Department of Health and Human Services

OFFICE OF INSPECTOR GENERAL

CAHABA SAFEGUARD ADMINISTRATORS, LLC, CLAIMED SOME UNALLOWABLE MEDICARE POSTRETIREMENT BENEFIT COSTS THROUGH ITS INCURRED COST PROPOSALS

Inquiries about this report may be addressed to the Office of Public Affairs at Public.Affairs@oig.hhs.gov.

Amy J. Frontz
Deputy Inspector General
for Audit Services

January 2024
A-07-23-00637

Office of Inspector General

https://oig.hhs.gov

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OFFICE OF AUDIT SERVICES FINDINGS AND OPINIONS

The designation of financial or management practices as questionable, a recommendation for the disallowance of costs incurred or claimed, and any other conclusions and recommendations in this report represent the findings and opinions of OAS. Authorized officials of the HHS operating divisions will make final determination on these matters.

Report in Brief
Date: January 2024
Report No. A-07-23-00637

U.S. DEPARTMENT OF HEALTH & HUMAN SERVICES
OFFICE OF INSPECTOR GENERAL

Why OIG Did This Audit

The Centers for Medicare & Medicaid Services (CMS) reimburses a portion of its contractors' postretirement benefit (PRB) costs.

The HHS, OIG, Office of Audit Services, Region VII pension audit team reviews the cost elements related to qualified defined-benefit, nonqualified defined-benefit, PRB, and any other pension-related cost elements claimed by Medicare administrative contractors and Cost Accounting Standards- and Federal Acquisition Regulation-covered contracts through Incurred Cost Proposals (ICPs).

Our objective was to determine whether the calendar years (CYs) 2017 through 2019 PRB costs that Cahaba Safeguard Administrators, LLC (Cahaba CSA), claimed for Medicare reimbursement, and reported on its ICPs, were allowable and correctly claimed.

How OIG Did This Audit

We reviewed $401,841 of Medicare PRB costs that Cahaba CSA claimed for Medicare reimbursement on its ICPs for CYs 2017 through 2019.

Cahaba Safeguard Administrators, LLC, Claimed Some Unallowable Medicare Postretirement Benefit Costs Through Its Incurred Cost Proposals

What OIG Found

Cahaba CSA claimed PRB costs of $401,841 for Medicare reimbursement, through its ICPs, for CYs 2017 through 2019; however, we determined that the allowable PRB costs during this period were $392,035. The difference, $9,806, represented unallowable Medicare PRB costs that Cahaba CSA claimed on its ICPs for CYs 2017 through 2019. Cahaba CSA claimed these unallowable Medicare PRB costs primarily because it used an incorrect methodology when claiming PRB costs for Medicare reimbursement. More specifically, Cahaba CSA incorrectly calculated its allocable PRB costs using the accrual method instead of the pay-as-you-go method.

What OIG Recommends and Auditee Comments

We recommend that Cahaba CSA work with CMS to ensure that its final settlement of contract costs reflects a decrease in Medicare PRB costs of $9,806 for CYs 2017 through 2019.

Cahaba CSA did not concur with our finding. Cahaba CSA referred to the management response letter that it had submitted to CMS in response to our previous audit report on its PRB costs claimed for CYs 2014 through 2016 (A-07-19-00578, Nov. 17, 2020). For this current audit, Cahaba CSA stated that it disagreed with our findings for CYs 2017 through 2019 for the same reasons that it offered in that management response letter. Furthermore, Cahaba CSA asked that we and CMS revisit the requirements set forth in the Federal Acquisition Regulation regarding use of the accrual method and added that Cahaba CSA's intended use of the accrual method was fully disclosed to and discussed with CMS in 2015.

After reviewing Cahaba CSA's comments, including its management response letter to our previous audit, we maintain that all of our calculations of the Medicare PRB costs remain valid and that both our finding and recommendation remain valid as well. We note as well that during audit resolution of our previous Cahaba CSA PRB report, CMS as the cognizant HHS Operating Division upheld that report's recommendation. In addition, we have concerns about several provisions of the funding mechanisms that Cahaba CSA has in place and do not believe that those mechanisms satisfy Federal requirements.

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INTRODUCTION

WHY WE DID THIS AUDIT

Medicare contractors are eligible to be reimbursed a portion of their postretirement benefit (PRB) costs, which are funded by contributions that these contractors make to their dedicated trust funds. The amount of PRB costs that the Centers for Medicare & Medicaid Services (CMS) reimburses to the contractors is determined by the cost reimbursement principles contained in the Federal Acquisition Regulation (FAR) as required by the Medicare contracts. Previous Office of Inspector General (OIG) audits found that Medicare contractors have not always complied with Federal requirements when claiming PRB costs for Medicare reimbursement.

At CMS's request, the Department of Health and Human Services, OIG, Office of Audit Services, Region VII pension audit team reviews the cost elements related to qualified defined-benefit, nonqualified defined-benefit, PRB, and any other pension-related cost elements claimed by Medicare administrative contractors (MACs) and Cost Accounting Standards (CAS)- and FAR-covered contracts through Incurred Cost Proposals (ICPs).

For this audit, we focused on one Medicare contractor, Cahaba Safeguard Administrators, LLC (Cahaba CSA). In particular, we examined the Cahaba CSA Medicare segment PRB costs that Cahaba CSA claimed for Medicare reimbursement and reported on its ICPs.

OBJECTIVE

Our objective was to determine whether the calendar years (CYs) 2017 through 2019 PRB costs that Cahaba CSA claimed for Medicare reimbursement, and reported on its ICPs, were allowable and correctly claimed.

BACKGROUND

Cahaba Safeguard Administrators, LLC, and Medicare

During our audit period, Cahaba CSA was a subsidiary of Blue Cross and Blue Shield of Alabama (BCBS Alabama), whose home office is in Birmingham, Alabama. The Cahaba CSA Medicare segment administered program safeguard functions under a contract with CMS, until its contract terminated on September 30, 2017. Cahaba CSA continued to perform Medicare work through a wage index contract with CMS.

BCBS Alabama has two Medicare segments that participate in its PRB plan: (1) Cahaba Government Benefits Administrators, LLC (Cahaba GBA) and (2) Cahaba CSA. On January 1, 2013, BCBS Alabama created the Healthcare Business Solutions, LLC (HBS), intermediate home office segment (HBS segment) by transferring assets into it from the Cahaba GBA and Cahaba

CSA segments.[1] On December 31, 2018, Cahaba GBA transferred the participants working on its Benefit Coordination & Recovery Center contract to the Cahaba CSA segment. The Cahaba GBA and HBS segments were then closed effective December 31, 2018.

This report addresses the allowable Medicare PRB costs claimed by Cahaba CSA under the provisions of its MAC contracts. We are addressing Cahaba GBA's compliance with the MAC contracts in a separate audit. Cahaba CSA claimed PRB costs using the accrual basis of accounting.

The disclosure statement that Cahaba CSA submits to CMS states that Cahaba CSA uses pooled cost accounting. Medicare contractors use pooled cost accounting to calculate the indirect cost rates (whose computations include pension and PRB costs) that they submit on their ICPs. The indirect cost rates are used to calculate contract costs reported on the ICPs. In turn, CMS uses these indirect cost rates in determining the final indirect cost rates for each contract.[2]

Medicare Reimbursement of Postretirement Benefit Costs

CMS reimburses a portion of the Medicare contractors' annual PRB costs. The PRB costs are included in the computation of the indirect cost rates reported on the ICPs. In turn, CMS uses indirect cost rates in reimbursing costs under cost-reimbursement contracts.

In claiming PRB costs, contractors must follow cost reimbursement principles contained in the FAR and applicable CAS as required by the Medicare contracts. To be allowable for Medicare reimbursement, pay-as-you-go PRB costs must be assigned to the period in which the benefits are actually provided, or when the costs are paid to an insurer, provider, or other recipient for current-year benefits or premiums.[3]

Incurred Cost Proposal Audits

At CMS's request, CohnReznick, LLC (CohnReznick), performed audits of the ICPs that Cahaba CSA submitted for the periods of CYs 2017 through 2019. The objectives of the CohnReznick ICP audits were to determine whether costs were allowable in accordance with the FAR, the U.S. Department of Health and Human Services Acquisition Regulation, and the CAS.

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[1] Although BCBS Alabama created the HBS segment, we determined that this segment was not a Medicare segment. Because HBS is not a Medicare segment, we do not opine on its costs.

[2] For each CY, each Medicare contractor submits to CMS an ICP that reports the Medicare direct and indirect costs that the contractor incurred during that year. The ICP and supporting data provide the basis for the CMS Contracting Officer and the Medicare contractor to determine the final billing rates for allowable Medicare costs.

[3] The pay-as-you-go method is a method of recognizing costs when benefits are paid to retired employees or their beneficiaries.

For our current audit, we relied on the CohnReznick ICP audit findings and recommendations when computing the allowable PRB costs discussed in this report.

We incorporated the results of the CohnReznick ICP audits into our computations of the audited indirect cost rates, and ultimately the PRB costs claimed, for the contracts subject to the FAR. CMS will use our report on allowable PRB costs, as well as the CohnReznick ICP audit reports, to determine the final indirect cost rates and the total allowable contract costs for Cahaba CSA for CYs 2017 through 2019. The cognizant Contracting Officer will perform a final settlement with the contractor to determine the final indirect cost rates. These rates ultimately determine the final costs of each contract.[4]

HOW WE CONDUCTED THIS AUDIT

We reviewed $401,841 of Medicare PRB costs that Cahaba CSA claimed for Medicare reimbursement on its ICPs for CYs 2017 through 2019.

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.

Appendix A contains details of our audit scope and methodology.

FINDING

Cahaba CSA claimed PRB costs of $401,841 for Medicare reimbursement, through its ICPs, for CYs 2017 through 2019; however, we determined that the allowable PRB costs during this period were $392,035. The difference, $9,806, represented unallowable Medicare PRB costs that Cahaba CSA claimed on its ICPs for CYs 2017 through 2019. Cahaba CSA claimed these unallowable Medicare PRB costs primarily because it used an incorrect methodology when claiming PRB costs for Medicare reimbursement. More specifically, Cahaba CSA incorrectly calculated its allocable PRB costs using the accrual method instead of the pay-as-you-go method.

ALLOCABLE POSTRETIREMENT BENEFIT PLAN COSTS UNDERSTATED

During this audit, we calculated the allocable PRB costs for CYs 2017 through 2019 in accordance with Federal requirements. We determined that the Cahaba CSA allocable PRB

[4] In accordance with FAR 42.705-1(b)(5)(ii) and FAR 42.705-1(b)(5)(iii)(B), the cognizant Contracting Officer shall "[p]repare a written indirect cost rate agreement conforming to the requirements of the contracts" and perform a "[r]econciliation of all costs questioned, with identification of items and amounts allowed or disallowed in the final settlement," respectively.

costs for CYs 2017 through 2019 totaled $427,305. Cahaba CSA identified allocable PRB costs of $401,633 for this period. Therefore, Cahaba CSA understated its Medicare segment allocable PRB costs by $25,672. This understatement occurred because of differences in the calculation of the assignable PRB costs.

We used the allocable PRB costs to adjust the indirect cost rates (i.e., the fringe benefit and general and administrative rates) and, in turn, to calculate the allowable PRB costs. Table 1 shows the differences between the allocable Medicare segment PRB costs that we determined for CYs 2017 through 2019 and the Medicare segment PRB costs that Cahaba CSA calculated for the same period.

Table 1: Medicare Segment Allocable PRB Costs

CY	Allocable Per Audit	Per Cahaba CSA	Difference
2017	$74,753	$153,964	($79,211)
2018	182,422	136,293	46,129
2019	170,130	111,376	58,754
Total	**$427,305**	**$401,633**	**$25,672**

SOME UNALLOWABLE POSTRETIREMENT BENEFIT PLAN COSTS CLAIMED

Cahaba CSA claimed PRB costs of $401,841 for Medicare reimbursement, through its ICPs, for CYs 2017 through 2019. After incorporating the results of the CohnReznick ICP audits and our adjustments to the indirect cost rates, we determined that the allowable PRB costs for CYs 2017 through 2019 were $392,035. Thus, Cahaba CSA claimed $9,806 of unallowable Medicare PRB costs on its ICPs for CYs 2017 through 2019. Cahaba CSA claimed these unallowable Medicare PRB costs primarily because it based its claim for Medicare reimbursement on an incorrect methodology. More specifically, Cahaba CSA incorrectly calculated its allocable PRB costs using the accrual method instead of the pay-as-you-go method.

We calculated the allowable Medicare PRB costs in accordance with Federal requirements. For details on the Federal requirements, see Appendix B.

Table 2 on the following page compares the Cahaba CSA Medicare PRB costs that we calculated (using our adjusted indirect cost rates) to the PRB costs that Cahaba CSA claimed for Medicare reimbursement for CYs 2017 through 2019.

Table 2: Comparison of Allowable PRB Costs and Claimed PRB Costs[5]

CY	Allowable Per Audit	Per Cahaba CSA	Difference
2017	$40,736	$154,149	($113,413)
2018	182,416	136,282	46,134
2019	168,883	111,410	57,473
Total	**$392,035**	**$401,841**	**($9,806)**

RECOMMENDATION

We recommend that Cahaba Safeguard Administrators, LLC, work with CMS to ensure that its final settlement of contract costs reflects a decrease in Medicare PRB costs of $9,806 for CYs 2017 through 2019.

AUDITEE COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE

In written comments on our draft report, Cahaba CSA did not concur with our finding. Cahaba CSA's comments included an attachment that referred to its management response letter, which Cahaba CSA had submitted to CMS in response to our previous audit report on its PRB costs claimed for CYs 2014 through 2016 (A-07-19-00578, Nov. 17, 2020). For this current audit, Cahaba CSA stated that it disagreed with our findings for CYs 2017 through 2019 for the same reasons that it offered in its management response letter after issuance of our previous audit report.

Furthermore, Cahaba CSA asked that we and CMS "revisit the FAR and the requirements set forth therein in order to utilize the accrual method" and that we review the 2015 communications between HBS and CMS regarding how HBS intended to satisfy the FAR's requirement to use the accrual method. Cahaba CSA added that it "strongly believe[s] that the account is effectively restricted per the requirements of the FAR" and that any retroactive disallowance of PRB costs "would be inequitable given the fact that the . . . intended use of an accrual method [was] fully disclosed to and discussed with CMS in 2015 during implementation. Not being made aware of government concerns we were unable to revise the practice to remove government concerns. . . ."

Cahaba CSA's comments, from which we have removed attachments that contained personally identifiable information, appear as Appendix C. We will provide Cahaba CSA's comments in their entirety to CMS.

After reviewing Cahaba CSA's comments, including the management response letter it submitted in response to our previous audit, we maintain that all of our calculations of the

[5] Our calculation does not appear in this report because those rate computations that Cahaba CSA used in its ICPs, and to which we referred as part of our audit, are proprietary information.

Medicare PRB costs remain valid and that both our finding and recommendation remain valid as well. Since the PRB plan's inception, Cahaba CSA has not effectively restricted its PRB funds and therefore cannot use the accrual method to calculate its allocable PRB costs. Accordingly, we calculated the allowable PRB costs using the pay-as-you-go method, as required by the FAR.

We note as well that during audit resolution of our previous Cahaba CSA PRB report, CMS as the cognizant HHS Operating Division upheld our recommendation to ensure that Cahaba CSA's final settlement of contract costs reflects a decrease in Medicare PRB costs of $675,457 for CYs 2014 through 2016. In addition, we have concerns about several provisions of the agreement between HBS and BCBS Alabama, and we continue to believe that the funding mechanisms that Cahaba CSA has in place do not satisfy the requirement of the FAR.

APPENDIX A: AUDIT SCOPE AND METHODOLOGY

SCOPE

We reviewed $401,841 of Medicare PRB costs that Cahaba CSA claimed for Medicare reimbursement on its ICPs for CYs 2017 through 2019.

Achieving our objective did not require that we review Cahaba CSA's overall internal control structure. We reviewed the internal controls related to the PRB costs that were included in Cahaba CSA's ICPs and ultimately used as the basis for Medicare reimbursement, to ensure that these costs were allowable in accordance with the FAR.

We performed our audit work at our office in Jefferson City, Missouri.

METHODOLOGY

To accomplish our objective, we:

- reviewed the portions of the FAR and Medicare contracts applicable to this audit;
- reviewed information provided by Cahaba CSA to identify the amounts of PRB costs used in Cahaba CSA's calculation of indirect cost rates for CYs 2017 through 2019;
- used information that Cahaba CSA's actuarial consulting firm provided, including benefit payments and employee contributions to calculate pay-as-you-go PRB costs that were allowable for Medicare reimbursement for CYs 2017 through 2019;
- determined the extent to which Cahaba CSA incurred PRB costs by paying premiums relating to PRB coverage;
- reviewed the results of the CohnReznick ICP audits and incorporated those results into our calculations of allowable PRB costs; and
- provided the results of our audit to Cahaba CSA officials on September 14, 2023.

We performed this audit in conjunction with the following audits and used the information obtained during these audits:

- *Cahaba Government Benefits Administrators, LLC, Did Not Claim Some Allowable Medicare Pension Costs Through Its Incurred Cost Proposals* (A-07-23-00634);
- *Cahaba Safeguard Administrators, LLC, Claimed Some Unallowable Medicare Pension Costs Through Its Incurred Cost Proposals* (A-07-23-00635); and

- *Cahaba Government Benefits Administrators, LLC, Claimed Some Unallowable Medicare Postretirement Benefit Plan Costs Through Its Incurred Cost Proposals* (A-07-23-00636).

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.

APPENDIX B: FEDERAL REQUIREMENTS RELATED TO REIMBURSEMENT OF POSTRETIREMENT BENEFIT COSTS

FEDERAL REGULATIONS

Federal regulations (FAR 31.205-6(o)(2)) address the allowability of pay-as-you-go PRB costs and require that PRB costs be assigned to the period in which the benefits are actually provided, or when the costs are paid to an insurer, provider, or other recipient for current-year benefits or premiums.

Federal regulations (FAR 52.216-7(a)(1)) address the invoicing requirements and the allowability of payments as determined by the Contracting Officer in accordance with FAR subpart 31.2.

MEDICARE CONTRACTS

The Medicare contracts require Cahaba CSA to submit invoices in accordance with FAR 52.216-7, "Allowable Cost & Payment." (See our citation to FAR 52.216-7(a)(1) in "Federal Regulations" above.)

APPENDIX C: AUDITEE COMMENTS

csa℠

October 30, 2023

Department of Health and Human Services
Office of Inspector General
Office of Audit Services
Attention: James I. Korn, Regional Inspector General for Audit Services
Region VII
601 East 12th Street, Room 0429
Kansas City, Missouri 64106

RE: Report Number A-07-19-00637 Cahaba Safeguard Administrators, LLC, Claimed Some Unallowable Medicare Postretirement Benefit Costs Through Its Incurred Cost Proposals

Dear Mr. Korn,

Management of Cahaba Safeguard Administrators, LLC ("Cahaba CSA") does not concur with the OIG's finding in its draft audit report that Cahaba CSA incorrectly calculated allocable postretirement benefit (PRB) costs for calendar years (CYs) 2017 – 2019.

Included for reference is the management response letter provided for Cahaba CSA's previous PRB cost audit, conducted for CYs 2014 – 2016. Management's basis for disagreement with the findings noted for CYs 2017 – 2019 is the same as that discussed in the letter provided for CYs 2014-2016.[6]

We continue to ask that the OIG and CMS revisit the FAR and the requirements set forth therein in order to utilize the accrual method. In addition, we also ask that the OIG review the 2015 communications (submitted with the previous management letter as Exhibit C) between HBS and CMS regarding how HBS intended to satisfy the FAR's requirements to use of the accrual method. We strongly believe that the account is effectively restricted per the requirements of the FAR and that any position by OIG that would retroactively disallow PRB cost would be inequitable given the fact that the details of the Agreement and intended use of an accrual method were fully disclosed to and discussed with CMS in 2015 during implementation. Not being made aware of government concerns we were unable to revise the practice to remove government concerns and avoid substantial analysis of potential cost disallowances.

[6]**Office of Inspector General Note—**The management response letter that is included in this Appendix had several attachments, which we have removed from this final report because those attachments included personally identifiable information.

375 Riverchase Parkway East • Birmingham, AL 35244

If you should have questions regarding this report, please contact Jon-Michael Ogletree, CFO, at (205)-820-6012 or via e-mail at jogletree@csallc.com.

Sincerely,

/Jon Michael Ogletree/
Jon Michael Ogletree
Chief Financial Officer
Cahaba Safeguard Administrators, LLC

CC: Randy Heal, President, Cahaba Safeguard Administrators, LLC
Jon Michael Ogletree, Chief Financial Officer, Cahaba Safeguard Administrators, LLC
Monique Houser, Compliance Officer, Cahaba Safeguard Administrators, LLC

October 16, 2020

Department of Health and Human Services
Office of Inspector General
Office of Audit Services
Attention: Jenenne Tambke, Assistant Regional Inspector General for Audit Services
Region VII
601 East 12th Street, Room 0429
Kansas City, Missouri 64106

RE: Report Number A-07-19-00578 Cahaba Safeguard Administrators, LLC, Claimed Some Unallowable Medicare Postretirement Benefit Costs Through Its Incurred Cost Proposals

Dear Ms. Tambke,

As set forth in more detail below, management of Cahaba Safeguard Administrators, LLC ("Cahaba CSA") does not concur with the OIG's finding in its draft audit report that Cahaba CSA incorrectly calculated allocable PRB costs for contract years 2014 – 2016.

- The OIG's draft audit report states that Cahaba CSA used an incorrect methodology when claiming PRB costs for Medicare reimbursement. Specifically, the draft report provides that "Cahaba CSA incorrectly calculated its allocable PRB costs using the accrual method instead of the pay-as-you-go method." It is important to note that an accrual method is an appropriate method provided the guidelines contained within FAR 31.205-6(o)(2)(iii) are satisfied.
- The rationale for the OIG's finding is not explained within the draft report and, therefore, the basis for the OIG's finding is unclear. However, based upon our communications with the OIG leading up to the draft audit report, we believe the OIG's finding that Cahaba CSA incorrectly calculated the PRB costs using the accrual method instead of the pay-as-you-go method is based on the OIG's concern over the effectiveness of the restriction on Cahaba CSA's retiree medical account under FAR 31.205-6(o)(2)(iii)(B). FAR 31.205-6(o)(2)(iii)(B) states that accrued PRB costs must be "[b]e paid to an insurer or trustee to establish and maintain a fund or reserve for the sole purpose of providing PRB to retirees. The assets shall be segregated in the trust, or otherwise effectively restricted, so that they cannot be used by the employer for other purposes."
- We note that the summary citation to FAR 31.205-6(o) included in Appendix B of the draft report states "[f]ederal regulations (FAR 31.205-6(o)) require that PRB cost be determined in accordance with SFAS 106 and funded into a dedicated trust fund, such as a Voluntary Employee Benefit Association trust." It appears the OIG's position is that the use of a trust (such as a VEBA) is required and funds cannot be effectively restricted unless held in a trust. The OIG's position is (a) inconsistent with the wording of the FAR and (b) contradicts our previous discussions with CMS regarding the arrangement and the use of an accrual method.

- In order to comply with the specific guidance to use an accrual method as set forth in FAR 31.205-6(o)(2)(iii), (including effective restriction of funds), the following steps were taken:
  - Healthcare Business Solutions, LLC ("HBS"), Cahaba CSA's parent company, paid PRB funds to its insurer, Blue Cross and Blue Shield of Alabama ("BCBSAL"), in order to establish and maintain a fund for the sole purpose of providing PRB to retirees.
  - A written agreement was entered into between HBS and BCBSAL which set forth the terms and conditions regarding the use of the funds paid by HBS to BCBSAL, a copy of which is enclosed herewith as Exhibit A (the "Agreement"). Paragraph 1 of the Agreement states "[t]he Restricted account will be used for the sole purpose of providing RMP benefits to and paying premiums for participants and is, therefore, not to be used for any other purpose." Paragraph 1 also provides that it is "HBS's intent that the Restricted Account meets the requirements for Federal Acquisition Regulations ("FAR") as well as the requirements for United States Generally Accepted Accounting Principles as prescribed by Accounting Standards Codification 715 and any Internal Revenue Service tax code requirements." Furthermore, Paragraph 4 of the Agreements states, "[f]unds will not be withdrawn for any other purpose other than for benefit or premium payments for the RMP." The Agreement is unambiguous that the funds cannot be used "for any purpose" other than "for benefit or premium payments for the RMP."
  - The PRB funds are held by BCBSAL in a money market account owned and controlled by BCBSAL as the insurer. The funds are not owned by HBS or Cahaba CSA and neither HBS nor Cahaba CSA (or any of their subsidiaries) have any access to these funds.
  - As noted in the minutes from the meeting of the Audit Committee of the BCBSAL Board of Directors (the "BCBSAL Audit Committee") held on July 21, 2015, the BCBSAL Audit Committee approved the funding arrangement and purpose of the funds received from HBS. The minutes of such BCBSAL Audit Committee expressly provide that the "account would be strictly used to pay HBS' retiree medical expenses." A copy of such Audit Committee minutes are attached hereto as Exhibit B. Like the Agreement, the BCBSAL Audit Committee minutes are unambiguous that the funds are to be "strictly used" for retiree medical expenses.
  - In addition to the operational steps above, the Agreement and use of an accrual method was discussed directly with CMS in 2015.
    - A copy of the Agreement was provided via email to the CMS Office of the Actuary in August 2015.
    - Another email communication from September 2015 includes CMS Office of the Actuary specifically asking a question to confirm the accounting effective date. The Company's response to this question states the accounting method was the "accrued method."
    - A copy of the BCBSAL Alabama Audit Committee minutes documenting Board approval of the restricted funding arrangement was provided to the CMS Office of the Actuary in September 2015.

- HBS proceeded with the Agreement and use of the accrual method since both were fully disclosed and discussed with CMS and CMS, raising no objections or concerns, seemingly approved of the arrangement. [1]

- As noted above, FAR 31.205-6(o)(2)(iii)(B) states that accrued PRB costs must be "[b]e paid to an insurer or trustee to establish and maintain a fund or reserve for the sole purpose of providing PRB to retirees. The assets shall be segregated in the trust, or otherwise effectively restricted, so that they cannot be used by the employer for other purposes (emphasis added)." Although the use of a VEBA or trust may be more common, the FAR does not mandate the use of a trust in order to use an accrual method. In addition to a VEBA or trust, funds may also be "paid to an insurer" or "otherwise effectively restricted" so that they cannot be used for any other purpose. The purpose of the Agreement is to ensure that the funds paid by HBS to BCBSAL are (a) "paid to an insurer" and (b) "effectively restricted", so that they cannot be used for purposes other than providing PRB to retirees. The Agreement and Audit Committee minutes are clear that the funds paid by HBS (the employer) to BCBSAL (the insurer) can only be used for one purpose, to pay for retiree medical expenses.
- Although not addressed in the draft audit report, in the discussions leading up to the draft report, the OIG auditors communicated that the BCBSAL board level approval is a reason they believe the funds are not effectively restricted. They argued that HBS' management could change the agreement at any time and gain access to the funds held by BCBSAL. We disagree. The Agreement does not give HBS the unilateral right to terminate the Agreement (only BCBSAL has the unilateral right to terminate the Agreement). Furthermore, even if BCBSAL were to terminate the Agreement, the Agreement specifies that the funds will be transferred to a VEBA or trust. If HBS does not transfer the funds to a VEBA or trust, HBS is required to terminate the retiree medical plan and treat any surplus assets in accordance with paragraph 5 of the Agreement, which would require a return to CMS of any required amounts in accordance with FAR 31.205-6(o)(2)(iii)(G)(5).

We ask that the OIG and CMS revisit the FAR and the requirements set forth therein in order to utilize the accrual method. In addition, we also ask that the OIG review the 2015 communications (submitted with this response as Exhibit C) between HBS and CMS regarding how HBS intended to satisfy the FAR's requirements to use of the accrual method. We strongly believe that the account is effectively restricted per the requirements of the FAR and that any position by OIG that would retroactively disallow PRB cost would be inequitable given the fact that the details of the Agreement and intended use of an accrual method were fully disclosed to and discussed with CMS in 2015 during implementation. Not being made aware of government concerns we were unable to revise the practice to remove government concerns and avoid substantial analysis of potential cost disallowances.

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[1] We note that CMS would have no reason to disagree with HBS' use of the accrual method since the FAR supports the arrangement described by HBS to CMS.

If you should have questions regarding this report, please contact Jon-Michael Ogletree, CFO, at (205)-820-6012 or via e-mail at jogletree@csallc.com.

Sincerely,

/Randy Heal/
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