title 48 – Federal Acquisition Regulations System Chapter 16 – Office of Personnel Management Federal Employees Health Benefits Acquisition Regulation Part 1631 – Contract Cost Principles and Procedures 1631.205-75 Selling Costs part (a).

We re-developed the FEHBP's rates by applying a credit to offset the broker commission. A comparison of the reconciled line 5 rates to our audited line 5 rates shows that the FEHBP was overcharged $374,167 in 2008 (see Exhibit B).

2009

We reviewed the FEHBP's rates and found that the Plan charged a market stabilization fee to the FEHBP. This market stabilization fee was built into the community rates for 2009. The market stabilization fee is an assessment imposed by the state of New York to fund a pool used to pay high cost claims for individual and small group insurance policies.

The market stabilization fee is an unallowable cost associated with Carrier Letter 2003-16, the Federal Employees Health Benefits Act, and the Omnibus Budget Reconciliation Act of 1990 at U.S.C. sub code 8909(f). The regulation states, "No tax, fee, or other monetary payment may be imposed, directly or indirectly, on a carrier or an underwriting or plan administration subcontractor of an approved health benefits plan by any State...with respect to any payment made from the Employees Health Benefits Fund." This regulation excludes the FEHBP from surcharges that subsidize indigent care and other health care initiatives through pooled funds.

We re-developed the FEHBP's rates by applying a credit to offset the market stabilization fee. A comparison of the reconciled line 5 rates to our audited line 5 rates shows that the FEHBP was overcharged $216,841 in 2009 (see Exhibit B).

Plan's Comments (See Appendix):

The Plan concurs that brokers commissions and market stabilization fees were improperly charged to the FEHBP.

Recommendation 1

We recommend that the contracting officer require the Plan to return $685,407 to the FEHBP for defective pricing in contract years 2006 through 2009.

2. Lost Investment Income **$61,438**

In accordance with the FEHBP regulations and the contract between OPM and the Plan, the FEHBP is entitled to recover lost investment income on the defective pricing findings in contract years 2006 through 2009. We determined that the FEHBP is due $61,438 for lost investment income, calculated through July 31, 2010 (see Exhibit C). In addition, the FEHBP is entitled to lost investment income for the period beginning August 1, 2010, until all defective pricing finding amounts have been returned to the FEHBP.

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

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

Plan's Comments (See Appendix):

The Plan concurs.

Recommendation 2

We recommend that the contracting officer require the Plan to return $61,438 to the FEHBP for lost investment income for the period January 1, 2006, through July 31, 2010. In addition, we recommend that the contracting officer recover lost investment income on amounts due for

IV. MAJOR CONTRIBUTORS TO THIS REPORT

Community-Rated Audits Group

[redacted] Auditor-In-Charge

[redacted] Staff Auditor

[redacted] Staff Auditor

[redacted] Chief

[redacted] Senior Team Leader

Exhibit A

Preferred Care - Rochester, NY

Summary of Questioned Costs

Defective Pricing Questioned Costs:

Contract Year 2006	$30,306	
Contract Year 2007	$64,093	
Contract Year 2008	$374,167	
Contract Year 2009	$216,841	
Total Defective Pricing Questioned Costs:		$685,407
Lost Investment Income:		$61,438
Total Questioned Costs:		**$746,845**

Preferred Care - Rochester, NY
Defective Pricing Questioned Costs

2006	**Self**	**Family**	
FEHBP Line 5 - Reconciled Rate	[redacted]		
FEHBP Line 5 - Audited Rate (Revised 6/4/2010)			
Overcharge	[redacted]		
To Annualize Overcharge:			
3/31/06 enrollment			
Pay Periods	26	26	
Subtotal	[redacted]		
Total 2006 Defective Pricing Questioned Costs			**$30,306**

2007	**Self**	**Family**	
FEHBP Line 5 - Reconciled Rate	[redacted]		
FEHBP Line 5 - Audited Rate			
Overcharge	[redacted]		
To Annualize Overcharge:			
3/31/07 enrollment			
Pay Periods	26	26	
Subtotal	[redacted]		
Total 2007 Defective Pricing Questioned Costs			**$64,093**

2008	**Self**	**Family**	
FEHBP Line 5 - Reconciled Rate	[redacted]		
FEHBP Line 5 - Audited Rate			
Overcharge			
To Annualize Overcharge:			
3/31/08 enrollment	[redacted]		
Pay Periods	26	26	
Subtotal	[redacted]		
Total 2008 Defective Pricing Questioned Costs			**$374,167**

Preferred Care - Rochester, NY
Defective Pricing Questioned Costs

	High Option		
2009	**Self**	**Family**	
FEHBP Line 5 - Reconciled Rate	[redacted]		
FEHBP Line 5 - Audited Rate			
Overcharge			
To Annualize Overcharge:			
3/31/09 enrollment			
Pay Periods	26	26	
Subtotal	[redacted]		
Total 2009 High Option Defective Pricing Questioned Costs			**$208,340**

	Standard Option		
2009	**Self**	**Family**	
FEHBP Line 5 - Reconciled Rate	[redacted]		
FEHBP Line 5 - Audited Rate			
Overcharge			
To Annualize Overcharge:			
3/31/09 enrollment	[redacted]		
Pay Periods	26	26	
Subtotal	[redacted]		
Total 2009 Standard Option Defective Pricing Questioned Costs			**$8,501**
Total 2009 Defective Pricing Questioned Costs			**$216,841**

EXHIBIT C

Preferred Care - Rochester, NY
Lost Investment Income

Year:	2006	2007	2008	2009	2010	Total
Defective Pricing:	$30,306	$64,093	$374,167	$216,841	$0	$685,407
Totals (per year):	$30,306	$64,093	$374,167	$216,841	$0	$685,407
Cumulative Totals:	$30,306	$94,399	$468,566	$685,407		
Avg. Interest Rate (per year):	5.4375%	5.5000%	4.9375%	5.2500%	3.2500%	
Interest on Prior Years Findings:	$0	$1,667	$4,661	$24,600	$12,994	$43,922
Current Years Interest:	$824	$1,763	$9,237	$5,692	$0	$17,516
Total Cumulative Interest Calculated Through July 31, 2010:	$824	$3,430	$13,898	$30,292	$12,994	**$61,438**

APPENDIX

MVP HEALTH CARE

625 State Street P.O. B[illegible]
Schenectady, NY 12301 [illegible]
mvphealthcare.com

2010 MAY 24 PM 12: 2

May 20, 2010

[redacted]
Chief, Community-Rated Audits Group
U.S. Office of the Inspector General
1900 E Street, NW
Room 6400
Washington, D.C. 20415-1100

RE: Report No. 1C-GV-00-10-004

Dear [redacted]:

Enclosed please find a CD in Microsoft word format as well as hard copies of the response to your letter of March 24, 2010 addressed to Mr. David Oliker, Chief Executive Officer, MVP Health Care (MVP) regarding Report No. 1C-GV-00-10-004, audit of Preferred Care for the time period 2006-2009.

The Office of Personnel Management/Office of Inspector General (OIG) has calculated a balance due of $914,049 for contract audit years 2006 through 2009 ($847,099 for defective pricing and $66,950 for lost investment income). After a thorough review, MVP has concluded that the figure should be amended to $734,765 ($686,285 for defective pricing and $48,480 for lost investment income). MVP accepts responsibility for the inclusion of broker commissions in the FEHB rate and concurs with the removal and credit back to FEHB of those funds plus interest. However in 2006 and 2007 we believe there is a computation error where a monthly amount is multiplied by 26 (pay period application) resulting in an overage of amount due as calculated by OIG. In 2008 the removal of broker commission is calculated correctly. Also in 2008, MVP disagrees with the SSSG discount as it pertains to the broker commission. Please see attached broker commission schedules outlining the revised payment schedule, thus removing the discount cited in the comparison to [redacted]. The pricing for [redacted] was rated in compliance with the formula and this amount should be excluded from [redacted]. MVP agrees with the findings for 2009 regarding the removal of the market stabilization fee. The attached documentation provides further detail for the year by year differences.

Thank you for your consideration of these items to aid in the preparation of the final audit report.

Please direct any questions you may have relative to this application to my attention.

Sincerely,

[redacted]
Vice President, Underwriting & Analysis