

**STATE OF NEW YORK
DEPARTMENT OF HEALTH**

In the Matter of the Appeal of	:	
	:	
Dumont Masonic Home	:	Decision After
Medicaid ID# [REDACTED]	:	Hearing
	:	
from a determination to recover Medicaid Program	:	
overpayments	:	#04 W04-3221
	:	

Before: John Harris Terepka
Administrative Law Judge

Held at: New York State Department of Health
90 Church Street
New York, New York 10007
September 8, November 23, 2010; March 9, 2011
445 Hamilton Avenue
White Plains, New York 10601
February 10, 2011

Record closed June 13, 2011

Parties: New York State Office of the Medicaid Inspector General
217 Broadway, 5th Floor
New York, New York 10007
By: Daniel V. Coyne, Esq.

Dumont Masonic Home
676 Pelham Road
New Rochelle, New York 10805
By: Raul A. Tabora, Jr., Esq.
Ruffo Tabora Mainello & McKay P.C.
300 Great Oaks Boulevard Suite 311
Albany, New York 12203

JURISDICTION

The New York State Department of Health (the Department) acts as the single state agency to supervise the administration of the Medicaid Program in New York State. Public Health Law 201(1)(v); Social Services Law 363-a. The New York State Office of the Medicaid Inspector General (OMIG) is an independent office within the Department, responsible for the Department's duties with respect to the recovery of improperly expended Medicaid funds. PHL 31.

The OMIG issued a final audit report for Dumont Masonic Home (the Appellant) in which the OMIG concluded that the Appellant had received Medicaid Program overpayments. The Appellant requested this hearing pursuant to SSL 22 and former Department of Social Services (DSS) regulations at 18 NYCRR 519.4 to review the overpayment determination.

SUMMARY OF FACTS

An opportunity to be heard having been afforded the parties and evidence having been considered, it is hereby found:

1. At all times relevant hereto Appellant Dumont Masonic Home, located in New Rochelle, New York, was a 196 bed residential health care facility (RHCF) licensed under PHL article 28 and enrolled as a provider in the Medicaid Program. Dumont Masonic Home (DMH) was owned and operated by The German Masonic Home Corporation (GMHC) from 1982 until 2010. (Appellant Exhibit L; Transcript, pages 14, 149.)
2. Auditors from the OMIG reviewed the Appellant's reimbursement from the Medicaid Program for the rate period October 1, 1998 through December 31, 2007.

(Department Exhibit 13.) Pursuant to 18 NYCRR 86-2.10(g), the Appellant's Medicaid rates for property cost reimbursement for the period 2002 through 2007 were based upon the Appellant's reported 2000 through 2005 property costs. (Department Exhibit 16.)

3. On January 11, 2010, the OMIG issued a final audit report that identified several property cost disallowances. The OMIG's letter accompanying the audit report advised the Appellant that it intended to recover Medicaid Program overpayments in the total amount of \$1,190,493 on the basis of the disallowances. (Department Exhibit 13.)

4. By letter dated January 12, 2010, the Appellant requested an administrative hearing to challenge OMIG's determination. (Department Exhibit 14.) The parties having settled all other issues raised in the Appellant's hearing request, audit report disallowances 1, 2 and 7 are the only issues remaining for this hearing decision. (Transcript, page 10.)

5. On its 2000 through 2005 form RHCF-4 cost reports submitted to the Medicaid Program, the Appellant reported gains on sales of securities from a "board designated fund." This reported investment income was not offset against interest expenses in the calculation of the Appellant's 2002 through 2007 Medicaid reimbursement rates. In this audit, the OMIG offset the reported gains against the Appellant's interest expenses. The adjustment resulted in disallowances of Medicaid reimbursement. (Department Exhibit 13, audit report disallowance 1 - "investment income offset.")

6. On its 2000 through 2005 cost reports, the Appellant reported interest expenses on working capital loans. It was reimbursed for these costs in its 2002 through 2007 Medicaid rates. In this audit, the OMIG disallowed Medicaid reimbursement for

interest on the working capital loans on the grounds that during the 2000 through 2005 cost years, the Appellant had available liquid assets in form of cash on hand, receivables due on loans made to an affiliate, and the “board designated fund” that could have been used to avoid incurring interest charges on working capital loans. (Department Exhibit 13, audit report disallowance 2 - “working capital interest.”)

7. On its 2004 and 2005 cost reports, the Appellant reported telephone equipment expenses for which it received reimbursement in the property component of its rate. In this audit, the OMIG disallowed the telephone costs included in the property component of the rate on the grounds that under Medicaid reimbursement methodology telephone costs are an operating expense for which reimbursement is provided in the operating component of the rate. (Department Exhibit 13, audit report disallowance 7 – “disallowance of telephone equipment expense.”)

ISSUES

Has the Appellant established that the OMIG’s audit report property expense disallowances 1, 2 and 7 are not correct?

APPLICABLE LAW

A residential health care facility (RHCF), or nursing home, can receive reimbursement from the Medicaid Program for costs that are properly chargeable to necessary patient care. 10 NYCRR 86-2.17. As a general rule, these kinds of costs are allowed if they are actually incurred and the amount is reasonable. Allowable costs usually include employee wages and benefits, administration, maintenance and supplies, utilities and other operating expenses. 10 NYCRR 86-2.10(a)(7). They can also include

a component for capital costs such as, in this case, interest on current and capital indebtedness. 10 NYCRR 86-2.10(a)(9); 86-2.20(a).

The facility's costs are reimbursed in the form of per diem rates set by the Department on the basis of costs reported by the facility. A facility's rates are provisional and subject to audit. If a Department audit identifies an overpayment it can retroactively adjust the rates. SSL Section 368-c; 10 NYCRR 86-2.7; 18 NYCRR 517.3. The Department may then require the repayment of any amounts not authorized to be paid under the Medicaid Program. 18 NYCRR 518.1.

If the Department determines to recover an overpayment, the facility has the right to an administrative hearing. 18 NYCRR 519.4. The facility has the burden of showing that the determination of the Department was incorrect and that all costs claimed were allowable. 18 NYCRR 519.18(d)(1).

DSS regulations pertinent to this hearing are found at 18 NYCRR parts 517, 518 and 519, and address the audit, overpayment and hearing aspects of this case. Also pertinent are DOH regulations at 10 NYCRR part 86-2 (reporting and rate certifications for RHCFS, in particular section 86-2.20 regarding interest expense), part 451 (RHCF uniform reporting – definitions) and part 452 (RHCF uniform reporting - basic concepts, reporting principles and specialized reporting areas.) Also applicable, unless otherwise provided in part 86-2, are the principles of reimbursement developed for determining payments under the Medicare Program. 10 NYCRR 86-2.17(a). These are primarily found at 42 CFR chapter IV and in the Medicare Provider Reimbursement Manual, Part I (PRM-I).

EVIDENCE

Witnesses for the OMIG:

George D. Vislocky	Rate audit manager of the OMIG's White Plains office who supervised this audit. (Transcript, pages 21, 23.)
Wanda Perez-Maldonado	Assistant attorney general for the State of New York. (Transcript, page 355.)

Witnesses for the Appellant:

Robert George Elliot	Appellant's director of finance. (Transcript, page 148.)
Gottfried Schuebler	Trustee and the president of GMHC. (Transcript, page 225.)
Richard Katz	General counsel to GMHC. (Transcript, page 248.)
Frank J. Granger	Certified public accountant with GMHC's outside auditors. (Transcript, page 318.)

OMIG Exhibits 1-17.

Appellant Exhibits A, E, F, H, I, J, K, L, N, O, P, Q.

A transcript of the hearing was made. (Transcript, pages 1-382.)

Each side submitted two post-hearing briefs.

DISCUSSION

Property expense disallowance 1. Investment income offset.

Necessary interest on both current and capital indebtedness is an allowable cost for all RHCs. 10 NYCRR 86-2.20(a). However, pursuant to 86-2.20(c):

- (1) Interest expense shall be reduced by investment income with the exception of income from funded depreciation, qualified pension funds, trustee malpractice insurance funds, or in instances where income from gifts or grants is restricted by donors.

The OMIG identified investment income that it applied in this case to reduce the Appellant's reported interest expense. The Appellant argues that the income in question falls within the exception for "instances where income from gifts or grants is restricted by donors." According to the Appellant, the "board designated funds" on which the gain

was realized are restricted funds and so investment income on them should not be applied to reduce interest expenses of DMH.

At the hearing, Mr. Vislocky used the figures reported for the cost year 2000 to explain the audit determination to treat gains on the board designated funds as unrestricted investment income. The 2000 cost report included \$317,283 as a “gain on sale of securities and gain on special events.” (Transcript, page 46; Department Exhibit 16, 2000 cost report page 29, audit workpaper c-3-30 line 69.) This gain was not offset against interest expenses when the 2002 rate was computed. (Transcript, page 47.)

Upon investigation, OMIG auditors determined that the gain resulted from the sale of securities invested with Merrill Lynch and U.S. Trust. (Transcript, pages 50-53; Department Exhibit 16, audit workpaper h-1-1.15.) These assets on which the gain was realized were identified on the Appellant’s financial statements as “board designated funds.” (Department Exhibit 16, 2000 financial statement, audit workpaper c-4-4.)

The Appellant’s own financial statements for the year ending December 31, 2000, and its tax filings for the year 2000, reported the board designated funds as unrestricted. (Transcript, pages 53-57; Department Exhibit 16, audit workpapers c-4-6, c-5-1 line 8d & 21, c-5-3 line 67.) The OMIG concluded that the \$317,283 gain reported in 2000 constituted unrestricted investment income within the meaning of 86-2.20(c), and that it was required to be offset against interest expense.

Mr. Vislocky explained how the OMIG’s determination for the 2000 cost year was reflected in the audit disallowance for the 2002 rate year. (Transcript, pages 57-61; Department Exhibit 16, audit workpapers h-1-1.8, h-1-1.4.) The audit adjustments for 2001 through 2005 cost reports and 2003 through 2007 rate years were identified in the

same manner and for the same reasons upon analysis of the rate sheets with their underlying and supporting documentation. (Department Exhibit 16; Transcript, pages 63-65.)

For Medicaid reimbursement purposes, “Nonrestricted funds” are defined as follows:

Unrestricted funds. Funds which are not restricted to a specific use by the donor. Examples of unrestricted funds include operating and board-designated funds. 10 NYCRR 451.194.

Pursuant to Residential Health Care Facility (RHCF) fund accounting rules:

(1) Unrestricted fund. (i) The Unrestricted Fund is used to account for funds derived from the day-to-day activities of the residential health care facility and unrestricted contributions. Funds which originate from unrestricted gifts or previously accumulated income may be designated by the governing board for special uses. If the governing board designates funds in this manner, it should be recognized that the board also has the authority to rescind its action. For this reason, such funds should be accounted for in the Unrestricted Fund as “board-designated funds”. A separate structure of accounts in the Unrestricted Fund has been provided for these assets.

(ii) The term *restricted* should not be used in connection with board or other internal appropriations or designations of funds. 10 NYCRR 452.3(c).

Mr. Elliot readily acknowledged that in this case the board designated funds were available to DMH. (Transcript, page 159.) The only real restriction was, as Mr. Elliot put it, “that it was money that they had gotten from donations, and it was not readily available to use for operations... Unless I requested it.” (Transcript, page 212.) Upon receiving a request, however, the board could and regularly did make the board designated funds available for DMH operations. The “restriction” was a “board restriction” which, as Department regulations explicitly point out, is no restriction at all. As the Appellant’s own hearing counsel explained, “a board restricted fund is really unrestricted because what the board of directors can restrict, they can unrestrict.”

(Transcript, page 18.) The Appellant's own outside auditor, Mr. Granger, also testified that under the applicable financial accounting standards the funds were unrestricted.

(Transcript, pages 319-20.)

The Appellant maintains that the board designated funds were restricted by the donors. All of its evidence, however, confirms the OMIG's determination that the funds were board, not donor restricted, and that they were not only available but in fact were actually used to operate DMH.

The Appellant claims that the board designated funds "were given exclusively by individual Masons affiliated with the Masonic Lodges that formed the membership of the German Masonic Home Corporation. (Tr. 257 and 261.)" (Appellant brief, page 1.) Mr. Katz conceded, however (in the very transcript pages the Appellant cites as the basis for its claim), that this claim is entirely speculative, based upon the supposition that if a bequest was made it probably came from a member. (Transcript, pages 257, 261.)

The Appellant's proof of the alleged source of the contributions consists of 17 bequests documented in its records, showing a total of \$33,500 in specific bequests and eight residual bequests of varying portions of estates that show no indications of being anything but modest in size. (Appellant Exhibit K.) None of the donors is actually identified as a member of a GMHC lodge. The Appellant did not offer any figure concerning what, if anything, it actually received as a result of these bequests, or when. This hardly explains the source of the millions of dollars in the board designated funds.

In any event, the Appellant's claims about the source of the funds, even if true, are not dispositive of the issue in this hearing. The pertinent issue is not the source of the funds, but whether they came with any donor restrictions.

The Appellant's own general counsel, Mr. Katz, conceded that even such evidence as the Appellant has brought forward (Appellant Exhibit K) fails to show an intention on the part of any GMHC donor to restrict a bequest in a manner that would prohibit its use for the support of DMH or for any other GMHC purpose:

In the Wills, itself, I don't believe there was any specific language that would restrict the donation other than being given to the entity for its purposes. (Transcript, page 298.)

Mr. Granger, the Appellant's outside auditor, confirmed that the Appellant tried but failed to find any evidence of donor restrictions. He testified:

Q. Did you have any conversations with Mr. Richard Katz, the corporate attorney for the German Masonic Home Corporation, relating to the restricted or unrestricted nature of this fund during the time that you were auditing?

A. Yes, we did.

Q. What was the nature of those discussions?

A. We inquired as to whether he could tell us whether there were, in fact, donor restrictions or documentation available regarding donor restrictions on the funds.

Q. Was there donor restrictions?

A. He did not come up with that, no. (Transcript, page 322.)

The Appellant's own general counsel and outside auditor both having conceded that the evidence brought forward does not support its claim that any contributions came with donor restrictions, the Appellant goes on to argue:

Given the historic nature of the fund and the manner in which all members were given the bylaws for the order which contained language restricting the uses of donated funds to those specified for the "capital account," it is perfectly reasonable to infer that these donations were intended to be in accordance with those bylaws and were therefore donor restricted by operation of law. (Appellant brief, page 12.)

As has already been noted, the Appellant has submitted no evidence that any donation to this fund actually came from a member. Even if one ignores this point of fact, as the Appellant does, the statement still comes perilously close to an absurd argument that even funds derived from unrestricted contributions to the GMHC are restricted funds for the purposes of 10 NYCRR 86-2.20(c) “by operation of law” simply because the contributions were made to an organization that had stated purposes.

The Appellant is apparently also making a somewhat less startling but considerably more muddled argument that the contributions are donor restricted “by operation of law” because of the “historical context and surrounding circumstances.” (Appellant brief, page 11.) The Appellant seems to be suggesting that contributors could reasonably believe that the uses specified for the “capital account” did not include at least some aspect of GMHC operations, and so are restricted in at least some way, and that is good enough to qualify the funds as donor restricted for the purposes of 86-2.20(c).

The Appellant relies on the following section of its 1963 GMHC Charter and Bylaws describing the “Capital Account,” which is where the board designated funds were kept (Appellant brief, page 5 par.16):

The Capital Account shall consist of donations and bequests, also accrued interest from invested funds, net income from real estate property and all other income which the Board of Directors shall designate for this account. In the event of the insufficiency of income from other sources, the capital and income of this fund may be used for the upkeep of the Home and Temple, as well as for the maintenance of the Guests at the Home. (OMIG Exhibit 12, 1963 Charter and Bylaws ¶8:02.)

The Appellant’s claim that this bylaw sets forth “language restricting the uses of donated funds” is a distortion of the plain language of the bylaw. A provision that “[i]n the event of the insufficiency of income from other sources” the capital fund “may be used for the

upkeep of the Home and Temple, as well as for the maintenance of the Guests at the Home” simply does not thereby restrict its use in any other way.

In any event, the supposition that every GMHC donor read or was familiar with details in the bylaws regarding the capital account, and so understood and specifically intended that his or her donation would go into a fund whose use would be restricted, is as flimsy as the claim that the bylaw in question sets forth a restriction to begin with. It would appear, from the Appellant’s argument, that it is not possible to make an unrestricted donation to GHMC: The bylaws provide that all donations go into the capital fund, which according to the Appellant makes them donor restricted. Perhaps the board could determine otherwise? But that would mean the restriction was a board, not donor restriction. Or perhaps donors can specify otherwise? This would mean that donations are presumed to be donor restricted unless specifically designated otherwise, which turns the entire concept of a restricted donation on its head. Would this, then, also mean that donations by non-members who have not been “given the bylaws for the order” and so have no reason to be aware of the bylaw in question, are also presumed restricted? But it is the Appellant who argues, as the foundation of its position, that donor/member awareness of the bylaws is what creates the restricted status of the fund. So, should one presumptively designate member donations to be restricted but non-member donations unrestricted? But pursuant to the bylaws all donations go together into the same capital account - and the Appellant was unable at this hearing to establish the membership status of even a single donor to that account.

Donor restriction is a fairly simple concept. The donor expresses and makes known, or “designates,” with the donation, some restrictive intent. 10 NYCRR 451.235.

The Appellant's theory that a perfectly straightforward donation made with no expression of any restrictive intent, can be turned into something else by casuistic argument about provisions in the bylaws of the donee, renders the concept unintelligible.

The Appellant does claim authority for its "historical context and surrounding circumstances" theory, but the facts in this case stand in stark contrast to the cited authority. The Appellant claims that in Application of Syracuse University, 3 N.Y.2d 665, 171 N.Y.S. 2d 545 (1958) the New York Court of Appeals "considered the donor's career and affiliation with Syracuse University as a Professor of Medicine in its medical school to find a restriction." (Appellant brief, pages 11-12.) This characterization significantly misrepresents that decision, which states:

Here, however, we have significant language indicating that if this money could not go to Syracuse University for the benefit of its medical college the testator did not intend to make the gift. His associations of long standing with Syracuse University evidently meant as much to him as making donations for the advancement of medicine... The intention of a testator regarding such a matter is to be gleaned first of all from what is expressed in the will [citations omitted]. He could not have made it clearer that unless Syracuse University were in position to use this money... he had no intention to give the money at all... Dr. Heffron had been professor or dean at Syracuse Medical College for a quarter of a century. He made it as clear as words can at the outset in making the gift [what] he wanted... the underlying intention is being sought in the language of the instrument, rather than in some ambiguous extrinsic evidence... The property is not sought to be transferred to the State [*i.e.* not Syracuse] University pursuant to directions contained in the will, but by a provision which the court is asked to engraft upon the will." *Id.* At 670-71.

In Syracuse University, the single donor was known and the explicit language in his bequest was evaluated and found controlling. The court found restrictive intent in the plain language of the bequest, not in the "career and affiliation" of the donor. The court simply noted that the donor's "career and affiliation" supported rather than contradicted the court's reading of and reliance on the express language of his bequest.

In this case, an unknown number of donors are barely even identified, and there are no expressions of intent to evaluate – other than expressions of intent, in Mr. Schuebler’s words “to use [the funds] for the purposes for which our German Masonic Home Corporation was created, which is mainly to help the elderly in a facility, whether it be Tappan or Dumont.” (Transcript, page 238.) As Mr. Katz said, “I don’t believe there was any specific language that would restrict the donation other than being given to the entity for its purposes.” (Transcript, page 298.) To the extent any intent is expressed, then – and that intent is quite clearly expressed precisely as Mr. Katz described it - it is contrary to, not supported by, the Appellant’s “ambiguous extrinsic evidence.”

“Historical context and surrounding circumstances” fail to suggest in any way that the capital account would not or could not be used to support DMH or for any other purpose the board deemed appropriate. The stated purposes of GMHC, and the uses specified for its capital account, always included the operation of a residential facility such as DMH. The Appellant’s own brief states:

GMHC’s historical mission has been to serve the elderly and to support a Masonic Temple. For the period 1982 through 2010 this was done through the operation of a Residential Health Care Facility and through the ownership of the 15th Street Temple. (Appellant brief, pages 16-17.)

The Appellant’s suggestion that “it is perfectly reasonable to infer” that anyone making contributions to GMHC could do so knowing that the use of such the income from such funds to support a nursing home such as DMH would be prohibited is completely unpersuasive in light of GMHC’s consistently and clearly stated mission.

The Appellant argues that the GMHC “always treated the fund as restricted and separate apart from the operating account for the Dumont Home.” (Appellant brief, page 12.) This internal recordkeeping practice does not establish anything about the uses to

which the fund could be put. The GMHC board indisputably did use board designated funds for the support of DMH. The Appellant does not suggest it was improper or beyond the board's authority to do so. To the contrary, the Appellant's own brief states: "The investment fund was properly utilized during the period from 1996 to 2010 to support the Home and the Temple (Ger-Mas.)" (Appellant brief, page 17.) It is difficult to understand, then, how it is "reasonable to infer" that contributors intended that the use of donations in this manner would be prohibited. The Appellant goes on to argue:

Over \$4.7 million was used to assure that patient care was not jeopardized and a significant amount was saved by the State in the process. To allow for a further invasion of this Capital Account by further offsets to interest expense of the Dumont Home is grossly out of line with the intended uses of the fund in question. (Appellant brief, page 17.)

Just what are the donor restrictions on "the intended uses of the fund" here? That the investment fund may be used to support DMH, but not too much?

The GMHC president, Mr. Schuebler, repeatedly made it clear (as does all the other evidence in this case as well) that the purpose of the board designated funds was co-extensive with the purposes of GHMC, that the operation of DMH was a central purpose of both GMHC and the board designated funds, and that the only restriction on these funds was a board restriction:

Q. Were you ever told that this – what's been described as the board-restricted fund in this hearing was restricted?

A. Yes. We all – myself, as president of the board, it's my opinion that the moneys that were collected by the people and the Masons that came before us, our brothers, those moneys are not at our discretion to spend willy-nilly but to use them for the purposes for which our German Masonic Home Corporation was created, which is mainly to help the elderly in a facility, whether it be Tappan or Dumont.... Whether it be Tappan or Dumont. (Transcript, page 238.)

...

- Q. Mr. Schuebler, what is your understanding of the term “restricted funds,” as you have testified?
- A. They were restricted by the board for the express purpose of helping out the home, both in Tappan and Dumont, when there was a need for additional funds that were not covered by the reimbursement that we received from the State.
- Q. Are you referring to Medicaid, sir, when you say money received from the State?
- A. Yes, Medicaid or Medicare, whatever the case was that we didn’t have enough money to care for the patients in the home.
- Q. And what did — what is your understanding as to the breadth of what the money can be used for with these board-restricted funds, as far as patients?
- A. Well, it includes all of the expenses that we had in the home for people that were working there, for our vendors, payroll, all of that was included in that. Sometimes we fell short. (Transcript, pages 243-44.)

This testimony effectively demolishes any argument that operating the Dumont facility was somehow not an authorized and intended use for the board designated funds.*

Nor has the Appellant identified any other restrictions on the board’s ability to use these funds. The Appellant claims some restriction that “they may only be used for the upkeep of the capital structures owned by the GMHC or the needs of residents.” (Appellant brief, page 11.) The Appellant cites Mr. Schuebler’s testimony that the funds could not be used “[f]or any capital improvement, for anything other than helping run the home, or buying any other property or anything like that.’ (Tr. 242.)” (Appellant brief, page 13.) As an example of the alleged restrictions, Mr. Schuebler pointed out that the funds were not used to buy a ventilator unit. (Transcript, page 245.) The Appellant’s

* There is also some bootstrapping going on here. The funds are only available for “helping out” DMH if Medicaid money is not available. If the fund is restricted, Medicaid money is available. If Medicaid money is available, the fund cannot be used. Therefore the fund is claimed to be restricted and the result is that the Medicaid Program, not the Appellant, bears these costs.

brief characterizes this as testimony that there were “items that the GMHC would have liked to be able to tap into the fund to pay for, such as adding a vent unit to the facility, but chose to borrow money instead because of the fund’s restricted nature.” (Appellant brief, page 13.) This is an attempt to present a board restriction as a donor restriction.

What Mr. Schuebler himself said about the vent unit was:

We used borrowed money, but we could have used some of that for that purpose, or for increasing the care for more people, making a bigger nursing home or assisted living, things like that. That was our charter, to care for the elderly, and it still is. (Transcript, page 246.)

The Appellant’s final version of its “historical context and surrounding circumstances” argument seems to be that because the board designated funds could be used for non-operating as well as operating purposes, they count as “[f]unds designated by the donors... for special nonoperating purposes” and therefore fit within the 10 NYCRR 451.235 definition of restricted funds. (Appellant reply brief, pages 4, 7.) This argument merits little discussion. It is certainly true that the board designated funds could be used for both non-operating and for operating purposes. Indeed, they could be used for whatever purpose the board deemed appropriate. That is precisely what makes them board restricted, not donor restricted funds, and precisely what fits them within the 10 NYCRR 451.194 definition of unrestricted funds.

The Appellant’s own outside auditors concluded, after specifically investigating the matter, that the board designated funds were unrestricted. (Transcript, pages 267-68, 319-20, 322.) The Appellant’s director of finance confirmed that they were available to DMH at the discretion of the GMHC board. (Transcript, page 159.) Their purpose was simply, as Mr. Schuebler said, “to use them for the purposes for which our German Masonic Home Corporation was created.” (Transcript, page 238.) The evidence, in

short, is overwhelming that these were board designated funds in precisely the sense described in 10 NYCRR 452.3(c)(1)(i)&(ii).

In connection with a substantial renovation of DMH in 1996, the Appellant obtained HUD financing. The GMHC charter was revised at the time. The Appellant suggests that this revision is somehow relevant to its explanation of its position on this audit adjustment. According to the Appellant, “[e]ffectively, the case law holds that assets held prior to a change in corporate purposes must continue to be restricted in line with the historical former corporate purposes.” (Appellant brief, page 15.)

This principle, and the charter revision, have little to do with this case. Insofar as the GMHC’s purpose before and after 1995-96 is concerned, it is very clear that there has been no change regarding its operation of a nursing home. “Home,” in the 1963 charter, meant the Home at Tappan. When it petitioned the state supreme court for approval to sell DMH in 2010, the Appellant itself described the purpose of GMHC, including a history in which DMH and its predecessor the Home at Tappan have fulfilled the same ongoing institutional purpose:

The Petitioner [GMHC] has been the owner and operator of various types of facilities for the care of the aged for over 100 years and, in 1982, moved it’s [sic] combined Health Related Facility and Skilled Nursing Facility from its original home in Tappan, New York, to New Rochelle, New York. (Appellant Exhibit L, petition ¶2.)

Regarding the board designated funds at issue herein, the Appellant claims that it was at this same time, in 1996, that the board designated funds, which had previously been listed on GMHC’s financial statements as “restricted” funds, began to be listed as “board designated.” (Transcript, page 176.) The Appellant also argues that these changes are somehow relevant to its explanation of its position on this audit adjustment.

The Appellant's own general counsel, Mr. Katz, and its director of finance, Mr. Elliot, both pointed out that the classification of the board designated funds as unrestricted in 1996 was not imposed by HUD, it was done in accordance with GAAP revised in 1995. Mr. Elliot said that the rules "changed on how board restricted funds could be recorded." Mr. Katz insisted, furthermore, that this change required by GAAP did not, in GMHC's view, in any way change the nature of the funds. (Transcript, pages 177, 268.) They both thereby again confirmed that the only "restriction" either before or after 1996 was a "board restriction" which, as has already been discussed, is no restriction at all for the purposes of this audit adjustment.

There is no more evidence that the board designated funds were donor restricted funds within the meaning of 10 NYCRR 86-2.20(c) before 1996 than after 1996. There is simply no evidence that they ever were in any sense donor restricted funds. The evidence overwhelmingly establishes, to the contrary, that they were always board restricted funds, whose use was subject entirely to the board's discretion.

The Appellant's argument about the 1995 and 1996 charter revisions, and indeed its entire case, is essentially an attempt to exploit the very ambiguity that Department regulations are careful to first explain at 10 NYCRR 452.3(c)(1)(i) and then address at 452.3(c)(1)(ii) by providing "the term *restricted* should not be used in connection with board or other internal appropriations or designations of funds."

This attempt includes a serious misrepresentation of the hearing testimony: In its reply brief, the Appellant asserts "prior to 1995, the fund in question had been reported as 'donor restricted,' at which time the facility's financial statements began categorizing the fund as 'board designated.' (See Elliot testimony, Tr. 176-177.)" (Appellant reply brief,

page 6.) The Appellant repeats this claim twice more in its briefs, citing the same transcript pages both times. (Appellant brief, page 5 par. 20; reply brief, page 2.) Mr. Elliot's testimony at the cited transcript pages, was, in its entirety:

Q. Do you recall reviewing a change in the restricted nature of this fund that occurred in 1995?

A. That I recall, because as we were looking through all the financial statements, I noticed that it went from being listed as restricted to, I believe it was titled, "board designated."

Q. When did that take place?

A. '95, '96.

Q. Did you look into why that had taken place?

A. I really didn't.

Hearing Officer: In 1995 it was designated on the balance sheet as what?
The Witness: Board-designated funds.

Q. This is going back 15 years to 1995, but do you recall whether you reviewed the accounting firms that had been used by the German Masonic Home Corporation?

A. As I was making copies, I believe there was two or three different accounting firms. At that particular time –

Q. From your recollection.

A. -- as far as – it changed, I believe in '95 or '96, I think there was a FASB rule that changed on how board restricted funds could be recorded. (Transcript, pages 176-77.)

Mr. Elliot never said "donor restricted." To the contrary, he explicitly stated that by "restricted" he meant "board restricted."

The Appellant argues the irrelevant point that in connection with financing that it provided in 1996, HUD imposed certain restrictions on expenditures from the board designated funds for such purposes as purchasing additional real estate. (Appellant brief,

page 13.) Conditions that a lender may have attached to financing are irrelevant to the issue in this case because none of these so-called restrictions on the Appellant's use of the board designated funds has anything to do with a donor restriction.

The Appellant alleges that HUD issued its approval for the 1996 financing without considering the board designated funds as available "project funds" that had to be used to reduce the amount of financing required. (Transcript, pages 327-28.) Even if that characterization is accurate, it is not relevant to this audit adjustment. There is no good reason why HUD methodology for determining how much financing it would approve for this facility should control the issue in this audit adjustment, which concerns how the Appellant's interest income should be treated for Medicaid reimbursement purposes.[†]

The Appellant suggests that it did not really use the board designated funds to support DMH. It claims GMHC granted them "as a loan or advance" to DMH for operating costs. (Appellant brief, pages 6-7.) According to the Appellant, the board designated funds DMH received were recorded as a liability "due to Dumont Home" and an asset to GMHC. (Transcript, pages 168-71, 265-66; Appellant Exhibit E.) The Appellant has not presented any persuasive evidence of a bona fide loan between GMHC and DMH. There is no evidence that any interest was charged on this alleged loan or what any of its other terms were. It is further noted that DMH appears to have "paid

[†] Different rules, policies and considerations can apply in different contexts for different purposes. For example, as the Appellant itself pointed out in a letter it sent to the OMIG during the course of this audit, building funds accumulated through contributions, whether restricted or unrestricted, are not to be considered in the evaluation of amounts necessary to be refinanced pursuant to the refinancing initiative set forth in PHL 2808.20 – and that is true simply because that statute specifically says so. (OMIG Exhibit 8, page 4 thereof.) It does not follow that any building fund that has been so disregarded in a refinancing calculation is then no longer a building fund.

back” only a small fraction, less than ten percent, of the funds transferred from the board designated fund. (Appellant Exhibit I.)[‡]

In any event, the Appellant’s internal records “basically couching that advance as a loan,” as Mr. Katz expressed it (Transcript, page 265), that “they were supposed to” pay back, as Mr. Elliot put it (Transcript, page 169) are of little relevance to this audit disallowance. The issue is whether the board designated funds were donor restricted. The board’s discretion in the use of the funds was clearly not subject to any donor restrictions regardless of how its internal appropriations of them were carried on the GMHC books.

The Appellant acknowledges that it preferred not to use the board designated funds to support DMH more than it had to, because lodge members might not like it. (Transcript, pages 195, 209.) GMHC’s concern for the views of its membership about how its resources should be used is certainly appropriate. It is apparently that very concern that contributed to GMHC’s eventual decision to sell DMH in 2010 and petition a court to change its charter to, for the first time, eliminate the purpose of “providing direct care for the elderly” in a residential facility. (Appellant Exhibit L, petition #30, 31; Transcript, pages 279, 291-92.) This was an understandable and legitimate response to

[‡] Borrowing from restricted funds is permitted and interest on such loans can be an allowable expense under the Medicaid Program. 10 NYCRR 86-2.20(c)(1). To support the existence of a loan, there should be a signed loan contract or correspondence stating the pertinent terms of the loan such as amount, rate of interest, method of payment, due date, etc. Authorization by the board should also be on file. PRM-I 202.1.

The Appellant has brought forward no evidence that the alleged “loan or advance” of board designated funds to DMH was documented in this manner. Of course, the Appellant was not obligated to comply with these documentation requirements if it did not report interest expenses on loans from restricted funds to the Medicaid Program or seek reimbursement for them.

The Appellant’s claim in this hearing that it did borrow restricted funds in this manner, however, gives rise to the question why, if the board designated funds truly were donor restricted funds, the Appellant did not borrow from them, document that borrowing appropriately, and seek Medicaid reimbursement for interest on the loan. This brings us, however, to property disallowance 2.

the membership's alleged concerns. Seeking to pass on inappropriate costs to the Medicaid Program is not.

The Appellant also argued, as an alternative, that if the board designated funds are unrestricted there should at least be some sort of "allocation" reducing the amount of income from the funds that is applied against interest expense. The Appellant failed to show what sort of "allocation" is appropriate in this case and why, and failed to identify any authority for any such "allocation" of investment income. The Appellant does cite 10 NYCRR 451.249, which is a definition of "stepdown method," and 456.1, which defines and describes "cost finding." (Appellant brief, page 19.) It failed, however, to explain or offer any authority for its apparent suggestion that these concepts have something to do with the application of 10 NYCRR 86-2.20(c)(1) in this case.

The Appellant suggested that various allocation methods could be devised (Transcript, pages 329, 350), but did not actually identify a method that it claims should be required. The Appellant's first allocation suggestion is that none of the gain on the board designated funds should be applied against DMH interest expense. The grounds for this suggested method of allocation are that HUD did not consider the board designated funds to be "project funds" in connection with the 1996 refinancing of DMH. (Appellant brief, page 20.) The irrelevance of the HUD refinancing to the Medicaid reimbursement issue in this case has already been discussed.

The second allocation example offered by the Appellant seems to be that since DMH had a low net asset value (because it carried a large mortgage) relative to other GMHC assets, a proportionally small allocation of the gain on the board restricted funds should be applied against DMH interest expenses. (Appellant brief, pages 21-22; reply

brief, page 10.) At the hearing Mr. Granger offered an account of such an allocation based upon admittedly erroneous figures. (Transcript, pages 343-349.) The reasoning offered for this method makes no more sense than Mr. Granger's figures.

Mr. Granger testified that "we felt this was the best way to allocate based on the facts and the circumstances." (Transcript, pages 350-51.) Mr. Granger was twice invited to explain "the facts and the circumstances," and his answers, in their entirety, were:

Q. Why did you pick this particular method that you outlined in your testimony?

A. The offset for the audit was based on the fact that there was mortgage interest on the Dumont building and equipment, and that they wanted to offset the income against that mortgage interest. So just having a mortgage interest, we didn't feel that was a good factor in allocation by itself. (Transcript, page 341.)

...

A. As I said, it depends how you want to do it. We felt that the best way would be based on the fact that the mortgage was the basis for putting the interest or offsetting the interest income against the mortgage interest, realizing the mortgage and related assets would be the proper allocation. Again, it is not the only method, but that is what we felt was the proper method. (Transcript, page 350.)

The Appellant's brief did not attempt to elucidate or to provide some other or more intelligible version of these statements. It simply asserted, with a similar opacity, that "this allocation methodology attempted to follow the purposes and intent of the Capital Account but without the limitation as to HUD restrictions." (Appellant brief, page 21.)

The Appellant cites Kaiser Foundation Hospitals v. Aetna Life, PRRB Hearing Dec. No. 89-D16, Feb. 6, 1989 (CCH Medicare and Medicaid Guide, ¶37,655) on the subject of allocation. (Appellant brief, page 18.) That decision, which held that "investment income must be associated with the parties benefiting from the investment,"

fails to suggest any persuasive reason why the amount of the OMIG's audit disallowance should be reduced to reflect any sort of "allocation" in this case.

Property expense disallowance 1 is affirmed.

Property expense disallowance 2. Working capital interest disallowance.

The Medicaid Program pays for costs properly chargeable to necessary patient care. Allowable costs shall not, however, include expenses which are determined not to be reasonably related to the efficient production of service because of either the nature or amount of the particular item. 10 NYCRR 86-2.17(a)&(d).

This audit adjustment disallowed expenses the Appellant reported on its 2000 through 2005 cost reports for interest on working capital loans. Interest on current and capital indebtedness can be an allowable cost provided the debt generating interest is reasonable, necessary, and incurred to satisfy a financial need. 10 NYCRR 86-2.20(a)&(b). The Medicaid Program will not, however, reimburse a provider for the cost of unnecessary borrowing.

As Mr. Vislocky explained:

When we look at the working capital loan and the interest on it, our main concern is whether the loan was necessary, whether the occurrence of interest was necessary, if this was really a financial need for the facility to borrow money. (Transcript, page 68.)

So in order for us to determine whether the working capital interest is necessary or not, we take a look at the facility's financial position. (Transcript, page 73.)

The OMIG auditors reviewed the Appellant's financial position and determined that at the time it was taking working capital loans the Appellant had ample unrestricted funds on hand to meet those working capital needs without incurring interest expenses that it passed on to the Medicaid Program. (Transcript, pages 78-79.)

As he did with audit adjustment 1, Mr. Vislocky explained the details of the audit disallowance taken for the 2000 cost year. The Appellant borrowed \$500,000 from Merrill Lynch in 2000 to cover a “cash flow shortage,” and incurred an interest expense on this loan in the amount of \$29,719 which it reported to the Medicaid Program as a reimbursable cost. (Department Exhibit 17, 2000 cost report page 7; Transcript, pages 69-70.) The Appellant’s financial statements, however, showed that it had at the time close to \$9 million available to it in the form of \$981,878 cash on hand, \$345,019 due from a loan made to an affiliate, and \$7,490,227 in “board designated funds” that the board, as has already been discussed, had the authority to use. (Transcript, pages 74-76, 127; Department Exhibit 17, audit workpaper c-4-4.) As Mr. Vislocky put it: “being that there is close to \$9 million available to use, we didn’t think the \$500,000 working capital loan was necessary.” (Transcript, page 84.)

The Appellant’s working capital borrowing in the other years under review in this audit was also disallowed because the OMIG’s analysis led to the same conclusions for the same reasons. (Transcript, pages 81-82.)

The Appellant did not dispute the OMIG’s determination that it had \$981,878 in cash on hand. Regarding the \$345,019 loaned to an affiliate, a transfer of funds from one related entity to another cannot serve to create a bona fide need to borrow on behalf of the entity providing the funds. Garden City Osteopathic Hospital v. Blue Cross and Blue Shield, PRRB Hearing Dec. no. 93-D88, Sept. 10, 1993 (CCH Medicare & Medicaid Guide ¶41,721.) The OMIG properly determined that any borrowing necessitated by the Appellant’s transfer of funds to an affiliate would be unnecessary borrowing, the cost of which is not reimbursable under the Medicaid Program. 10 NYCRR 86-2.17(a); 86-

2.20(a). As Mr. Vislocky said, “if the facility truly has a cash flow shortage, why did they have money to lend to an affiliate?” (Transcript, page 75.)

The Appellant failed to establish there was any error in the OMIG findings that it had over \$1.3 million attributable to these two sources alone, available to use for working capital purposes, when it borrowed \$500 thousand instead. The Appellant did claim, however that “without consideration of the investment fund, the borrowing for working capital would have passed the tests of necessity.” (Appellant brief, page 23.) Mr. Vislocky conceded that in this case the OMIG considered “anything in the 2 to \$3 million range is appropriate” to have on hand and still be justified in short term capital borrowing. (Transcript, pages 82-83.) This audit adjustment, then, turns on the OMIG determination that the board designated funds in excess of \$7 million were also available as an alternative to working capital loans.

The Appellant’s objection to the OMIG’s determination that the board designated funds were available to meet a “cash flow shortage” relies on the same arguments advanced in response to property disallowance 1, “investment income offset.” It claims that the “board designated funds” were restricted funds and so not available to address the cash flow shortage. The evidence, however, shows not only that the board designated funds were available, it shows that they were regularly used to address cash flow needs.

Mr. Schuebler, the GMHC president, testified:

A, If we, for some reason, needed funds to support the home in Dumont, the operation, then we had to have a vote of the Board of Trustees, we got the information from our controller who told us how much we needed, and we voted at a meeting of the Board of Trustees whether we will give those funds to the home or whether we are going to keep them restricted.

Most of the time we voted to give the funds for the operation of the Dumont Home.

Q. Was there any occasions where the fund was needed with regard to other matters relating to the [GMHC]?

A. No. It was not used for anything else but to support the home...

Q. "The home," meaning whether it was Tappan or Dumont?

A. Right, but in my case, it was always Dumont. (Transcript, pages 239-40.)

...

Q. And what did -- what is your understanding as to the breadth of what the money can be used for with these board-restricted funds, as far as patients?

A. Well, it includes all of the expenses that we had in the home for people that were working there, for our vendors, payroll, all of that was included in that. Sometimes we fell short. (Transcript, pages 243-44.)

Mr. Elliot, director of finance for DMH, also testified that the GMHC board designated funds were available to meet cash flow needs. He occasionally asked the board to draw down funds to meet costs such as payroll, and they had the ability to do so and did. (Transcript, page 159.)

Mr. Elliot said the board did not like to use the board designated funds in this manner because members might object if they felt their contributions to GMHC were just being used to support DMH. (Transcript, page 195.) Asked "Why would you borrow funds if you have over \$5 million?" Mr. Elliot testified:

Because, again, the board would have rather take a line of credit out so as not to have to use the board-designated funds. They would rather have had the loan, then Dumont would have been responsible to pay the loan back, rather than reduce the investment account, and then have to explain to the lodge members why the investments are down. (Transcript, page 209.)

While the Appellant was entitled to use its discretion in light of such concerns and obtain a loan instead of using available funds to pay DMH operating expenses, it cannot oblige the Medicaid Program to bear the cost of this decision. Northwest Hospital, Inc. v.

Hospital Service Corp., 500 F. Supp. 1294 (N.D. Ill. 1980.) The GMHC board clearly had the authority to use the funds for DMH operating costs – and the responsibility to do so “[i]n the event of the insufficiency of income from other sources.” (OMIG Exhibit 12, 1963 Charter and Bylaws ¶8:02.) Its preference for borrowing instead does not oblige the Medicaid Program to pay the cost of that borrowing. The ultimate resolution of this concern, of course, occurred in 2010 when the GMHC sold DMH, terminated its history of providing residential care for the elderly, and turned to other activities in furtherance of its mission. (Appellant Exhibit L, par. 13, 31.)

Property expense disallowance 2 is affirmed.

Property expense disallowance 7. Disallowance of telephone equipment expense.

The Appellant offered neither evidence nor argument to meet its burden of proving that the OMIG’s disallowance of telephone equipment as a property cost was incorrect. 18 NYCRR 519.18(d)(1).

Property expense disallowance 7 is affirmed.

DECISION: Property expense disallowance 1 is affirmed.
Property expense disallowance 2 is affirmed.
Property expense disallowance 7 is affirmed.

This decision is made by John Harris Terepka, Bureau of Adjudication, who has been designated to make such decisions.

DATED: Rochester, New York
July 14, 2011

_____/s/_____
John Harris Terepka
Bureau of Adjudication