



DEPARTMENT OF HEALTH AND HUMAN SERVICES

Office of Inspector General
Office of Audit Services

AUG 20 2008

REGION IV
61 Forsyth Street, S.W., Suite 3T41
Atlanta, Georgia 30303

Report Number: A-04-07-04019

Mr. Bruce W. Hughes, President
Palmetto Government Benefits Administrators
2300 Springdale Drive
BLDG One, Mail Code: AG-A03
Camden, South Carolina 29020

Dear Mr. Hughes:

Enclosed is the U.S. Department of Health and Human Services (HHS), Office of Inspector General (OIG) final report entitled "Audit of Palmetto Government Benefits Administrators' Railroad Retirement Board Final Administrative Cost Proposals for Fiscal Years 2002 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.

Pursuant to the principles of the Freedom of Information Act, 5 U.S.C. § 552, as amended by Public Law 104-231, OIG reports generally are made available to the public to the extent the information is not subject to exemptions in the Act (45 CFR part 5). Accordingly, this report will be posted on the Internet at <http://oig.hhs.gov>.

If you have any questions or comments about this report, please do not hesitate to call me, or contact Mark Wimple, Audit Manager, at (919) 790-2765, extension 24 or through e-mail at Mark.Wimple@oig.hhs.gov. Please refer to report number A-04-07-04019 in all correspondence.

Sincerely,

Peter J. Barbera
Regional Inspector General
for Audit Services

Enclosure

Page 2 – Bruce W. Hughes

Direct Reply to HHS Action Official:

Nanette Foster Reilly, Consortium Administrator
Consortium for Financial Management & Fee for Service Operations
Centers for Medicare & Medicaid Services
601 East 12th Street, Room 235
Kansas City, Missouri 64106

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**AUDIT OF PALMETTO
GOVERNMENT BENEFITS
ADMINISTRATORS' RAILROAD
RETIREMENT BOARD FINAL
ADMINISTRATIVE COST
PROPOSALS FOR FISCAL YEARS
2002 THROUGH 2006**



Daniel R. Levinson
Inspector General

August 2008
A-04-07-04019

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 and 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.

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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.

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Notices

THIS REPORT IS AVAILABLE TO THE PUBLIC
at <http://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.

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 Centers for Medicare & Medicaid Services (CMS) administers the Medicare program through contracts with private organizations that process and pay Medicare claims. The contracts provide for reimbursement of allowable administrative costs incurred in processing Medicare claims.

During the audit period, which covered the period October 1, 2001, through September 30, 2006, CMS contracted with Palmetto Government Benefits Administrators (Palmetto) to serve as the Medicare Part B carrier for the Railroad Retirement Board nationwide. Palmetto reported Railroad Retirement Board costs totaling \$95,488,615 in its Final Administrative Cost Proposals (cost proposals) for fiscal years 2002 through 2006. (See Appendix B.)

OBJECTIVE

Our objective was to determine whether the administrative costs that Palmetto reported on its cost proposals were allowable, allocable, and reasonable in accordance with part 31 of the Federal Acquisition Regulation (FAR) and the Medicare contract.

SUMMARY OF FINDING

Palmetto reported expenditures that substantially complied with the FAR and the Medicare contract provisions. However, Palmetto reported in its cost proposals \$386 of miscellaneous expenses that it was unable to support with adequate documentation. Because Palmetto was unable to provide supporting documentation for certain individual costs claimed in the cost proposals, these costs did not meet the criteria for Federal reimbursement.

RECOMMENDATION

We recommend that Palmetto refund to the Federal Government \$386 of unallowable costs.

PALMETTO COMMENTS

In response to the draft report, Palmetto agreed that there were \$386 of unallowable costs.

TABLE OF CONTENTS

	<u>Page</u>
INTRODUCTION	1
BACKGROUND	1
OBJECTIVE, SCOPE, AND METHODOLOGY	1
Objective.....	1
Scope	1
Methodology.....	2
FINDING AND RECOMMENDATION	3
UNALLOWABLE COSTS	3
RECOMMENDATION	3
PALMETTO COMMENTS	3
APPENDIXES	
A – SAMPLING METHODOLOGY	
B – COSTS CLAIMED ON FINAL ADMINISTRATIVE COST PROPOSALS	
C – OIG RECOMMENDED COST DISALLOWANCES	
D – COMPARISON OF ADMINISTRATIVE COSTS CLAIMED TO BUDGET AUTHORIZATION	
E – PALMETTO COMMENTS	

INTRODUCTION

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 Centers for Medicare & Medicaid Services (CMS) administers the Medicare program through contracts with private organizations that process and pay Medicare claims.

The contracts with CMS provide for the reimbursement of allowable administrative costs incurred in processing Medicare claims. After the close of each fiscal year (FY), contractors submit a Final Administrative Cost Proposal (cost proposal) reporting Medicare costs. Once CMS accepts a cost proposal, the contractor and CMS negotiate a final settlement of allowable administrative costs.

During our audit period (FYs 2002 through 2006), CMS contracted with Palmetto Government Benefits Administrators (Palmetto) to serve as the Medicare Part B carrier for the Railroad Retirement Board nationwide. The Railroad Retirement Board is an independent Federal agency that administers comprehensive retirement-survivor, and unemployment-sickness benefit programs for railroad workers and their families under the Railroad Retirement and Railroad Unemployment Insurance Acts.

The contract between Palmetto and CMS set forth principles of reimbursement for administrative costs. The contract cited the Federal Acquisition Regulation (FAR), 48 CFR chapter 1, as regulatory principles to be followed for application to the Medicare contract and provided additional guidelines for specific cost areas.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to determine whether the administrative costs that Palmetto reported on its cost proposals were allowable, allocable, and reasonable in accordance with part 31 of the FAR and the Medicare contract.

Scope

Our audit covered the period October 1, 2001, through September 30, 2006 (FYs 2002 through 2006). For this period, Palmetto reported administrative costs to CMS totaling \$95,488,615. This total included pension costs of \$1,680,834 that we excluded from this review because pension costs will be the subject of a separate audit. In addition, the total costs included \$27,224 in forward funding that we did not audit because the funds had not yet been expended at the time of our audit. According to chapter 1, section 90.9M, of the Medicare Financial Management Manual, forward-funding costs are expenses to be incurred for CMS-approved items for which

funding has been received but (1) the services will extend into the subsequent FY and (2) the costs will be redistributed to other categories as the expenses are incurred.

In planning and performing our audit, we reviewed Palmetto's internal controls for allocating costs to cost objectives in accordance with the FAR and the Medicare contract. We conducted this analysis to accomplish our objective and not to provide assurance on the internal control structure.

We conducted fieldwork at Palmetto's office in Columbia, South Carolina, from July 2007 through December 2007.

Methodology

To accomplish our objective, we:

- reviewed applicable Medicare laws, regulations, and guidelines, including the FAR section 31.201-2(d), the Medicare Financial Management Manual, chapter 2, section 190.3 and Palmetto's contract with CMS;
- reconciled the cost proposals from FYs 2002 through 2006 to Palmetto's accounting records;
- performed analytical tests of Palmetto's trial balances;
- selected and reviewed a judgmental sample of invoices, expense vouchers and reports, and journal entries;
- interviewed Palmetto officials about their cost accumulation processes for cost proposals and gained an understanding of their cost allocation systems;
- reviewed payroll journals, corporate bonus plans, and personnel records;
- selected a stratified random sample of 150 individual employee pay periods and verified that the amount paid was in accordance with the employee's pay rate, the salary was charged to the correct cost center, and the number of hours paid agreed with the time sheets (see sampling methodology at Appendix A); and
- tested costs for allowability, allocability, and reasonableness.

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.

FINDING AND RECOMMENDATION

Palmetto reported expenditures that substantially complied with the FAR and the Medicare contract provisions. However, Palmetto reported in its cost proposals \$386 of miscellaneous expenses that it was unable to support with adequate documentation. Because Palmetto was unable to provide supporting documentation for certain individual costs claimed in the cost proposals, these costs did not meet the criteria for Federal reimbursement.

UNALLOWABLE COSTS

Pursuant to FAR section 31.201-2(d), Palmetto 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” Likewise, 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.”

Palmetto was unable to provide adequate supporting documentation for miscellaneous expenditures totaling \$386 that it claimed in its FY 2002 cost proposal.

Palmetto did not provide invoices, contracts, or other such documentation to support these expenses. Because Palmetto was unable to provide adequate supporting documentation for these costs, they were unallowable for Federal reimbursement.

RECOMMENDATION

We recommend that Palmetto refund to the Federal Government the \$386 of unallowable costs.

PALMETTO COMMENTS

In response to the draft report, Palmetto agreed that there were \$386 of unallowable costs.

APPENDIXES

SAMPLING METHODOLOGY

OBJECTIVE

Our objective was to determine whether the salary costs that Palmetto reported on its cost proposals were allowable, allocable, and reasonable in accordance with part 31 of the Federal Acquisition Regulation (FAR) and the Medicare contract.

POPULATION

The population consisted of 32,582 employee pay periods related to \$41,624,605 of Railroad Retirement Board salaries and wages that were charged to Medicare from October 1, 2001, through September 30, 2006.

SAMPLE UNIT

The sample unit was an employee pay period¹.

SAMPLE DESIGN

We used a stratified random sample of employee pay periods for fiscal years (FYs) 2002, 2003, 2004, 2005, and 2006. Each FY represented a separate stratum.

SAMPLE SIZE

We selected a sample of 150 employee pay periods that included 30 each from FYs 2002, 2003, 2004, 2005, and 2006.

¹An "employee pay period" consists of one employee's salaries, wages, and related fringe benefits for one pay period.

APPENDIX B

**COSTS CLAIMED ON FINAL ADMINISTRATIVE COST PROPOSALS
BY COST CLASSIFICATION
October 1, 2001, Through September 30, 2006**

	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>	<u>FY 2005</u>	<u>FY 2006</u>	<u>Total</u>
Salaries & Wages	\$ 11,505,365	\$ 9,839,848	\$ 11,251,583	\$ 10,124,058	\$ 8,673,203	\$ 51,394,057
Fringe Benefits	3,028,330	2,677,673	3,251,315	3,290,778	2,998,243	15,246,339
Facilities or Occupancy	993,054	1,097,613	1,126,415	1,399,139	1,121,994	5,738,215
EDP Equipment	2,309,594	1,952,716	1,901,556	2,073,457	460,344	8,697,667
Subcontracts	808,055	826,531	804,802	683,375	162,806	3,285,569
Outside Professional Services	161,771	17,805	5,867	92,072	7,084	284,599
Telephone & Telegraph	168,895	221,003	197,084	203,335	155,845	946,162
Postage & Express	3,521,814	3,272,909	3,080,724	2,782,348	486,038	13,143,833
Furniture & Equipment	286,507	255,481	264,979	250,631	81,582	1,139,180
Materials & Supplies	695,154	670,919	549,080	683,520	3,047,902	5,646,575
Travel	224,188	107,303	143,856	165,366	75,347	716,060
Return on Investment	129,474	68,274	47,084	30,376	20,279	295,487
Miscellaneous	207,646	94,166	211,327	643,650	895,950	2,052,739
Other	0	0	0	0	0	0
Credits	(2,452,796)	(2,562,845)	(2,715,849)	(2,873,409)	(2,757,881)	(13,362,780)
Forward Funding	0	0	0	237,689	27,224	264,913
Total Costs Claimed on FACP	<u>\$ 21,587,051</u>	<u>\$ 18,539,396</u>	<u>\$ 20,119,823</u>	<u>\$ 19,786,385</u>	<u>\$ 15,455,960</u>	<u>\$ 95,488,615</u>
OIG Recommended Disallowance*	<u>(386)</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>(386)</u>
OIG Recommended for Acceptance	<u>\$ 21,586,665</u>	<u>\$ 18,539,396</u>	<u>\$ 20,119,823</u>	<u>\$ 19,786,385</u>	<u>\$ 15,455,960</u>	<u>\$ 95,488,229</u>

* See Appendix C

OIG RECOMMENDED COST DISALLOWANCES
For Fiscal Year (FY) 2002

<u>Finding Categories</u>	<u>FY 2002</u>	<u>Total Railroad Retirement Board Disallowances</u>
Unallowable Costs		
Miscellaneous	\$386	\$386
Total OIG Recommended Disallowances	<u>\$386</u>	<u>\$386</u>

Palmetto GBA
Final Administrative Cost Proposal - Railroad Retirement Board

FY 2002 Comparison of Administrative Costs Claimed to Budget Authorization

<u>Operation</u>	<u>Budget Authorization</u>	<u>Administrative Costs Claimed</u>	<u>Variance Favorable (Unfavorable)</u>
<u>Program Management</u>			
Bills/Claims Payment	\$ 14,981,108	\$ 15,672,167	\$ (691,059)
Appeals/Reviews	828,300	811,343	16,957
Beneficiary Inquiries	1,788,000	1,821,223	(33,223)
PM Provider Communications	245,400	259,090	(13,690)
Participating Physician	26,500	25,780	720
Productivity Investment	3,115,000	2,295,741	819,259
Provider Telephone Inquiries	1,393,700	1,445,460	(51,760)
Credits	(2,500,000)	(2,452,797)	(47,203)
Subtotal Program Management	19,878,008	19,878,007	1
<u>Medicare Integrity Program</u>			
Medical Review	744,000	761,515	(17,515)
Medicare Secondary Payer Pre-Payment	447,400	432,702	14,698
Benefits Integrity	359,000	384,052	(25,052)
Local Provider Education & Training	139,000	130,775	8,225
Subtotal Medicare Integrity Program	1,689,400	1,709,044	(19,644)
Totals	\$ 21,567,408	\$ 21,587,051	\$ (19,643)

Note: All amounts were taken from Final Administrative Cost Proposal (Supplement No. 4) and Notification of Budget Approval (Supplement No. 18).

Palmetto GBA
Final Administrative Cost Proposal - Railroad Retirement Board

FY 2003 Comparison of Administrative Costs Claimed to Budget Authorization

<u>Operation</u>	<u>Budget Authorization</u>	<u>Administrative Costs Claimed</u>	<u>Variance Favorable (Unfavorable)</u>
<u>Program Management</u>			
Bills/Claims Payment	\$ 13,262,186	\$ 13,403,479	\$ (141,293)
Appeals/Reviews	929,600	934,372	(4,772)
Beneficiary Inquiries	1,840,700	1,826,043	14,657
PM Provider Communications	51,700	52,856	(1,156)
Participating Physician	29,100	17,431	11,669
Productivity Investment	105,200	105,445	(245)
Provider Enrollment	1,515,000	1,528,831	(13,831)
Provider Telephone Inquiries	1,503,400	1,485,768	17,632
Credits	(2,445,500)	(2,562,846)	117,346
Subtotal Program Management	16,791,386	16,791,379	7
<u>Medicare Integrity Program</u>			
Medical Review	669,600	634,767	34,833
Medicare Secondary Payer Pre-Payment	73,522	189,181	(115,659)
Benefits Integrity	370,100	369,479	621
Local Provider Education & Training	202,300	166,172	36,128
MIP Provider Communications	167,600	112,801	54,799
Medicare Secondary Payer Post-Payment	264,900	275,617	(10,717)
Subtotal Medicare Integrity Program	1,748,022	1,748,017	5
Totals	\$ 18,539,408	\$ 18,539,396	\$ 12

Note: All amounts were taken from Final Administrative Cost Proposal (Supplement No. 5) and Notification of Budget Approval (Supplement No. 16).

**Palmetto GBA
Final Administrative Cost Proposal - Railroad Retirement Board**

FY 2004 Comparison of Administrative Costs Claimed to Budget Authorization

<u>Operation</u>	<u>Budget Authorization</u>	<u>Administrative Costs Claimed</u>	<u>Variance Favorable (Unfavorable)</u>
<u>Program Management</u>			
Bills/Claims Payment	\$ 13,774,400	\$ 13,689,214	\$ 85,186
Appeals/Reviews	966,800	917,455	49,345
Beneficiary Inquiries	2,151,800	2,118,133	33,667
PM Provider Communications	114,400	109,638	4,762
Participating Physician	33,800	31,004	2,796
Productivity Investment	122,000	60,700	61,300
Provider Enrollment	2,005,200	1,972,098	33,102
Provider Telephone Inquiries	2,128,800	2,064,358	64,442
Credits	(2,708,300)	(2,715,849)	7,549
Subtotal Program Management	<u>18,588,900</u>	<u>18,246,751</u>	<u>342,149</u>
<u>Medicare Integrity Program</u>			
Medical Review	716,400	704,512	11,888
Medicare Secondary Payer Pre-Payment	208,000	177,311	30,689
Benefits Integrity	228,000	238,460	(10,460)
Local Provider Education & Training	168,500	152,182	16,318
MIP Provider Communications	167,700	115,571	52,129
Medicare Secondary Payer Post-Payment	505,000	485,036	19,964
Subtotal Medicare Integrity Program	<u>1,993,600</u>	<u>1,873,072</u>	<u>120,528</u>
Totals	<u>\$ 20,582,500</u>	<u>\$ 20,119,823</u>	<u>\$ 462,677</u>

Note: All amounts were taken from Final Administrative Cost Proposal (Supplement No. 02) and Notification of Budget Approval (Supplement No. 09).

**Palmetto GBA
Final Administrative Cost Proposal - Railroad Retirement Board**

FY 2005 Comparison of Administrative Costs Claimed to Budget Authorization

<u>Operation</u>	<u>Budget Authorization</u>	<u>Administrative Costs Claimed</u>	<u>Variance Favorable (Unfavorable)</u>
<u>Program Management</u>			
Bills/Claims Payment	\$ 13,366,500	\$ 13,065,840	\$ 300,660
Appeals/Reviews	950,300	1,019,241	(68,941)
Beneficiary Inquiries	2,144,300	1,925,829	218,471
PM Provider Communications	123,700	105,792	17,908
Participating Physician	32,700	23,663	9,037
Productivity Investment	83,200	83,200	0
Provider Enrollment	2,154,300	2,352,690	(198,390)
Provider Telephone Inquiries	2,250,100	2,345,654	(95,554)
Credits	(2,777,100)	(2,873,409)	96,309
Subtotal Program Management	<u>18,328,000</u>	<u>18,048,500</u>	<u>279,500</u>
<u>Medicare Integrity Program</u>			
Medical Review	658,100	652,785	5,315
Medicare Secondary Payer Pre-Payment	103,600	114,559	(10,959)
Benefits Integrity	231,800	230,746	1,054
Local Provider Education & Training	166,500	160,330	6,170
MIP Provider Communications	118,500	102,552	15,948
Medicare Secondary Payer Post-Payment	458,800	476,913	(18,113)
Subtotal Medicare Integrity Program	<u>1,737,300</u>	<u>1,737,885</u>	<u>(585)</u>
Totals	<u>\$ 20,065,300</u>	<u>\$ 19,786,385</u>	<u>\$ 278,915</u>

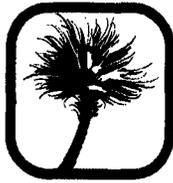
Note: All amounts were taken from Final Administrative Cost Proposal (Supplement No. 6) and Notification of Budget Approval (Supplement No. 11).

Palmetto GBA
Final Administrative Cost Proposal - Railroad Retirement Board

FY 2006 Comparison of Administrative Costs Claimed to Budget Authorization

<u>Operation</u>	<u>Budget Authorization</u>	<u>Administrative Costs Claimed</u>	<u>Variance Favorable (Unfavorable)</u>
<u>Program Management</u>			
Bills/Claims Payment	\$ 12,214,700	\$ 12,092,573	\$ 122,127
Appeals/Reviews	926,200	964,692	(38,492)
Beneficiary Inquiries	1,043,400	1,025,327	18,073
PM Provider Communications	50,800	52,741	(1,941)
Participating Physician	10,700	875	9,825
Productivity Investment	78,100	62,000	16,100
Provider Enrollment	888,900	882,070	6,830
Provider Telephone Inquiries	1,858,200	1,831,219	26,981
Credits	(2,898,800)	(2,757,881)	(140,919)
Subtotal Program Management	14,172,200	14,153,616	18,584
<u>Medicare Integrity Program</u>			
Medical Review	597,900	567,454	30,446
Medicare Secondary Payer Pre-Payment	49,000	43,974	5,026
Benefits Integrity	182,900	168,218	14,682
Local Provider Education & Training	63,100	42,084	21,016
MIP Provider Communications	92,500	70,978	21,522
Therapy Cap	0	3,586	(3,586)
Medicare Secondary Payer Post-Payment	400,500	406,050	(5,550)
Subtotal Medicare Integrity Program	1,385,900	1,302,344	83,556
Totals	\$ 15,558,100	\$ 15,455,960	\$ 102,140

Note: All amounts were taken from Final Administrative Cost Proposal (Supplement No. 0)
and Notification of Budget Approval (Supplement No. 15).



Palmetto GBA
PARTNERS IN EXCELLENCE™

Bruce W. Hughes
President and Chief Operating Officer

July 11, 2007

RE: Audit Report Number A-04-07-04019

Peter J. Barbera
Regional Inspector General for Audit Services
Region IV
60 Forsyth Street, S.W., Suite 3T41
Atlanta, Georgia 30303

RECEIVED

JUL 16 2008

Office of Audit Svcs.

Dear Mr. Barbera:

We are responding to your draft audit report dated June 13, 2008 entitled "Review of Railroad Retirement Board Final Administrative Cost Proposals for Fiscal Years 2002 through 2006."

The audit contained the following recommendation with which we do not concur.

Recommendation:
Refund to the Federal Government \$98,945 of unallowable costs.

Comment:
We have submitted additional documentation to support \$98,559 of the original unallowable cost of \$98,945 leaving \$386 of unallowable cost. The OIG has determined that the additional documentation submitted is adequate to support the cost. We therefore await the OIG's final draft audit report which will reflect the amount of \$386 as the amount to be refunded to the Federal Government by Palmetto GBA.

If you have any questions, please feel free to contact me at 803-763-7130

Sincerely,

Bruce Hughes
Bruce Hughes

Office of Inspector General Note: Portions of this response are no longer applicable because we reduced the unallowable costs based on additional documentation submitted by the auditee.

CC: William R. Horton, BCBSSC
Joe Wright, Palmetto GBA
Mark Wimple, OIG