



Office of Audit Services, Region IV  
61 Forsyth Street, SW, Suite 3T41  
Atlanta, GA 30303

March 16, 2011

Report Number: A-04-07-00031

Mr. Steve Bishop  
Director of Finance  
CIGNA Government Services  
Two Vantage Way  
Nashville, TN 37228

Dear Mr. Bishop:

Enclosed is the U.S. Department of Health & Human Services (HHS), Office of Inspector General (OIG), final report entitled *Review of CIGNA Government Services Part B Final Administrative Cost Proposals for Fiscal Years 2004 Through 2006*. We will forward a copy of this report to the HHS action official noted on the following page for review and any action deemed necessary.

The HHS action official will make final determination as to actions taken on all matters reported. We request that you respond to this official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

Section 8L of the Inspector General Act, 5 U.S.C. App., requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at <http://oig.hhs.gov>.

If you have any questions or comments about this report, please do not hesitate to call me at (404) 562-7800, or contact Eric Bowen, Audit Manager, at (404) 562-7789 or through email at [Eric.Bowen@oig.hhs.gov](mailto:Eric.Bowen@oig.hhs.gov). Please refer to report number A-04-07-00031 in all correspondence.

Sincerely,

/John T. Drake, Sr./for  
Peter J. Barbera  
Regional Inspector General  
for Audit Services

Enclosure

**Direct Reply to HHS Action Official:**

Nanette Foster Reilly  
Consortium Administrator  
Consortium for Financial Management & Fee for Service Operations (CFMFFSO)  
Centers for Medicare & Medicaid Services  
601 East 12<sup>th</sup> Street, Room 235  
Kansas City, MO 64106

**Department of Health & Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF CIGNA  
GOVERNMENT SERVICES PART B  
FINAL ADMINISTRATIVE COST  
PROPOSALS FOR FISCAL YEARS  
2004 THROUGH 2006**



**Daniel R. Levinson  
Inspector General**

**March 2011  
A-04-07-00031**

# *Office of Inspector General*

<http://oig.hhs.gov>

---

The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health & Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

## *Office of Audit Services*

The Office of Audit Services (OAS) provides auditing services for HHS, either by conducting audits with its own audit resources or by overseeing audit work done by others. Audits examine the performance of HHS programs and/or its grantees and contractors in carrying out their respective responsibilities and are intended to provide independent assessments of HHS programs and operations. These assessments help reduce waste, abuse, and mismanagement and promote economy and efficiency throughout HHS.

## *Office of Evaluation and Inspections*

The Office of Evaluation and Inspections (OEI) conducts national evaluations to provide HHS, Congress, and the public with timely, useful, and reliable information on significant issues. These evaluations focus on preventing fraud, waste, or abuse and promoting economy, efficiency, and effectiveness of departmental programs. To promote impact, OEI reports also present practical recommendations for improving program operations.

## *Office of Investigations*

The Office of Investigations (OI) conducts criminal, civil, and administrative investigations of fraud and misconduct related to HHS programs, operations, and beneficiaries. With investigators working in all 50 States and the District of Columbia, OI utilizes its resources by actively coordinating with the Department of Justice and other Federal, State, and local law enforcement authorities. The investigative efforts of OI often lead to criminal convictions, administrative sanctions, and/or civil monetary penalties.

## *Office of Counsel to the Inspector General*

The Office of Counsel to the Inspector General (OCIG) provides general legal services to OIG, rendering advice and opinions on HHS programs and operations and providing all legal support for OIG's internal operations. OCIG represents OIG in all civil and administrative fraud and abuse cases involving HHS programs, including False Claims Act, program exclusion, and civil monetary penalty cases. In connection with these cases, OCIG also negotiates and monitors corporate integrity agreements. OCIG renders advisory opinions, issues compliance program guidance, publishes fraud alerts, and provides other guidance to the health care industry concerning the anti-kickback statute and other OIG enforcement authorities.

# *Notices*

---

**THIS REPORT IS AVAILABLE TO THE PUBLIC**  
at <http://oig.hhs.gov>

Section 8L of the Inspector General Act, 5 U.S.C. App., requires that OIG post its publicly available reports on the OIG Web site.

## **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.

## **EXECUTIVE SUMMARY**

### **BACKGROUND**

Title XVIII of the Social Security Act established the Health Insurance for the Aged and Disabled (Medicare) program, which provides for a hospital insurance program (Part A) and a related supplementary medical insurance program (Part B). The Part B program includes certain medical equipment and related services, including durable medical equipment and other medical services. The Centers for Medicare & Medicaid Services (CMS) administers the Medicare program by contracting with private organizations to process and pay claims for services provided to eligible beneficiaries.

CIGNA is a holding company for Connecticut General Life Insurance Company, the legal entity that holds the Medicare contracts. CIGNA HealthCare, one of the main lines of business (also called operating divisions), administered the Medicare contracts via CIGNA Government Services, a wholly owned subsidiary of CIGNA. During the period October 1, 2003, through September 30, 2006, CMS contracted with CIGNA to serve as the Medicare Part B carrier for the States of Tennessee, North Carolina, and Idaho.

CIGNA's Medicare Part B carrier contract with CMS provided for reimbursement of allowable administrative costs incurred. Such administrative costs include the direct costs of administering the contract as well as allocations of certain indirect costs of services or assets used by Medicare and other entities. CIGNA claimed reimbursement of administrative costs through submission to CMS of a Final Administrative Cost Proposal (FACP). For October 1, 2003, through September 30, 2006 (fiscal years (FY) 2004 through 2006), CIGNA claimed \$139,296,260, including \$69,886 in forward funding, in reimbursement for direct and indirect costs related to its Medicare Part B carrier contract.

### **OBJECTIVE**

Our objective was to determine whether the administrative costs claimed on CIGNA's Part B FACPs for FYs 2004 through 2006 were reasonable, allocable, and allowable for Medicare reimbursement.

### **SUMMARY OF FINDINGS**

Of the \$139,226,374 in administrative costs reviewed, CIGNA appropriately claimed \$138,656,789 on its FACPs for FYs 2004 through 2006. However, we identified \$569,585, composed of \$47,757 of direct costs and \$521,828 in indirect costs that CIGNA did not support as reasonable, allocable, or allowable for Medicare reimbursement because it did not comply with Federal requirements for maintaining adequate accounting records covering the use of funds.

## **RECOMMENDATIONS**

We recommend that CIGNA:

- reduce direct costs claimed on its FACPs by \$47,757,
- reduce indirect costs claimed on its FACPs by \$521,828, and
- strengthen its procedures for maintaining documentation to support costs included on its FACPs.

## **CIGNA COMMENTS**

In comments on our draft report, CIGNA agreed with most of our findings, except for those related to caption accounts 1709 (Legal Services/Fees) and 1494 (Hardware/Software Maintenance). CIGNA stated that unallowable legal expenses were accumulated in the expense center Outside Counsel SEC Law – Central (expense center 5000151T), and it agreed with removal of this expense center. However, because of this removal, caption account 1709 would no longer include unallowable legal fees. Accordingly, CIGNA did not agree that the entire caption account (1709) should be excluded. With regard to caption account 1494 (Hardware/Software Maintenance), CIGNA stated that it obtained and would provide invoices supporting expenses we identified as unsupported. It believed that the additional documentation would show that these expenses were allowable for allocation to CIGNA Government Services.

CIGNA's comments are included in their entirety as Appendix D.

## **OFFICE OF INSPECTOR GENERAL RESPONSE**

We concurred with CIGNA's comments regarding caption account 1709 (Legal Services/Fees), and we revised the report to allow caption account 1709 expenses, except expense center 5000151T, as pooled expenses allocable to the Medicare contract. With regard to caption account 1494 (Hardware/Software Maintenance), CIGNA did not provide invoices supporting these expenses with its comments to the draft report. Therefore, we could not determine whether these expenses were allowable for allocation to CIGNA Government Services, and we maintain that caption account 1494 is not allocable to Medicare.

**TABLE OF CONTENTS**

	<u>Page</u>
<b>INTRODUCTION</b> .....	1
<b>BACKGROUND</b> .....	1
Medicare Program.....	1
Connecticut General Life Insurance Company Medicare Contract.....	1
Prior Audit of CIGNA’s Corporate Cost Allocation Methodology.....	1
CIGNA’s Methodology for Allocating Costs.....	1
<b>OBJECTIVE, SCOPE, AND METHODOLOGY</b> .....	2
Objective.....	2
Scope .....	2
Methodology.....	2
<b>FINDINGS AND RECOMMENDATIONS</b> .....	4
<b>FEDERAL REQUIREMENTS</b> .....	4
<b>DIRECT COSTS NOT SUPPORTED</b> .....	5
<b>INDIRECT COSTS NOT SUPPORTED AS REASONABLE, ALLOCABLE,     AND ALLOWABLE</b> .....	5
<b>RECOMMENDATIONS</b> .....	6
<b>CIGNA COMMENTS</b> .....	6
<b>OFFICE OF INSPECTOR GENERAL RESPONSE</b> .....	7
<b>OTHER MATTERS</b> .....	7
 <b>APPENDIXES</b>	
A: SAMPLING METHODOLOGY	
B: CIGNA’S PART B ADMINISTRATIVE COSTS CLAIMED FOR FISCAL YEARS 2004 THROUGH 2006	
C: RESULTS OF REVIEW OF CIGNA’S PART B ADMINISTRATIVE COSTS FOR FISCAL YEARS 2004 THROUGH 2006	
D: CIGNA COMMENTS	

## INTRODUCTION

### BACKGROUND

#### Medicare Program

Title XVIII of the Social Security Act established the Health Insurance for the Aged and Disabled (Medicare) program, which provides for a hospital insurance program (Part A) and a related supplementary medical insurance program (Part B). The Part B program includes certain medical equipment and related services, including durable medical equipment and other medical services. The Centers for Medicare & Medicaid Services (CMS) administers the Medicare program by contracting with private organizations to process and pay claims for services provided to eligible beneficiaries.

#### Connecticut General Life Insurance Company Medicare Contract

CIGNA is a holding company for Connecticut General Life Insurance Company, the legal entity that holds the Medicare contracts. CIGNA HealthCare (CHC), one of the main lines of business (also called operating divisions), administered the Medicare contracts via CIGNA Government Services, a wholly owned subsidiary of CIGNA. During the period October 1, 2003, through September 30, 2006, CMS contracted with CIGNA to serve as the Medicare Part B carrier for the States of Tennessee, North Carolina, and Idaho.

CIGNA's Medicare Part B carrier contract with CMS provided for reimbursement of allowable administrative costs incurred. Such administrative costs include the direct costs of administering the contract as well as allocations of certain indirect costs of services or assets used by Medicare and other entities. CIGNA claimed reimbursement of administrative costs through submission to CMS of a Final Administrative Cost Proposal (FACP). For October 1, 2003, through September 30, 2006 (fiscal years (FY) 2004 through 2006), CIGNA claimed \$139,296,260 in reimbursement for direct and indirect costs related to its Medicare Part B carrier contract.

#### Prior Audit of CIGNA's Corporate Cost Allocation Methodology

The Office of Inspector General (OIG) previously addressed CIGNA's corporate cost allocation methodology in a report entitled *Review of CIGNA HealthCare Medicare Administration's Proposed Corporate Cost Allocation Methodology*. OIG considered the allocation methodology to be reasonable, but it determined that the allocation system should be reviewed yearly to ensure a reasonable allocation to Medicare.

#### CIGNA's Methodology for Allocating Costs

For FYs 2004 through 2006, CIGNA used the previously reviewed cost allocation methodology as described in general below.

CIGNA uses caption accounts and expense centers to group costs for allocation. A caption account is used to record and summarize similar expenses (e.g., caption account 0801, Salaries-

FT Benefit Eligible, records salaries for full-time employees). The caption accounts are equivalent to a chart of accounts used in the general ledger. Expenses are accumulated by caption account (type of expense) and expense center (business unit).

CIGNA allocated indirect expenses to Medicare using three expense pools representing actual overhead expenses:

- a pool of corporate expenses (CIGNA pool),
- a pool of CIGNA HealthCare division expenses (CHC pool), and
- a pool of CIGNA Information Technology (CIT) expenses (CIT pool).

CIGNA allocated expenses in the CIGNA pool and CHC pool to its operating divisions, including Medicare, based on a ratio of total Medicare expenses to total divisional expenses. CIGNA allocated expenses in the CIT pool to its operating divisions, including Medicare, based on utilization rates developed by CIT.

## **OBJECTIVE, SCOPE, AND METHODOLOGY**

### **Objective**

Our objective was to determine whether the administrative costs claimed on CIGNA's Part B FACPs for FYs 2004 through 2006 were reasonable, allocable, and allowable for Medicare reimbursement.

### **Scope**

Our review was limited to \$139,226,374 in direct and indirect administrative costs claimed by CIGNA on its FACPs submitted to CMS for FYs 2004 through 2006. We did not review \$69,886 in forward funding claimed because the funds had not yet been expended at the time of our audit.

We limited our internal control review to controls related to the recording and reporting of costs on the FACPs. We accomplished our objectives through substantive testing.

We conducted our fieldwork at CIGNA offices in Nashville, Tennessee.

### **Methodology**

To accomplish our objective, we:

- reviewed applicable Medicare laws, regulations, and guidelines including the Federal Acquisition Regulation (FAR) section 31.201-2(d); the Medicare Financial Management Manual, Chapter 2, section 190.3; and CIGNA's contract with CMS;

- reconciled FACPs from FYs 2004 through 2006 to CIGNA’s accounting records;
- interviewed CIGNA officials about its cost accumulation processes for FACPs and gained an understanding of its cost allocation systems;
- tested direct salaries and wages by selecting a stratified random sample of 105 monthly employee salary payments (Appendix A) and by:
  - tracing the payments to payroll journals, corporate bonus plans, and personnel records;
  - verifying the amount paid was consistent with the employee’s pay rate;
  - verifying the salary was charged to the correct expense center;
  - reconciling the number of hours paid to time sheets; and
  - reviewing approvals of time sheets;
- tested certain other direct costs by selecting 11 caption accounts, judgmentally sampling 30 expense items in each selected caption account, and tracing these 330 expense items to supporting documents including invoices, expense vouchers, reports, and journal entries;<sup>1</sup>
- tested certain other direct costs by selecting two caption accounts and tracing all expense items to supporting documents including invoices, reports, and journal entries;<sup>2</sup>
- reviewed CIGNA’s corporate cost allocation methodology, including comparing it to the previously reviewed methodology and reviewing the accuracy and consistency of allocation calculations during the audit period;
- performed a general review of indirect cost allocations for reasonableness and allocability to Medicare by ensuring consistency of all 568 expense centers for FY 2004 with prior OIG audit findings and by obtaining explanations for new and deleted expense centers;
- tested indirect costs by judgmentally sampling 88 expense centers for FYs 2005 and 2006 and reviewing them for reasonableness and allocability to Medicare;<sup>3</sup>
- tested indirect costs by judgmentally sampling 41 caption accounts for FYs 2004, 2005, and 2006 and reviewing them for reasonableness and allocability to Medicare;<sup>4</sup> and

---

<sup>1</sup> We selected these caption accounts based on materiality and variance analysis.

<sup>2</sup> We selected these caption accounts based on materiality and variance analysis.

<sup>3</sup> We selected these expense centers based on materiality and variance analysis.

<sup>4</sup> We selected these caption accounts based on the nature of the account.

- provided our audit adjustments to the indirect cost pools to CIGNA and requested that CIGNA revise its cost allocations accordingly to determine the total unallowable expenses allocated to Medicare based on CIGNA’s methodology for allocating costs.

See Appendix A for details on our sampling methodology, Appendix B for costs claimed, and Appendix C for results of review.

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 objective.

## **FINDINGS AND RECOMMENDATIONS**

Of the \$139,226,374 in administrative costs reviewed, CIGNA appropriately claimed \$138,656,789 on its FACPs for FYs 2004 through 2006. However, we identified \$569,585, composed of \$47,757 of direct costs and \$521,828 in indirect costs that CIGNA did not support as reasonable, allocable, or allowable for Medicare reimbursement because it did not comply with Federal requirements for maintaining adequate accounting records covering the use of funds.

### **FEDERAL REQUIREMENTS**

The contract between CMS and CIGNA set forth principles of reimbursement for administrative costs. The contract cited the FAR, Title 48, Chapter 1 of the CFR, as regulatory principles to be followed for application to the Medicare contract and provided additional guidelines for specific cost areas.

FAR 31.201-2(d) (48 CFR § 31.201-2(d)) states that CIGNA is responsible for “...maintaining records, including supporting documentation, adequate to demonstrate that costs claimed have been incurred, are allocable to the contract, and comply with applicable cost principles....”

Additionally, Chapter 2 section 190.3 of the *Medicare Financial Management Manual* states that the contractor must maintain records “...in such detail as will properly reflect all net costs, direct and indirect, ... for which reimbursement is claimed under the provisions of the agreement.”

Pursuant to FAR 31.201-4 (48 CFR § 31.201-4), which establishes guidelines for determining allocability of contract costs, 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.”

FAR 31.202(a) (48 CFR § 31.202(a)) states, “All costs specifically identified with other final cost objectives of the contractor are direct costs of those cost objectives and are not to be charged to the contract directly or indirectly.”

FAR 31.204(a) (48 CFR § 31.204(a)) states that “[c]osts are allowable to the extent they are reasonable, allocable, and determined to be allowable....”

### **DIRECT COSTS NOT SUPPORTED**

The majority of the direct costs claimed on the FACPs were adequately supported. However, contrary to 48 CFR § 31.201-2(d), CIGNA did not provide any supporting documentation for direct costs totaling \$47,757 as follows:

- \$16,009 claimed in FY 2006 for outside professional services and
- \$31,748 claimed in FYs 2004 through 2006 for depreciation expenses.

### **INDIRECT COSTS NOT SUPPORTED AS REASONABLE, ALLOCABLE, OR ALLOWABLE**

The majority of the indirect costs claimed on the FACPs were adequately supported and allowable. However, the expense pools used to allocate corporate expenses to Medicare included executive compensation and various other expenses in two expense centers and two caption accounts that were not supported or were not allocable to Medicare and were therefore unallowable for Medicare reimbursement. In total, these expense pools included approximately \$20.9 million in unallowable expenses, resulting in unallowable Medicare reimbursement of \$521,828, including:

- Executive compensation included bonuses in various expense centers. Contrary to 48 CFR § 31.201-2(d), CIGNA did not provide support demonstrating how the bonus amounts were determined or that they were reasonable. Therefore, these bonuses, totaling \$14,064,765, should not have been included in the expense pools used to allocate expenses to Medicare.
- Contrary to 48 CFR § 31.201-4 and § 31.202(a), the following two expense centers were not supported as allocable to the Medicare contract and were, therefore, unallowable:
  - Outplacement Central (expense center 5000130T) accumulates non-executive outplacement expenses related to outside party services. These expenses, totaling \$2,700,556 for FYs 2004 and 2005, are not considered allocable to Medicare.
  - Outside Counsel SEC Law – Central (expense center 5000151T) accumulates unallowable legal expenses associated with SEC finance and tax law. These expenses, totaling \$534,365 for FYs 2004, 2005, and 2006, are not considered allocable to Medicare.
- Contrary to 48 CFR § 31.201-2(d), CIGNA did not provide any support for two caption accounts. Because we could not evaluate the extent to which these costs were reasonable, allocable, and allowable as required by 48 CFR § 31.204(a), the following caption accounts should be excluded from the indirect costs allocated to Medicare:

- Hardware/Software Maintenance (caption account 1494) accumulates costs for computer related hardware and software maintenance. These expenses, totaling \$3,086,556 for FYs 2005 and 2006, are not considered allowable for Medicare reimbursement.
- HR&S Warehousing (caption account 2305) accumulates warehousing costs. These expenses, totaling \$550,882 for FYs 2005 and 2006, are not considered allowable for Medicare reimbursement.

CIGNA's removal from the indirect cost pools of the \$20,937,124 in expenses and its revision of the indirect cost allocations<sup>5</sup> reduced indirect costs allocable to Medicare by \$721,245.<sup>6</sup> Of this amount, \$521,828 related to its Part B contract and \$199,417 related to its Durable Medical Equipment Regional Carrier contract.<sup>7</sup>

## RECOMMENDATIONS

We recommend that CIGNA:

- reduce direct costs claimed on its FACPs by \$47,757,
- reduce indirect costs claimed on its FACPs by \$521,828, and
- strengthen its procedures for maintaining documentation to support costs included on its FACPs.

## CIGNA COMMENTS

In comments on our draft report, CIGNA agreed with most of our findings, except for those related to caption accounts 1709 (Legal Services/Fees) and 1494 (Hardware/Software Maintenance). CIGNA stated that unallowable legal expenses were accumulated in the expense center Outside Counsel SEC Law – Central (expense center 5000151T), and it agreed with removal of this expense center. However, because of this removal, caption account 1709 would no longer include unallowable legal fees. Accordingly, CIGNA did not agree that the entire caption account (1709) should be excluded. With regard to caption account 1494 (Hardware/Software Maintenance), CIGNA stated that it obtained and would provide invoices supporting expenses we identified as unsupported. It believed that the additional documentation would show that these expenses were allowable for allocation to CIGNA Government Services.

---

<sup>5</sup> See the *Background* section above for CIGNA's *Methodology for Allocating Costs*.

<sup>6</sup> This amount is composed of \$174,541 and \$546,704 per CIGNA's Impact Summary at Appendix D.

<sup>7</sup> See CIGNA's Impact Summary at Appendix D and the Office of Inspector General report number A-04-07-00032, *Review of CIGNA Government Services Durable Medical Equipment Regional Carrier Final Administrative Cost Proposals for Fiscal Years 2004 Through 2006*.

CIGNA's comments are included in their entirety as Appendix D.

## **OFFICE OF INSPECTOR GENERAL RESPONSE**

We concurred with CIGNA's comments regarding caption account 1709 (Legal Services/Fees), and we revised the report to allow caption account 1709 expenses, except expense center 5000151T, as pooled expenses allocable to the Medicare contract. With regard to caption account 1494 (Hardware/Software Maintenance), CIGNA did not provide invoices supporting these expenses with its comments to the draft report. Therefore, we could not determine whether these expenses were allowable for allocation to CIGNA Government Services, and we maintain that caption account 1494 is not allocable to Medicare.

## **OTHER MATTERS**

As identified in the previous Office of Inspector General audit of CIGNA's Part B costs, CIGNA's corporate capitalization policy is not consistent with Appendix B of its CMS contract, and CIGNA's software capitalization policy is not consistent with Federal criteria.

# **APPENDIXES**

## **APPENDIX A: SAMPLING METHODOLOGY**

### **POPULATION**

The population consisted of 22,994 “employee months” related to \$74,923,351 in Part B salaries and wages that were charged to Medicare from October 1, 2003, through September 30, 2006. An “employee month” included one employee’s salaries, wages, and related fringe benefits for one month.

### **SAMPLING FRAME**

For fiscal years (FYs) 2004, 2005, and 2006, we obtained three Microsoft Excel files detailing the individual employees’ monthly salaries and wages that were recorded as expenses in general ledger salary account code 0801 and charged to Medicare on the Final Administrative Cost Proposal (FACP). Total salaries and wages for each of the 3 FYs were reconciled to the related general ledger and FACP.

The sampling frame included:

- 7,208 “employee months” related to Part B salary and wages of \$22,604,278 for FY 2004,
- 7,810 “employee months” related to Part B salary and wages of \$25,193,555 for FY 2005, and
- 7,976 “employee months” related to Part B salary and wages of \$27,125,518 for FY 2006.

### **SAMPLE UNIT**

The sample unit was an “employee month.”

### **SAMPLE DESIGN**

We used a stratified random sample of “employee months” from the general ledger salary and wages account (0801) for FYs 2004, 2005, and 2006. Each FY represented a separate stratum.

### **SAMPLE SIZE**

We selected a sample of 105 “employee months” by selecting 35 items from each of the 3 FYs (2004, 2005, and 2006).

### **SOURCE OF THE RANDOM NUMBERS**

We used the Office of Inspector General, Office of Audit Services (OIG/OAS) statistical software to generate the random numbers.

**APPENDIX B: CIGNA'S PART B ADMINISTRATIVE COSTS CLAIMED FOR  
FISCAL YEARS 2004 THROUGH 2006**

	<b>FY 2004 Expenses Claimed</b>	<b>FY 2005 Expenses Claimed</b>	<b>FY 2006 Expenses Claimed</b>	<b>Total Expenses Claimed</b>
Salaries & Wages	\$21,370,227	\$22,927,239	\$24,682,148	\$68,979,614
Fringe Benefits	5,922,240	6,905,439	7,868,377	20,696,056
Facilities or Occupancy	2,793,986	3,362,264	3,194,754	9,351,004
EDP Equipment	8,690,087	8,851,860	7,970,153	25,512,100
Subcontracts	173,279	78,394	57,188	308,861
Outside Professional Services	311,822	569,474	824,102	1,705,398
Telephone & Telegraph	383,591	301,790	224,804	910,185
Postage and Express	9,085,425	11,098,724	7,155,840	27,339,989
Furniture & Equipment	288,755	325,566	259,590	873,911
Materials & Supplies	679,567	609,597	562,627	1,851,791
Travel	268,946	279,362	280,481	828,789
Return on Investment	279,342	306,970	275,166	861,478
Miscellaneous	4,137,971	4,061,124	4,445,999	12,645,094
Other	0	0	0	0
Credits	(9,899,809)	(10,536,049)	(12,202,038)	(32,637,896)
Forward Funding	0	63,349	6,537	69,886
<b>Total</b>	<b>\$44,485,429</b>	<b>\$49,205,103</b>	<b>\$45,605,728</b>	<b>\$139,296,260</b>

**APPENDIX C: RESULTS OF REVIEW OF CIGNA'S PART B ADMINISTRATIVE  
COSTS FOR FISCAL YEARS 2004 THROUGH 2006**

<b>Fiscal Year</b>	<b>Total Expenses Claimed</b>	<b>Total Expenses Deferred</b>	<b>Total Expenses Reviewed</b>	<b>Total Allowable Expenses</b>	<b>Total Unallowable Expenses</b>
2004	\$44,485,429	\$0	\$44,485,429	\$44,394,438	\$90,991
2005	49,205,103	63,349	49,141,754	48,869,440	272,314
2006	45,605,728	6,537	45,599,191	45,392,911	206,280
<b>Total</b>	<b>\$139,296,260</b>	<b>\$69,886</b>	<b>\$139,226,374</b>	<b>\$138,656,789</b>	<b>\$569,585</b>



May 27, 2010

Routing 795  
Two Vantage Way  
Nashville, TN 37221  
Telephone 615-782-4616  
Facsimile 615-252-3650  
stephen.bishop@cigna.com

Peter J. Barbera  
Regional Inspector General for Audit Services  
Office of Audit Services, Region IV  
61 Forsyth Street, SW, Suite 3T1  
Atlanta, GA 30303

Re: Audit Report No. A-04-07-00031

Dear Mr. Barbera:

This letter is in response to Audit Report No. A-04-07-00031, which noted an overstatement of claimed costs on our Title XVIII Part B contract for the fiscal years 2004 – 2006 of \$569,585. The report indicates \$47,757 of unallowable direct costs and \$521,828 of unallowable indirect costs.

CGS agrees with the two findings associated with the direct costs and will reduce our claimed costs as follows:

- \$16,009 in FY 2006 for outside professional services and;
- \$10,511 in FY 2004, \$5,498 in FY 2005 and \$12,699 in FY 2006 for depreciation expenses.

As noted in the OIG report, the majority of the indirect costs claimed on the FACPs were adequately supported and allowable. However, the expense pools used to allocate corporate expenses to CGS included executive compensation and various other expenses in two expense centers and three caption accounts that were deemed by the OIG to be not supported or not allocable to CGS and were therefore noted as unallowable for Medicare reimbursement. In total, these expense pools included about \$20.9 million in unallowable expenses, including:

- Executive compensation included bonuses in various expense centers – CGS agrees with this finding and removal of these bonuses, totaling \$14,064,765 for FY 2004;

May 27, 2010  
Page 2

- Outplacement Central (expense center 5000130T) – this expense center accumulates non-executive outplacement expenses related to outside party services. CGS agrees with this finding and removal of these expenses, totaling \$2,700,556 for FYs 2004 and 2005;
- Outside Counsel SEC Law – Central (expense center 5000151T) – this expense center accumulates unallowable legal expenses associated with SEC finance and tax law. CGS agrees with this finding and removal of these expenses, totaling \$534,365 for FYs 2004, 2005, and 2006;
- Legal Services/Fees (caption account 1709) – this caption account accumulates costs for general legal services. CGS does not agree that this entire caption account should be excluded and had agreed to exclude EC 5000151T noted above, which includes costs in caption account 1709, but not to exclude the entire 1709 caption account;
- Hardware/Software Maintenance (caption account 1494) – this caption account accumulates costs for computer related hardware and software maintenance. CGS agrees with this finding as being not supported during the audit, however, we have been able to obtain supporting documents for expenses in this caption account and will provide to the OIG. Pending approval of this support we have included these expenses as unallocable to CGS, totaling \$3,086,556 for FYs 2005 and 2006 (see further discussion below);
- HR&S Warehousing (caption account 2305) – this caption account accumulates warehousing costs. CGS agrees with this finding and removal of these expenses, totaling \$550,882.

The attached schedule shows each of the individual findings noted above, by fiscal year, and the resulting impact on the home office allocation to CGS and the allocation of the findings to the Part B and DMERC contracts.

The exclusion of the \$20.9 million from the expenses pools results in unallowable Medicare reimbursement of \$721,245, of which \$521,828 would be allocated to the Part B contract. The total amount deemed unallowable or unallocable for Medicare reimbursement is \$769,002 of which \$569,585 would be allocated to the Part B contract. CGS will adjust its claimed expenses on the Part B contract based on the attached schedule, pending resolution of the item noted below.

#### **Additional Discussion of Finding on Caption Account 1494**

Caption account 1494 was deemed not allowable, allocable, or reasonable due to lack of support during the audit fieldwork. In particular it was noted there was a substantial increase in the expense recorded in this caption account from 2004 to 2005 and 2006. In researching the increase, CGS identified that the majority of expense in this caption account resides in the CIT hierarchy and is therefore a component of the IT adjustment factor.

May 27, 2010  
Page 3

In 2005, 85% of the expense in caption account 1494 in the CIT hierarchy was charged to expense center 8621. In 2006, 39% of the expense in the caption account was charged to expense center 8621 and 38% was charged to expense center 93C3 for a total of 77% coverage.

Both expense centers 8621 and 93C3 capture IT "Enterprise Expenses." Enterprise expense represents costs of goods or services for all of CIGNA. The expenses are not specifically identifiable to one segment but are instead costs associated with IT infrastructure and management. Examples of these types of costs would be data networks, information protection, and Chief Information Officer.

CGS has obtained invoices that support the expenses in the above referenced expense centers. The majority of these invoices are for maintenance on infrastructure equipment. CGS believes these expenses are allowable for allocation to CGS and subsequent Medicare reimbursement and will provide invoices in support of this caption account to the OIG. Further, CGS has identified that in 2005 CIGNA obtained two dedicated maintenance technicians from IBM which resulted in approximately \$500,000 of additional expense over the prior year. This was a change from the prior year as CIGNA had not used IBM technicians previously that were fully dedicated to CIGNA work.

If the OIG subsequently deems these to be allowable and allocable expenses the amounts noted on the attached schedule would need to be adjusted to remove this finding.

Please free to contact Mike Logan at 615.782.4595 or myself at 615.782.4616 if you have questions regarding this response.

Sincerely,

/Steve Bishop/

Steve Bishop

Cc: Eric Bowen, OIG  
Joseph Turner, OIG  
Mike Logan, CGS

**CIGNA Government Services, LLC  
2004-2006 Administrative Cost Audit  
Impact Summary**

**Impact to Medicare Allocation**

	Net Expenses Removed from Cost Pool				Impact to Medicare Allocation*			
	2004	2005	2006	Total	2004	2005	2006	Total
Executive Bonus	\$ 14,064,765	\$ -	\$ -	\$ 14,064,765	\$ 32,110	\$ -	\$ -	\$ 32,110
5000130T-Outplacement Central	2,271,974	428,582	-	2,700,556	41,123	9,643	-	50,766
5000151T-O/S Council SEC Law	161,568	265,751	107,046	534,365	2,924	5,979	2,077	10,980
1709-Legal Service Fees (Note 1)	-	-	-	-	-	-	-	-
1494 Hardware/Software Maintenance	-	669,627	2,416,929	3,086,556	-	969	84.21	1,053
2305 HR&S Warehousing	-	492,952	57,930	550,882	-	11,089	1,121	12,210
<b>Total</b>	<b>\$ 16,498,307</b>	<b>\$ 1,856,912</b>	<b>\$ 2,581,905</b>	<b>\$ 20,937,124</b>	<b>\$ 76,157</b>	<b>\$ 27,680</b>	<b>\$ 3,282</b>	<b>\$ 107,119</b>

**Impact on IT Adjustment Factor**

	Amount Removed from CIT Allocable		
	2004	2005	2006
Executive Bonus	\$ 172,364	\$ -	\$ -
5000130T-Outplacement Central	253,490	68,848	-
5000151T-O/S Council SEC Law	18,079	42,813	17,609
1709-Legal Service Fees (Note 1)	-	-	-
1494 Hardware/Software Maintenance	-	633,837	2,413,303
2305 HR&S Warehousing	-	79,726	9,756
<b>Total</b>	<b>\$ 445,937</b>	<b>\$ 827,229</b>	<b>\$ 2,442,674</b>

Change in IT Adjustment Factor		
2004 Before	2004 After	Inc/(Dec)
0.71%	0.62%	(0.09%)
Oct-Dec '04 Before	Oct-Dec '04 After	Inc/(Dec)
8.01%	5.02%	(2.99%)
Jan-Sept '05 Before	Jan-Sept '05 After	Inc/(Dec)
6.20%	3.49%	(2.71%)
2006 Before	2006 After	Inc/(Dec)
8.34%	5.53%	(2.81%)

Impact of IT Adjustment Factor Change to Medicare Allocation*			
2004	2005	2006	Total
\$ 23,788	\$ 34,276	\$ 9,358	\$ 67,422

Impact of IT Adjustment Factor on CGS Direct EDP Costs*			
2004	2005	2006	Total
\$ 11,311	\$ 289,415	\$ 245,978	\$ 546,705

**Overall Summary**

Total Reduction in Medicare allocation	\$ 99,945	\$ 61,956	\$ 12,640	\$ 174,541
Adjustment to CGS direct EDP	11,311	289,415	245,978	546,704
Direct Costs Adjustments - Part B only	6,350	12,699	28,708	47,757
<b>Total Adjustment</b>	<b>\$ 117,606</b>	<b>\$ 364,070</b>	<b>\$ 287,326</b>	<b>\$ 769,002</b>

**Allocation to Contracts**

Part B	\$ 84,642	\$ 259,615	\$ 177,571	\$ 521,828
Part B - direct costs adjustments	6,350	12,699	28,708	47,757
DMERC	26,614	91,756	81,047	199,417
<b>Total</b>	<b>\$ 117,606</b>	<b>\$ 364,070</b>	<b>\$ 287,326</b>	<b>\$ 769,002</b>

\* Amounts shown are decreases to the allocation

Note 1: The entire caption of 1709 was not removed per agreement with the OIG. Only expenses in caption 1709 and expense center 5000151T were removed. The impact for this caption is included in the impact for 5000151T