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OFFICE OF PERSONNEL MANAGEMENT

48 CFR Chapter 16

RIN 3206-AJ10

Federal Employees Health Benefits Program

Revision of Contract Cost Principles and Procedures, and Miscellaneous Changes

Parts 1631 and 1652

AGENCY: Office of Personnel Management

ACTION: Proposed rule.

SUMMARY: The Office of Personnel Management (OPM) proposes to issue a regulation amending the Federal Employees Health Benefits Acquisition Regulation (FEHBAR) to delete the Federal Government's Cost Accounting Standards (CAS) requirements from the Federal Employees Health Benefits (FEHB) Program experienced-rated contracts, and revises and adds additional contract cost accounting principles and procedures for such contracts. These principles and procedures will enable OPM to enhance its oversight of the Program's experience-rated contracts and eliminate the remaining CAS requirements that provide no value to the FEHB Program.

DATES: Comments must be received on or before (**insert 60 days from date of publication in the Federal Register**).

ADDRESSES: Comments may be sent to Abby L. Block, Assistant Director, Office of Insurance Programs, OPM, Room 3400, 1900 E Street NW, Washington, DC; 20415-0001

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FOR FURTHER INFORMATION CONTACT: Anne Easton, (202) 606-0004.

SUPPLEMENTARY INFORMATION: OPM has determined that it could enhance its oversight of experience-rated FEHB contracts by requiring carriers to apply certain cost accounting principles and procedures. The FEHB Program currently contracts with about 250 health benefits carriers. Thirty-one are experience-rated fee-for-service carriers and HMOs. The rest are community-rated Health Maintenance Organizations (HMO's). The CAS only have application to enrollee and Government costs in the experience-rated segment of the FEHB Program.

OPM has a responsibility under the FEHB law to taxpayers, since the Government pays 72 percent of the premium on average. It is part of OPM's mission, as well, to ensure that premiums "reasonably and equitably reflect the cost of benefits provided." Our interest from the financial point of view is paying the right price for the health care coverage we purchase for FEHB Program enrollees.

OPM's independent Inspector General has historically audited the experience-rated carriers to determine if they are in compliance with the Cost Principles in Part 31 of Title 48, Code of Federal Regulations (the Federal Acquisition Regulation (FAR)) and Chapter 16 of Title 48, Code of Federal Regulations (Federal Employees Health Benefits Acquisition Regulation (FEHBAR)). OPM also has significant other practices in place that provide assurance to FEHB Program managers that carrier financial reporting and auditing requirements are met. Nevertheless, implementation of certain additional cost accounting principles and procedures will add value to those practices currently in place. Conversely, the other requirements of CAS (other than those already applicable to the FEHB Program by way of the provisions of the FAR) provide no value and should not apply.

The Treasury and General Government Appropriations Act, FY 2000, Public Law 106-58, waived the application of the CAS to FEHBP contracts, and by Public Law 106-554, Congress has waived the applicability of the CAS to the FEHBP contracts for Fiscal Year 2002 as well. It is understandable that, from a program management standpoint, obtaining legislative authorization for agency procedures on a year-to-year basis is not the most efficient way to administer a Federal program. It impedes the ability of the agency to administer a program, and delays the development of a permanent and acceptable administrative procedure.

Both the FAR and FEHBAR recognize the authority of an agency head to waive requirements of those regulations the agency head determines are inappropriate for that agency's contracts. In addition, the CAS call for their application only when it is determined that the benefit of the CAS outweigh their cost and specifically allow agency heads to waive the requirements of CAS. 48 C.F.R.§ 9903.201-5(b). With respect to the CAS, with the exception of those requirements already contained in the FAR and those added herein, we have determined that the CAS provide no value to the FEHB Program and by this regulation we waive their application to experienced-rated contracts.

Similarly, the National Defense Authorization Act of Fiscal Year 2000, Public Law 106-65, enables agency heads to waive the application of the CAS on a contract-by-contract basis. The agency must determine that exceptional circumstances exist where waiving the requirements produce benefits that outweigh the risks associated with the waiver. Such circumstances exist with respect to experience-rated FEHB contracts such that the waiver is justified under this law as well.

We have been working collaboratively with affected FEHB health carriers on this issue for several years. That work has led to the development of an appropriate set of principles and procedures that assure an equitable allocation of costs to the FEHB Program. When added to the body of financial and related standards that currently apply, these new provisions will enhance integrity and economy in the Program. They will also demonstrate that accounting methods and related financial disclosures by health plans are consistent with sound business practices. Because they have been developed in a collaborative manner with the health plans, they can be implemented within the FEHB Program without impediments.

OPM is revising the Federal Employees Health Benefits Acquisition Regulation (FEHBAR) Clause Matrix in Section 1652.3 to delete the references to the CAS clauses. Since this regulation deletes the CAS requirements from experienced-rated contracts (other than those already in the FAR and those added herein) it is no longer necessary to include the CAS clauses in experienced-rated contracts.

The existing cost principles in the FAR do not contain sufficient guidance on procedures for allocating certain indirect costs to FEHB experienced-rated contracts. OPM is therefore proposing a four-step procedure that sets out techniques for allocating groupings of indirect costs (FEHBAR 1631.203-70). In addition, OPM is proposing more specific guidance on the allocation of business unit general and administrative expenses, and the allocation of home office expenses to a carrier's segments (FEHBAR 1631.203-71 AND 1631.203-72).

As another enhancement of the existing FEHBAR cost principles, we are adding subrogation settlements, prescription drug rebates, and volume discounts to the list of FEHB credits in 1631.201-70. The applicable portion of any credit relating to any allowable cost and received by or accruing to the carrier must be credited to the FEHB Program. OPM has always intended that the FEHB Program receive these credits. Specifically identifying them makes it clear that they are to be credited to the Program. While the list of credits is not intended to be all inclusive, we have added the additional three items to raise the carriers' awareness of how they should be treated.

Other proposed enhancements of existing cost principles include (i) the modification of FAR 31.205-10 to allow the cost of money under certain circumstances even though cost of money is not specifically identified in a proposal (FEHBAR 1631.205-10); (ii) an option to adopt CAS 409 for computing depreciation (FEHBAR 1631.205-11); (iii) a clarification that costs incurred under an existing contract for a benefit and rate proposal in connection with contract renewal are not bid and proposal costs for the purpose of FAR 31.205-18 (FEHBAR 1631.205-18); and, (iv) a provision which specifies that compensated personal absence must be assigned to the cost accounting period in which the entitlement was earned (FEHBAR 1631.205-72).

A transition rule is provided to permit carriers to recover prior years' allocable liability for compensated personal absence not previously charged to FEHBP contracts.

Regulatory Flexibility Act

I certify that this regulation will not have a significant economic impact on a substantial number of small entities because it is based on requirements already in place in the Federal Acquisition Regulation (FAR).

List of Subjects in 48 CFR Parts 1631, 1652, and 1699

Administrative practice and procedure, Government employees, Government procurement, Health facilities, Health insurance, Health professions, Reporting and record keeping requirements, Retirement.

Office of Personnel Management

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Kay Coles James
Director

Accordingly, OPM proposes to amend Chapter 16 of Title 48, Code of Federal Regulations, as follows:

CHAPTER 16—OFFICE OF PERSONNEL MANAGEMENT FEDERAL EMPLOYEES HEALTH BENEFITS ACQUISITION REGULATION

1. The authority citation for 48 CFR Parts 1631 and 1652 continue to read as follows:

Authority: 5 U.S.C. 8913; 40 U.S.C. 486(c); 48 CFR 1.301.

PART 1631—CONTRACT COST PRINCIPLES AND PROCEDURES

1631.001 Definitions.

The definitions in FAR 31.001 are applicable to this section unless otherwise noted.

Subpart 1631.2—Contracts with Commercial Organizations

2. Paragraph 1631.201-70 is revised to read as follows:

1631.201-70 Credits.

The provisions of FAR 31.201-5 shall apply to income, rebates, allowances, and other credits resulting from benefit payments that include, but are not limited to –

(a) Coordination of benefit refunds, including subrogation settlements.

(b) Hospital year-end settlements.

(c) Uncashed and returned checks.

(d) Utilization review refunds.

(e) Prescription drug rebates.

(f) Volume discounts.

(g) Refunds attributable to litigation with subscribers or providers of health services.

(h) Erroneous benefit payment, overpayment, and duplicate payment recoveries.

3. A new section 1631.203 is added to read as follows:

1631.203 Indirect costs.

For the purposes of applying FAR 31.203(e) to FEHB Program contracts, OPM considers the monthly or quarterly rates used by some carriers to be a general practice in the industry.

4. Section 1631.203-70 is revised to read as follows:

1631.203-70 Allocation Techniques.

(a) Carriers shall use the following methods for allocating groupings of business unit indirect costs.

(1) **Input Method** – The preferred allocation technique is one which represents the consumption of resources in performance of the activities (input) for the function(s) represented by the cost grouping. This allocation technique should be used in circumstances where there is a direct and definitive relationship between the function(s) and the benefiting cost objectives. Measures of the activities (input) ordinarily can be expressed in terms like labor hours or square footage. This means costs can be allocated by use of a rate, such as a rate per labor hour or cost per square foot.

(2) **Output Method** – Where input measures are unavailable or impractical to determine, the basis for allocation can be a measure of the output of the function(s) represented by the cost grouping. The output becomes a substitute measure for the use of

resources and is a reasonable alternative when a direct measure of input is impractical. Output can be measured in terms of units of end product produced by the functions. Examples of output measures include number of claims processed by a claims processing center, number of printed pages in a print shop, number of purchase orders processed by a purchasing department, or number of hires by a personnel office.

(3) **Surrogate Method** – Where neither activity (input) nor output of the functions can be measured practically, a surrogate must be used to measure the resources utilized. Surrogates used to represent the relationship generally measure the benefit to the cost objectives receiving the service and should vary in proportion to the services received. For example, a personnel department may provide various services that cannot be measured practically on an activity (input) or output basis. Number of personnel served may reasonably represent the use of resources of the personnel function for the cost objectives receiving the service, where this base varies in proportion to the services performed.

(4) **Other Method** – Some cost groupings cannot readily be allocated on measures of specific beneficial or causal relationships under paragraph (a) (1), (a) (2), or (a) (3) of this section. Such costs do not have a direct and definitive relationship to the benefiting cost objectives. Generally, the cost of overall management activities falls in this category. Overall management costs should be grouped in relation to the activities managed. The base selected to measure the allocation of these indirect costs to cost objectives should be a base representative of the entire activity being managed. For example, the total operating expenses of activities managed might be a reasonable base for allocating the general indirect costs of a business unit. Another reasonable method for allocating general indirect costs

could be based on a percentage of contracts. These examples are not meant to be all-inclusive, but rather are examples of allocation methods that may be acceptable under individual circumstances. See also General and Administrative (G&A) expenses, 161.203-71.

(b) Carriers that use multiple cost centers to accumulate and allocate costs shall apply the techniques in paragraph (a) of this section at each step of the allocation process. Accordingly, the allocation of costs among cost centers at the initial entry into the cost accounting system shall be made in compliance with paragraph (a) of this section. Likewise, the allocation of the cost of interim cost centers to final cost centers is subject to paragraph (a) of this section. If costs of final cost centers are allocated among final cost objectives, the allocation shall also be made in accordance with paragraph (a) of this section. It is possible that carriers using multiple cost centers to accumulate and allocate costs may not have any direct costs, i.e., costs identified specifically with a final cost objective.

(c) The allocation of business unit general and administrative expenses and the allocation of home office expenses to segments are also subject to FEHBAR 1631.203-71 and FEHBAR 1631.203-72, respectively.

5. A new section 1631.203-71 is added to read as follows:

1631.207-71 General and Administrative (G&A) expenses.

G&A expenses shall be allocated to final cost objectives by a base or method which represents the total activity of the business unit.

6. A new section 1631.203-72 is added to read as follows:

1631.203-72 Home Office Expense.

The practices for allocating home office expenses to the segments of the carrier are acceptable for the purposes of FAR 31.203(b) if they are in accordance with 48 CFR 9904.403. Home office expenses not allocated in accordance with 48 CFR 9904.403 shall be allocated on a basis of the beneficial or causal relationship between the home office activities and the segments to which the expenses are allocated. Expenses that cannot be allocated on a basis of a more specific beneficial or causal relationship should be allocated on a basis representative of the entire activity being managed. The compliance of such allocations with FAR 31.203 shall be determined on the basis of the facts and circumstances of each situation.

7. A new section 1631.205-10 is added to read as follows:

1631.205-10 Cost of Money.

For the purposes of FAR 31.205-10(a)(2)(iii), the estimated facilities capital cost of money is specifically identified if it is identified in the prior year's Annual Accounting Statement or, for new experience-rated carriers, the supplemental information supporting submitted costs (such as the Supplemental Schedule of Administrative Expenses).

8. A new section 1631.205-11 is added to read as follows:

1631.205-11 Depreciation.

FEHBP carriers may elect to adopt CAS 409, consistent with the conditions in FAR 31.205-11(b), in lieu of FAR 31.205-11(c) through (e).

9. A new section 1631.205-18 is added to read as follows:

1631.205-18 Independent research and development (IR&D) and bid and proposal (B&P) costs.

(a) Carrier costs incurred under an existing contract for a benefit and rate proposal in connection with contract renewal are not bid and proposal costs for the purpose of FAR 31.205-18.

(b) The carrier meets the requirement for the accumulation of IR&D and B&P costs by individual projects if the carrier charges the project's direct and indirect costs to a cost center established for these purposes or otherwise identifies and accumulates the costs of each IR&D and B&P project.

10. In section 1631.205-72, the existing paragraph is designated as paragraph (a) and add a new paragraph (b) to read as follows:

1631.205-72 FEHBP Compensation for Personal Services.

(a) * * *

(b)(1) The costs of compensated personal absence shall be assigned to the cost accounting period or periods in which entitlement was earned. Entitlement means an employee's right, whether conditional or unconditional, to receive a determinable amount of compensated personal absence, or pay in lieu thereof.

(2) If at the beginning of the first year a carrier subject to paragraph (b)(1) of this section has recorded on its books a liability for accrued but unpaid expenses for compensated personal absences that would otherwise be allocable to FEHBP contracts, the carrier may include such costs in a suspense account. The suspense account may be amortized and included in government contract costs at a rate not exceeding 20 per cent per year.

Part 1652-CONTRACT CLAUSES

11. The FEHBP Clause Matrix in Subpart 1652.3 is revised by removing FAR clauses 52.230-2, 52.230-3, and 52.230-6 in their entirety.

PART 1699—COST ACCOUNTING STANDARDS

For experienced-rated contracts entered into under the FEHB Program, the Cost Accounting Standards, found at Section 9904, et seq., of Title 48 of the Code of Federal Regulations, are hereby waived.

Billing Code: 6325-50