

United States Government

Department of Energy

# memorandum

DATE: June 23, 1994

REPLY TO  
ATTN OF: IG-1

SUBJECT: INFORMATION: Report on "Audit of Health Benefit Costs at the  
Department's Management and Operating Contractors"

TO: The Secretary


BACKGROUND:

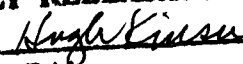
Management and Operating (M&O) contractors are generally reimbursed for all costs incurred in operating the Department's various facilities, including employee-sponsored health benefit programs. The Department of Energy spent about \$600 million on its M&O contractors' employee health benefit programs in Fiscal Year 1991. Requirements for Departmental approval of health benefit plan costs are set forth in the Department of Energy Acquisition Regulation (DEAR). The DEAR prescribes that to be allowable, costs must be: reasonable when compared to the costs of similar firms and when compared to costs of the contractor's own commercial operations, and in accordance with the contractor's contractual agreement with the Department.

DISCUSSION:

We found that the Department's policies and procedures did not ensure that M&O contractors paid their fair share of health benefit costs. We audited \$95 million in health benefit costs paid to six M&O contractors and determined that \$15.4 million of these costs were excessive when compared to those of other firms as established by a national survey.

Department management agreed with the audit results and is developing standards and procedures for Contracting Officers to use in determining the reasonableness of these costs. The Department's actions, when implemented, should correct this problem.

  
John C. Layton  
Inspector General

This document is  
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Hugh Kinser   
Authorizing Official  
Date: 2/2/09

Attachment

cc: Deputy Secretary  
Under Secretary  
Deputy Assistant Secretary for Procurement  
and Assistance Management

**MASTER**

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U.S. DEPARTMENT OF ENERGY  
OFFICE OF INSPECTOR GENERAL

AUDIT OF HEALTH BENEFIT COSTS AT  
THE DEPARTMENT'S  
MANAGEMENT AND OPERATING CONTRACTORS

Report Number: DOE/IG-0350  
Date of Issue: June 23, 1994

Western Regional Audit Office  
Albuquerque, NM 87185

AUDIT OF HEALTH BENEFIT COSTS  
AT THE DEPARTMENT'S  
MANAGEMENT AND OPERATING CONTRACTORS

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AUDIT OF HEALTH BENEFIT COSTS  
AT THE DEPARTMENT'S  
MANAGEMENT AND OPERATING CONTRACTORS

Audit Report Number: DOE/IG- 0350

SUMMARY

The Department of Energy (Department) spent about \$600 million in Fiscal Year 1991 on its Management and Operating contractors' employee health benefit programs. These contractors are generally reimbursed for all costs incurred in operating the Department's various facilities, including employer-sponsored health benefit programs. Because of the significant amount of funds used in support of these health benefit plans, and increased national interest in this area, we conducted an audit to determine whether the Department's share of costs for contractor employee health benefits was reasonable.

The Assistant Secretary for Human Resources and Administration has overall responsibility for developing policies and procedures needed to direct Management and Operating contractor health benefit plans. Requirements for Departmental approval of health benefit plan costs are set forth in the Department of Energy Acquisition Regulation (DEAR). The DEAR prescribes that to be allowable, costs must be: reasonable when compared to the costs of similar firms, reasonable when compared to the costs of the contractor's own commercial operations, and in accordance with the contractor's contractual agreement with the Department.

The audit disclosed that the Department and certain of its contractors had initiated several positive actions to contain health benefit costs. These actions included: improving data collection, increasing training, reviewing changes to health plans, improving the language in one contract, increasing the employees' share of health costs at one contractor, and initiating self-insurance at another contractor. Despite these actions, we concluded that further improvements were needed in the administration of the contractor employee health benefit plans. We found that the Department did not have the policies and procedures necessary to ensure that the health benefit costs met the tests for reasonableness prescribed by the DEAR. Our audit of \$95 million in health benefit costs incurred at six Management and Operating contractors showed that \$15.4 million of these costs were excessive when compared to national norms.

To resolve these issues, we recommended that the Department develop standards and procedures for Contracting Officers to use in determining the reasonableness of health benefit costs. Management concurred with the finding and has initiated action to correct the conditions disclosed in our audit.

Office of Inspector General

## PART I

### APPROACH AND OVERVIEW

#### INTRODUCTION

During FY 1993, the Department of Energy (Department) used 52 Management and Operating (M&O) contractors to operate its various facilities. These contractors had more than 140,000 employees. In FY 1991, the Department reimbursed the M&O contractors approximately \$600 million for health benefits.

Because M&O contractors were reimbursed for health benefit costs, and because of increased national interest in this area, we initiated an audit to determine whether the Department's share of health benefit costs for M&O contractor employees was reasonable. The audit included an examination of the adequacy of the Department's policies and procedures, and compared M&O health benefit costs to industry norms and to the costs incurred by the contractor's private sector operations.

#### SCOPE AND METHODOLOGY

The audit was performed from October 1992 to July 1993 at Department Headquarters, the Department's Chicago and Richland Operations Offices, the Rocky Flats Office, and the Golden Field Office. The entities reviewed included the Office of Contractor Human Resource Management (Contractor Resource Management) at Headquarters and six M&O contractors. The M&O contractors were EG&G Rocky Flats, Inc. (EG&G); Wackenhut Services Incorporated, Rocky Flats Plant; the Midwest Research Institute at the National Renewable Energy Laboratory; Westinghouse Hanford Corporation; Hanford Environmental Health Foundation; and Battelle Memorial Institute at the Pacific Northwest Laboratory.

The audit was accomplished by:

- testing management of health benefit plans at M&O contractors for compliance with the Department of Energy Acquisition Regulation (DEAR) and Department Orders;
- reviewing the health benefits portions of the personnel appendices of the six M&O contracts;
- interviewing personnel from Headquarters, the four Department offices, and the six M&O contractors; and,
- comparing M&O contractors' health benefit plan costs to national norms and, where applicable, to the contractors' private sector practices.



The audit was performed according to generally accepted Government auditing standards for performance audits and included tests of internal controls and compliance with laws and regulations to the extent necessary to satisfy the objective of the audit. Accordingly, we assessed the significant internal controls with respect to the Department's management of health benefit plans for M&O contractor employees. Because our audit was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit.

The firm of KPMG Peat Marwick participated with the Office of Inspector General in conducting the audit. An exit conference was waived by the Director, Office of Procurement, Assessment, and Property.

## BACKGROUND

The cost of employer-sponsored health benefits is a major expense for both the nation's businesses and the U.S. Government. The cost of health care is a primary concern which the Administration has said must be addressed if we are to control the national deficit. In a May 1992 report, the General Accounting Office estimated that health care spending for 1991 totalled nearly \$700 billion, or more than 12 percent of the gross national product. The General Accounting Office expects health care spending to increase by about 10 percent per year through 1995, when health benefits spending will exceed \$1 trillion.

## Cost Containment Measures

Private sector employers have attempted to hold down increases in the cost of providing health benefits to their employees by (1) switching from traditional indemnity programs to managed care plans, (2) requiring employees to pay higher premiums, and (3) increasing employees' share of claims costs through higher deductibles, co-payments, and out-of-pocket maximums. For example, in the 1992 U.S. Chamber of Commerce Survey of Health Benefits, 80 percent of the surveyed employers required their employees to contribute to the cost of their health care; nearly half increased employee premiums in 1991; and 73 percent instituted or increased deductibles.

## Departmental Initiatives

The Department, through Contractor Resource Management, has initiated various actions to contain health benefit costs. These actions included: (1) improved data collection, (2) increased training of field personnel, (3) an active review of changes to

benefit plans, and (4) improved contract language. In addition, two of the M&O contractors we reviewed had taken action to contain health benefit costs.

Contractor Resource Management had developed and was implementing a new report for the Group Insurance Data System. The new report required contractors to submit detailed annual reports of total expenditures for group insurance and other health benefit programs. Contractor Resource Management had also included various cost saving measures in its seminars and orientation meetings for the Department's Industrial Relations employees. In addition, Contractor Resource Management personnel had reviewed health benefit programs submitted to them by various contractors and had disapproved some requested changes because they were too costly.

Language was also included in the Sandia National Laboratory Request for Proposal (RFP) calling for contractors to "annually examine the design and administration of the group insurance plans and propose whatever changes are appropriate and consistent with industry standards and norms." In addition, the Sandia RFP required mandatory employee contributions toward the premium cost of contractor provided health benefit plans. Contractor Resource Management personnel stated they believed the Department intends to use the Sandia RFP as a model for future M&O contracts.

At the time of our review, some of the M&O contractors had also implemented changes to contain health benefit costs. For example, the Midwest Research Institute at the National Renewable Energy Laboratory sought to contain costs by increasing employee deductibles, increasing out-of-pocket maximums, and making their employees aware of the importance of reducing the use of unneeded medical services. Another contractor, EG&G, sought to contain costs by changing from a minimum premium arrangement to a self-insured administrative services only arrangement, as a method of funding health benefit plans for their employees.

#### OBSERVATIONS AND CONCLUSIONS

Despite the positive actions taken by the Department and its contractors, we concluded that further improvements were needed in the Department's administration of M&O contractor employee health benefit plans. The Department's policies and procedures were not adequate to ensure that the Department's share of health benefit costs was reasonable. Our review of \$95 million in health benefit costs incurred at six M&O contract sites showed that \$15.4 million of those costs were excessive when compared to the costs of other firms as established by a national survey.

Departmental procedures require the examination of total employee compensation, of which health benefits is one component. However, our examination disclosed that total employee

compensation costs for FY 1991 had not been evaluated for reasonableness at any of the six contractors audited. When health benefit costs were specifically reviewed, the Department and its contractors were not consistent in their approach. For example, the health benefit costs of one M&O contractor had been examined for reasonableness by comparing those costs to costs at similar firms using national norms. The health benefit costs of three other M&Os were compared to the cost of other M&O contractors, but not to any private sector operations, including their own.

Based on this information, we concluded that the Department had not taken effective action to determine the reasonableness of health benefit costs at its M&O contractors. To establish more effective Departmental management of M&O health benefit costs, we recommend that the Deputy Assistant Secretary for Procurement and Assistance Management: (1) publish quantitative measurement techniques or standards to test the reasonableness of health benefit costs; (2) require tests of reasonableness to be performed on a periodic basis; and (3) provide guidance concerning specific health care provisions to be included in the personnel appendix of M&O contracts.

In our opinion, the finding in this report disclosed a material internal control weakness that the Department should consider when preparing its yearend assurance memorandum on internal controls.

## PART II

### FINDING AND RECOMMENDATIONS

#### Health Benefit Costs at the Department's Management and Operating Contractors

##### FINDING

The Department of Energy Acquisition Regulation (DEAR) required that costs incurred by Management and Operating (M&O) contractors, including health benefit costs, be reasonable. According to the DEAR, reasonableness was to be measured by comparing the M&O contractor's health benefit costs to the costs incurred by other firms, and to costs incurred by the contractor's own private sector operations. We found that the Department's share of M&O contractor health benefit costs was not reasonable based on either comparative measure. The Department incurred additional costs because it had not developed the policies, procedures, and standards necessary to ensure that required standards for reasonableness were being met. Specifically, the Department had not (1) published quantitative measurement techniques or standards to test reasonableness; (2) required tests of the reasonableness to be performed on any periodic basis; and (3) provided guidance concerning specific health care provisions to include in the personnel appendix of its M&O contracts. As a result, in FY 1991, the Department paid \$15.4 million in excess of industry norms for health benefit costs at the six M&O contractors audited.

##### RECOMMENDATIONS

We recommend that the Deputy Assistant Secretary for Procurement and Assistance Management:

1. Publish quantitative measurement techniques or standards that can be used to test the reasonableness of the Department's M&O contractor employees' health benefit costs.
2. Require tests of the reasonableness of the Department's M&O contractor employees' health benefit costs to be performed on a periodic basis.
3. Provide guidance concerning specific health care provisions to be included in the personnel appendix of the Department's M&O contracts.

## MANAGEMENT REACTION

Management concurred with the finding and recommendations and initiated corrective actions.

## DETAILS OF FINDING

### DEPARTMENT POLICIES AND PROCEDURES ON HEALTH BENEFIT COSTS

The DEAR sets forth requirements for Departmental approval of M&O contractors' health benefit plan costs. The overall requirement was that to be allowable, costs -- including health benefit costs -- must be reasonable. The DEAR defined reasonableness by prescribing three generic measuring techniques: (1) comparison to similar firms, (2) comparison to the M&O contractor's own private sector operations, and (3) comparison to provisions in the M&O contract.

#### Comparison to Similar Firms

The DEAR Part 970.3102-2(c) defines reasonableness of total compensation for personal services (including health benefits) as comparable compensation for similar work at other firms of the same size, in the same industry, or in the same geographic area.

Although we sought to test the reasonableness of health benefit costs using this comparison technique, we found that the Department had not provided any guidance for developing standards which could serve as the basis for a comparison. As a result, we researched the availability of compilations of actual health care costs and found that several firms and agencies periodically publish such compilations.

As a basis for comparison, we selected a national survey performed by the benefits consulting practice of a major accounting firm. Other studies could have served as a basis for comparison, and we do not advocate use of any particular survey as representing a sole national norm. However, quantitative measuring techniques are necessary to assess the "reasonableness" of health benefit costs.

#### Comparison to the Contractor's Own Private Sector Operations

The second comparative measure for reasonableness cited by the DEAR was the practice of comparing costs to the contractor's private operation. DEAR Part 970.3102-2(n) required that an M&O contractor's health benefits be no more, or no less, favorable than the benefits offered to employees in the contractor's private operations, even if the total compensation package was otherwise reasonable.

Additionally, benefit plans offered in a contractor's private operations that are proposed for contract work are to be disallowed if they do not meet Department standards for reasonableness. Even those benefit plans specifically established to meet the particular needs of the contract were required to conform to Department policy.

#### Comparison to Provisions in the M&O Contract

The DEAR also established a minimum test of reasonableness for fringe benefits based on the content of the M&O contract. DEAR Part 970.3102-2(n) provided that, subject to the determination that total compensation was reasonable, costs of employee insurance were to be treated as allowable if the employee insurance plan met certain conditions. One condition was that, to the fullest extent possible, definite limitations or terminal points should be established for the employee insurance plan, so that the Department's full liability with respect to employee insurance was established under the contract.

#### HEALTH BENEFIT COSTS

The audit disclosed that none of the six M&O contracts audited had been formally reviewed to determine if total employee compensation for FY 1991 was reasonable. The DEAR required this overall determination to be performed before individual components, such as health benefits, were evaluated. For this reason, and other reasons discussed on page 13, we did not assess the reasonableness of costs in comparison to contract provisions.

However, our examination disclosed that the costs of six M&O contractor health benefit programs were excessive when compared to national norms and to the contractors' own private sector operations.

#### Comparison to National Norms

In 1991, the national norm for an employer's contribution was 87 percent for single coverage, and 77 percent for family coverage. National norms also showed that employees were responsible for deductibles of \$200 for single coverage and \$400 for family coverage, and had an out-of-pocket maximum of \$700. As discussed below, the M&O contractors' employer share of both premium and claims costs was significantly higher than national norms.

#### Premium Costs

The employer's share of premiums at the M&O contractors reviewed was higher than the national norm. For example:

- In 1991, EG&G paid 100 percent of the premium cost of both single and family health benefit coverage. This amounted to \$5.2 million more in costs to the Department than if the cost-sharing structure had matched the national norm.
- In 1991, Westinghouse Hanford Corporation employees contributed 0.3 percent of their base salary for single coverage and 0.3 percent of base salary plus \$8.33 per month for family coverage. In 1991, employer contributions at Westinghouse Hanford were \$4.1 million more than they would have been if the cost-sharing structure had matched the national norm.

### Claims Costs

The Department's share of the cost of M&O contractor employee health claims was also greater than national norms. Private industry has required employees to pay higher coinsurance, deductibles, and out-of-pocket maximums as a means of containing health care costs. However, M&O employees' costs for coinsurance, deductibles, and out-of-pocket maximums were lower than the national norms. For example:

- Westinghouse Hanford employees had coinsurance levels, deductibles, and out-of-pocket maximums that were 12 percent less than the national norms. This included deductible levels of \$125 for individual and \$300 for family coverage compared to national norms of \$200 and \$400, respectively.
- EG&G employees had deductible levels of \$100 for individual and \$200 for family coverage. These were 50 percent lower than the national norms.

Additionally, some contractors had not increased employee coinsurance levels, deductibles, or out-of-pocket maximums for several years. For example, between 1990 and 1993 there had been no increase in EG&G employees' coinsurance, deductibles, and out-of-pocket maximums. We noted that after the union contract expired in September 1993, the M&O contractor negotiated to have both union and non-union members pay a percentage of their health benefit costs under the new contract.

These comparisons were discussed with Departmental officials who disagreed with our use of national norms. Management stated that a determination of reasonableness should include regional differences. As an example, management noted that according to one study, 54 percent of employers in the Pacific region and 42 percent of those in the north central region did not require employee contributions for conventional health insurance. While we agree that such regional standards could be used to measure the reasonableness of health benefit costs, the Department

currently has no published guidance to facilitate the use of regional standards or any other standards.

#### Comparison to Parent Company

A comparison also showed that the Department's M&O contractors paid higher premium costs and higher claims costs than those paid by the contractors' private sector operations.

##### Premium Costs

The M&O contractors contributed a greater portion of the cost of health insurance premiums for their employees working on an M&O contract than for their employees working in their private sector operations. For example, EG&G Rocky Flats paid 100 percent of the premiums for their employees health insurance, while EG&G Corporate Headquarters paid about 80 percent of the premium.

Battelle Pacific Northwest Laboratory also paid a greater share of premiums than its parent organization, Battelle Memorial Institute. For example, a Laboratory non-bargaining unit employee making \$40,000 per year would contribute only \$32.79 per month for family coverage, while Battelle Memorial Institute employees pay \$91.50 per month for equivalent family coverage.

##### Claims Costs

The M&O contractors also contributed more towards the cost of their employees health benefit claims than the contractors' private sector operations. For example, EG&G employees had deductible levels of \$100 for individual and \$200 for family coverage, while EG&G Headquarters employees had deductibles of \$250 for individual and \$750 for family coverage. Wackenhut employees at Rocky Flats had deductible levels of \$100 for individual and \$200 for family coverage. Wackenhut's corporate employees had higher deductibles of \$500 for individual and \$1,000 for family coverage.

Management stated that both EG&G and Wackenhut's health benefit plans were inherited from previous contractors in 1990. In such cases, we believe that management should seek to bring the plans into alignment with the parent company. Although almost 3 years had elapsed since the plans were inherited, we saw no evidence that actions were being taken to align the plans. However, during the audit, one M&O contractor initiated actions to bring the plans into alignment.



## MANAGEMENT OF CONTRACTORS' HEALTH BENEFIT COSTS

The Department paid M&O contractors a greater portion of health benefit costs because it had not developed the policies, procedures, and standards necessary to ensure that the DEAR's tests for reasonableness were being met. Although the DEAR and DOE Order 3890.1A, "Contractor Insurance and Other Health Benefit Programs," assign responsibilities for developing the policies and procedures and setting the standards needed to direct M&O contractor health benefit plans, Department officials had not established specific policies, procedures, and standards. In addition, M&O contract language and the Department's approval practices were inadequate to prevent the incurrence of unreasonable health benefit costs. Specifically, the Department had not: (1) published quantitative measurement techniques or standards to test the reasonableness of health benefit costs; (2) required tests of the reasonableness of health care costs to be performed on any periodic basis; and, (3) provided guidance concerning specific health care provisions to include in the personnel appendix of M&O contracts.

### Quantitative Measurement Techniques and Standards

DOE Order 3890.1A assigned to the Office of Contractor Human Resource Management (Contractor Resource Management) the task of developing and implementing policies, procedures, and standards for group insurance. However, Contractor Resource Management had not developed specific policies, procedures, and standards for field personnel to follow in reviewing and approving M&O contractors' health benefit plans. Specifically, current Department policy sets no standard for the employer share that the Department will pay for health benefits.

### Periodic Testing of Reasonableness

DOE Order 3890.1A paragraph II.5.c and paragraph II.6.a.(1) prescribed that Contractor Resource Management is responsible for determining the reasonableness of health benefit costs prior to approval by the Contracting Officer. However, there were no published procedures describing how to perform this determination of reasonableness or how often to perform it. We did find that some Contracting Officers had made their own comparisons, but the comparison methods were not consistent. For example, two M&O contractors were compared to other M&O contractors, one M&O contractor was compared to national norms, and three M&O contractors were not compared to any outside health care costs.

### Guidance on Personnel Appendix Provisions

Rather than using industry and parent company practices as criteria, management advocated relying exclusively on the provisions contained in the negotiated personnel appendices of the M&O contracts. However, the audit disclosed that these

appendices were not adequate to serve as an effective control mechanism.

The DEAR required that an advance agreement on health benefits be reached and included in the contract to establish definite limitations or terminal points for health benefit costs, so that the Department's full liability with respect to those benefits is established under the contract. However, the Department had not implemented policies or procedures to ensure that contracts included specific language limiting the amount of health benefit costs that the Department would pay. We found that the appendices did not provide enough detail to determine reasonableness. For example, each appendix listed the medical, dental, and vision insurance plans available, and stated that health benefit costs, with some generalized exceptions, were allowable. In addition, the Department had not published specific language, for inclusion in the personnel appendices, to support disallowance of excessive health benefit costs.

Management stated that one reason a Department standard for allowability of health benefit costs had not been established was that it would make union negotiations more difficult. We agree that union negotiations are a consideration; however, the Department should develop methods to contain health benefit costs and ensure the reasonableness of such costs.

#### FUTURE EXPENDITURES

By not developing specific policies, procedures and standards, the Department permitted the expenditure of more than was necessary for M&O contractor health benefit costs. Our review showed that in FY 1991, the Department paid \$15.4 million more than was reasonable when compared to national norms. Specifically, the M&O contractors paid about \$10.1 million more than necessary as a result of not requiring employees to contribute a sufficient amount to the premium costs. These contractors also paid about \$5.3 million more than necessary for claim costs. (See Part V on page 19 for details.)

Because the Department may pursue many different approaches to implementing the recommendations contained in this report, the actual savings achieved may be larger or smaller than the \$15.4 million we estimated. For example, differences could arise from using data compiled through an alternative health benefit survey. Differences could also arise from using alternative analytical techniques, such as applying regional or local standards instead of national standards. Although the specific dollar savings may vary, the magnitude of the Department's potential savings would be significant.

Based on our discussions with personnel in Contractor Resource Management, we believe that the six M&O contractors

cited in this report are representative of the Department's M&O contractors. Accordingly, significant cost savings should be possible by implementing the recommendations in this report at all the Department's M&O contractors.

## PART III

### MANAGEMENT AND AUDITOR COMMENTS

In responding to this report, the Director, Office of Procurement, Assessment, and Property concurred with our finding and recommendations. A summary of management's comments and our responses follows.

#### GENERAL COMMENTS

Management Comments. Management was concerned with the conclusion in the report that the Department of Energy (Department) paid \$15.4 million more than was reasonable when compared to costs of other firms as established by a national survey.

Auditor Comments. We used the data from a national survey to underscore the point that management needs to develop procedures to compare M&O contractor health benefit costs to the costs of similar firms. As noted in the report, we are not necessarily advocating the use of a national survey, but rather development of a systematic approach to assure that the costs of the M&O health benefit programs are consistent with criteria set forth in the Department of Energy Acquisition Regulation (DEAR).

#### RECOMMENDATION 1

Management Comments. Concur.

Management stated that it was forming a process improvement team to review the DEAR and Department Orders relating to benefits, workers' compensation, and dependent care. The team will develop measurement criteria against which benefit cost reasonableness can be tested. Management expected that there were a number of sources upon which to rely and that no single number or standard was appropriate. The measurement standard for reasonableness would, therefore, be a quantitative range which will require a certain amount of qualitative judgement in its application.

Management believed it was not an industry or individual employer practice to determine what was "reasonable" with respect to health benefit program costs by selecting "a" number from a sample of normative data. Also, employers did not have uniform provisions among the different health benefit plans they offered their employees. Plans were designed differently based on benefit program goals and objectives. Diversity among

organizational cultures, missions and strategic goals was likely to be the norm. Thus, management concluded, there will be a range of acceptable plan provisions among diverse organizations.

Management also believed that the report strongly implies that the standard to be developed will be "a" number. Management did not believe that this was an appropriate way to develop policy or establish elements of reasonableness. The final output, in terms of policy and guidance for health benefit costs, must incorporate input from all stakeholders to recognize the diversity (as opposed to sameness) among contractors and their work forces and the force of legal contracts, historical influences, and the parameters defining change and opportunity.

Management stated that contractor benefit programs which reflect the diversity of work forces, organizational cultures, mission, and employee benefit needs best serve the strategic goals of the Department.

Additionally, management described two new cost analysis efforts it initiated. First, management stated that it had just completed, assisted by a support service contractor, a study of the health benefit programs of Wackenhut Services, Inc., at Rocky Flats. This study made a number of recommendations regarding minimum cost sharing provisions. Secondly, another support service contractor was in the process of conducting a detailed benefits survey of the Department's national laboratories that will be compared against a national database as well as to other laboratories within and outside the Department. Management believes this survey will provide useful information in evaluating the health benefit programs of a significant number of M&O contractors.

Auditor Comments. Management's comments are responsive to the recommendation. The intent of the recommendation will be met when the Department publishes the measurement criteria developed by the process improvement team.

## RECOMMENDATION 2

Management Comments. Concur.

Management stated that the measurement criteria developed by the process improvement team will be used to determine whether total benefit costs and/or plan provisions and financial arrangements are within acceptable boundaries.

Auditor Comments. Although management's comments were partially responsive to the recommendation, they did not address how often the Department would require tests of reasonableness to

be performed. We believe that these tests should be done on a periodic basis to assure that criteria set forth in the DEAR are met.

### RECOMMENDATION 3

Management Comments. Concur.

Management stated that the process improvement team will develop the Department (policy) Order on Contractor Employee Benefits. It will be the responsibility of Field and Operations Offices to incorporate the provisions of the Order in their M&O contracts.

Auditor Comments. Management's planned actions are responsive to the recommendation.

## **PART IV**

### **OTHER MATTERS**

#### **SELF-INSURANCE**

In addition to the methods for determining the reasonableness of health benefit costs, we also researched the national trend toward self-insurance as a tool to contain costs. From 1988 to 1991, the number of private sector businesses choosing self-insurance increased, regardless of whether their health insurance was provided by conventional or preferred provider organizations. Businesses choosing self-insurance paid no risk charges to insurance companies and could often avoid paying state taxes on premiums. Private sector businesses commonly considered self-insurance as a method of containing health benefit costs if they had at least 500 employees.

The audit disclosed that five of the six contractors reviewed had more than 500 employees, and two of these contractors were not self-insured. (See Part V for details.) We estimated that, in 1991, these two contractors could have avoided about \$400,000 in risk charges and premium taxes by self-insuring. In 1993, during the course of the audit, the larger of the two contractors implemented a self-insurance program for health benefits.

We brought the issue of self-insurance to the attention of Departmental officials during the course of our audit. These officials stated that they would review industry practices on this issue and would adjust Departmental policy should it become necessary. They also stated that self-insurance would not be appropriate in all cases. These officials indicated that they would continue to review proposals for self-insurance and approve self-insurance in situations where study indicated it would be in the best interest of the Department.

Management's continuing review of this issue addresses our concerns regarding self-insurance. However, we continue to believe that the Department could reduce health benefit costs by adopting a more proactive approach to determining whether an M&O contractor should self-insure.

**PART V**

**ANALYSIS OF 1991 HEALTH BENEFIT COSTS AT SIX M&O CONTRACTOR SITES**

M&O Contractor Location	EG&G ROCKY FLATS	WACKENHUT ROCKY FLATS	NREL GOLDEN	WHC HANFORD	PNL/BATTELLE HANFORD	HEHF HANFORD	TOTAL OF ALL SITES
Total Number of Employees	6,917	517	557	8,437	3,774	180	20,382
Self-Insured	No	Yes	No	Yes	Yes	No	

<b>POTENTIAL ANNUAL SAVINGS FROM INCREASED CONTRIBUTIONS FROM ACTIVE EMPLOYEES</b>							
PREMIUM COST SHARING							
Estimated Reasonable Contribution (1)	\$5,241,681	\$132,336	(2)	\$6,846,225	\$1,580,981	\$179,406	\$13,980,629
Actual Employee Contribution	0	0	(2)	2,724,500	1,149,972	(3) 30,030	3,904,502
Potential Savings	\$5,241,681	\$132,336	\$0	\$4,121,725	\$431,009	\$149,376	\$10,076,127
CLAIMS COST SHARING							
Actual Claims Cost	\$7,689,471	\$429,850	(2)	\$28,662,505	\$7,788,344	\$564,264	\$45,134,434
Estimated Reasonable Claims Costs (4)	6,843,629	382,566	(2)	25,223,004	6,853,743	530,408	39,833,350
Potential Savings	\$845,842	\$47,284	\$0	\$3,439,501	\$934,601	\$33,856	\$5,301,084
TOTAL POTENTIAL SAVINGS RELATED TO INCREASED EMPLOYEE CONTRIBUTIONS	\$6,087,523	\$179,620	\$0	\$7,561,226	\$1,365,610	\$183,232	\$15,377,211
<b>POTENTIAL ANNUAL SAVINGS FROM SELF-INSURING</b>							
State Premium Taxes Avoided	\$181,332	\$0	\$35,276	\$0	\$0	\$0	\$216,608
Risk Charges Avoided	143,563	0	34,918	0	0	0	178,481
TOTAL POTENTIAL SAVINGS RELATED TO SELF-INSURING	\$324,895	\$0	\$70,194	\$0	\$0	\$0	\$395,089
<b>TOTAL POTENTIAL SAVINGS</b>	<b>\$6,412,418</b>	<b>\$179,620</b>	<b>\$70,194</b>	<b>\$7,561,226</b>	<b>\$1,365,610</b>	<b>\$183,232</b>	<b>\$15,772,300</b>

(1) Estimated Reasonable Contribution is the amount the employees would have paid (based on actual cost of the plan) if the employee contribution percent matched the national norms found in the KPMG Peat Marwick Survey of 1991.

(2) Not analyzed

(3) Actual employee contributions for HEHF were estimated based on average enrollment

(4) Estimated Reasonable Claims Costs are those that would have been paid if the plans adhered to the national norm (from the KPMG survey of 1991) for a comprehensive Major Medical Plan with the following benefits:  
\$200 calendar year deductible/2 per family  
80%/20% coinsurance  
\$700 maximum out-of-pocket expense



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