Subpart 1631.2—Contracts With Commercial Organizations

Parent topic: PART 1631—CONTRACT COST PRINCIPLES AND PROCEDURES

1631.200 Scope of subpart.

The cost principles under this subpart apply only to contracts in which premiums and subscription income are determined on the basis of experience rating, in which cost analysis is performed, or in which price is determined on the basis of actual costs incurred.

1631.201-70 Credits.

The provisions of FAR 31.201-5 shall apply to income, rebates, allowances, and other credits resulting from benefit payments. Examples of such credits include:

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

(b) Hospital year-end settlements and other applicable provider discounts;

(c) Uncashed and returned checks;

(d) Utilization review refunds;

(e) Contract prescription drug rebates;

(f) Volume discounts;

(g) Refunds and other payments or recoveries attributable to litigation with subscribers or providers of health services; and,

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

1631.203 Indirect costs.

For the purposes of applying FAR 31.203(g)(2) to FEHB Program contracts, OPM considers the monthly rates used by some carriers to be a general practice in the insurance industry.

1631.203-70 Allocation techniques.

(a) Carriers shall use the following methods for allocating groupings of business unit indirect costs. Carriers shall consistently apply the methods and techniques established to classify direct and indirect costs, to group indirect costs and to allocate indirect costs to cost objectives.

(1) *Input method.* The preferred allocation technique is one that shows 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 input ordinarily may be expressed in terms such as labor hours or square footage. This means costs may 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 may 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 may be measured in terms of units of end product produced by the function(s). Examples of output measures include number of claims processed by a claims processing center, number of pages printed 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 function(s) 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, if a personnel department provides various services that cannot be measured practically on an activity (input) or output basis, number of personnel served might 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 might be to base them on a percentage of contracts. These examples are not meant to be exhaustive, but rather are examples of allocation methods that may be acceptable under individual circumstances. See also General and Administrative (G&A) expenses, FEHBAR 1631.203-71.

(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.

1631.203-71 Business unit General and Administrative (G&A) expenses.

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

1631.203-72 Home office expense.

A carrier's practices for allocating home office expenses to the segments of the carrier will be acceptable for purposes of FAR 31.203 if they are allocated on the 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 the 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.

1631.205 Selected costs.

1631.205-10 Cost of money.

For the purposes of FAR 31.205-10(b)(3), 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).

1631.205-41 Taxes.

5 U.S.C. 8909(f)(1) prohibits the imposition of taxes, fees, or other monetary payment, directly or indirectly, on FEHB premiums by any State, the District of Columbia, or the Commonwealth of Puerto Rico, or by any political subdivision or other governmental authority of those entities. Therefore, FAR 31.205-41 is modified to include those taxes as unallowable costs. The prohibited payments, referred to elsewhere in these regulations as “premium taxes,” applies to all payments directed by States or municipalities, regardless of how they may be titled, to whom they must be paid, or the purpose for which they are collected, and it applies to all forms of direct and indirect measurements on FEHBP premiums, however modified, to include cost per contract or enrollee, with the sole exception of a tax on net income or profit, if that tax, fee, or payment is applicable to a broad range of business activity.

1631.205-70 FEHBP public relations and advertising costs.

(a) The cost of media messages that are directed at advising current FEHBP subscribers on how to obtain benefits shall be an allowable expense within the meaning of FAR 31.205-1 because this service is directly related to performance of the FEHBP contract. If there is any question about the allowability of such a cost, the carrier may request advance approval regarding the content and cost of the message.

(b) Costs of media messages not provided for in paragraph (a) of this section are allowable if the content is specifically approved by the contracting officer and all of the following criteria are met:

(1) The primary effect of the message is to disseminate information on health care cost containment or preventive health care;

(2) The costs of the carrier's messages are allocated to all underwritten and non-underwritten lines of business; and

(3) The contracting officer approves the total dollar amount of the carrier's messages to be charged to the FEHBP in advance of the contract year.

(c) Costs of messages that are intended to, or which have the primary effect of, calling favorable attention to the carrier (or subcontractor) for the purpose of enhancing its overall image or selling its health plan are not allowable.

1631.205-71 FEHBP bad debts.

Erroneous benefit payments are not automatically disallowed by FAR 31.205-3.

1631.205-72 FEHBP compensation for personal services.

(a) Overtime on an FEHBP contract would normally meet the condition specified in FAR 22.103. Premiums for overtime, extra-pay shifts, and multi-shifts meeting the specified conditions shall be allowed without prior approval.

(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 1st year a carrier subject to paragraph (b)(1) of this section has a liability for accrued but unpaid expenses for compensated personal absences that would otherwise be allocable to FEHB 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 percent per year.

1631.205-73 FEHBP interest expense.

(a) Interest charges incurred in the administration of FEHBP contracts are not allowable in accordance with FAR 31.205-20. However, interest charges that are associated with the carrier's investment of FEHBP account funds are not considered administrative costs and may be allowable under very limited circumstances if all of the following criteria are met:

(1) Borrowing is limited to the positive balance of the carrier's entire FEHBP investment portfolio;

(2) FEHBP funds are tied up in long-term securities;

(3) Liquidation of long-term securities would cost more than the cost of the interest;

(4) The interest rates charged are at or below current market rates; and

(5) Advance written approval of the contracting officer is obtained before such costs are incurred.

(b) The carrier must demonstrate on a case-by-case basis that borrowing rather than cashing in long-term investments shall actually result in cost savings to the FEHB Program. Satisfactory demonstration of cost savings is a prerequisite to contracting officer approval of the interest cost as a charge to the contract.

(c) If the interest charge is allowed, the risk factor in the service charge will be adjusted downward so that the carrier does not recover interest costs through both the service charge and an allowance under this paragraph.

1631.205-74 FEHBP losses on other contracts.

FAR 31.205-23 shall not be construed to prohibit the application of the normal “loss carry forward” principle that is fundamental to continuing insurance contracts that are based on experience rating.

1631.205-75 Selling costs.

(a) FAR 31.205-38 is modified to eliminate from allowable costs those costs related to sales promotion and the payment of sales commissions fees or salaries to employees or outside commercial or selling agencies for enrolling Federal subscribers in a particular FEHB plan.

(b) Selling costs are allowable costs to FEHBP contracts to the extent that they are necessary for conducting annual contract negotiations with the Government and for liaison activities necessary for ongoing contract administration. Personnel and related travel costs are allowable for attendance at Open Season Health fairs and other similar activities at which carriers give enrollees information about their choices among health plans (but see FAR 31.205-1 ‘Public relations and advertising costs’, and The Federal Employees Health Benefits Handbook for Personnel and Payroll Offices, Subchapter S2-3(f) ‘Controlling contacts between employees and carriers’).

1631.205-76 Trade, business, technical, and professional activity costs.

(a) FEHBP participating plans, carriers, and underwriters shall seek the advance written approval of the contracting officer for allowability of all or part of the costs associated with trade, business, technical, and professional activities (FAR 31.205-43) when the allocable costs of such participation to the FEHBP will exceed $1,000 annually and when the carrier or underwriter allocates more than 50% of the membership cost of a trade, business, technical, or professional organization to the FEHBP.

(b) When approval of costs for membership in an organization is required, the carrier or underwriter must demonstrate conclusively that membership in such an organization and participation in its activities extend beyond the contractual relationship with OPM, have a reasonable relationship to providing care and services to FEHBP enrollees, and that the organization is not engaged in activities such as those cited in FAR 31.205-22 (lobbying costs) for which costs are not allowable.

1631.205-77 FEHBP start-up and other nonrecurring costs.

Precontract costs (FAR 31.205-32) shall be allowed only to the extent provided for by advance agreement in accordance with FAR 31.109.

1631.205-78 FEHBP printed material costs.

Unless OPM determines that it is in the best interest of the FEHBP to do otherwise, if a carrier orders printed material that is available from the Government Printing Office (GPO) under the “rider system” from another source, the allowable contract charges shall be the lesser of the amount actually paid or the cost that would have been incurred had the carrier ridden OPM's GPO order.

1631.205-79 Mandatory statutory reserves.

Charges for mandatory statutory reserves are not allowed unless provided for in the contract. When the term “mandatory statutory reserve” is specifically identified as an allowable contract charge without further definition or explanation, it means a requirement imposed by State law upon the carrier to set aside a specific amount or rate of funds into a restricted reserve that is accounted for separately from all other reserves and surpluses of the carrier and which may be used only with the specific approval of the State official designated by law to make such approvals. The amount chargeable to the contract may not exceed an allocable portion of the amount actually set aside. If the statutory reserve is no longer required for the purpose for which it was created, and these funds become available for the general use of the carrier, a pro rata share based upon FEHBP's contribution to the total carrier's set aside shall be returned to the FEHBP in accordance with FAR 31.201-5.

1631.205-80 Major subcontractor service charges.

In a subcontract for enrollment and eligibility determinations, administration of claims and payment of benefits, and payment or provision of actual health services, and/or assumption of insurance risk or underwriting, when costs are determined on the basis of actual costs incurred or experience rating, any amount that exceeds the allowable cost of the subcontract (whether entitled service charge, profit, fee, contribution to reserve, surplus, or any other title) is not allowable under the contract. Amounts which exceed allowable costs may be paid to a major subcontractor only from the service charge negotiated between OPM and the Carrier.

1631.205-81 Inferred reasonableness.

If the carrier follows the notification and consent requirements of paragraphs (a), (b) and (c) of 1652.244-70, and subsequently obtains the Contracting officer's consent or ratification, then the reasonableness of the subcontract's costs shall be inferred.

1631.205-82 Audits.

Carriers should ensure that the public accounting firms with which they contract for audits of FEHB accounts are registered with the Public Company Accounting Oversight Board (PCAOB).