



DEPARTMENT OF HEALTH & HUMAN SERVICES

OFFICE OF INSPECTOR GENERAL

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

March 16, 2011

Report Number: A-04-07-00032

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 Durable Medical Equipment Regional Carrier 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. Please refer to report number A-04-07-00032 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 12th Street, Room 235
Kansas City, MO 64106

Department of Health & Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF CIGNA
GOVERNMENT SERVICES DURABLE
MEDICAL EQUIPMENT REGIONAL
CARRIER FINAL ADMINISTRATIVE
COST PROPOSALS FOR FISCAL YEARS
2004 THROUGH 2006**



**Daniel R. Levinson
Inspector General**

**March 2011
A-04-07-00032**

Office of Inspector General

<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 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 Durable Medical Equipment Regional Carrier (DMERC) for Alaska, Arizona, California, Guam, Hawaii, Idaho, Iowa, Kansas, Missouri, Montana, Nebraska, Nevada, North Dakota, Oregon, South Dakota, Utah, Washington, Wyoming, Northern Mariana Islands, and American Samoa.

CIGNA's DMERC 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 \$75,434,990, including \$124,660 in forward funding, in reimbursement for direct and indirect costs related to its DMERC contract.

OBJECTIVE

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

SUMMARY OF FINDINGS

Of the \$75,310,330 in administrative costs reviewed, CIGNA appropriately claimed \$75,110,913 on its FACP for FYs 2004 through 2006. However, we identified \$199,417 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 indirect costs claimed on its FACPs by \$199,417 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.

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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 Durable Medical Equipment Regional Carrier (DMERC) for Alaska, Arizona, California, Guam, Hawaii, Idaho, Iowa, Kansas, Missouri, Montana, Nebraska, Nevada, North Dakota, Oregon, South Dakota, Utah, Washington, Wyoming, Northern Mariana Islands, and American Samoa.

CIGNA's DMERC 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 \$75,434,990 in reimbursement for direct and indirect costs related to its DMERC 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 DMERC FACP's for FYs 2004 through 2006 were reasonable, allocable, and allowable for Medicare reimbursement.

Scope

Our review was limited to \$75,310,330 in direct and indirect administrative costs claimed by CIGNA on its FACP's submitted to CMS for FYs 2004 through 2006. We did not review \$124,660 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 FACP's. 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 7 caption accounts, judgmentally sampling 30 expense items in each selected caption account, and tracing these 210 expense items to supporting documents including invoices, expense vouchers, reports, and journal entries;¹
- tested certain other direct costs by selecting two caption accounts and tracing all expense items to supporting documents including invoices, reports, and journal entries;²
- 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;

¹ We selected these caption accounts based on materiality and variance analysis.

² We selected these caption accounts based on materiality and variance analysis.

- tested indirect costs by judgmentally sampling 88 expense centers for FYs 2005 and 2006 and reviewing them for reasonableness and allocability to Medicare;³
- tested indirect costs by judgmentally sampling 41 caption accounts for FYs 2004, 2005, and 2006 and reviewing them for reasonableness and allocability to Medicare;⁴ and
- 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 \$75,310,330 in administrative costs reviewed, CIGNA appropriately claimed \$75,110,913 on its FACPs for FYs 2004 through 2006. However, we identified \$199,417 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."

³ We selected these expense centers based on materiality and variance analysis.

⁴ We selected these caption accounts based on the nature of the account.

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....”

INDIRECT COSTS NOT SUPPORTED AS REASONABLE, ALLOCABLE, OR ALLOWABLE

The majority of the indirect costs claimed on the FACP 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 \$199,417, 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 and one caption account 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 allocations⁵ reduced indirect costs allocable to Medicare totaling \$721,245.⁶ Of this amount, \$521,828 related to its Part B contract and \$199,417 related to its Durable Medical Equipment Regional Carrier contract.⁷

RECOMMENDATIONS

We recommend that CIGNA:

- reduce indirect costs claimed on its FACP by \$199,417 and
- strengthen its procedures for maintaining documentation to support costs included on its FACP.

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.

⁵ See the *Background* section above for CIGNA's *Methodology for Allocating Costs*.

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

⁷ See CIGNA's Impact Summary at Appendix D and the Office of Inspector General report number A-04-07-00031 *Review of CIGNA Government Services Part B Final Administrative Cost Proposals for Fiscal Years 2004 Through 2006*.

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 9,090 “employee months” related to \$25,476,558 in DMERC 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:

- 3,414 “employee months” related to Durable Medical Equipment Regional Carrier (DMERC) salary and wages of \$9,439,870 for FY 2004,
- 3,329 “employee months” related to DMERC salary and wages of \$9,387,026 for FY 2005, and
- 2,347 “employee months” related to DMERC salary and wages of \$6,649,662 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 DURABLE MEDICAL EQUIPMENT ADMINISTRATIVE
COSTS CLAIMED FOR FISCAL YEARS 2004 THROUGH 2006**

	FY 2004 Expenses Claimed	FY 2005 Expenses Claimed	FY 2006 Expenses Claimed	Total Expenses Claimed
Salaries & Wages	\$13,296,660	\$13,378,024	\$11,346,560	\$38,021,244
Fringe Benefits	3,766,592	4,129,600	3,494,183	11,390,375
Facilities or Occupancy	1,060,392	1,187,013	1,492,305	3,739,710
EDP Equipment	2,231,960	2,987,414	2,939,906	8,159,280
Subcontracts	257,081	698	17,333	275,112
Outside Professional Services	670,635	1,174,320	750,412	2,595,367
Telephone & Telegraph	114,106	69,720	87,814	271,640
Postage and Express	4,042,580	3,947,564	3,818,069	11,808,213
Furniture & Equipment	124,230	131,710	95,757	351,697
Materials & Supplies	403,783	347,431	197,599	948,813
Travel	290,495	256,021	139,331	685,847
Return on Investment	102,266	112,243	101,634	316,143
Miscellaneous	1,521,659	2,233,272	1,488,688	5,243,619
Other	0	0	0	0
Credits	(2,540,949)	(2,810,077)	(3,145,704)	(8,496,730)
Forward Funding	0	0	124,660	124,660
Total	\$25,341,490	\$27,144,953	\$22,948,547	\$75,434,990

**APPENDIX C: RESULTS OF REVIEW OF CIGNA'S DURABLE MEDICAL
EQUIPMENT ADMINISTRATIVE COSTS FOR FISCAL YEARS 2004 THROUGH 2006**

Fiscal Year	Total Expenses Claimed	Total Expenses Deferred	Total Expenses Reviewed	Total Allowable Expenses	Total Unallowable Expenses
2004	\$25,341,490	\$0	\$25,341,490	\$25,314,876	\$26,614
2005	27,144,953	0	27,144,953	27,053,197	91,756
2006	22,948,547	124,660	22,823,887	22,742,840	81,047
Total	\$75,434,990	\$124,660	\$75,310,330	\$75,110,913	\$199,417



May 27, 2010

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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;

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- 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.

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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
Total	\$ 16,498,307	\$ 1,856,912	\$ 2,581,905	\$ 20,937,124	\$ 76,157	\$ 27,680	\$ 3,282	\$ 107,119

Impact on IT Adjustment Factor

	Amount Removed from CIT Allocable			Change in IT Adjustment Factor		
	2004	2005	2006	2004 Before	2004 After	Inc/(Dec)
Executive Bonus	\$ 172,364	\$ -	\$ -	0.71%	0.62%	(0.09%)
5000130T-Outplacement Central	253,490	68,848	-			
5000151T-O/S Council SEC Law	18,079	42,813	17,609	Oct-Dec '04 Before	Oct-Dec '04 After	Inc/(Dec)
1709-Legal Service Fees (Note 1)	-	-	-	8.01%	5.02%	(2.99%)
1494 Hardware/Software Maintenance	-	633,837	2,413,303			
2305 HR&S Warehousing	-	79,726	9,756	Jan-Sept '05 Before	Jan-Sept '05 After	Inc/(Dec)
Total	\$ 445,937	\$ 827,229	\$ 2,442,674	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
Total Adjustment	\$ 117,606	\$ 364,070	\$ 287,326	\$ 769,002

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
Total	\$ 117,606	\$ 364,070	\$ 287,326	\$ 769,002

* 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