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**REPORT TO THE SUBCOMMITTEE
ON INTERGOVERNMENTAL RELATIONS
COMMITTEE ON GOVERNMENT
OPERATIONS
HOUSE OF REPRESENTATIVES**

74-0587



**Award Of Subcontract
For Processing Medicare Claims
For Physicians' Services
In Ohio And West Virginia**

B-164031(4)

Social Security Administration
Department of Health, Education,
and Welfare

**BY THE COMPTROLLER GENERAL
OF THE UNITED STATES**

AUG. 2, 1973

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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-164031(4)

The Honorable L. H. Fountain, Chairman
Subcommittee on Intergovernmental Relations
Committee on Government Operations
House of Representatives

Dear Mr. Chairman:

In accordance with your September 7, 1972, request, we are sending you our report on the award of the subcontract for processing Medicare claims for physicians' services in Ohio and West Virginia.

Pursuant to your letter dated April 30, 1973, we are handling separately the applicability of Federal Procurement Regulations to Medicare contracts and other issues concerning contracting with carriers under part B of the Medicare program.

We requested and received written comments on the matters in this report from the Department of Health, Education, and Welfare; the Medicare carrier for Ohio and West Virginia; and the three offerors involved.

As your office agreed, we are sending a copy of this report to Congressman Clarence J. Brown, a member of your Subcommittee. We do not plan to further distribute this report unless you agree or publicly announce its contents.

Sincerely yours,

A handwritten signature in cursive script that reads "Thomas P. Skates".

Comptroller General
of the United States

ABBREVIATIONS

ASDC	Applied Systems Development Corporation
BHI	Bureau of Health Insurance
EDP	electronic data processing
EDS	Electronic Data Systems Corporation
EDSF	E.D.S. Federal Corporation
FPRs	Federal Procurement Regulations
GAO	General Accounting Office
GHI	Group Health Incorporated
HEW	Department of Health, Education, and Welfare
MCAUTO	McDonnell Douglas Automation Company
RFP	request for proposal
SSA	Social Security Administration
UCC	University Computing Company

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COMPTROLLER GENERAL'S
REPORT TO THE SUBCOMMITTEE
ON INTERGOVERNMENTAL RELATIONS
COMMITTEE ON GOVERNMENT OPERATIONS
HOUSE OF REPRESENTATIVES

AWARD OF SUBCONTRACT FOR
PROCESSING MEDICARE CLAIMS
FOR PHYSICIANS' SERVICES
IN OHIO AND WEST VIRGINIA
Social Security Administration
Department of Health, Education,
and Welfare
B-164031(4)

D I G E S T

WHY THE REVIEW WAS MADE

At the request of the Subcommittee Chairman, GAO examined procurement policies and practices followed in subcontracting for electronic data processing services by Nationwide Mutual Insurance Company under its contract with the Social Security Administration (SSA).

Nationwide serves as the carrier, or organization making Medicare payments for physicians' services and other medical services in Ohio and West Virginia.

The Subcommittee wanted GAO to determine whether Nationwide and SSA had followed sound procurement policies and practices in awarding a Medicare data processing subcontract to E. D. S. Federal Corporation.

SSA has taken the position that its contracts with Medicare carriers and intermediaries are not subject to the Federal Property and Administrative Services Act of 1949 and the related Federal Procurement Regulations which generally apply to the contracting activities of civilian agencies. Because opinions on this issue have differed, the Subcommittee asked GAO to deal with it separately.

In the absence of a specific requirement imposed as a condition of subcontract approval, the award of the Medicare subcontract by the carrier generally was not subject to the statutory and regulatory requirements governing direct procurements by the Federal Government.

Background

Nationwide has been a Medicare carrier since the program's inception in 1966. Early in 1969 Nationwide realized its Medicare claims processing system was no longer acceptable to SSA. Nationwide therefore subcontracted with the Applied Systems Development Corporation for a new system which became operational in July 1971.

A significant backlog of unprocessed claims, plus problems with the new system, triggered the search for another data processing subcontract. Nationwide requested system proposals from E. D. S. Federal, McDonnell Douglas Automation Company, and University Computing Company.

FINDINGS AND CONCLUSIONS

Nationwide did not follow sound, competitive procurement practices in developing specifications or in soliciting and evaluating proposals.

--Responding offerors considered the specifications in the request for proposals vague, although they generally understood what Nationwide wanted. Further, the type of system Nationwide preferred apparently emerged after proposals were requested.

--Initially the offerors were informed verbally of factors which would be used to evaluate the proposals, but only one was given the relative weights which would be given to the factors.

--Some of the original evaluation factors and their weights were later changed or were not used, without notifying the offerors. (See pp. 16 and 27.)

--As a condition of SSA's approval of the proposed award to E. D. S. Federal, significant changes were negotiated in the terms and conditions of the proposed subcontract; the other offerors were not given the opportunity to respond to the modified terms and conditions. (See p. 53.)

SSA had not established adequate procurement procedures for carriers to follow in developing specifications or obtaining and evaluating competitive proposals from competent sources.

Proposals received

Proposals received differed significantly in type of system and services proposed, term of subcontract, and average cost to process a claim.

--E. D. S. Federal proposed total facilities management under a 6-year contract at an average price of 93.6 cents per claim.

--McDonnell Douglas proposed three versions of the model B system-- batch, online, and hybrid (combination of batch and online processing)--at prices averaging from 28.1 cents to 53 cents per claim.

--University Computing proposed a batch version of the model B system at 23.5 cents per claim under a 1-year contract and 21.2 cents per claim under a 6-year contract. It later revised its proposal to an online system at an average price of 29.3 cents and 25.3 cents per claim under a 1-year and a 6-year contract, respectively. (See pp. 27 to 29.)

Nationwide's evaluation of proposals

SSA allowed Nationwide considerable discretion in determining how to evaluate proposals and what factors to consider in selecting a particular subcontractor.

Nationwide's evaluations were based on the offerors' estimates of the total cost of processing claims under each system rather than on the offerors' proposed prices for processing a Medicare claim.

Nationwide added to the proposed prices of 93.6, 53, and 25.3 cents estimates of Nationwide's other costs for paying Medicare claims. These adjustments resulted in estimates of total cost per claim under the E. D. S. Federal, McDonnell Douglas, and University Computing proposals of \$2.40, \$2.31, and \$2.06, respectively. (See p. 30.)

Using Nationwide's estimated cost per claim and its estimate of claims volume, the total annual cost of processing claims using E. D. S. Federal was about \$6.2 million, using

McDonnell Douglas was about \$5.9 million, and using University Computing was about \$5.3 million. (See p. 27.)

Nationwide considered E. D. S. Federal's proposal superior to the others and, in making its recommendation to select E. D. S. Federal, considered of primary importance the contractor's and system's performance capabilities, the cost, and the system's impact on its personnel requirements. (See p. 35.)

SSA's evaluation of proposals

SSA made two evaluations, concluding that approval of the recommended award to E. D. S. Federal was not warranted because of the cost difference between the E. D. S. Federal and the lowest cost proposal.

SSA's approach to evaluating the cost of proposals differed from Nationwide's. This difference--together with different assumptions on future workload, salary increases, and manpower requirements--was significant enough, in one of the evaluations, to change the proposals' ranking so that University Computing had the lowest cost, E. D. S. Federal had the second lowest, and McDonnell Douglas had the highest. (See p. 44.)

Nationwide and E. D. S. Federal agreed to modify the proposed subcontract substantially. The modifications involved guarantees of the total claims processing costs. Despite SSA's suggestion that other offerors be given the opportunity to compete, Nationwide did not give University Computing and McDonnell Douglas such an opportunity.

Because Nationwide viewed E. D. S. Federal's proposal to be superior to the others, GAO believes negotiations with the other offerors probably would not have had much effect on the ultimate selection of E. D. S. Federal.

However, GAO believes that this procurement action was not consistent with SSA's stated policy of fostering competition among the various suppliers of data processing services because:

- SSA's intervention to permit other offerors to respond to the modified terms and conditions was ineffective.
- Only one of the offerors could meet Nationwide's preference for a proven online system.

RECOMMENDATIONS OR SUGGESTIONS

In line with its policy of fostering competition, SSA should consider requiring that potential offerors be advised, in writing, of the evaluation criteria which will be used to evaluate their proposals. They should be advised of the relative importance that will be given to all evaluation factors, particularly price or cost. (See p. 43.) GAO expects that SSA, as part of its approval authority, will insure adherence to such evaluation criteria.

SSA should give careful attention to the validity of the basic approaches and assumptions to be used in computing the total cost of a proposal and should advise carriers and intermediaries--as well as potential data processing subcontractors--just how the factors, over and above the quoted prices, are to be computed. (See p. 51.)

AGENCY ACTIONS AND UNRESOLVED ISSUES

2. The Department of Health, Education, and Welfare (HEW); Nationwide; and the offerors were given an opportunity to review a draft of this report. HEW concurred in GAO's suggestions and said it would revise its instructions to the carriers. (See p. 66.)

Nationwide did not agree with GAO's general findings as

previously stated. (See pp. 66 to 69.)

E. D. S. Federal maintained that the report did not recognize sufficiently the differences between its proposal and those of the other offerors. (See pp. 69 and 70.)

University Computing concurred in GAO's assessment, and McDonnell Douglas had no comments. (See p. 71.)

CHAPTER 1

INTRODUCTION

In accordance with a September 7, 1972, request from the Chairman of the Intergovernmental Relations Subcommittee, House Committee on Government Operations, (see app. I), we have examined the procurement policies and practices followed in subcontracting for certain electronic data processing (EDP) services by the Nationwide Mutual Insurance Company in its capacity as the Medicare carrier in Ohio and West Virginia.

Title XVIII of the Social Security Act (42 U.S.C. 1395)--commonly referred to as Medicare--effective July 1, 1966, provides the following basic forms of health care benefits to eligible persons aged 65 and over.

--Part A, Hospital Insurance Benefits for the Aged, covers inpatient hospital services and certain post-hospital care in skilled-nursing facilities and in patients' homes. Part A is financed by special social security taxes paid by employees, employers, and self-employed persons.

--Part B, Supplementary Medical Insurance Benefits for the Aged, is a voluntary program and covers physicians' services and other medical and health benefits. Part B is financed by premiums collected from eligible beneficiaries who have elected to be covered by the program and by matching amounts appropriated from the general revenues of the Federal Government.

Medicare is administered by the Social Security Administration (SSA) of the Department of Health, Education, and Welfare (HEW). To help administer Medicare benefits, the Congress authorized HEW to contract with public agencies or private organizations to pay (1) hospitals and other institutions for services provided to eligible beneficiaries and (2) for physicians' and other covered services provided to such beneficiaries.

The organizations making payments to hospitals and other institutions under part A are called fiscal intermediaries. The organizations making payments for physicians' and other services under part B are called carriers.

"In the performance of their contractual undertakings, the carriers and fiscal intermediaries would act on behalf of the Secretary [of HEW], carrying on for him the governmental administrative responsibilities imposed by the bill. The Secretary, however, would be the real party in interest in the administration of the program, * * *."

Because of the language in section 1842 of the Medicare act, SSA has taken the position that its contracts with carriers and intermediaries are not subject to the Federal Property and Administrative Services Act of 1949 (41 U.S.C. 251 et seq.) and the related Federal Procurement Regulations (FPRs) which generally apply to the contracting activities of civilian agencies.

Because an HEW Assistant General Counsel has had differing opinions on this issue and because of its importance to contracting and subcontracting activities under the Medicare program, the Chairman of the Subcommittee asked us to deal with it separately. Nevertheless, in this instance, in the absence of a specific contract provision or other specific requirement imposed as a condition of subcontract approval, the procurement practices and procedures followed by the carrier in awarding the subcontract were generally not subject to the statutory and regulatory requirements which would govern direct procurements by the Federal Government.

SSA officials have stated, however, that as a matter of policy they attempt to follow the provisions of the FPRs. Some of these provisions, dealing with cost reimbursement and examination of records by HEW and GAO, have been included in the contracts with the carriers and intermediaries.

Contract provisions pertaining
to subcontracting

The current HEW standard contracts with its carriers, as revised in July 1970, include the following provisions on subcontracting.

"The carrier shall not enter into any subcontracts with a third party to perform any of the functions and duties set forth in this agreement unless

such subcontract is approved by the Secretary.

"The carrier shall enter into leases and other subcontracts and agreements for the purchase or rental of articles, supplies, equipment and services only in the manner provided in Article I of Appendix A to this agreement."

Article I of appendix A of the standard carrier contracts provides that:

"A. The carrier may enter into leases and may purchase articles, supplies, equipment and services which are necessary for the performance of the work required under this agreement, except that the following shall require prior written approval of the Secretary: (1) any lease of real property entered into the administration of the Medicare program, if more than 50% of the cost thereof will be charged to the Medicare program; and (2) subcontracts for materials or for services, or leases for equipment, which are to be used for the administration of the Medicare program, if the estimated cost to Medicare will exceed 50% of the cost over the term of such lease or subcontract and such estimated cost exceeds _____^[1]; or the estimated cost to Medicare will exceed _____^[2], irrespective of the percentage of the cost of such subcontract or lease to be charged to Medicare. Without regard for the requirements of prior approval under (2) above, the carrier shall give the Secretary advance notification of any subcontract or lease for

¹This amount is \$10,000, \$25,000, or \$50,000, depending on the size of the carrier's Medicare operation.

²This amount is \$25,000, \$50,000, or \$75,000, depending on the size of the carrier's Medicare operation.

equipment which provides for payment on a cost or cost-plus-fixed-fee basis, regardless of amount, or any fixed price subcontract or lease which results in payment by the Secretary of more than \$25,000. The carrier agrees that no subcontract placed under this agreement shall provide for payment on a cost plus-a-percentage-of-cost-basis. Prior written approval given by the Secretary under the provisions of this Article shall not be construed to constitute a determination of the allowability or unallowability of any costs under this agreement unless so stipulated."

SSA instructions to carriers on procedures to be followed in subcontracting

Early in the program, intermediary and carrier subcontracting activities were largely concentrated in the intermediary subcontracts with various public accounting firms to audit annual cost reports of institutional providers of service, such as hospitals and skilled-nursing facilities. SSA developed a standard audit subcontract and required that the intermediaries obtain price or cost proposals from at least two responsible firms. The audit subcontracts, as well as increases in subcontract amounts of more than 10 percent--increased to 15 percent in 1972--were subject to SSA's approval.

In March 1967 the Blue Shield carrier for Rhode Island entered into a subcontract with the Applied Systems Development Corporation (ASDC) to develop a Medicare claims processing system. In early 1968 the Blue Shield carrier for Texas subcontracted with Electronic Data Systems Corporation (EDS) to provide all data processing services to the carrier for its Medicare and other business. Under this subcontract EDS was responsible for a significant portion of Texas Blue Shield's Medicare claims processing function.

During the next 2 years, over 20 additional carriers entered into subcontracts with various firms for a variety of EDP systems and/or services. These services ranged from implementation, maintenance, and operation of a system to only implementation or maintenance of the system. At June 30, 1972, 27 of the 47 carriers had EDP subcontracts.

As the extent of the carriers' subcontracting activities increased, SSA issued additional general instructions to its contractors pertaining to (1) procurement policies and procedures and (2) SSA's requirements for prior approval of subcontracts.

In a November 1969 letter to its carriers, SSA advised that competitive proposals should be obtained for subcontracts for EDP services and that subcontractual arrangements should be submitted to SSA for approval before they are finalized.

In an August 1971 letter to its intermediaries and carriers, SSA required that certain technical and cost data on proposed systems modifications and development for processing Medicare claims be submitted to SSA for prior approval.

Finally, in an August 1972 manual release, SSA issued more detailed instructions to its carriers on the procedures for

- justifying the need for subcontracting for EDP software or related operating services,
- developing the technical specifications,
- obtaining sufficient proposals to produce at least three acceptable ones, and
- evaluating the proposals.

In summary, although the general requirement for prior SSA approval of intermediary and carrier subcontracts has existed since the program's inception, the instructions on the specific procurement policies and practices to be followed by SSA contractors appear to have gradually evolved as subcontracting activities have increased.

THE ROLE OF NATIONWIDE AS A MEDICARE CARRIER

Nationwide has been a carrier under part B of the Medicare program since the program's inception in July 1966. Initially, Nationwide was responsible for paying claims in West Virginia and in Ohio except for the five counties of

Ashtabula, Cuyahoga, Geauga, Lake, and Loraine. In July 1971 Nationwide took over these five counties when SSA did not renew the contract of the previous carrier--Medical Mutual of Cleveland, Inc. As of June 1972 Nationwide was responsible for paying the claims for about 1.2 million Medicare beneficiaries in Ohio and West Virginia.

During fiscal year 1972 Nationwide paid about \$77 million in benefits and incurred administrative costs of about \$7 million. In terms of claims processed, Nationwide was the ninth largest carrier in the country that year.

EXPLANATION OF TERMS

This report uses certain terms, explained below, to identify various systems or units of measurement commonly used in the Medicare program.

SSA model B system--The development of this claims processing system was initiated by SSA in collaboration with the McDonnell Douglas Automation Company (MCAUTO) and the Pilot Life Insurance Company--which until July 1969 was the carrier in North Carolina. Design of this system began in mid-1968, and the system began operating in North Carolina in June 1969. In July 1969 Pilot Life was replaced by the Prudential Insurance Company which continued to use the model B system for that State. SSA said that through June 1972 about \$4.4 million had been spent for the design, development, and maintenance of the model B system.

EDSF system--This system, including facilities management services, was proposed to Nationwide for processing part B claims. EDS designed and developed the system which, according to E. D. S. Federal Corporation (EDSF) officials, is a modification of other EDS data processing systems. These systems originated in early 1968 under a subcontract with the SSA carrier in Texas (Texas Blue Shield), and by June 1972 the systems had been installed at nine other Medicare carriers. EDSF, a wholly owned subsidiary of EDS, administers these systems.

Batch and online systems--These are types of EDP systems. According to SSA the major difference between a batch and an online system is the method of data entry and the amount of human intervention required for processing data.

In a batch system, claims are generally grouped (batched); and data from the claims is entered into the system by some regularized method, such as keypunch or keytape; and no edits are performed except by the batch programs in the computer.

In an online system, claims data is generally entered directly into the system and immediately subjected to some basic validation and verification edits. The system has the capability to immediately identify some errors or inconsistencies in the data and in many instances can make corrections before the process goes on. Another basic difference between these two systems is that persons entering data into an online system have more ready access to information already stored in the computer.

Opinions differ on the extent to which the EDSF and the part B model systems proposed to Nationwide are online systems. Our discussion with SSA and EDSF officials indicated that the systems are combinations of batch and online processing. Nationwide and the other subcontractor officials we interviewed generally referred to the systems as online. Therefore, for purposes of this report, we have referred to these systems as online.

Payment record--Under part B SSA requires carriers to prepare a record for each separate bill on which reimbursement is made. The record may or may not be the same as a request for payment (a claim). A payment record is one of a number of standard units used for workload measurement under Medicare.

CHAPTER 2

EARLIER DATA PROCESSING SYSTEMS AT NATIONWIDE

During the first 5 years of its participation in Medicare as a part B carrier, Nationwide processed claims using its own system. By July 1971, however, Nationwide had fully implemented a change from its system to a system developed by ASDC. Nationwide personnel operated the new system. The problems encountered by Nationwide with the ASDC system and with the subcontractor triggered the search for a new subcontractual arrangement.

IMPLEMENTATION OF THE ASDC SYSTEM

Early in 1969 it became apparent that Nationwide's Medicare data processing system was not effective and not acceptable to SSA. To resolve this problem, Nationwide decided to implement a new system.

Nationwide officials told us that one of the overriding considerations for selecting the ASDC system was that they wanted an existing system--one which had been used by other carriers to process Medicare claims. Nationwide looked at six potential sources and obtained proposals in May 1970 from three companies--ASDC; Computer Technology, Inc. (now part of University Computing Company (UCC)); and MCAUTO--which Nationwide considered qualified.

The ASDC proposal featured the use of the ASDC system which, at that time, was operational at the carrier for Rhode Island and at the carrier for New Hampshire and Vermont. The Computer Technology and MCAUTO proposals featured the use of the model B system which, at that time, was operational at the carriers for Alabama, Colorado, Louisiana, Nevada, North Carolina, and South Dakota.

After evaluating the proposals, Nationwide officials prepared a staff report recommending that, with the approval of SSA, Nationwide enter into a contract with ASDC for acquiring and implementing the ASDC system. These officials stated that their decision was based on interviews, system presentations, SSA performance statistics, and an evaluation of the proposals submitted. Their recommendation was presented to SSA for approval in September 1970.

In reviewing Nationwide's recommendation, SSA expressed reservations about the capabilities of the ASDC system to meet Medicare program requirements. However, in December 1970, after discussions and negotiations among Nationwide, ASDC, and SSA, SSA approved the subcontractual arrangements with ASDC with certain conditions. These conditions involved certain changes in contractual language to provide for access to system documentation and some modification of the ASDC system to bring it more in line with program requirements. In January 1971 Nationwide entered into separate subcontracts with ASDC for systems implementation and maintenance, respectively.

The ASDC system was implemented in May 1971 for West Virginia and in July 1971 for Ohio.

PROBLEMS WITH THE ASDC SYSTEM

Implementation of the ASDC system in Ohio coincided with Nationwide's assumption of responsibility for processing claims for the five counties in northern Ohio which had previously been served by Medical Mutual of Cleveland, Inc. Thus, Nationwide was making a major system conversion while assuming responsibility for a significant increase in its Medicare claims workload. Nationwide also had a backlog of unprocessed claims from the previous carrier which had an additional impact on its Medicare operation. These factors--the necessary accommodations to implementing and shaking down a new system, adapting the new system to Nationwide's requirements, hiring and training new staff, and retraining the old staff in the new system--all contributed to the accumulation of a very substantial backlog of unprocessed claims in a relatively short time after the new system became operational.

During the year ended June 30, 1972, Nationwide experienced a 73-percent increase in the volume of part B claims processed. A part of this increase resulted from the takeover of the five-county area. Nationwide's backlog of unprocessed claims jumped from about 57,000 claims in May 1971 to over 360,000 claims in September 1971. According to Nationwide officials, efforts to improve the ASDC system were not very successful and problems in obtaining system documentation made any modification of the system slow and very difficult. Both Nationwide and SSA officials said that

the situation continued to deteriorate during the latter part of 1971.

At SSA's request Nationwide officials attended a meeting at SSA headquarters on March 22, 1972. According to Nationwide officials, the primary purpose of the meeting was to introduce Nationwide's new vice president for Medicare to SSA officials. Discussions, however, soon turned to Nationwide's claims processing problems and its data processing system. SSA officials expressed dissatisfaction with Nationwide's situation and were primarily concerned with

- target dates for corrective actions which were not met,
- the large number of claims pending,
- the high number of beneficiary and congressional complaints, and
- Nationwide's plan to resolve these problems.

There was also extensive discussion of the technical phases of Nationwide's Medicare operation and some discussion of the possible use of SSA's model B system as an alternative and some of the problems with that system.

Nationwide officials told us that, although no firm commitments for a new system were made at the March 22 meeting, they had concluded that the only suitable solution to their claims processing problems was to obtain a new system. They stated that SSA officials had advised them that the EDSF system could be considered.

On March 27, 1972, the Bureau of Health Insurance (BHI) regional office representative in Chicago told Nationwide that SSA's position on selecting a new Medicare data processing system was neutral and that the decision was entirely up to Nationwide. According to the BHI representative, he had suggested that, if Nationwide decided on a new system, it should look at all available systems including the model B system and the EDSF system. He suggested also that competitive bids should be obtained from at least three qualified bidders.

CHAPTER 3

DEVELOPMENT OF SPECIFICATIONS AND

SOLICITATION AND INITIAL SUBMISSION OF PROPOSALS

In March 1972, when Nationwide decided to obtain a new system for its Medicare claims processing operation, SSA had not established adequate Medicare procurement procedures for

- developing specifications or
- obtaining competitive proposals from competent sources.

Further, as stated on page 7, the procurement practices and procedures followed by Medicare carriers and intermediaries are generally considered not subject to the requirements of the FPRs which govern direct procurements by the Federal Government.

As stated in SSA's testimony before the Intergovernmental Relations Subcommittee of the House Committee on Government Operations on May 31 and June 1, 1972, however, SSA's policy has been to foster competition among the suppliers of Medicare data processing services. Since November 1969 SSA has required its carriers to obtain competitive bids for data processing services without limiting the authority of the carriers to exercise their independent judgment in selecting the contractors that will best satisfy their requirements. SSA's role has been primarily that of reviewing and approving or not approving the carriers' selection.

We believe that sound competitive procurement practices--as set forth by the FPRs--were not followed in developing specifications and soliciting proposals for this procurement action.

- Nationwide's written specifications in the requests for proposals were vague. Therefore, it appears in retrospect that the type of system Nationwide really preferred emerged during the evaluation process rather than when the proposals were requested.
- Although all offerors were informally given the factors which would be used to evaluate the proposals, only

MCAUTO was given the weights which would be given to the factors. Furthermore, some of these factors and their weights apparently changed or were not used, without notifying the offerors.

We found no evidence that any of the three principal offerors had received advance notification of Nationwide's intention to solicit proposals.

SSA GUIDANCE TO NATIONWIDE

Nationwide officials advised us that they had received very little assistance or guidance from SSA for preparing technical specifications and identifying acceptable vendors. In addition to the November 1969 and August 1971 letters (see p. 10), SSA officials reminded Nationwide early in April 1972 of the need to get competitive bids from more than one qualified bidder. The officials also stressed the importance of getting comparable bids and of allowing sufficient time for preparing responses.

As a result of these contacts, SSA furnished Nationwide:

- A letter dated April 5, 1972, outlining some of the steps which should be followed in obtaining competitive proposals and developing technical specifications and a list of factors which should be considered in evaluating proposals.
- A draft copy of a proposed change to the Part B Intermediary Manual dealing with carrier subcontracting for EDP services, which was essentially the same as the August 1972 manual release discussed on page 10.

Nationwide officials stated, however, that they had received most of this information after they had given the request for proposals (RFP) to the prospective bidders.

Selection of potential offerors and notification of intention to solicit proposals

According to Nationwide officials, their selection of potential offerors was guided by their desire to deal with vendors experienced in operating ongoing and proven EDP

systems for processing Medicare claims. Therefore, other than continuing with ASDC, Nationwide officials maintained that they had two alternatives.

- Install the SSA model B system for which there were two experienced vendors (UCC and MCAUTO).
- Install the EDSF system which was owned and administered by EDSF.

According to FPRs, each RFP should be released to all prospective offerors at the same time and no offeror should be given the advantage of advance knowledge that proposals are to be requested.

We were told that initial contacts with the three potential offerors (EDSF, UCC, and MCAUTO) were made by telephone on March 30, 1972. We found no evidence that any of the potential offerors had received advance notification of Nationwide's intention to solicit proposals.¹ During the initial contacts the companies were advised that Nationwide was planning to change its Medicare system and that, if they were interested in proposing a system, they should prepare and submit their proposals by April 10, 1972. This date was subsequently changed to May 5, 1972.

After the initial contacts, some arrangements were made for company representatives to meet with Nationwide officials to discuss system requirements, review Nationwide's Medicare operations, and obtain any additional information considered necessary for developing responsive proposals. These meetings were held as follows:

¹In early February 1972 MCAUTO representatives made a sales trip to Columbus, Ohio, to acquaint Nationwide with MCAUTO's recent development of an online system. On March 3, 1972, an EDSF representative contacted Nationwide to indicate EDSF's interest in proposing a new system.

<u>Offeror</u>	<u>1972 date</u>	<u>Locations</u>
EDSF	Mar. 31	Nationwide
UCC	Apr. 3 and 4	do.
EDSF	Apr. 5 and 6	do.
MCAUTO	Apr. 6	MCAUTO, St. Louis
MCAUTO (note a)	Apr. 13 and 14	Nationwide

^aTo review Nationwide's Medicare operation. According to Nationwide officials, this was the first mutually acceptable date after the meeting of April 6 in St. Louis.

During these meetings, the offerors were furnished certain material to assist them in developing proposals. This material included:

1. A list of Nationwide's computer equipment configuration with monthly rental costs.
2. A copy of Nationwide's February 1972 Medicare personnel report.
3. Projections of claims processing volumes for fiscal year 1973.
4. A list of requirements expected to be met by the proposals.
5. Some file and documentation layouts.

According to officials of both Nationwide and the three offerors, Nationwide emphasized its need for a proven system capable of processing its relatively large volume of Medicare claims. Nationwide officials maintained that, because of their experience with the ASDC system, they did not intend to pioneer the development or modification of another system.

ASDC permitted to submit a proposal

When EDSF, UCC, and MCAUTO were initially contacted for proposals, Nationwide's intentions to acquire a new EDP system were not disclosed to ASDC, because Nationwide still had a systems maintenance subcontract with that firm and did not wish to further strain their relationship.

On April 20, 1972, however, Nationwide did tell ASDC that it had requested proposals from the three other vendors. ASDC asked for and received permission to submit a proposal also.

ASDC submitted a proposal and made its presentation to Nationwide on May 12, 1972. Nationwide told us that it did not consider the proposal acceptable since it was to take over operation of the ASDC system at Nationwide with few system changes. Because Nationwide was not satisfied that this approach would resolve its problem, it eliminated the ASDC proposal from further consideration.

DEVELOPMENT AND DISTRIBUTION OF REQUESTS FOR PROPOSALS

Nationwide officials said Nationwide personnel had developed and prepared the RFP with no outside assistance. According to these officials, the specifications were in a letter dated April 7, 1972, to the prospective offerors, requesting proposals for a new Medicare claims processing system on two bases.

"The first is that the proposing organization would assist in the installation of the new system, and processing would be accomplished on Nationwide's computer using computer programs that would be turned over to Nationwide personnel to alter and use as they desire.

"The second is a full facilities management basis on which Nationwide would do all manual processing and the facilities management organization would provide all services related to the computer. They [subcontractor] would provide all computer programs, maintain these programs as necessary, and provide on a remote basis the actual processing time on their computer. The facilities management organization would also assist in the installation of the system."

Nationwide's letter also advised the offerors that:

"In making your proposal two things should be emphasized. First we must be convinced that

your system has the ability to process our claim volume on a regular 24-hour a day cycle, leaving enough computer time in order that we may perform maintenance on our files, process our Part A, provide program testing time, and absorb increases in volume. Second, we must be convinced that your organization has the ability and number of persons to formally train our personnel prior to installation of the system and that your organization will provide the needed support until the installation is running smoothly."

Attached to this letter was the material previously furnished to the offerors during their initial meetings. (See p. 19.)

Nationwide's April 7 letter further specified that each proposal

- must be received by Nationwide by April 17, 1972, or the company would be eliminated from further consideration and

- must provide for installation of the system before October 1, 1972.

Nationwide officials said that the deadline for receiving proposals was changed from April 10 to April 17 because of SSA's request that the offerors be given sufficient time to develop their proposals.

On April 10, 1972, MCAUTO officials told Nationwide that they could not meet the April 17 date. According to Nationwide, MCAUTO had also told SSA that it could not meet that date. After being contacted by both SSA and MCAUTO, Nationwide agreed to extend the date to May 5, 1972, and so advised the three offerors by letter dated April 12, 1972.

Written specifications considered vague

Federal procurement policies provide that RFPs contain the information necessary for a prospective offeror to prepare a proposal properly. The RFPs are to be as complete as possible concerning the statement of work and related specifications.

Nationwide officials stated that from April 7 through May 5, 1972, the three offerors contacted them--by telephone and/or visits--on numerous occasions. The primary purpose of most of these contacts was to

- obtain additional information on system requirements,
- get clarification of information already obtained, or
- sell the merits of a particular system.

Although the responding offerors interviewed acknowledged that the written RFPs were vague, they told us that they generally understood what Nationwide wanted or needed. For example, although the written RFPs did not specify that the proposed system be online or that it be proven, the responding offerors acknowledged that Nationwide, during its discussions with them, had emphasized its requirement for a proven system. Further, all the offerors were trying to sell Nationwide on the merits of an online system, although at the time two of the offerors (UCC and MCAUTO) did not have proven online systems that were operational.

It appears to us, in retrospect, that what Nationwide really wanted in terms of technical requirements--a proven online system to be operated by the subcontractor--emerged during the evaluation process and that only EDSF was in a position to truly compete on that basis.

Factors to be used in evaluating the proposals

To encourage responsive proposals and maximum competition, sound Federal procurement policy requires that the offerors should be advised of the factors to be used in evaluating proposals and the relative importance of each of the factors. Nationwide told us that it orally furnished the factors to each of the offerors at the various meetings listed on p. 19. MCAUTO, however, desired more specific information, so on April 27, 1972, Nationwide informally provided a list of the factors and the weights which would be given to the factors. According to data supplied to us by MCAUTO, these 18 factors, in order of their relative importance, were as follows:

<u>Evaluation factor</u>	<u>Weight</u>
Control of system by Nationwide	10
Projected cost per claim	9
Projected reduction in personnel	8
Capacity for growth	7
Equipment facilities for processing	6
Assistance after installation	5
Volume of Medicare claims being processed	4
Commitment to installation in terms of attitude	3
Commitment to installation in terms of people	2
Response to request for proposal	1
Number of previous Medicare installations	1
Training material (Manual & Training Aids)	1
Contractual agreement	1
Installation costs	1
Rating of clients according to SSA standards	1
Blessing of SSA and Congress	1
Capacity to make changes in system	1
System sophistication	2

According to MCAUTO each of these factors was to be scored from 1 to 3 (3 for the most desirable proposal and 1 for the least desirable proposal).

As discussed in more detail in the next chapter, however, when the proposals were evaluated, the foregoing factors were apparently changed or their weights were changed or not used. For example, the factor given the most weight initially--control of system by Nationwide--was not considered very important when Nationwide evaluated the proposals. Further, MCAUTO was not advised of any change to the evaluation factors.

INITIAL SUBMISSION OF PROPOSALS

On April 7, 1972, EDSF made an informal system presentation to Nationwide officials. EDSF said that this was basically a "chalk board" presentation on how the system would work. The EDSF formal proposal dated April 10, 1972, was presented to Nationwide officials on April 12, 1972. On May 1, 1972, EDSF submitted a revision to its proposal which modified its estimates of Nationwide's claims volume and staffing requirements. The UCC and MCAUTO proposals were presented to Nationwide officials on May 5, 1972.

EDSF proposed total facilities management, including an online system which EDSF would

- install within 90 days of acceptance and
- operate for 6 years.

The proposal also provided that, at the end of the subcontract period, EDSF would assist Nationwide in operating the system by providing personnel training and documentation and by remaining onsite until Nationwide had gained a thorough knowledge of the system. The system would remain the property of EDSF, but Nationwide could use it under mutually agreeable terms and conditions; however, the proposal did not indicate what terms and conditions would be acceptable to EDSF.

Although Nationwide's April 7, 1972, letter had requested proposals on two bases--system installation only and system installation and operation--EDSF's proposal was limited to system installation and operation for at least 6 years.

UCC formally proposed a batch version of the model B system which would be installed within 15 weeks of acceptance. UCC's proposal indicated that it was proposing the batch system as a proven system but recommended that Nationwide consider installing a model B online system after it had gained some experience with the new system and the peak workload season had passed. UCC expressed the willingness to contract for operating the system for any term from 1 to 6 years.

MCAUTO formally proposed three versions of the model B system: a 100-percent batch processing system, a 100-percent online system, and a hybrid version of the batch and online systems. This hybrid version initially called for 10 percent of the claims to be processed online and 90 percent to be processed in batch. According to the proposal, as Nationwide gained confidence in the system, the percentage of claims to be processed online would increase until all claims were processed online. The MCAUTO proposal provided for installing the system within 90 days and for operating it for 1 year.

In accordance with Nationwide's April 7 request, both UCC and MCAUTO made proposals on the two bases, that is, installation or installation and operation of an EDP system.

The systems proposed and the price quotations under the three offerors' initial proposals are summarized below.

Offeror	Date submitted	Estimated installation costs (note a)	Type of system	Contract period	Operation of EDP system	
					Estimated number of claims per month	Average price per claim
EDSF	4-10-72	\$ 75,000	Online	6 years	200,000	\$0.973
	5- 1-72				213,000	.969
MCAUTO	5- 5-72	247,406	Batch	1 year	242,000	.281
			Online			.530
UCC	5- 5-72	132,540	Hybrid	1 to 6 years	242,000	b.470 to .520
			Batch			.235 (1 year)
						.212 (6 years)

^aThe proposals for the installation and conversion costs were not based on firm fixed prices but rather on a time and materials basis for man and machine time actually used, except that EDSF did not charge for personnel time during conversion and implementation.

^bPrice would vary depending on the proportions of claims to be processed by the batch and online methods, respectively.

Thus, on the basis of the average price per claim quoted by the offerors, UCC was the lowest, MCAUTO was the next lowest, and EDSF was the highest.

CONCLUSIONS

Although the specifications were considered vague, our interviews with representatives of the responding offerors generally indicated that they basically understood Nationwide's requirements and the importance of certain of those requirements. Therefore, we cannot say that in the initial solicitation of proposals Nationwide denied the offerors an equal opportunity to compete.

Nationwide's oral notice to the offerors of the criteria to be used in the evaluation of proposals is subject to some question. In our experience, reliance on oral communications in critical matters can create problems because of the uncertainty of what was communicated. Therefore, we believe that Nationwide should have advised the offerors in writing of the evaluation factors which would be used and their relative

importance. In addition, when Nationwide provided MCAUTO additional information--the weights to be assigned to the factors--it should have provided the same information to EDSF and UCC.

CHAPTER 4

NATIONWIDE'S EVALUATION OF PROPOSALS

At the time Nationwide received the proposals, it had the draft of SSA's evaluation guidelines which were essentially the same as the guidelines in the August 1972 manual release. Further, in early June 1972 SSA intervened in Nationwide's evaluation to help establish a more uniform basis for the offerors to estimate what Nationwide's manpower requirements and other costs would be under the various proposals.

Nationwide's cost evaluations of the proposals were based on the estimated total cost of processing claims which included the carrier's projected total staffing requirements-- which were outside the offerors' control. We noted that Nationwide made several adjustments to the offerors' cost estimates which lowered the total costs under the EDSF proposal and increased the total cost under the UCC and MCAUTO proposals. According to Nationwide officials, some of these adjustments were discussed with the offerors and others were not. In our opinion, certain of these adjustments were questionable and should have been discussed fully with the offerors. Notwithstanding Nationwide's adjustments, its cost evaluation concluded that UCC's proposal produced the lowest cost, MCAUTO's produced the next lowest, and EDSF's produced the highest.

Because of EDSF's past performance record and other factors (see p. 34) considered in its evaluation, Nationwide maintained that EDSF's proposal was the superior one and on June 26, 1972, recommended to SSA that EDSF be awarded the subcontract.

The steps Nationwide followed in evaluating the proposals and SSA's guidance are discussed in more detail in the following sections of this chapter.

SSA GUIDANCE TO NATIONWIDE

The material SSA furnished to Nationwide in early April 1972 (see p. 17) included a list of 18 evaluation factors which SSA stated should generally apply to all EDP software firms whose proposals were being considered. SSA pointed out that certain of the factors may be more important than others and,

as such, should be weighted accordingly. These factors were not as specific as the factors Nationwide furnished to MCAUTO on April 27, 1972. (See p. 23.)

SSA intervention in Nationwide's
evaluation and submission of
revised proposals

At Nationwide's request each offeror's initial proposal contained an estimate of the number of Nationwide support staff required to complement the proposed system; however, these estimates were presented in different formats, were broken down into different operational functions, and included varying levels of required management staff.

On June 6, 1972, SSA representatives met with Nationwide officials to discuss Nationwide's evaluation of the proposals. SSA had some problems with the methodology Nationwide was using to compute the total claims processing costs under the various proposals. Specifically, the SSA officials questioned whether

- the proposals could logically differ in the estimated staffing requirements for such carrier operations or departments as executive, financial, professional relations, and office services and
- the various estimates of staffing requirements for certain other operations or departments were truly comparable, because of variations in the formats of the offerors' proposals.

In addition, SSA officials maintained that the staffing estimates Nationwide was applying to the offerors (UCC and MCAUTO) proposing the model B system were too high.

As a result of this meeting, SSA requested that Nationwide obtain from each offeror a more detailed manpower breakdown for each of the carrier's operations or departments to support the cost projections. On June 7, 1972, the offerors were notified of the need for this information and were provided copies of an SSA-approved format for furnishing the required information.

A UCC representative visited Nationwide on June 9, 1972, to discuss the status of the UCC proposal and Nationwide's request for staffing estimates. This representative informed us that during the meeting he asked whether UCC would be in a better position to compete if its proposal were revised to offer an online version of the model B system. Nationwide officials told him UCC should propose the system it believed would be the most effective. Nationwide, however, again emphasized its requirement that the system proposed have a "proven track record." According to UCC officials, they were not given a definition of "proven track record" and they believed that the successful tests then being conducted on their first online installation at Group Health Incorporated (GHI) in New York City qualified it as a proven system.

On June 19, 1972, UCC representatives visited Nationwide to formally present its online system--amending UCC's proposal from a batch to an online system--and invited Nationwide officials to visit GHI to look at the system in operation. This offer was declined because, in Nationwide's opinion, the system was not yet proven. UCC submitted, along with the revised proposal, its estimate of Nationwide's support staff which would be required to complement its version of the model B online system.

MCAUTO officials informed us that Nationwide had requested that they submit their staffing estimates on the basis of their online proposal. According to a MCAUTO official, Nationwide was interested in MCAUTO's proposal for implementing a hybrid system. Since this system would ultimately be online, the staffing estimates, submitted on June 15, 1972, for the online system were used for evaluation purposes.

A summary of estimated carrier staffing requirements and prices quoted by the three offerors in their revised proposals follows.

<u>Offeror</u>	<u>Date submitted</u>	<u>Type of system</u>	<u>Estimated carrier staffing requirements</u>	<u>Contract period</u>	<u>Average EDP price per claim</u>
EDSF	6-16-72	Online	331	6 years	^a \$0.936
MCAUTO	6-15-72	Online	392	1 year	.530
UCC	6-19-72	Online	407	1 year	.293
				6 years	.253

^aThe reduction in EDSF's average price of \$0.969 per claim resulted from a \$0.10 per claim reduction in the price of processing every claim in excess of 125,000 during a month.

EVALUATION OF PROPOSALS ON THE BASIS
OF TOTAL CLAIMS PROCESSING COSTS

Because the offerors' quoted prices for EDP services represented only a portion of the total costs of processing and paying a Medicare claim, Nationwide expanded its cost analysis to include estimates of other costs which would be incurred under its contract with SSA. These costs included all personnel, equipment, administrative, and related data processing costs. This cost comparison showed that total costs using the UCC system would be the lowest and that total costs using the EDSF system would be the highest. However, the cost difference between the highest and the lowest proposal was substantially decreased because Nationwide estimated that the total carrier manpower needed to support the EDSF system would be 78 employees less than for the MCAUTO system and 103 employees less than for the UCC system.

On the basis of Nationwide's total cost evaluation, the prices quoted by the offerors for data processing services represented only about 12 to 39 percent of the total estimated costs to process a claim under the various systems proposed. Conversely, the carriers estimated personnel services costs represented about 50 to 77 percent of the total estimated costs. A summary of these costs, plus the total carrier personnel requirements projected by Nationwide, follows.

	<u>EDSF</u>	<u>Percent of total cost</u>	<u>MCAUTO</u>	<u>Percent of total cost</u>	<u>UCC</u>	<u>Percent of total cost</u>
Average EDP price per claim	\$0.936	39.0	\$0.530	22.9	\$0.253	12.3
Carrier personnel service costs per claim	1.190	49.6	1.520	65.8	1.590	77.2
Other carrier costs per claim	<u>.274</u>	<u>11.4</u>	<u>.260</u>	<u>11.3</u>	<u>.217</u>	<u>10.5</u>
Total estimated cost per claim	<u>\$2.400</u>	<u>100.0</u>	<u>\$2.310</u>	<u>100.0</u>	<u>\$2.060</u>	<u>100.0</u>
Total carrier personnel requirement according to Nationwide's evaluation	330		408		433	

Using Nationwide's total estimated cost per claim and its estimate of claims volume, the cost differential between the lowest and the highest proposals would amount to about \$870,000 for 1 year and about \$5.2 million for the proposed 6-year period of the EDSF subcontract.

We obtained differing views on the validity of using estimates of the carrier's total personnel requirements to compare the EDP prices quoted by the offerors. EDSF and MCAUTO representatives expressed the view that supporting personnel requirements would vary among online systems. EDSF representatives stated that the extent and type of services provided by the subcontractors could have a major impact on carrier personnel requirements. MCAUTO representatives stated that they believed supporting personnel requirements would differ even if identical systems were offered by different companies because of the different ways a system might be implemented.

On the other hand, UCC representatives were of the opinion that, no matter what online system was to be used, the supporting personnel requirements should be about the same. Under this assumption, the only major cost to be considered should be the EDP prices quoted by the offerors. The UCC representatives added that UCC's philosophy was that the carrier, not the EDP subcontractor, should be responsible for the productivity of the carrier's own employees.

Nationwide officials viewed UCC's reluctance to take responsibility for its manpower projections as a lack of confidence in its estimates. As a result, Nationwide did not believe that the total estimated cost projected for the UCC system was credible. In addition, Nationwide officials were wary of the EDP prices proposed by UCC. Nationwide's vice president for systems and processing stated that he could not operate his own computer operation in-house at or near the price quoted by UCC. He expressed concern that UCC might seek to renegotiate the price after the subcontract was awarded.

UCC representatives stated that, when they made their first proposal for the batch system, Nationwide officials were surprised at the proposed price and expressed some concern that UCC might be quoting a price it knew would produce a loss and might later try to renegotiate a higher rate.

According to the UCC representatives, they had assured Nationwide that the price quoted was real and profitable and that UCC would stand behind it. They informed us that the prices quoted for both the batch and the online proposals were in line with a national pricing schedule being established by UCC and that they were the lowest prices offered to date because Nationwide was the largest volume carrier to whom UCC had made a proposal.

Adjustments to personnel requirements

In evaluating the costs of the three proposals, Nationwide made certain adjustments to the estimates of manpower requirements without adequately consulting the offerors. These adjustments, which narrowed the price gap between (1) the EDSF and UCC proposal by about \$0.10 a claim and (2) the EDSF and MCAUTO proposal by about \$0.06 a claim, are summarized below.

<u>Offeror</u>	<u>Number of carrier personnel required to support proposed systems</u>		
	<u>Per offeror</u>	<u>Per Nationwide</u>	<u>Adjustment</u>
EDSF	331	330	- 1
MCAUTO	392	408	+16
UCC	407	433	+26

These personnel adjustments added to the UCC and MCAUTO proposals 11 employees for reviews of physicians' customary charge profiles and for manual interpretation. According to MCAUTO representatives, Nationwide had not consulted them on the need for these adjustments, and the functions covered by these adjustments either were provided for under other job titles or, as in the case of reviewing customary charge profiles, were built into MCAUTO's data processing system.

A UCC representative said that Nationwide had informed him that some manpower adjustments would be made to all proposals but that UCC had not been consulted on specific adjustments. After we reviewed the adjustments with him, he did not object to the need for this added staffing.

Nationwide also added five computer programers to MCAUTO's estimate and six programers and eight data processing

support staff to UCC's estimate, although the EDSF estimate did not include such positions. After we advised them of the adjustments for programmers, UCC and MCAUTO representatives strongly objected because they maintained the adjustments were based on Nationwide's assumption that such programmers would be required if it elected to take over the system after the first year of operation. UCC representatives stated that, if such an assumption was made for UCC's proposal, the same assumption should also have been made for the EDSF proposal. UCC did not object to the need for the added support staff.

Adjustments to other estimated costs

In addition to the costs of the carrier support personnel, other costs to be borne by Nationwide--such as supplies, rent, hardware, and computer terminals--were also estimated by the offerors and included in Nationwide's evaluation of the total costs. To a large extent these costs needed to be considered to insure comparability because of differences in what the offerors had included in their basic unit prices. Further, because the computers which would be used to process the claims would not be located on Nationwide's premises in Columbus, the costs of telephone lines to the offerors' computer centers needed to be considered to insure comparability.

During the evaluation of the EDSF proposal, some confusion developed about exactly where the claims were to be processed. The original EDSF proposal included an estimated cost of \$46,260 a year for leased lines from Columbus to Dallas, Texas, on the assumption that Nationwide's claims would be processed in Dallas. EDSF's revised June 16, 1972, proposal included an estimated cost of \$27,110 a year for leased lines from Columbus to the EDSF computer facility in Camp Hill, Pennsylvania. Nationwide's evaluation of the proposal included an estimated cost of \$5,830 a year for leased lines from Columbus to Camp Hill.

We were advised by EDSF that the claims were to be processed at the EDSF computer center in Dallas and that Nationwide had acquired the required lines for \$46,260 a year. The difference between the cost as initially submitted by EDSF and the estimated cost (\$40,430) as reduced by Nationwide is equivalent to about \$0.016 a claim.

OTHER FACTORS CONSIDERED
IN EVALUATING PROPOSALS

According to the June 1972 justification for Nationwide's recommendation to award the subcontract to EDSF, Nationwide considered the following 17 factors, including estimated costs, in judging each offeror's ability to insure superior performance.

1. The status of the proposed system; that is, was it fully tested and in productive use? Had it ever been used productively with claims volume as large as Nationwide's?
2. The Medicare-related experience of contractor personnel.
3. The contractor's experience in previous installations.
4. The contractor's commitment for onsite personnel, both during and after the conversion.
5. The contractor's response to the RFP and his conformance to specifications.
6. Equipment facilities for processing.
7. Commitments to installation in terms of people, attitudes, and professional approach.
8. Ability to handle Nationwide's volume.
9. Training approach.
10. Conversion approach.
11. Assistance after installation.
12. Contractual agreement (length, availability of documentation, and willingness to train Nationwide personnel for the takeover).
13. Installation cost.

14. Projected cost per claim.
15. Realism of personnel projections.
16. The capability of the system to conform to SSA standards.
17. The contractor's acceptability to SSA and the Congress.

According to Nationwide officials, no weights were applied to the 17 factors and no rating sheet was prepared to show how the offerors' proposals compared under each factor.

In recommending the selection of EDSF, however, Nationwide stated that the following four considerations were of primary importance.

- The capability of the contractor to insure the level of system performance described by the proposal.
- The ability of the proposed system to meet or exceed Nationwide's defined specifications.
- The relative cost of the proposed system and the offeror's ability to perform.
- The impact of the proposed system on Nationwide's personnel requirements.

The 17 evaluation factors listed in Nationwide's justification were similar in many respects to the 18 factors furnished to MCAUTO on April 27, 1972 (see p. 23); however, the factor given the most weight in April 1972--control of the system by Nationwide--was not included in the June 1972 evaluation factors or in the four considerations given primary importance in Nationwide's recommendation to select the EDSF proposal. In our opinion, this indicates that Nationwide revised its evaluation factors after it received the proposals.

Evaluation of offerors' past performance

In addition to reviewing the offerors' proposals as submitted, Nationwide personnel made onsite visits to offerors' installations and analyzed SSA's reports on the offerors'

performance. On the basis of each offeror's past performance, Nationwide concluded that EDSF had the superior record.

Onsite visits

On April 18, 1972, Nationwide personnel visited EDSF's installation at Arkansas Blue Shield in Little Rock; on April 24, 1972, they visited UCC's installation at Illinois Medical Service and UCC's data processing center in Chicago; and on April 27, 1972, they visited St. Louis, Missouri, for a demonstration of MCAUTO's version of the model B system and its computer operations.

Nationwide officials informed us that the proposed systems were demonstrated at each location. At the two carrier locations--Arkansas and Illinois--they discussed with carrier personnel their experience with the claims processing system, their working relationship with the applicable subcontractor, and the amount of onsite assistance provided to the carrier by the subcontractor.

Nationwide officials said they were particularly impressed with the onsite EDSF personnel and their close working relationship with the carrier's people.

Analysis of SSA reports on carrier activities

Nationwide analyzed various SSA-prepared administrative reports for carriers using systems installed and operated by EDSF and for those using systems operated and/or installed by UCC or MCAUTO. The reports included administrative cost and performance data for July through September 1971 and workload reports for January 1972.

Nationwide made the analysis to compare the performance record of each subcontractor with its projected performance at Nationwide. Because the analysis was not limited to those carriers using the same type of system proposed to Nationwide, it was, to some extent, an analysis of subcontractors' performance generally and not system performance. The areas of performance compared were the number of payment records processed, the average manpower used, the average number of payment records processed per man-year (average production), the average cost per claim processed, and the average number of weeks' work on hand (backlog). Following is a summary of Nationwide's analysis.

PERFORMANCE COMPARISONS PER NATIONWIDE'S ANALYSIS

JULY to SEPTEMBER 1971

	Payment records processed (note a)	Average manpower	Payment records processed per carrier man-year	Cost per claim	Weeks' work on hand (note b)
EDSF					
customers:					
A	836,455	820.3	4,079	\$3.30	1.7
B	946,608	685.7	5,522	3.21	2.2
C	593,740	390.5	6,082	2.37	1.6
D	550,619	438.7	5,020	2.80	1.6
E	330,934	211.3	7,211	2.68	1.4
F	149,574	170.1	3,517	3.58	.9
G	103,889	151.2	2,748	4.11	2.5
H (note c)	112,371	140.4	3,201	2.34	2.2
I	99,733	141.0	2,829	3.41	2.7
J	55,792	62.5	3,571	3.94	3.4
Nationwide's fiscal year 1973 EDSF projections					
	618,250	329.9	7,490	2.40	2.0
UCC					
customers:					
K (note d)	204,317	385.2	2,122	5.57	3.2
L	100,554	130.4	3,084	4.32	3.1
Nationwide's fiscal year 1973 UCC projections					
	618,250	432.9	5,712	2.06	(not computed)
MCAUTO					
customers:					
M	96,668	133.8	2,890	4.24	2.6
N	121,757	173.6	2,805	2.49	3.4
O	309,262	480.9	2,572	3.47	2.0
P (note e)	653,949	892.5	2,931	3.05	2.7
Q (note f)	139,401	211.6	2,635	3.58	2.7
R	105,630	168.2	2,512	2.95	2.5
S	57,891	107.9	2,146	3.63	2.5
Nationwide's fiscal year 1973 MCAUTO projections					
	618,250	407.9	6,062	2.31	(not computed)

^aFor definition of a "payment record," see page 12.

^bAs of January 1972.

^cData shown is for a period before EDSF involvement.

^dUCC operated the system for this carrier only.

^eFigures apply to the entire operation of a multi-State carrier. The MCAUTO-installed system was used in only one State.

^fMCAUTO operates the system for this carrier only.

The analysis showed that only carrier C--using EDSF's batch system--which had processed about the same volume of payment records as projected for Nationwide had operated at a cost per claim approximating the \$2.40 cost projected for Nationwide. Carrier A--using EDSF's online system--with a considerably higher workload operated at a cost per claim about 37 percent higher than the estimated Nationwide cost under the EDSF proposal. Carrier E--also using EDSF's online system--which, according to EDSF officials, processed about the same number of claims as projected for Nationwide operated at a cost per claim about 12 percent higher than that projected for Nationwide.

Nationwide's analysis of the data for the two carriers using systems installed by UCC showed the cost per claim to be more than double the estimated Nationwide cost of \$2.06 for UCC's proposal. In addition, the cost per claim experienced by the UCC customers exceeded any of the costs experienced by EDSF customers, regardless of volume.

UCC told us in April 1973 that, had Nationwide used more current data in its performance comparisons, UCC's performance at both locations would have shown significant improvements. According to UCC, Nationwide was furnished data in June 1972 which more accurately reflected UCC's performance. For example, at carrier K the average production (payment records processed per man-year) for February 1972 was 3,748 compared with the 2,122 used by Nationwide. Similarly, the average cost of processing a claim had decreased from \$5.57 per claim to \$3.78, and weeks' work on hand had decreased from 3.2 to 2.5.

None of the carriers using the MCAUTO-installed systems operated at a cost per claim as low as the \$2.31 projected for Nationwide, although carrier N, with a workload about one-fifth that of Nationwide, approached it.

In the opinion of Nationwide officials, the credibility of UCC's manpower projections was further strained because Nationwide's operation would have to be more than twice as efficient as that of UCC's best customer.

Evaluation factors favoring
the EDSF proposal

The EDSF proposal was clearly superior, according to Nationwide officials, to one or both of the other two offerors' proposals in its proven online system, computer backup, or onsite staff support.

Proven system

Nationwide placed significant emphasis on the proven track record of the offerors and the experience of the proposed systems with large-volume carriers. The reason for this emphasis was primarily the alleged failure of the ASDC system which was then in use at Nationwide. This system had proven itself at a small-volume carrier but ran into trouble when it was adopted and modified for use by a large-volume carrier.

In addition, Nationwide officials emphasized the need for a proven system because of the desire to end their bad publicity and to establish a high level of service to Medicare beneficiaries in Ohio and West Virginia.

In June 1972 EDSF had data processing subcontracts with 10 carriers. Six of these carriers were using a version of the EDSF online system, and four were using EDSF's batch system. EDSF operations involved carriers which have both larger and smaller claims volumes than Nationwide.

According to Nationwide officials, they viewed EDSF as an organization with a proven record of accomplishments at large-volume carriers and considered the EDSF-proposed on-line system to be proven in operation at a large-volume carrier (Massachusetts Blue Shield).

In June 1972 UCC operated the model B batch system at one carrier, Illinois Medicare Service. UCC was also in the process of installing and testing its first model B on-line system at GHI in New York City. That system is to be operated by the carrier.

Nationwide considered UCC's online proposal to be for an unproven system and, as stated on page 29, originally

declined an invitation to make an onsite visit to GHI to look at the system in operation. However, Nationwide later made a visit on July 13, 1972, at the request of an SSA official. After their visit Nationwide officials advised SSA that they were very impressed with the entire GHI operation and organization. Nationwide told SSA that at the time of the visit only a small percentage of claims were being processed by the system, programs were still being checked out, and the system was not ready for implementation elsewhere.

UCC officials told us that, when they made their online proposal, the system at GHI was being successfully tested. The GHI system, however, did not become fully operational until mid-August 1972. The UCC representatives stated that from their viewpoint the successful testing at GHI qualified their system as proven.

MCAUTO had experience in installing and maintaining a number of model B batch systems and in operating the system for one carrier. MCAUTO's version of a model B online system was developed and tested but had not been put in operation at any carrier.

MCAUTO representatives said they believed their online system was the best system for Nationwide's large-volume operation. Since it was unproven under operational conditions, however, they elected to submit their original proposal with three options. As indicated on page 24, the first option was for the model B batch system which was in use at a number of carriers and was considered to be proven. The second was for MCAUTO's version of a model B online system which was unproven. The third, a hybrid version of the model B batch and model B online systems, was an attempt by MCAUTO to qualify with a proven batch system while phasing in the more desirable online system. This proposal called for 10 percent of the claims to be processed online with a gradual increase of that percentage as the system proved itself under operating conditions.

Nationwide officials stated that they were not enthusiastic about pioneering or phasing in an untried system.

Computer backup

Nationwide considered it essential that the subcontractor have additional onsite computer equipment to continue processing Medicare claims if the primary equipment failed. Nationwide viewed this requirement as met if other onsite computer equipment was available to process, on a priority scheduling basis, a portion of the Medicare claim workload.

Nationwide officials stated that both EDSF and MCAUTO had assured them that Medicare claims would be processed at computer centers with adequate equipment backup. However, Nationwide officials questioned UCC's backup capabilities because their tour of UCC's computer facility in Chicago revealed that UCC had only one computer of sufficient size to handle Nationwide's volume of claims. UCC offered to increase the capacity of its computer, but Nationwide officials said they did not consider a larger computer to be responsive to their desire for backup capabilities.

UCC representatives stated that they had informed Nationwide of a number of other alternatives available to satisfy the backup requirement but that they had not been requested to provide the details. According to these representatives, they were not aware that the lack of backup capabilities was considered a serious deficiency until an August 18, 1972, meeting at Nationwide.

Onsite staff support

Nationwide maintained that a large portion of its past data processing problems was due to a poor working relationship with its subcontractor. In Nationwide's opinion, the poor relationship was largely due to the fact that knowledgeable and competent subcontractor personnel were not available to adjust or amend the system to Nationwide's needs. Nationwide officials said that using the telephone or correspondence did not provide them satisfactory or timely subcontractor actions. As a result, Nationwide considered the commitment of subcontractor onsite support staff, during and after system implementation, to be an important aspect of each proposal.

Nationwide considered EDSF's proposal, with its commitment of a minimum of 10 people onsite after system implementation, to be more responsive to its needs than UCC's and MCAUTO's proposals of 1 man. Both UCC and MCAUTO believed that one man would be sufficient to provide adequate technical assistance, since SSA was responsible for maintaining the model B system.

In explaining MCAUTO's rationale for proposing a one-man onsite staff, one MCAUTO official pointed out that the list of proposed evaluation factors furnished by Nationwide in April 1972 (see p. 23) gave considerable weight to a proposal which would provide Nationwide with control of the claims processing system. According to this official, a small subcontractor onsite staff would have been most compatible with Nationwide's stated preference to control the system.

CONCLUSIONS AND MATTERS REQUIRING FURTHER ATTENTION BY SSA

According to sound Federal procurement policy, whenever the pricing or technical aspects of any proposal are uncertain, the procurement authority should not award a contract without further exploring and discussing the uncertainty. Although Nationwide made several adjustments to the offerors' cost estimates--which might not have been made had the adjustments been fully discussed with the offerors--we cannot conclude that such adjustments significantly affected Nationwide's selection of EDSF, because the selection was based on evaluation factors other than costs.

In evaluating the proposals, SSA permitted Nationwide considerable discretion to exercise its independent judgment in determining what was important in making its recommendation to award the subcontract to EDSF. Although SSA intervened in Nationwide's evaluation process regarding the method of estimating the total costs of the proposals, the development of evaluation factors other than costs and the importance assigned to them were left to Nationwide's discretion. In fact, we found no evidence that SSA was aware that Nationwide had furnished MCAUTO with weighted evaluation criteria or that Nationwide had changed its emphasis to favor such factors as onsite support.

In implementing its overall policy of encouraging competition among the potential EDP subcontractors, SSA has required its carriers since November 1969 to obtain competitive proposals from responsible data processing firms and since August 1972 to obtain sufficient competitive proposals to get at least three acceptable ones. On the other hand, SSA allows its carriers considerable discretion in determining how the proposals are to be evaluated once they are received.

In line with SSA's overall policy of fostering competition, it seems to us that a logical follow-on to requiring competitive proposals would be a requirement that, depending on the circumstances at a particular carrier, offerors be advised of the relative importance that will be given to all evaluation factors, particularly price or cost. In summary, we believe that a competitive atmosphere would be fostered if the offerors were able to determine the importance these factors will have in the carrier's evaluation process.

We recognize that such a procedure would limit the carriers' authority to exercise their independent judgments of what proposals would best satisfy their requirements. We recognize also, however, that under cost-type contracts, carriers' self-interests do not necessarily rest with obtaining service at the lowest cost or with implementing a national policy fostering competition among data processing contractors.

RECOMMENDATION

In line with the foregoing conclusions, we recommend that the Secretary of HEW provide for SSA to instruct its intermediaries and carriers to advise potential offerors, in writing, of the evaluation criteria which will be used to evaluate their proposals, including the relative importance that will be given to all evaluation factors, particularly price or cost.

CHAPTER 5

SSA EVALUATION OF PROPOSALS

After Nationwide submitted its evaluation and recommendation to SSA for approval, SSA made two additional evaluations: one by a two-man team of experts independent of BHI and the second, which expanded on the first, by top-level BHI management.

SSA's approach to evaluating the three proposals differed from the approach which it suggested and Nationwide used. The differences between the Nationwide and SSA approach, together with different assumptions on future workload, manpower, and salary increases, were significant enough to reverse the order of the MCAUTO and EDSF proposals in terms of total costs.

We believe that, as long as SSA continues to evaluate data processing proposals on the basis of their effect on total carrier costs, it should determine which of the various evaluation approaches are the most effective. These approaches should then be made available to the carriers--as well as to potential EDP subcontractors--for use in preparing and evaluating proposals.

SSA REVIEW TEAM EVALUATION

To insure an objective approach in its initial analysis of Nationwide's subcontract evaluation and recommendation, SSA established a review team of two specialists from bureaus outside BHI. One member of the team was a systems analyst from SSA's Office of Administration, and the second was a division director from the Bureau of Data Processing.

The review team was charged with reviewing the various proposals and the basis of the carrier's recommendation. The team was to report its findings to BHI and to recommend whether or not SSA should approve Nationwide's choice of a subcontractor. The team evaluated the (1) competency, capacity, and past performance of each offeror, (2) adequacy and reliability of the systems proposed, and (3) total cost to the Medicare program.

Results of the evaluation

On July 24, 1972, the review team submitted its report to BHI. The team concluded that:

- The systems proposed by all three companies had the technical capacity for processing all part B workloads which were estimated for the subcontract periods.
- All offerors had the technical capacity to provide adequate management control and audit data required by SSA.
- All offerors met the requirements for providing a high level of uninterrupted service.
- All offerors had demonstrated at numerous installations, both in and out of the part B environment, their capabilities in high-quality facilities management.
- All offerors had clear, well-laid-out plans demonstrating their commitment of adequate managerial and technical resources.
- All of the offerors' estimates of carrier personnel requirements were unrealistic, but no offeror should be evaluated on the basis of the reasonableness of these estimates.
- The effectiveness of the model B and EDSF systems in processing the workload did not differ.
- On the basis of a 2-year cost model constructed for each proposal, UCC's proposal would result in the lowest total carrier cost, EDSF's proposal would cost about \$515,000 more, and MCAUTO's would cost about \$1.77 million more than UCC's.
- Nationwide may experience fewer surprises and receive more comprehensive support from EDSF; however, by selecting EDSF in face of its additional costs without substantial and specific differences in performance, Nationwide's management was valuing its subjective confidence in EDSF at over \$1.5 million during the 6-year period of the proposed subcontract.

- MCAUTO's proposal provided excess equipment backup capabilities for an online operation; UCC and EDSF did not completely document how they would handle possible online problems.
- A 6-year subcontract, such as in the EDSF proposal, should be avoided unless it includes substantial provisions for renegotiating prices.
- No specific condition existed which indicated that the model system would not perform adequately for Nationwide.
- If every large carrier followed the reasoning that experience can be obtained only on the basis of prior satisfactory experience, no large carrier could ever subcontract for the SSA model B system. Such a philosophy would lock in the EDSF system for large carriers simply because it was developed first and has an established track record.

Cost analysis

To determine the reasonableness of Nationwide's decision to select EDSF on qualitative grounds, the review team sought to express the qualitative factors in terms of dollars and cents so that a decision could be reached on the basis of total cost. The team constructed a cost model to compare the overall costs of the three systems under a set of assumptions which, according to the review team, tended to favor EDSF.

These assumptions included:

- The workload would increase 14 percent in the second year of operation, which was the lowest probable rate of increase that could be estimated. (A higher rate would have tended to increase the cost of the EDSF proposal well above that projected.)
- In accordance with a general guarantee given by EDSF in its proposal, EDSF's claims count for billing purposes would not exceed, by more than 1 percent, the claims count used by SSA for its statistical reports. (Other EDSF carriers had recently experienced a difference of about 7.3 percent.)

- Labor costs per man-year were based on total carrier averages instead of distinguishing the lower cost positions which are affected more by the type of system adopted.
- A labor rate increase of 6 percent in the second year was used. (According to the review team, the EDSF system was substantially less sensitive to labor costs than the current model system; therefore, any increases in labor cost would tend to favor EDSF.)

The basis used by the SSA review team to estimate and evaluate total carrier cost for each of the proposed systems differed from that used by Nationwide. In accordance with suggestions made by SSA representatives (see p. 28), Nationwide's approach was to have each offeror make detailed estimates of the carrier's total manpower requirements and related costs and then to determine whether the estimates were reasonable.

The review team expressed the opinions that the total carrier cost depended partly on the strength of carrier management and that this is a factor that the offeror, the carrier, and SSA cannot objectively assess. In making its analysis the team preferred to rely on national norms and trends to estimate total carrier costs for each of the systems proposed.

The team decided that the most detailed level of staffing data acceptable for computing national norms would be the net manpower requirement per thousand claims processed. This was accomplished by using the average carrier staffing per 1,000 claims processed for (1) 5 large-volume carriers using EDSF systems and (2) 8 medium-size carriers using the model B system. The staffing data for the model B carriers was then adjusted by applying a factor which recognized the increased efficiency of a large-volume carrier. This adjustment--which represents the experience efficiency factor between medium-sized and large carriers using the EDSF systems--was necessary because no large carriers were currently using the model B system.

The review team evaluated all three offerors on the basis of the installation and operation of their online systems for 2 years. In addition, 2-year cost analyses were made for UCC's batch system both as originally proposed and

assuming that UCC would install its online system after operating the batch system for 9 months. These cost analyses, based on the previously mentioned assumptions which favored EDSF, showed that UCC's systems would result in the lowest costs, EDSF's would be second lowest, and MCAUTO's would be third, as follows:

<u>Proposed system</u>	<u>Estimated carrier cost for 2 years</u>	<u>Estimated average cost per claim (note a)</u>
MCAUTO: online	\$12,165,889	\$2.22
EDSF: online	10,912,564	1.99
UCC: online	10,397,388	1.90
UCC: 9-month batch		
15 month online	10,291,787	1.88
UCC: batch	10,096,097	1.84

^aEstimated on the basis of SSA's assumption that 5,478,000 claims would be processed in the first 2 years.

The cost differences between the EDSF system recommended by Nationwide and the low-cost UCC systems were about \$515,000 for UCC's online proposal, about \$621,000 for UCC's 9-month batch with conversion to online, and about \$816,000 for UCC's batch proposal. The analysis of the 9-month batch with conversion was based on the assumption that UCC would not be able to install its online system in time to process claims during the 1972-73 winter peak workload period.

The review team noted in its report that:

"* * * An 'unfavorable' analysis using rapidly increasing workloads, increasing relative efficiency of the Model system, reasonably static labor rates and EDSF excess billing counts as experienced by many carriers would produce a cost spread significantly higher than the 1.7^[1] million dollars projected by Nationwide.

¹A 2-year projection based on Nationwide's \$0.34 estimated cost difference between UCC's and EDSF's proposals.

The point of the analysis is that under any set of reasonable assumptions which incorporate all relevant considerations of workload, efficiency, etc., a substantially higher cost total over the low bid is predictable for the EDSF proposal, at least on the order of one million dollars over the six-year period of the proposed EDSF contract and over \$400,000 [²] during a 2-year life evaluation period."

Evaluation team's conclusions
and recommendations

The SSA review team concluded that

- the evidence did not support Nationwide's recommendation to award the subcontract to EDSF;
- the grounds Nationwide used for rejecting the low offer were not reasonable or substantial;
- on a 2-year basis, the proposal made by EDSF was significantly higher than the low offeror's;
- the various qualitative factors with which Nationwide was concerned were not substantial enough to overcome the significant cost differences involved; and
- all offerors displayed more than adequate capabilities for handling Nationwide's workload.

Accordingly, the review team recommended that Nationwide's proposed subcontract with EDSF be disapproved.

BHI EVALUATION

After receiving the review team's analysis, BHI officials maintained that more attention should have been given to the effects that the introduction of an online system by

²Subsequent review team revisions of cost projections show the 2-year cost difference between the UCC and the EDSF online proposals to be about \$515,000.

MCAUTO and UCC would have on Nationwide's staffing requirements. They maintained also that the analysis should have (1) compensated, on a cost basis, for the deficiencies Nationwide identified in the other proposals and (2) projected the estimated costs of the proposals over the 6-year term of the subcontract which Nationwide had recommended.

To insure that the concerns expressed by Nationwide were adequately dealt with and to make the various proposals as comparable as possible, BHI adopted the following assumptions.

- Using the 14-percent annual increase in workload calculated by the SSA review team, there would be a corresponding average 10-percent increase in the number of personnel and an average 6-percent increase in salary costs.
- To meet the concern that Nationwide expressed regarding adequate computer backup by UCC, one-half the cost of a medium-sized computer (IBM 360, model 65) would be added to UCC's proposal.
- To meet the concern of having adequate onsite support, additional onsite personnel, equivalent to the number maintained by EDSF at another carrier using its online system, would be added to the UCC and MCAUTO proposals.
- Installations of the EDSF online system could begin on September 1, 1972, and the system could be operational by December 1, 1972. Implementation of the model B online system could not begin until April 1, 1973, and the system could be operational on July 1, 1973.
- Recognizing that the model B online system was untested in a large-volume environment and that the EDSF system would be in operation 7 months longer, total operating personnel needs for the first full calendar year of operation (Jan. 1 to Dec. 31, 1974) under the MCAUTO and UCC systems was set at 10 percent above that of EDSF. The second-year staffing differential would be set for the succeeding years.

--Nationwide would continue to use its current data processing subcontractor until the new system became operational.

BHI's analysis concluded that, between September 1, 1972 (the EDSF implementation date), and December 31, 1973, Nationwide's costs under the EDSF proposal would be about \$260,000 more than under UCC's proposal. In addition, the analysis showed that, with both systems fully operational for calendar years 1974 through 1978, the UCC system would cost Nationwide about \$2.19 per claim and the EDSF system would cost about \$2.53 per claim. The difference in total claims processing costs for the period would amount to about \$7 million.

While recognizing that mathematical projections may substantially differ from actual experience, BHI concluded that the projected cost difference clearly offset other considerations presented by Nationwide. Accordingly, on August 4, 1972, SSA informed Nationwide that it did not concur in the recommendation under the terms proposed.

CONCLUSIONS AND MATTERS REQUIRING
FURTHER ATTENTION BY SSA

The Nationwide, SSA, and BHI cost evaluations of the proposals differed in basic assumptions and periods of time for which costs were computed. These differences resulted in varying overall cost estimates and varying conclusions about the comparative ranking of the proposals in terms of total cost, as follows:

<u>Evaluation</u>	<u>Estimated cost per claim</u>		
	<u>UCC</u>	<u>EDSF</u>	<u>MCAUTO</u>
Nationwide	\$2.06	\$2.40	\$2.31
SSA review team	1.90	1.99	2.22
BHI	2.19	2.53	Not computed

We believe that SSA should give careful attention to the validity of the basic assumptions used in computing the total cost of a proposal. Cost factors which cannot be quantified with reasonable certainty should not, in our view, be used. SSA should determine the appropriate factors to be used and should modify its August 1972 instructions to

advise its carriers and intermediaries--as well as potential EDP subcontractors--just how cost factors, over and above the offerors' quoted prices, are to be computed.

In our opinion, the availability of such information would ultimately foster competition by (1) permitting offerors to be more responsive to the requirements of the carriers and intermediaries and (2) assuring potential offerors that their proposals will be fairly evaluated on a common basis.

RECOMMENDATION

We recommend that the Secretary of HEW provide for SSA to (1) determine just how cost factors, over and above the offerors' quoted prices, are to be computed and (2) advise its carriers and intermediaries--as well as potential EDP subcontractors--accordingly.

CHAPTER 6

NEGOTIATIONS WITH RECOMMENDED OFFEROR

After learning that SSA could not concur in its recommendation that a 6-year data processing subcontract be awarded to EDSF under the terms proposed, Nationwide requested a meeting with SSA officials to review SSA's analysis and explore whatever alternatives might be available to permit the approval of the proposed subcontract.

During this and subsequent meetings among EDSF, Nationwide, and/or SSA, modifications to the proposed subcontract were negotiated, including a guarantee to Nationwide of the overall claims processing costs during the last 5 years of the subcontract. These changes were beyond the scope of the original RFP, and the unsuccessful offerors told us that they had not been given a similar opportunity to modify their proposals. We were told also that they would have been amenable to such negotiations, and one had asked SSA to be permitted to do so.

According to Federal competitive negotiation procedures, when a modification involves a material departure from the stated requirements, all offerors should be given an opportunity to respond.

MEETING OF NATIONWIDE, EDSF, AND SSA

Nationwide told us that, after making its recommendation to SSA on June 26, 1972, it had not notified any of the offerors of the status of the proposals, as requested by SSA. Each of the offerors, however, had contacted Nationwide on numerous occasions to obtain information on the status of the proposals.

According to Nationwide officials, all parties involved were concerned with the passage of time because the date specified in the RFP for implementing the new system was October 1, 1972. Nationwide officials maintained that, if the subcontract was not approved and awarded at an early date, it would be too late to try implementing a new system before the peak claims processing season--generally December, January, and February.

Pressured by their desire to implement a new system before the peak season, Nationwide officials contacted SSA on August 4, 1972, to ascertain the status of SSA's consideration of the recommendation. SSA told Nationwide that the evaluation team was proposing that the recommendation not be approved. Nationwide then requested a meeting with SSA to discuss the evaluation team's recommendation and to present its views to the SSA staff involved in the evaluation. Nationwide also made arrangements to have representatives from EDSF present at the meeting which was scheduled for August 9, 1972.

At this meeting SSA advised Nationwide and EDSF officials that it was SSA's intention not to direct Nationwide's action but to deal objectively with the recommendation. SSA officials stated that they were concerned with the overall cost which would be incurred under the EDSF proposal over a 6-year period, compared with the projected overall cost under the lowest cost proposal--a difference of over \$1 million a year, according to SSA's estimates. SSA officials maintained that the performance advantages cited for the EDSF system were not worth the difference in price.

SSA officials stated that the current developments with the SSA model B online system needed to be recognized. Although the cost of the EDSF system--at the outset of the contract period--might be judged reasonable, this would not necessarily be so over the life of the subcontract, particularly since differences in personnel requirements would be eliminated over a period of time with use of online systems.

SSA officials maintained also that, after an initial shakedown and adjustment period, online systems--designed to do the same things--should have basically the same needs for supporting personnel. Further, technical improvements in the model B online system, which are possible, could significantly affect future claims processing costs. With a long-term, fixed-price subcontract of the type proposed by EDSF, the Government might not be able to realize the resulting cost advantages.

Nationwide officials maintained that their objective was to provide Medicare beneficiaries effective service at a reasonable price and that only EDSF could immediately provide

a proven ongoing system which, in the long run, would best serve Nationwide and Medicare beneficiaries in Ohio and West Virginia. Special emphasis was placed on the complete facilities management services offered by EDSF as opposed to the EDP services offered by the other two companies. Nationwide also emphasized EDSF's past record of achievement in service provided and overall administrative costs and pointed out that, in view of its past claims processing difficulties, it had no desire to be a pioneer in implementing an unproven system, such as those proposed by MCAUTO and UCC.

These discussions led to the exploration of alternative approaches, such as EDSF's guaranteeing to Nationwide the overall administrative unit cost of processing a claim and modifying the terms of the proposed subcontract.

PROPOSED GUARANTEES

To overcome SSA's objections to Nationwide's recommendation, EDSF expressed a willingness at the August 9 meeting to

- guarantee total claims processing costs as submitted (about \$2.40 per claim),
- negotiate a subcontract for a term less than 6 years (possibly 3 years),
- renegotiate the subcontract if the SSA model B system proved superior to the EDSF system or if EDSF could not perform as promised.

Although no commitments were made at the meeting, the parties agreed that some form of guarantee would be further considered. Also, SSA officials expressed the view that, if EDSF were given an opportunity to guarantee total carrier costs, the other offerors should be given a similar opportunity.

On August 14, 1972, Nationwide sent a telegram to SSA urging prompt approval of the EDSF subcontract because it felt that the EDSF proposal was the most favorable and credible. Nationwide stated that the EDSF proposal was the only one that provided adequate onsite staff and that was based on proven performance at large carriers. Further,

Nationwide told SSA that EDSF had agreed to guarantee the cost projections in its proposal and that, if SSA wished to assure itself of both maximum performance and lowest cost, EDSF would accept either of the following requirements as a condition of subcontract approval.

--EDSF will guarantee to reduce the overall cost per claim to \$2.40 by the end of the first full year after conversion to the EDSF system. If Nationwide's overall costs are above \$2.40 per claim, EDSF will reduce its price enough to reduce the overall cost per claim to \$2.40.

--If, at the end of 3 years, the average overall cost per claim of the SSA model B system users is lower than the overall cost per claim at Nationwide and if performance is comparable to that at Nationwide, EDSF will adjust its price to match those of the model B system users.

Nationwide stated that its job was to consider the best interest of the Government on the basis of costs and all other pertinent factors and emphasized that the subcontract should not be awarded to the other offerors because:

"We should not and will not accept estimates unjustified either by past performance or current guarantees. We should not and will not turn over the facilities management responsibility for Medicare data processing to companies who have not demonstrated both a full understanding of what is required at Nationwide and the ability to accomplish it."

Nationwide also expressed the belief that failure to approve the EDSF subcontract would cause a serious crisis in Medicare claims processing during the peak winter months and would be detrimental to the interests of the Government, the people of Ohio and West Virginia, and Nationwide.

REVISED GUARANTEES

The proposed guarantees apparently were not acceptable to SSA, and after SSA raised some questions, Nationwide and EDSF agreed on additional guarantees which should be

incorporated into the subcontract. The revised guarantees were conveyed to SSA by memorandum dated August 22, 1972.

EDSF was agreeable also to a termination-for-convenience provision, under certain circumstances, after the end of 3 years of operation; however, upon termination of the subcontract, Nationwide would lose the right to use the EDSF system and the cost guarantees would not apply after the notice of terminations.

Nationwide advised SSA by memorandum dated August 22, 1972, that the EDSF-proposed guarantees were "quite acceptable." As for the contract termination provision, Nationwide advised that "it appears acceptable." Nationwide again urged prompt approval of the subcontract to enable EDSF to begin onsite plans and implementation of its system.

On August 22, 1972, Nationwide also contacted SSA about SSA's evaluation and the acceptability of the proposed guarantees. According to Nationwide officials, SSA again suggested that the other two offerors be given a chance to propose similar cost guarantees. Nationwide was not willing to do this since it had closed the negotiations, it had made its selection, and the guarantees merely improve the original recommendation.

On August 24 EDSF officials met with SSA to discuss subcontract provisions, and SSA stated the conditions that would be required as prerequisites to subcontract approval. Although Nationwide did not participate in this meeting, it notified SSA on August 24 that:

"* * * MCAUTO and UCC have been notified that our selection was EDS and that our proposal was unacceptable to SSA, but cost guarantees and term modification now appear acceptable and we are anticipating approval and implementation in 1972. If approval is not received, we are abandoning plans for conversion of system. Please advise us of your decision."

On August 28 SSA told Nationwide it would approve the EDSF subcontract subject to certain conditions and subcontract amendments. On that day Nationwide formally notified MCAUTO and UCC that SSA had finally approved the

proposed EDSF subcontract and that it was proceeding with plans to implement the EDSF system beginning about September 1, 1972. Nationwide advised the unsuccessful offerors also that its decision to select EDSF was based on EDSF's past performance record and its proven ability to perform an expedient conversion and thus help clean up the claims backlog before the end of 1972.

CONDITIONAL APPROVAL OF EDSF SUBCONTRACT

The conditions and contract amendments required by SSA for subcontract approval were forwarded to Nationwide by letter dated September 1, 1972, which stated:

"Even though we recognize the desirability of an early installation of a proven system and even though we recognize that the Government is not in a position to mandate your acceptance of any given submission by a potential subcontractor, there is not in our opinion sufficient assurance of the reasonableness of the costs which may be incurred under your proposal. On the basis of raw data processing costs, the EDSF submission is by far the highest, and even when the overall administrative cost per claim is considered, there is nothing in the proposal which you submitted which would afford the Government a reasonable guarantee that the amounts which it will expend will not exceed those which might be available if other systems or subcontractors were used.

"In order to provide such assurance, this is to advise you that our approval of your proposal to enter a subcontract with EDSF must be conditioned upon your acceptance of the following terms and upon the inclusion of such terms in the subcontract agreement with EDSF or in the form of an addendum thereto."

The conditions specified by SSA are summarized below.

1. Actual costs during the first period (Sept. 1, 1972, to Dec. 31, 1973) will be recognized for purposes of reimbursements. These costs are not to exceed amounts included in the approved budget for the period involved.
2. SSA's reimbursement to Nationwide on a total-cost-per-claim basis beginning January 1, 1974, will not exceed the lowest of

- actual total cost per claim,
 - total cost per claim incurred by the lowest of any non-EDSF carriers which are described by SSA as large carriers,¹ and
 - the average adjusted total cost per claim incurred by the three lowest cost carriers using the model B online system.
3. In computing comparison cost averages, the carriers' total unit costs per claim will be adjusted for volume based on a specified scale and, for carriers using the SSA model system, based on an appropriate adjustment for systems development and maintenance cost.²
 4. Carrier performance will be compared on the basis of standard criteria developed and used by SSA. If Nationwide's overall performance fails to at least meet the performance of the "comparison carriers," this may, under certain circumstances, be grounds for terminating the subcontract.
 5. The subcontract can, under certain circumstances, be terminated after the third year of operations if significant developments materially change either the method or the cost of processing part B claims.

¹SSA classifies Medicare carriers into four groups, depending generally on the number of payment records processed. Large carriers are those with the highest volume, generally over 1 million payment records processed each year.

²The U.S. Government expends funds each year to develop and maintain the model B system. This adjustment is made to recognize these expenditures when comparing the costs of a proprietary system with those of the Government-supported model B system.

6. The term of the carrier's prime contract with the Secretary of HEW shall in no way be affected by the foregoing conditions, and if the Secretary does not renew the carrier's prime contract before the end of any contract term, the subcontract will automatically terminate.

SSA also required that the subcontract provide for the subcontractor to bear the financial burden of any items of nonreimbursement resulting from the foregoing guarantees. In addition, SSA wanted a specific provision recognizing Nationwide's full authority to carry out its carrier functions without being subject to the direction of the subcontractor. Nationwide and EDSF accepted the conditions imposed by SSA, and by letter dated September 5, 1972, Nationwide transmitted copies of the signed agreement to SSA for review and approval.

In an internal memorandum explaining the rationale for granting conditional approval of the EDSF subcontract, SSA maintained that Nationwide had taken a firm position that the system would have to be changed now and that it would not consider entering into a subcontract with either MCAUTO or UCC at the time. Further, SSA maintained that guaranteeing competitively controlled costs and realizing the projected overall cost advantages which could have been secured under the lower proposals had removed its primary objection to Nationwide's recommendation.

In addition, SSA stated that provisions for (1) earlier renegotiation of the subcontract by Nationwide on its own initiative or at the direction of the Secretary, which may result in terminating the subcontract, and (2) termination at any time if performance is unsatisfactory provided safeguards not previously provided in EDSF Medicare subcontracts.

Subsequent offers to reduce price

Upon hearing of SSA's decision to approve the EDSF subcontract, UCC, by letter to SSA dated September 5, 1972, questioned the decision because the higher charges approved represented additional costs exceeding \$1 million a year. Further, UCC said the negotiation of cost guarantees with EDSF went beyond the scope of the original RFP and appeared to be an abandonment of Nationwide's basic administrative

responsibility under Medicare. UCC told SSA that, if this was the approach to be followed, it welcomed the opportunity to revise its proposal. UCC also questioned SSA's method of promoting competition in the Medicare program and requested a meeting with SSA to discuss these issues.

On September 13, 1972, UCC representatives met with SSA officials, and according to UCC representatives, UCC offered to guarantee that it would process Nationwide's projected workload at a total cost to Nationwide which would be approximately \$1 million a year less than what was described as EDSF's proposed total cost. According to UCC representatives, SSA rejected the offer since it would have required soliciting similar proposals from other vendors.

FINAL CONTRACT GUARANTEES

Although SSA had originally taken a hands-off attitude in the selection of potential subcontractors and in the solicitation of bids, it took a very active part in the negotiation and final writing of the subcontract. After receiving a copy of the proposed subcontract, SSA requested another meeting with Nationwide officials to discuss and agree on final language. EDSF representatives were also present at this meeting, held at SSA on September 19, 1972. The revised subcontract was signed by EDSF on September 20, 1972, and by Nationwide on September 24 and was approved by SSA on September 25.

As finally negotiated, the subcontract provides that, for each calendar year beginning with 1974, EDSF will reduce its charge per claim processed by the amount that Nationwide's average cost per claim exceeds the lowest of any of the following.

1. The model system average cost per claim obtained by (a) dividing the total cost incurred by model system carriers by the total number of claims processed by these carriers and (b) adding to the quotient an amount for system maintenance and support. The involved carriers are to be the three online model system carriers with the lowest average costs per claim. If there are only two such carriers, only those two will be used; if there is only one, that carrier plus the two regular model system (that is,

batch system) carriers with the lowest average costs per claim will be used.

2. The lowest average cost per claim of any SSA-designated large carrier, other than a carrier whose data processing is performed by EDS or any affiliated corporation--provided that, if such carrier is a model system user, the cost of model system support is to be added to the carrier's average cost per claim.
3. The model system adjusted average cost per claim obtained by making the same computation as provided for in item 1, except that the total model system carrier cost is to be adjusted downward for lower volume as specified in the subcontract. This option applies only to the extent that it does not reduce the model system average cost per claim below \$2.20.

The subcontract permits termination before the expiration of its 6-year term, under certain circumstances. (See p. 61.) However, Nationwide will then lose the right to use the EDSF system to process its Medicare claims. Also, the cost guarantees will not apply after the notice of termination is given.

In a summary of its justification for approving Nationwide's recommendation that the subcontract be awarded to EDSF, SSA maintained that the control (cost guarantee) that is most likely to limit the Government's obligation under the subcontract is the model system adjusted average cost per claim of the three lowest cost carriers using the model B online system. Although the model B online system was not operational when Nationwide sent out its request for proposals in April 1972, SSA told us in January 1973 that the system was operational at three carrier locations--GHI in New York, Blue Shield of Alabama, and Illinois Medical Service in Chicago. GHI, the first carrier to install the system, projected a unit cost of \$2.46 per claim for fiscal year 1973.

Although SSA had previously concluded that the cost differential between the EDSF and the UCC proposals was too great, it maintained that the effect of the cost guarantees would reduce Nationwide's per claim cost to a level

consistent with that projected for the lowest proposal. Further, SSA maintained that realizing, through the guarantee, the cost advantage that would have been realized with the lowest bidder had removed its primary objection to Nationwide's recommendation to award the subcontract to EDSF. However, it does not appear that SSA, in its evaluation and approval process, adequately considered what effect its decision would have on its overall policy of encouraging competition among the various suppliers of Medicare data processing services.

Although we agree that the contract as finally negotiated provides the Government with some safeguards not previously provided in any other subcontracts, SSA and Nationwide have no assurance that the guarantee provision of the subcontract will result in offsetting cost adjustments which will equalize the EDSF proposal with that of the lowest proposals. SSA projected a cost differential averaging over \$1 million a year during the 6-year subcontract, and we have no basis, at this time, for estimating whether the operation of the guarantee provision will offset SSA's estimated cost differential.

CONCLUSIONS

The changes negotiated in EDSF's proposal as a condition of approval by SSA were substantial. Accordingly, Federal competitive negotiation procedures, if applicable, would require that all offerors be given an opportunity to respond to the modified terms and conditions. We note that, at the August 9 meeting with Nationwide and EDSF, SSA suggested this approach in response to EDSF's initial offer to guarantee total carrier costs. SSA's suggestion that the other offerors be given an opportunity to respond to the modifications was renewed on August 22, 1972. However, in view of Nationwide's position that EDSF's proposal of a proven online system was superior to the proposals of UCC and MCAUTO, regardless of cost, giving the other offerors an opportunity to respond probably would not have had much effect on the ultimate selection of EDSF.

On the other hand, we believe the results of this procurement action were not consistent with SSA's stated policy of fostering competition among the various suppliers of data processing services, because

- SSA's intervention to permit other offerors to respond to the modified terms and conditions was ineffective and
- Nationwide's preference for a proven online system could be met by only one of the offerors.

CHAPTER 7

COMMENTS OF AGENCY, CARRIER,

AND SUBCONTRACTORS AND GAO EVALUATION

We received comments on this report from HEW, Nationwide, EDSF, MCAUTO, and UCC. (See apps. II through VI.) By letter dated May 23, 1973, HEW concurred in our suggestion that offerors be advised of (1) the evaluation criteria which will be used to evaluate their proposals, (2) the precise weights which will be given to price and total costs, and (3) the method of computing the cost factors, over and above the quoted prices. Specifically, HEW said its instructions to carriers would be revised to restrict cost comparisons to the services specified in the RFP, such as

- computer operations,
- onsite personnel,
- installation charges,
- transmission lines and terminals, and
- other specified equipment and supplies.

HEW maintained that such an approach appears practical since it now has an operationally tested part B online model system, which it did not have when Nationwide solicited proposals. (See app. II.) We expect that SSA, as part of its authority to approve subcontracts, will see to it that the evaluation criteria furnished to the offerors are strictly adhered to.

NATIONWIDE'S COMMENTS

By letter dated April 23, 1973 (see app. III), Nationwide advised us that its position needed to be clarified in certain parts of the report. These involve (1) the clarity of the specifications, (2) the evaluation factors furnished to one offeror, (3) not giving all offerors the opportunity to modify the terms or conditions of their proposals, and (4) the use of the terms "online" and "proven online system."

Nationwide maintained that its RFP was very specific and that the system requirements were clear and emphasized volume capabilities and proven experience. The field of data processing is rapidly developing and changing, and what Nationwide expected was proposals of the most effective claims processing system for Nationwide.

According to the information we obtained from the responding offerors, the written specifications were vague. Federal procurement policy provides that RFPs should be as complete as possible about the work to be performed and that the related specifications should contain all information necessary for the prospective offerors to prepare responsive proposals. This apparently was not done, as evidenced by the several meetings and contacts between Nationwide and the prospective offerors. According to Nationwide, the meetings and contacts were primarily to (1) obtain additional information on system requirements, (2) get clarification on the information already obtained, or (3) sell the merits of a particular system. As previously pointed out, it appears to us in retrospect that what Nationwide really wanted evolved during the solicitation and evaluation process, after the RFP had been issued.

For example, Nationwide's original RFP requested proposals on two bases--system installation only and system installation and operation (facilities management). The RFP emphasized (1) system performance requirements (e.g., processing the claims volume on a regular 24-hour cycle) and (2) the training of Nationwide personnel prior to installation. Both of these points were directed toward a proposal for only installation where the claims would be processed by Nationwide on its computer facilities. The RFP included virtually no information as to what was specifically desired in terms of a proposal for system installation and operation, which was the alternative ultimately selected by Nationwide.

Nationwide affirmed that it had informally furnished MCAUTO with the evaluation factors and their weights; however, they were not used in the final evaluation. Nationwide maintained that the factors were in rough draft and that the weights had been arbitrarily assigned as examples of how such an evaluation technique could be used. It maintained further that MCAUTO knew that the factors were in rough draft and therefore subject to change or to not being used at all.

Nationwide said also that the offerors were well aware of the factors used in the final evaluation.

The evaluation factors and their weights were provided to MCAUTO on April 27, 1972--about 8 days before MCAUTO submitted its proposal. Whether or not MCAUTO became aware of the different factors used in the final evaluation is not significant because MCAUTO told us that it used the information furnished on April 27 in preparing its proposal.

We believe that Nationwide's oral notice to the offerors of the criteria to be used in the evaluations was not in accord with sound procurement policy. When Nationwide provided MCAUTO information on the factors and weights that might be used, it should have provided similar information to EDSF and UCC. In our opinion, sound procurement policy requires that offerors be advised in writing of the evaluation criteria and their relative importance. We believe that such information would ultimately promote competition by

- permitting the offerors to be more responsive to the requirements of the carriers and intermediaries and

- assuring potential offerors that their proposals will be fairly evaluated on a common basis.

Nationwide maintained also that it had not given MCAUTO and UCC an opportunity to modify the terms and conditions of their proposals because it had already decided to award the subcontract to EDSF, so reopening negotiations would have been improper. Nationwide maintained that to lead the unsuccessful offerors to believe they were still being considered would have been unfair. Further, Nationwide stated that it had included the modified terms and conditions in the EDSF subcontract to make its recommendation acceptable to SSA.

Nationwide made its recommendation to SSA in June 1972, yet at SSA's request the unsuccessful offerors were not notified of this recommendation until the latter part of August, when the modified terms and conditions were still being negotiated with EDSF. Further, in mid-July 1972 Nationwide officials visited GHI to look at the model B online system installed by UCC; this visit could have led UCC to presume that its proposal was still being considered.

We believe that it would not have been unreasonable to ask the other offerors to respond to the proposed changes in contract terms when they were first considered, since they had not yet been notified of Nationwide's recommendation. The proposed changes were significant, and all offerors should be given an opportunity to respond to such changes.

Nationwide objected to our use of the terms "online" and "proven online" system, since the RFP did not mention either. Nationwide stated that the terms mean different things to different people and even different things to the same people at different times and suggested the terms be eliminated from the report.

Because of the variations in the proposals and related evaluations, we used these terms to clarify and match prices and evaluations with the systems proposed and to conform with the terms used in Nationwide's and SSA's evaluations.

EDSF'S COMMENTS

In its letter dated April 26, 1973 (see app. IV), EDSF maintained that our report did not sufficiently recognize the qualities and capabilities of its system or clearly point out the significant differences between its proposal and those of the other offerors. These differences, according to EDSF, would clearly show that the EDSF proposal for full facilities management and its prior experience were superior to those of the other offerors and were the only logical choice for Nationwide. EDSF maintained that SSA's evaluation also did not sufficiently recognize these differences which affect pricing, overall cost, credibility, and ability of the offerors to perform.

We recognize that EDSF proposed and implemented a total facilities management system which included services over and above basic data processing services. We believe, however, that the cost of these services was shown in the considerably higher price proposed by EDSF. When the services offered differ significantly, the vendors should be required to separately price the costs of their data processing systems and ancillary services, to permit comparisons and evaluations on common bases.

With respect to EDFS's observations about the inadequacies of the other offerors' proposals and prior experience, we did not attempt to evaluate the merits of each proposal. It should be pointed out, however, that according to SSA about 13 data processing firms with apparent capabilities to process part B claims have demonstrated an interest in competing for a share of Medicare claims processing. Of these firms, only three--all of which were actually operating such systems at other locations--were invited by Nationwide to submit proposals. In terms of fair competitive procurement practices, this seems to imply that those firms selected to submit proposals were presumed by Nationwide to have been capable of doing the job; we reviewed the procurement procedures and policies followed by SSA and Nationwide in that light.

EDSF maintained that it is being subjected to unfair competition when it has to compete with the SSA developed and maintained model system. Further, carriers' data processing subcontracts are subject to approval by SSA, and EDSF claims SSA has a vested interest in the model system.

It appears that most of the current competition for Medicare claims processing systems is between the EDSF system and SSA's model system, even though other systems are available. It is not unusual for the Federal Government to develop, or participate in the development of, alternate sources of products and services when it believes that is the only way to achieve an effective competitive environment. Further, we found no evidence that SSA did anything to prevent EDSF from competing in this procurement.

As discussed in chapter 5, we share some of EDSF's concerns about the various assumptions SSA used to evaluate the proposals. However, by establishing and publicizing the evaluation criteria before the proposals are submitted--as we suggested and HEW agreed to--the same rules would apply to SSA's evaluations and those of the carriers or intermediaries. Strict adherence to preestablished rules should help minimize any possible bias in the evaluation process because of SSA's vested interest in one of the systems.

MCAUTO'S COMMENTS

MCAUTO, by letter dated March 30, 1973 (see app. V), told us it had reviewed our proposed report and had no further comments.

UCC'S COMMENTS

In its letter dated April 12, 1973 (see app. VI), UCC said it concurred in our assessment of the procurement irregularities involved in the award of the EDSF subcontract. UCC maintained that these irregularities were permitted by SSA and were ultimately condoned by SSA's approval of Nationwide's recommendation.

CHAPTER 8

SCOPE OF REVIEW

We made our review at SSA headquarters in Baltimore, Maryland; Nationwide in Columbus, Ohio; MCAUTO in Falls Church, Virginia; and EDSF and UCC in Dallas, Texas.

We reviewed the basic legislation which established the Medicare program and HEW's authority to contract with carriers. We also reviewed the HEW-Nationwide carrier contract; legislative hearings and reports pertaining to HEW-carrier relationships; pertinent provisions of the Federal Property and Administrative Services Act of 1949, as amended, and related FPRs; and other pertinent regulations, instructions, records, reports, and documents on file at SSA.

We interviewed SSA and Nationwide officials, as well as representatives of EDSF, MCAUTO, and UCC. We did not make detailed analyses of the evaluations of the various proposals.

At the conclusion of the review, we discussed our findings and conclusions with SSA, Nationwide, EDSF, MCAUTO, and UCC representatives.

L. H. FOUNTAIN, CHAIRMAN
 ROBERT E. JONES, ALA.
 BENJAMIN S. ROSENTHAL, N.Y.
 JOHN C. CULVER, IOWA
 DON FUQUA, FLA.
 BILL ALEXANDER, ARK.

NINETY-SECOND CONGRESS
Congress of the United States
House of Representatives
 INTERGOVERNMENTAL RELATIONS SUBCOMMITTEE
 OF THE
 COMMITTEE ON GOVERNMENT OPERATIONS
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 J. KENNETH ROBINSON, VA.
 225-2548

Gerry Brown, Mich.

September 7, 1972

Honorable Elmer B. Staats
 Comptroller General
 U.S. General Accounting Office
 441 G Street, N.W.
 Washington, D.C. 20548

BEST DOCUMENT AVAILABLE

Dear Mr. Staats:

As you know, the Intergovernmental Relations Subcommittee is examining the administration of the Medicare program by the Social Security Administration, with particular attention being given to data processing operations.

Since November 1969, SSA instructions to Part B Medicare carriers have required that competitive proposals be obtained from at least three separate sources prior to awarding of data processing subcontracts. In April of this year, Nationwide Insurance Company, the Part B carrier for Ohio and West Virginia, requested proposals from three firms for installation and operation of a new Part B data processing system.

Preliminary information available to the Subcommittee indicates that three proposals for on-line direct data entry processing systems were submitted to Nationwide. It is my understanding that the high proposal was for a charge of nearly 90 cents per claim processed, while the lowest proposal was for less than 30 cents per claim. Despite the three to one discrepancy between the high and low proposals, it appears that Nationwide, with the apparent approval of SSA, intends to award the subcontract to the firm which submitted the high proposal.

In view of the obvious questions concerning procurement policy and fair competition which appear to be involved, I would appreciate it if

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Honorable Elmer B. Staats
September 7, 1972
Page 2

you will look into the matter on a priority basis and provide a report
as soon as possible.

Sincerely,

L. H. Fountain

L. H. Fountain
Chairman



DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE
WASHINGTON, D.C. 20201

OFFICE OF THE SECRETARY

MAY 23 1973

Mr. John D. Heller
Associate Director
Manpower and Welfare Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Heller:

The Secretary has asked that I respond to your letter of March 15, 1973, in which you requested our comments on your draft report "Award of Sub-contract for Processing Medicare Claims for Physicians' Services in Ohio and West Virginia". The Department's comments are enclosed.

We appreciate the opportunity to express our views prior to the issuance of the final report.

Sincerely yours,

A handwritten signature in cursive script, appearing to read "J. B. Cardwell".

James B. Cardwell
Assistant Secretary, Comptroller

Enclosure

COMMENTS ON GAO DRAFT REPORT ENTITLED "AWARD OF SUB-
CONTRACT FOR PROCESSING MEDICARE CLAIMS FOR PHYSICIANS'
SERVICES IN OHIO AND WEST VIRGINIA"

The report deals with GAO's review of a subcontract for electronic data processing (EDP) services entered into by Nationwide Mutual Insurance Company, one of the carriers that DHEW has contracted with under Part B of the Medicare program. In keeping with legislative intent, carriers have basic responsibility for the administration of payments for benefits for physicians' services, including responsibility for obtaining necessary services and deciding upon the subcontractors that will provide them. To aid the carriers, SSA has drawn up guidelines designed to assure sound procurement practices, and these guidelines generally are along the lines of the Federal Procurement Regulations. But it's important to recognize that carriers are not legally or contractually bound by the Federal Procurement Regulations.

As the report indicates, the carrier had experienced serious problems in processing claims, first with a system of its own design and then with an EDP system developed by an outside contractor. Faced with a heavy influx of new claims, a rapidly expanding workload, and a growing backlog of unprocessed claims, the carrier concluded that the capacity and capability of the existing system were inadequate to its needs and that a new system should be contracted for. In light of this experience, the carrier's preference was for a proven system that would be capable of handling its relatively large Medicare claims workload, and could be fully operational before the onset of its peak claims processing season.

Systems proposals were requested of and received from three firms and --although GAO noted some shortcomings in the development of specifications and in the solicitation and evaluation of the proposals--the report does not indicate that the firm selected was not the best choice.

SSA's policy of encouraging competition among suppliers of EDP services, together with the requirements set forth in the standard contract with carriers and related instructions, attest to our continuing concern that sound procurement practices be followed in the acquisition of services whose costs will be borne or shared by Medicare. At the same time, it should be remembered that the carrier's activities, constituting as they do the delivery of the services the Medicare program is designed to provide, cannot be interrupted and that the assurance of not only continuation of this service but its improvement was of particular concern to both Nationwide and SSA.

It is particularly significant to recognize in this case that while some procedures followed in the development of specifications and solicitation of proposals may not have coincided with the Federal Procurement Regulations--and again, the carrier was not legally or contractually bound by them--at the same time GAO did find that each of the offerors generally understood what kind of system the carrier needed and wanted. It is important to note also that after the decision was made to obtain a new system, the carrier spent considerable time in studying the initial proposals including visits to other carriers to observe the operation of the types of systems proposed. SSA too evaluated the proposals and reviewed the carrier's evaluations. The results ultimately led to the inclusion in the subcontract of cost guarantees which act to limit the carrier's cost-per-claim to levels consistent with those projected for the lowest proposal. Along with these cost guarantees the carrier achieved one of its primary objectives, namely, the acquisition of an automated claims processing system whose capability and effectiveness in handling large workloads had been previously demonstrated.

In line with SSA's policy of fostering competition, GAO suggests that:

- SSA should consider a requirement that potential offerors be advised, in writing, of the evaluation criteria used to evaluate their proposals. They should be advised particularly and as precisely as possible of the weight that prices or cost will be given in the evaluation and selection process.
- SSA should determine the validity of the basic approaches and assumption to be used in computing the total cost of a proposal. SSA should then advise carriers and intermediaries--as well as potential data processing subcontractors--just how the factors over and above the offerors' quoted prices are to be computed. The availability of such information should help foster competition by (1) permitting offerors to be more responsive to requirements of carriers and intermediaries, and (2) assuring potential offerors that their proposals will be fairly evaluated on a common basis.

We concur in these suggestions and will revise our instructions to give effect to them. In dealing with carrier proposals to secure EDP services, we intend to specify in our revised instructions that cost comparison will be restricted to the services specified in the request for proposal e. g. , computer operations, on-site personnel, installation charges, lines, terminals, and other specified equipment and supplies. This approach appears now practical and attainable since we have available for the first time in our Medicare administration fully competitive, operationally tested on-line Part B Systems, a situation that did not exist at the time Nationwide solicited proposals.

NATIONWIDE MUTUAL INSURANCE COMPANY • MEDICARE HEALTH INSURANCE
P.O. BOX 57 • COLUMBUS, OHIO 43216



April 23, 1973

Mr. Robert E. Iffert, Jr.
Assistant Director
U. S. General Accounting Office
Washington, D. C. 20548

RE: Award of the Subcontract for
Processing Medicare Part B
Claims in Ohio and West
Virginia

Dear Mr. Iffert:

We appreciated the opportunity to review, in some detail, the draft of your report with Mr. Daigle and Mr. Conley on April 13. As a result of this discussion, some minor revisions have been made to the draft. There are certain areas where we feel it is important that Nationwide's position be clarified and it is these points I would like to speak to:

- ...The report concludes written specifications for proposals were vague and it appears that the type of system preferred by Nationwide emerged after proposals were requested. Nationwide's requests for proposals were, in our judgment, very specific. We clearly set forth the requirements of processing as defined by SSA and understood by Nationwide. A sincere effort to obtain competitive proposals was made by Nationwide and SSA. The field of data processing is rapidly developing and changing, and we expected from the bidders their proposal of what would be the most effective processing system for Nationwide. We emphasized volume capabilities and proven experience.
- ...Reference is made several times in the report to evaluation factors provided to MCAUTO which were used by Nationwide in evaluating the proposals. These factors, as published on Page 31 of the report, were not used in the final evaluation. The criteria actually used in the evaluation is that shown on Pages 45 and 46 of the report. In Nationwide's judgment, all bidders were well aware of the factors that were used in the final evaluation.

An understanding of the factors referred to by MCAUTO may place them in better perspective. The factors, which were in rough draft form, were used by Nationwide personnel as a basis for discussion during their April 27, 1972 trip to MCAUTO. They had been assembled by one of Nationwide's people as

factors he believed Nationwide may want to consider in its comparison of vendors. It was not an exhaustive listing and was one man's thoughts only. The weights were arbitrarily assigned as examples of how such an evaluation technique could be used.

During the discussion with MCAUTO that day, Mr. R. Harman asked about the technique Nationwide was planning to use in its evaluation. He was told of the morning's discussion during which no conclusions had been reached. He asked if he could have a copy of our rough draft material; he accepted it, knowing full well that they were in rough draft form, and that as a consequence, they were subject to change or to no use at all. Nationwide was very surprised that such a big issue was made of these factors in the report.

- ...Page 4 of the report indicates that the other bidders, namely, MCAUTO and UCC, were not given the opportunity to respond to the modified terms and conditions that ultimately appeared in the EDSF contract. Nationwide maintains that we made a conscious evaluation of the three proposals submitted and recommended EDSF to SSA. SSA found our original proposal unacceptable until we inserted the additional guarantees and contract terms. With these modifications, SSA found the proposal acceptable and approved the contract. We felt reopening the bids to MCAUTO and UCC would be improper as our decision had been made and approval was pending subject to these modifications. We felt it was not fair to the two bidders to lead them to believe they were still being considered when our decision had been made and submitted to SSA on June 22, 1972.
- ...The term 'on-line' was not used in Nationwide's request for proposals. Bidders were asked for their recommendation for a system that would best handle Nationwide's requirements. We were seeking a proven system with 'on-line', regardless of how defined, not being a prerequisite.

The terminology 'on-line' appears a number of times in the report. Since this terminology means very different things to different people, and even different things to the same people at different times, it was strongly recommended that it be eliminated from the report.

...The final conclusion indicates, "Nationwide's preference for a proven on-line system--its definition of proven emerged during the evaluation process rather than at the time proposals were requested--could be met by only one of the offerors". Nationwide entered into the selection of a data processing subcontractor with the only objective being one of finding the system which would provide Nationwide with the best possible data processing services to fulfill our Medicare Part B contract with SSA. EDSF was chosen by us because in our judgment, taking all factors into consideration, it is the company which would do the required job most efficiently and most dependably at the lowest overall cost. Our primary interest was in doing a good job, which we feel conforms exactly with the interests of the government and the beneficiary.

Sincerely,



R. H. Ourant
Vice President
Medicare

RHO:bls

cc: B. D. Kirk
G. W. Schmidt

GAO note: The page numbers referred to in these comments are those of our draft report, not this final report.

E. D. S. FEDERAL CORPORATION

DALLAS, TEXAS 75235

1300 EDS CENTER
EXCHANGE PARK
FLEETWOOD B-3171

April 26, 1973

Mr. Robert E. Iffert, Jr.
Assistant Director
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Iffert:

Thank you for the opportunity to comment on the draft of your report to the Subcommittee on Intergovernmental Relations concerning the subcontract awarded by Nationwide Mutual Insurance Company to Electronic Data Systems Federal Corporation (EDSF).

Our principal problem with the draft report is that it reflects certain underlying misassumptions or misunderstandings which are implicit in much of the draft and occasionally explicit in it. This in turn may stem from the fact that perhaps there are areas which have not been explored sufficiently by the General Accounting Office in connection with this matter.

The first critical point is the failure of the draft sufficiently to evaluate and comment upon the substantial differences in the proposal made by EDSF and the proposals made by its competitors and to accept uncritically certain of the commentary by the Social Security Administration staff (both of the special review team and the BHI group) with respect to these proposals. EDSF offered a substantial package of services to Nationwide. This included the installation and operation of one of the EDSF Medicare Part B data processing systems.

EDSF's proposal, however, also encompassed total facilities management of which operation of the electronic data processing system is only a part. It included additions to and modifications and enhancement of that system in order to tailor it to Nationwide's needs. It included very substantial support on site at Nationwide throughout the life of the contract by systems engineers, operators, and industrial engineers to assure maximization of performance improvements and cost reductions. It included

APPENDIX IV

Mr. Robert E. Iffert, Jr.
April 26, 1973
Page II

procurement or furnishing of supplies, services (such as microfilming), on-site hardware, communications, etc. providing single-point accountability.

On the other hand, the other two vendors offered simply to install and run on computers one or another version of the Model B system developed by the Social Security Administration. Their price did not even include installation of systems enhancements designed by SSA and provided virtually no on-site support.

This difference, of course, explains in part why the pricing of the proposals was different as among the vendors since EDSF was offering significantly greater services.* More important than the pricing of the specific proposals, this great difference in services has had in the past, and will have in the future, a significant impact on the total cost per claim processed incurred by the carrier, as well as on carrier performance.

The statement of SSA officials quoted in your draft as indicating that there should be no difference in manning or clerical costs for the various systems is inconsistent with proven fact and SSA's own prior position-- and becomes totally untenable in the context of this procurement. One of the other vendors (MCAUTO), according to your draft, recognized that different vendors as well as different systems could produce different carrier staffing requirements. So, too, will the varying circumstances at different carriers. In fact, SSA has recognized in public testimony that in instances where carriers were in difficulty in the past it was the ability of EDSF to provide the necessary skilled and trained manpower which permitted EDSF to help carriers turn around disastrous, or potentially disastrous, situations. Thus the comprehensiveness of the services being furnished, as well as the skill of the vendor's personnel, hardly are insignificant factors, and, of course, differences in the systems also have a significant affect.

*The pricing difference is also impacted by the fact that SSA has spent many millions of dollars, and apparently will continue to spend many millions of dollars, on the design, modification, and maintenance of the Model B System; whereas, EDSF bears such costs for its systems. Except for a passing reference to what we believe is but a portion of the total costs expended by SSA to date in this regard, your draft report makes no reference to this subsidy, which runs, at minimum, between \$.17 and \$.27 per claim processed.

APPENDIX IV

Mr. Robert E. Iffert, Jr.

April 26, 1973

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system are not pertinent to the procurement under review). Each of those locations uses the Model B Batch System--though certain on-line functions are being added to one at this time.

The carrier cost where one vendor, UCC, operates the data processing system, is briefly adverted to once in your draft report. Not only (and after several years of operation of the Model B System by that vendor) were the carrier costs at that location (Chicago) 250% greater per claim processed than those that vendor projected for Nationwide, but also simultaneously that carrier had one of the worst performance records in the nation. In fact, SSA sent a team there to try to help the carrier and its vendor improve services and costs, and a year later those costs and performance are still among the worst. The manning levels at that carrier were approximately double those which the vendor estimated would be achieved at Nationwide.

With respect to the other vendor, MCAUTO, the carrier costs per claim at its one location are \$1.18 per claim higher than an estimated cost used by Nationwide in evaluating the EDSF proposal. The manning levels achieved by that carrier after several years of operation of the Model B System by that vendor were approximately 50% higher than that vendor estimated for Nationwide.

In terms of sound procurement, should Nationwide be required to gamble on estimates by vendors whose records do not support those estimates? In that same connection, EDSF has helped other carriers (both large and small) achieve manning levels comparable to its estimate for Nationwide. Moreover, the performance of EDSF-serviced carriers has been consistently superior to Model System carriers, and substantially so with respect to the two served by the two other vendors.

This brings us to the crux of the myth versus reality. You reported on page 71 of your draft statements by SSA officials as follows:

"SSA officials stated that the current developments being made with the SSA Model B on-line system needed to be recognized. SSA maintained that although the cost of the EDSF system--at the outset of the contract period--might be judged reasonable, this would not necessarily be so

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over the life of the subcontract, particularly since differences in personnel requirements would be eliminated, over a period of time, with use of on-line systems.

SSA officials maintained also that after an initial shakedown and adjustment period, on-line systems-- designed to do the same things--should have basically the same needs with respect to supporting personnel. Further, technical improvements in the Medicare Model B on-line system, which are likely to be possible, could have a significant effect on future claims processing cost. With a long term fixed-price subcontract, of the type proposed by EDSF, the Government would not be able to realize the resulting cost advantages. "

Those comments recognized that at the inception of the Nationwide contract EDSF costs were reasonable. SSA's objection was based on its optimistic projections as to what the Model B System in its on-line mode might accomplish in the future, projections made at a time, according to your draft, when that system was first becoming operational and at a small carrier only.

It assumes that all systems and all vendors, and in all circumstances, ultimately will result in the same performance and costs. The record is to the contrary. We know that the ASDC system, with ASDC assistance, works well at some small carriers, but did not work at Nationwide. SSA officials publicly testified at the very time of this procurement as to their uncertainties as to the Model System's performance and costs at a large carrier. MCAUTO, who has been deeply involved in the development of the Model System, is quoted by you as stating that different systems and different vendors will produce different costs. Thus, the basic SSA assumption appears without basis.

SSA also assumes improvements will occur in the future in the Model System, but credits none to EDSF in the future. This not only is contrary to history and common sense, but contrary to the record in the very procurement where EDSF proposed systems enhancements to meet Nationwide's specific needs.

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Your draft fails to condemn the SSA procurement policy, where the SSA, which has spent millions of dollars developing a system and has spent several years promoting that system (without requiring competition from vendors of other systems*), relies upon the very staff that has a vested interest in demonstrating the success of the Model B System (and upon others in the same agency) in evaluating the Nationwide recommendation, and (a) evaluates competitive proposals with respect to both costs and performance based upon unproven assumptions as to the Model B System; (b) makes unwarranted assumptions as to equivalence of systems and vendors; and (c) takes no cognizance of the actual performance at other locations of the vendors involved.

Surely these are shortcomings, with respect to the establishment of a competitive environment, which should not be permitted.

It may be helpful to you in recognizing, and perhaps evaluating the differences in services being offered by the vendors, and in evaluating the realism of the respective estimates of total costs per claim, to be aware of three of the significant electronic data processing differences between the Model B and the EDSF systems, and their related support and service functions.

First, because Nationwide has a very low assignment rate, EDSF recognized the necessity to handle through the data processing system the inquiries which Nationwide must make in order to obtain the necessary information after a claim is received to complete processing of that claim. EDSF specifically proposed that it would tailor its system to provide such an additional service. This is not provided by the Model B System and was not considered, as far as we can tell, in any of the evaluations. This service alone, which has already been implemented, will result in annual savings of approximately 20 people at Nationwide. More important, it

*Note the 1969 directive to which you refer requires carriers to obtain competition vis-a-vis the Model B System by requiring bids by vendors of the Model B System, but does not require proposals from vendors of other systems. To the best of our knowledge, despite the alleged policy of SSA of fostering competition, promulgated in November, 1969, EDSF was not invited to propose to a great many of the other carriers who have contracted for the Model B System since November, 1969; nor to our knowledge did SSA ever insist that such competition be obtained.

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demonstrates what it is that EDSF does that is not done by other vendors. Throughout the life of the program, EDSF will provide additional services which improve performance and reduce costs and will do so based on the need of the particular carrier. With Model B, under the umbrella of the SSA, it is a matter of when that agency, considering all of the carriers serviced, determines that it has the people and the funding necessary to provide some particular enhancement (when this may result in the vendor increasing its per claim price). It is the difference between custom-made and bought-off-the-rack. It is the difference between a vendor who thoroughly understands a carrier's needs and demonstrates its credibility in its proposal and vendors who simply have a limited understanding of what full facilities management means.

Another such item, in fact, required by SSA but still not implemented in the Model B System, to our knowledge, which has been designed and implemented by EDSF for a number of its carriers without cost is the prepayment utilization review system (which is being furnished to Nationwide). This system not only saves personnel, with respect to a carrier that is properly doing its job, but is a major money saver to the Government in terms of what ultimately it will pay out in benefit dollars (which are the biggest part of the Medicare Part B cost pie). We assume that SSA proponents of the Model B System would say, "But, oh yes, we are developing such a system, and one day we will have it." Should Nationwide have been required to make its selections on that basis?

In this same connection, the EDSF service provides resource management systems. These systems provide extensive data on costs and performance throughout the claims processing system. The EDSF on-site personnel, working with the carrier personnel, utilize these cost and performance "controls" to effectively upgrade performance and reduce costs. The Model B System does not provide this data, and the Model B vendors do not provide these services. This, of course, would explain in part why EDSF's price is higher; but more importantly, it explains why its estimates are more credible and why Nationwide chose to accept them in preference to the other vendors.

The willingness and ability to tailor systems as required, together with the furnishing of substantial "controls" to the carrier and an on-site staff to facilitate their effective use, also provide the carrier with far greater control over its operation than can be obtained from a "service-

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bureau" type contract for the Model B System. The carrier has the means to execute its "functions" more effectively by having a responsive and skilled facilities management organization there to assist it and subject to its direction.

Your draft makes no endeavor to review or comment on these very significant differences--differences which affect pricing, differences which affect overall costs to the Government, differences which affect credibility, and differences which affect ability of the vendors. The SSA evaluations totally ignore them.

In closing, we should point out that, perhaps most ironically, SSA is now implementing a carrier performance evaluation system in which costs constitute only 20% of the total evaluation. The SSA review team found less than a 5% difference in the total cost per claim between what it considered the low proposer, UCC (at \$1.90 total cost per claim), and EDSF (at \$1.99). Nationwide, a very large carrier, in serious operating difficulty with respect to Medicare Part B, and (1) being told by UCC that it was unwilling to take any responsibility for on-site support; (2) aware that UCC's only track record is a customer whose performance and costs have been considered by SSA to be among the worst in the nation; and (3) knowing that UCC was offering a system not yet operational, and only being piloted at a small carrier--nevertheless was told in effect by the SSA special review team that it should reject a firm fixed price proposal by EDSF, even though EDSF alone had a proven track record of a successful operation, and alone offered both substantial on-site support and known ability to assist carriers in serious operational difficulty. That is not common sense, and it is not sound procurement. And the second SSA evaluation had even less merit and reflected greater bias in favor of the Model B System (which, after all, is the child of the SSA staff nurtured by millions of Government dollars).

As your report is intended to improve competitive procurement, we hope that you will point these matters out. A competitive environment must be a fair environment--and this can be accomplished only by either ending the SSA subsidy of, and thus stake in, the Model B System, or if the Model B System and its vendors are too weak to exist without such subsidy, then removing the SSA proponents of the Model B System from the competitive procurement evaluation process.

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We cannot in the available time comment line-by-line on your draft report. We appreciate having had the opportunity to meet with you and discuss some of our concerns and objections. We should make clear that our comments are not intended to in any way question your objectivity-- but rather to point out areas where we believe you have perhaps not received all the information you need to permit the type of comprehensive and accurate report which we are sure you desire to complete.

Very truly yours,

A handwritten signature in cursive script that reads "Gary R. Anderson". The signature is written in black ink and is positioned above the typed name and title.

Gary R. Anderson
Vice President
Health Care

GRA:lr

MCDONNELL DOUGLAS AUTOMATION COMPANY

2990 Telestar Court, Falls Church, Virginia 2204

March 30, 1973

Mr. Robert E. Iffert, Jr.
Assistant Director
United States General Accounting Office
Manpower and Welfare Division
Washington, D.C. 20548

Dear Mr. Iffert:

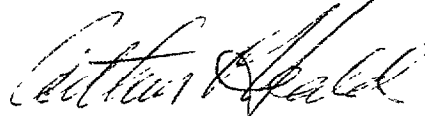
McDonnell Douglas Automation Company is in receipt of the draft report to the House Sub-Committee on Inter-Governmental Relations on the award of the sub-contract for processing Medicare claims in Ohio and West Virginia.

After careful review of the subject document, McDonnell Douglas Automation Company has no further comments to make. However, if we can be of any further assistance to you, please do not hesitate to call George Fanady or myself at any time.

We appreciate your courtesy in sending us an advance copy of this report.

Sincerely,

MCDONNELL DOUGLAS AUTOMATION COMPANY



Arthur F. Heald
Director, Mid-Atlantic Region

AFH:sr



UCC
UNIVERSITY COMPUTING UTILITY COMPANY

7200 Stemmons Freeway
P.O. Box 47911
Dallas, Texas 75247
214/637-5010

April 12, 1973

Mr. Robert E. Iffert, Jr.
Assistant Director
Manpower and Welfare Division
United States General Accounting Office
Washington, D. C. 20548

Dear Mr. Iffert:

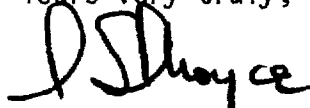
We have reviewed the contents of the draft report on the award of the sub-contract for processing Medicare claims for physicians' services in Ohio and West Virginia and offer the following comments:

1) The criteria used in Nationwide's performance comparisons (Page 49) for UCC's customers were not those submitted to Nationwide on June 9. These more current statistics reflect a 32% cost improvement and a 22% improvement in weeks work on hand for customer K; customer L shows a 45% cost improvement and 64% improvement in weeks work on hand, making customer L's cost less than \$2.50 per claim with a 1.0 weeks work on hand.

In our opinion, these revised figures more accurately reflect UCC's customers' performance and, most importantly, negate the tendency that the reader of the chart has to conclude that UCC's customers have the poorest performance record.

2) We concur with your assessment of the procurement irregularities. Unfortunately, these practices were permitted to exist by SSA and were ultimately condoned by virtue of SSA's approval of Nationwide's recommendation.

Yours very truly,



C. S. Choyce, Vice President
Market Development

CSC:jw

GAO note: The page number referred to in these comments is from our draft report, not this final report.

