

Jurisdiction and Relevant Statutes and Regulations

The New York State Department of Health (Department) acts as the single state agency to supervise the administration of the Medicaid Program in New York State. Public Health Law (PHL) §201(1)(v); Social Services Law (SSL) §363-a. The New York State Office of the Medicaid Inspector General (OMIG), an independent office within the Department, is responsible for the Department's duties with respect to the recovery of improperly expended Medicaid funds. PHL §§30, 31, 32.

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. Title 10 of the New York Code, Rules and Regulations (NYCRR) 86-2.17. 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 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 the rates can be retroactively adjusted. SSL §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, whether paid as a result of inaccurate or improper cost reporting, improper claiming, unacceptable practices, fraud, abuse or mistake. 18 NYCRR 518.1(c).

The Department determined to recover Medicaid Program overpayments from Riverhead Care Center (Appellant). Appellant requested an appeal pursuant to SSL §22 and 18 NYCRR 519.4 to review the overpayment determination, and a hearing was held. A transcript (T) of the hearing was made, witnesses testified, and exhibits (Ex) were admitted into evidence as OMIG's 1-15 and Appellant's A and B.

Regulations of the former Department of Social Services (DSS) pertinent to this hearing are found at 18 NYCRR parts 517, 518 and 519; they 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). Appellant has the burden of showing by substantial evidence that the determination of the Department was incorrect and that the costs claimed were allowable. 18 NYCRR 519.18(d) and (h).

Findings of Fact

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 Riverhead Care Center, located in Riverhead, New York, was a privately-owned 181-bed RHCF licensed under PHL article 28 and enrolled as a provider in the Medicaid Program. [Ex 8; T 50, 131-132]
2. The daily rates upon which facilities such as Appellant are reimbursed by the Medicaid Program are calculated based on annual cost reports submitted to DOH by the facility. DOH's Bureau of Long Term Care Reimbursement (BLTCR) calculates and sets the rates. [Ex 14; T 50-51, 82-83]

3. OMIG auditors reviewed Appellant's reimbursement from the Medicaid Program for the rate period January 1, 2005 through December 31, 2008. On December 10, 2013, OMIG issued a final audit report. OMIG's letter accompanying the audit report advised Appellant that it intended to recover Medicaid Program overpayments in the amount of \$175,550 based on the disallowances identified in the report. [Ex 4; T 56]

4. By letter dated January 22, 2014, Appellant requested an administrative hearing to challenge OMIG's determination. The disallowance for property item number 2, Interest Expense, for the years 2005 and 2006 was the only issue remaining for this hearing, as all other issues raised in the audit report were settled by the parties. The basis stated in the final audit report for this disallowance was "excessive equity withdrawals necessitated the borrowing of funds to finance leasehold improvements. Consequently, interest associated with the unnecessary borrowing was disallowed as it was not necessary to satisfy a financial need or properly chargeable to patient care." [Ex 4; Ex 5; T 4-5, 42, 70, 80-81]

5. Pursuant to 10 NYCRR 86-2.10(g), capital costs, which include property costs, are reimbursed on a two-year "lag." Appellant was therefore reimbursed in its 2005 and 2006 Medicaid rates for its reported capital costs for 2003 and 2004. Those reported capital costs included interest on a loan for property improvements in the amount of \$13,120 for 2003 and \$46,155 for 2004. [Ex 8; T 53-54, 90-91]

6. In the years 2000 to 2003, the owners of Riverhead Care Center, Inc. (Riverhead) made equity withdrawals of \$4.57 million: \$1,450,000 in 2000, \$1,350,000 in 2001, \$1,270,000 in 2002, and \$500,000 in 2003. In 2003, the equity remaining in the business was approximately \$2.2 million. [Ex 15; T 94-97, 99-100]

7. In 2003, Appellant sought approval from DOH for a renovation project for this RHCF. On March 10, 2003, DOH's Bureau of Architectural & Engineering Facility Planning [Ex A, attachment 1] granted Appellant approval to commence construction. On July 15, 2004, DOH's Division of Health Care Financing [Ex A, attachment 2] approved the amount of \$1,201,935 as "the maximum cost allowable for reimbursement in accordance with [PHL], Part 710.6..." and this letter also informed Appellant that "the submitted costs are subject to audit and the approved portions thereof are subject to audit adjustment." [Ex A, attachments 1 and 2; T 98]

8. Appellant borrowed \$1.3 million at an interest rate of 4.25% for five years to pay for the renovation. [T 86]

9. OMIG's grounds that "excessive equity withdrawals necessitated the borrowing of funds" refers to the \$4.57 million equity withdrawals from 2000 to 2003. [T 94]

ISSUE

Has Appellant established that OMIG's audit report property expense disallowance 2 was not correct?

DISCUSSION

OMIG presented the audit file and summarized the case at hearing. OMIG presented Exhibits 1-15 and one witness, Keith Amato, an OMIG Principal Medical Facilities Auditor. [REDACTED], C.P.A., Appellant's accountant for twenty-five years, represented Appellant, presented Exhibits A (with eight attachments) and B, and testified in Appellant's behalf. OMIG and Appellant each submitted a post-hearing brief, and OMIG submitted a response to Appellant's post-hearing brief.

In the subject audit, OMIG disallowed Medicaid reimbursement in 2005 and 2006 for interest on Appellant's property improvement loan on the grounds that this interest expense was not necessary to satisfy a financial need or properly chargeable to patient care because excessive equity withdrawals by Riverhead's owners necessitated the borrowing of funds. OMIG contends that the disallowance is consistent with the regulations' requirements, and cites a July 14, 2011 Decision after Hearing by ALJ John H. Terepka, in Matter of Dumont Masonic Home, Audit #04-W04-3221, as administrative hearing precedent in support of its position. Appellant must prove that OMIG's disallowance for the interest on this loan was not correct.

Appellant's contention is that DOH approved not only the project (an interior renovation of this 1967-built facility) but also the cost and the financing of the project, and in so doing was allowing reimbursement for the interest associated with such financing. Appellant inaccurately claims, on page 2 of its closing brief, that "[b]y letter, dated March 10, 2003, the D.O.H. approved financing of the project ..." That letter [Ex A, attachment 1], from DOH's Bureau of Architectural & Engineering Facility Planning, approved construction, not financing, of the project. The DOH Division of Health Care Financing's July 15, 2004 letter, which notified Appellant of its approval of \$1,201,935 as "the maximum cost allowable for reimbursement in accordance with [PHL], Part 710.6..." addressed the cost allowable for reimbursement; that letter also apprised Appellant that "the submitted costs are subject to audit and the approved portions thereof are subject to audit adjustment" [Ex A, attachment 2]¹. The interest expense incurred by Appellant, in addition to the "maximum cost allowable for reimbursement," was audited

¹ Neither the March 10, 2003 letter nor the July 15, 2004 letter was from the DOH rate setters, BLTCR.

by OMIG in the subject audit and found to be not necessary to satisfy a financial need and not properly chargeable to patient care, as required by the regulations.

OMIG's auditors' review of Appellant's financial records for the 3-4 years prior to the loan revealed \$4.57 million of equity withdrawals in that period, and the auditors determined that there would have been no need for a loan had those withdrawals not occurred. The basis for the withdrawals, unknown to OMIG's auditors², did not factor into the disallowance determination. Making the withdrawals for its stated purpose (to pay personal income taxes) or for other purposes and then obtaining a loan to finance a patient care-related renovation project might make good financial and accounting sense for the owners and the business, but should the Medicaid Program pay those costs? I find that it should not.

Appellant had \$2.25 million positive equity in 2003. Had the \$4.57 million equity withdrawals not occurred from 2000-2003, the positive equity in 2003 would have been more than \$6.75 million. Mr. Amato's testimony at pages 117 and 118 that

the [\$4.5 million] withdrawal caused[d] the need [for the loan]... if the facility had the money and the funds ... there's no need for the loan

is consistent with the comments hand-written by DOH in the "Interest on Leasehold Improvements" section on Appellant's November 15, 2006 letter to BLTCR. The hand-written comments which relate to BLTCR's denial of the 2005 and 2006 interest costs for setting the 2007 and 2008 rates read,

Deny as expressed in (2). The Facility has taken equity withdrawals of \$4,500,000 in the years 2000-2003. Why finance the leasehold imp[rovement]?

² *The basis for the withdrawals (for the owner(s) to pay personal income taxes) was learned at the hearing [T 96, 138-139]*

[Ex 12; Ex A, attachment 5; T 104, 109-112; 117-118]

Finally, Appellant cites PHL §2808(5)(c), which was not in effect during the years under audit in this audit report (2003-2008). §2808(5)(c), which reads, in relevant part:

... on and after April first, two thousand ten, no non-public residential health care facility ... may withdraw equity or transfer assets which in the aggregate exceed three percent of such facility's total reported annual revenue for patient care services, based on the facility's most recently available reported data, without the prior written approval of the commissioner. ... In reviewing such requests the commissioner shall consider the facility's overall financial condition, any indications of financial distress ... and such other factors as the commissioner deems appropriate...

is irrelevant to this decision. OMIG's disallowance for the interest claimed on the loan used for the leasehold improvements was not based on the legality or appropriateness of the equity withdrawals or whether the Facility had positive or negative net worth.

The \$4.57 million withdrawals from 2000-2003, which left \$2.5 million net worth in 2003, put Appellant in a position to make business and accounting decisions to finance the project rather than have the full \$6.75 million on hand for the project. Obtaining a loan, at Medicaid expense, to finance a patient care-related renovation project might make good financial and accounting sense for the owners and the business, but the Medicaid Program should not pay those costs as it will not reimburse a provider for the cost of unnecessary borrowing. This conclusion is consistent with the intent and purpose of the reimbursement regulations and with the findings in Dumont, *supra*.

Appellant failed to establish that OMIG's audit report property expense disallowance 2 was not correct. Property expense disallowance 2 is affirmed.

DECISION

OMIG's property expense disallowance 2 is **affirmed**. This decision is made by Ann H. Gayle, Bureau of Adjudication, who has been designated to make such decisions.

DATED: New York, New York
March 15, 2016

Ann H. Gayle
Administrative Law Judge

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