#47 Joseph Vengrin Federal-Auditor

DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Washington, D.C. 20201

APR 18 2007

Ms. Wendy M. Comes
Executive Director
Federal Accounting Standards Advisory Board
441 G Street NW.
Washington, DC 20548

Dear Ms. Comes:

Thank you for the opportunity to comment on the Federal Accounting Standards Advisory Board's proposed standard, "Accounting for Social Insurance, Revised: Preliminary Views," dated October 23, 2006. Our comments, which focus on the Medicare program, are enclosed.

If you have any questions about our comments, please do not hesitate to call me, or your staff may contact Lori S. Pilcher, Assistant Inspector General for Financial Management and Regional Operations, at (202) 619-1157 or Janet Kramer, Director of Financial Management and Audits, at (410) 786-7107.

Sincerely,

Joseph E. Vengrin
Deputy Inspector General
for Audit Services

Enclosure

Below are answers to questions posed by the FASAB in "Accounting for Social Insurance, Revised: Preliminary Views," dated October 23, 2006, with respect to the Statement of Social Insurance for CMS – Medicare.

QUESTIONS 1, 2, and 3.1

Which obligating event do you believe creates a liability and expense that should be recognized?

Do you believe that Medicare obligations are measurable for purposes of recording a liability after 40 quarters or equivalent of work in covered employment?

Do you believe that the Primary View proposal to add line items to the SOSI that tie to revised expense and liability amounts reported on the statement of net cost and the balance sheet, respectively, should be adopted?

HHS OIG agrees with the Alternative View that a liability is not created, and therefore should not be recognized, until the following conditions are met: (1) the participant meets all eligibility requirements for benefits and (2) benefit payments become due and payable. This is consistent with the recognition that entitlement to Medicare benefits is not a contractual right. It is also consistent with principles of liability recognition found in SFFAS No.5.

In Flemming v. Nestor (36 U.S. 603, 1960), the Supreme Court articulated the principle that entitlement to Social Security benefits is not a contractual right. The Supreme Court acknowledged that many individuals who contribute to Social Security through payroll taxes are expected to ultimately become beneficiaries of that program. However, the Court noted that while a worker's benefits may derive from the contributions made via payroll taxes, those benefits do not depend on the amount of taxes paid. We believe that the nexus between contributions and benefits is even more tenuous in the Medicare system, where the value of benefits provided to beneficiaries will vary widely depending on their medical needs.

SFFAS No. 5, paragraph 19, defines a liability for Federal accounting purposes as a probable future outflow or sacrifice of resources as a result of past transactions or events. We do not believe that when an individual engages in covered employment for 40 quarters, a "transaction or event" triggering a probable future outflow has taken place.

Therefore, an individual's engagement in covered employment for 40 quarters would not create an obligation for the Medicare program because not all eligibility requirements have been met and no services have been provided that would result in recording a liability on the financial statements.

As noted above, HHS OIG does not believe that the Primary View proposal to add line items to the SOSI that tie to revised expense and liability amounts should be adopted.

QUESTION 3.2

Do you believe that the reasons for changes in SOSI amounts during the reporting period should be reported and, if so, do you favor such reporting (1) as proposed by the Primary View, (2) as proposed by the Alternative View, or (3) some other approach?

HHS OIG does not believe that the reasons for changes in SOSI amounts during the reporting period and related presentations should be reported as proposed. The current 75-year projections involve many variables and assumptions that are inherently uncertain. The cost of preparing and auditing a SOSI statement of change by reconciling each actuarial variable would be prohibitive and of little practical use. Because the programmatic changes required to ensure the solvency of the Medicare program would be of such significance and complexity, they would require extensive narrative to explain the impact of the changes. Furthermore, we believe that changes of this magnitude would be adequately disclosed in the:

- Summary of Significant Accounting Policies,
- Statement of Social Insurance footnotes,
- Management Discussion and Analysis, and
- Required Supplementary Information sections of the financial statements.

Major changes in the SOSI estimates are currently disclosed in the annual Boards of Trustees Report and the CMS financial statements. For example, in their 2006 report, the Trustees noted: "Under the intermediate assumptions the HI trust fund is projected to be exhausted in 2018, 2 years earlier than in last year's report, due to slightly higher costs in 2005 than previously estimated and some upward revisions in the short-range assumptions . . . ."

QUESTION 4

Do you believe the proposal for presenting a statement of fiscal sustainability in the consolidated Financial Report of the U.S. Government should be adopted?

HHS OIG does not believe that a statement of fiscal sustainability, as currently written, should be adopted. We believe that the SOSI, as currently presented, provides the information necessary to assess the long-term sustainability of the program, as well as the ability of the program to raise resources from future program participants to pay for benefits to present participants. The Boards of Trustees and the SOSI are absolutely clear on the sustainability of the various programs. For example, the Trustees' 2006 report noted: "The financial outlook for the Medicare program continues to raise serious concerns, despite its lower projected costs at the end of the 75-year projection period." The Trustees further noted: "These projections demonstrate the need for timely and effective action to address Medicare's financial challenges."

QUESTION 5

Do you believe that the Board should consider recognizing deferred revenue for earmarked revenues in excess of related program costs?

HHS OIG does not believe that the Board should consider recognizing deferred revenue for earmarked revenues in excess of related program costs because the proposal would require the recognition of an additional liability that does not include all revenue received by the Medicare program. This liability would be difficult to determine because a subsidiary ledger of detailed beneficiary information would need to be maintained, similar to an accounts payable or accounts receivable. Also, the amounts paid by beneficiary, the number of months paid, and the beneficiary's enrollment status would need to be tracked to determine the amount of the deferred credit.

As defined by the United States Standard General Ledger, deferred credits are based on revenue or income received and not yet earned, which implies an exchange transaction. Therefore, under this proposal, the deferred revenue would be limited to premiums paid by beneficiaries and would require the matching of benefits received to those premiums. However, a significant portion of Medicare revenue is nonexchange, and all revenue not needed to pay current benefits is used to purchase Treasury securities, which are reported as investments on the CMS financial statements.

QUESTION 6

Please offer any comments that you wish to make on the Primary View or Alternative View provisions.

We have no additional comments.