PROVIDER REIMBURSEMENT REVIEW BOARD
HEARING DECISION

ON-THE-RECORD
2000-D16

PROVIDER -
California Health Professionals, Inc.
Chico, California

Provider No. 05-7299

vs.

INTERMEDIARY -
Blue Cross and Blue Shield Association/
Wellmark Blue Cross and Blue Shield

DATE OF HEARING-
November 8, 1999

Cost Reporting Period Ended -
December 31, 1994

CASE NO. 97-0080

INDEX

ISSUES:

1. Was the Intermediary's adjustment to reclassify supplies' salaries to the administrative and general cost center proper?

2. Was the Intermediary's adjustment to disallow costs paid to a related organization proper?

3. Was the Intermediary's adjustment to allocate cost shared with the related company using the pooled cost method proper?

STATEMENT OF THE CASE AND PROCEDURAL HISTORY:

California Health Professionals ("Provider") located in Chico, California is a free-standing home health facility. The Provider was certified for Medicare participation in August 1992 and performs approximately 44,000 visits per year.

By letter dated July 31, 1996, Wellmark Blue Cross and Blue Shield ("Intermediary") issued a Notice of Program Reimbursement ("NPR") which resulted in the disallowance/reclassification of costs relative to those issues referenced above.[1] On October 21, 1996, the Provider filed a timely appeal with the Provider Reimbursement Review Board ("Board") which met the jurisdictional requirements of 42 C.F.R. §§ 405.1835.-1841.[2] The total reimbursement effect of the amounts in controversy is approximately $ 107,000.

The Provider is represented by Mr. John P. Ruocco, Consultant. The Intermediary is represented by Bernard M. Talbert, Esquire, of the Blue Cross and Blue Shield Association.

Issue No. 1. - Reclassification of Supplies' Salaries to the Administrative and General ("A&G") Cost Center

Facts:

The Provider employed three individuals whose responsibilities included the maintenance of billable medical supplies. On its Medicare cost report, the Provider included the entire salary paid to one individual, and 50% of the salaries paid to the other two individuals, as a direct cost of billable medical supplies. The Intermediary reclassified the salaries in question to the A&G cost center because the Provider did not maintain detailed records of the activities performed by these employees.

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1 See Provider's Request for PRRB Appeal.

2 Id.

PROVIDERS'S CONTENTIONS:

The Provider contends that the position descriptions for the individuals in question fully support their responsibilities for medical supplies, both billable and non-billable.[3] In addition, the Provider asserts that records were kept which reflected the total time related to medical supplies, and the individuals in question had no responsibilities for other types of supplies i.e. office supplies. As such, the Provider believes the only issue in dispute is whether continuous time records should have been kept to differentiate the time spent between billable and non-billable medical supplies; which would allow a ratable portion of compensation to be assigned to the billable medical supply cost center.

The Provider also disagrees with the Intermediary's reliance on two sections of the Medicare manuals as a basis for its adjustment. The first, HCFA Pub. 15-1 § 2115[4] states that:

> [A]ll HHAs are expected to separately identify in their records the cost of medical supplies that are not routinely furnished in conjunction with patient care visits and which are directly identifiable services to an individual patient.

The second section, HCFA Pub. 15-2 § 3206[5], which discusses the creation of a cost center for Medical Supplies at line 12 of the cost report states in part that:

> [L]ine 12- The cost of medical supplies reported in this cost center are those costs which are directly identifiable non-routine supplies furnished to individual patients and for which a separate charge is made. These supplies are generally specified in a patient's plan of treatment and furnished under the specific direction of the patient's physician. Medical supplies which are not reported on this line are those minor routine medical and surgical supplies which would not be expected to be specifically identified in the plan of treatment for which a separate charge is not made. . . .

Id.

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3 Provider Exhibit P-3.

4 Provider Exhibit P-4.

5 Provider Exhibit P-5.

The Provider contends that nothing in the sections quoted above requires the maintenance of detailed time records to differentiate between a supply clerks' handling of "non-billable" medical supplies versus "billable" medical supplies. The Intermediary reclassification of costs causes costs that are specifically not subject to Medicare per visit cost limitations (billable medical supplies) to be combined with visiting costs for comparison with aggregate cost limits.

The Provider further contends that, alternatively, the cost of medical supplies could be used as an auditable statistical basis for cost assignment on worksheets A-1 (salaries) and A-2 (Fringe benefits) in the Medicare cost report. Such cost assignment would be in keeping with the general instructions for cost assignment on such worksheets as set forth in HCFA Pub. 15-2 § 1704,[6] which states:

> [A]ll salaries and wages for the HHA will be entered on this worksheet for the actual work performed within the specific area or cost center in accordance with the column headings . . . . The records necessary to determine the split in salary between two or more cost centers must be maintained by the HHA and must adequately substantiate the method used to split the salary.

Id.

The Provider contends that its proposal to rationally split the salaries and related costs of its supply staff between billable and non-billable supplies, and its proposed use of "raw supply cost" of each category as the statistic to do so, is in accordance with the instructional concepts noted above. The Provider asserts that the Intermediary's non-acceptance of the "raw supply cost" as a statistic is without merit. Throughout the Medicare program's principles of cost reimbursement the use of the best available statistic is commonplace. Although the efforts of a supply staff may not be directly proportional to the cost of supplies in an absolute sense, the Provider contends the use of the "raw supply cost" as a statistic is far more accurate than the Intermediary's reclassification of everything into the A&G.

INTERMEDIARY'S CONTENTIONS:

The Intermediary contends that the adjustment to include supplies' salaries in the administrative and general cost center was made in accordance with HCFA Pub. 15-1 Sections 2304 (Adequacy of Cost Information), 2115 (Treatment of Medical Supply Costs in HHA), 2221 (Apportionment Of Home Health Agency Medical Supply Costs), and 2307 (Direct Assignment of General Service Cost).

The Provider directly assigned salaries for three employees to the supplies cost center. The Provider submitted 100% of one employee's salary and 50% of the salaries of the remaining two. The

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[6] Provider Exhibit 6

Intermediary has not reviewed the position descriptions for these employees, however, it appears that these employees had job duties related to billable and non-billable supplies, as well as non-supplies related duties. The Intermediary contends that only the cost of billable medical supplies should be included in the supplies cost center as billable supplies are reimbursed based on charges. The cost of routine supplies, including salaries of those handling supplies, must be included in administrative and general and allocated to all cost centers as is specifically stated in the manual references listed below.

HCFA Pub. 15-1 § 2221 states:

> [S]ome types of medical supplies such as thermometers, nursing bags, etc., are purchased by the provider for all patients. The costs of these supplies must be apportioned to all patients.

HCFA Pub. 15-1 § 2115 states:

> [D]o not separately classify the cost of those minor medical and surgical supplies which are not expected to be specifically identified in the physician's plan of treatment, or for which a separate charge is not made. It must be included in the per visit cost. These supplies (e.g., cotton balls, alcohol prep) are items which are frequently furnished to patients or utilized individually in small quantities (even though these items in certain situations may be used in greater quantity). For proper cost report treatment of medical supply costs in HHAs, see PRM-11, Sec. 404.

Id.

The Intermediary notes that no time records were maintained to show the amount of time spent by these employees working on billable, non-billable or non-supplies related tasks.
According to HCFA Pub. 15-1 § 2304:

> [C]ost information as developed by the Provider must be current, accurate and in sufficient detail to support payments made for services rendered to beneficiaries. This includes all ledgers, books, records and original evidences of cost (purchase requisitions, purchase orders, vouchers, requisitions for materials, inventories, labor time cards, payrolls, bases for apportioning costs, etc.), which pertain to the determination of reasonable cost, capable of being audited.

Id.

The Intermediary contends that since no time records were maintained to support the 50% allocation of two of the employees, this percentage appears to be an estimate. The use of such an estimate to directly assign salaries is not allowed. See HCFA Pub. 15-1 § 2307 which states:

> [T]he basis for assigning directly allocable costs of a general service cost center to the benefiting cost centers must be on a factual and auditable basis. This precludes the use of averages, estimates or statistical surrogates such as square feet.

Id.

Further, the Intermediary does not agree with the Provider's position that using the direct cost of billable and non-billable supplies would be a more appropriate method of allocating the salaries of the employees in question. The Intermediary believes this would be inappropriate for two reasons:

1 .Job descriptions for these employees have not been reviewed by the Intermediary. These employees appear to have non-supplies related duties as the Provider originally assigned 50% of two of the employees' salaries to the administrative and general cost center.

2. The cost of supplies does not directly relate to the time spent handling the supplies. More expensive supplies do not necessarily require a greater amount of handling time.

The Intermediary contends that since the Provider does not have time records available to support the actual amount of time spent by employees handling billable and non-billable supplies and other non-supplies related duties, the salaries should be included in the administrative and general cost center and allocated to all cost centers using cost finding.

Issue 2 - Disallowance of Costs Paid to a Related Organization

Facts:

In its as filed cost report, the Provider included the costs paid to the related company, Home Health Care Management (HHCM), for janitorial services, and staff relief services, as allowable costs. The Intermediary adjustment reduced these amounts to the actual cost to the related organization stating that the Provider does not qualify for the related organization exception.

Medicare Statutory and Regulatory Background:

Rules governing related organizations are set forth in HCFA Pub. 15-1 § 1000 (Costs to Related Organizations), and HCFA Pub. 15-1 § 1010 (Exception to the Related Organization Principle)

Section 1000 states:

> [C]osts applicable to services, facilities, and supplies furnished to the provider by organizations related to the provider by common ownership or control are includable in the allowable cost of the provider at the cost to the related organization. However, such cost must not exceed the price of comparable services, facilities or supplies that could be purchased elsewhere. The purpose of this principle is twofold: (1)to avoid the payment of a profit factor to the provider through the related organization (whether related by common ownership or control,) and (2)to avoid payment of artificially inflated costs which may be generated from less than arms-length bargaining.

Section 1010 states:

> [A]n exception is provided to the general rule applicable to related organizations. The exception applies if the provider demonstrates by convincing evidence to the satisfaction of the intermediary that the following criteria have been met:
>
> a. The supplying organization is a bona fide separate organization. This means that the supplier is a separate sole proprietorship, partnership, joint venture, association or corporation and not merely an operating division of the provider organization.
>
> b. A substantial part of the supplying organization's business activity of the type carried on with the provider is transacted with other organizations not related to the provider and the supplier by common ownership or control and there is an open, competitive market for the type of services, facilities, or supplies furnished by the organization. In determining whether the activities are of similar type, it is important to also consider the source of the activity. For example, a full service management contract would not be considered the same type of business activity as a minor data processing contract. The requirement that there be an open, competitive market is merely intended to assure that the item suppled has a readily discernible price

> that is established through arm's length bargaining by well informed buyers and sellers.
>
> c. The services, facilities, or supplies are those which commonly are obtained by institutions such as the provider from other organizations and are not a basic element of patient care ordinarily furnished directly to patients by such institutions. This requirement means that institutions such as the provider typically obtain the items of services, facilities, or supplies from outside sources, rather than producing the item internally.
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> d. The charge to the provider is in line with the charge for such services, facilities, or supplies in the open market and no more than the charge made under comparable circumstances to others by the organization for such services, facilities, or supplies. The phrase "open market" takes the same meaning as "open competitive market" in b. above.

Id.

When all of the conditions of this exception are met, the charges by the supplier to the provider for such services, facilities, or supplies are allowable as costs.

PROVIDER'S CONTENTIONS:

The Provider contends that it and HHCM are separately incorporated entities operating autonomously. They each maintain separate books and records and produce their own financial statements. Both are separate providers under the Medicare program and have separate provider numbers, and are served by different intermediaries. Some individuals are employees of both entities, but their time is separately maintained and they are paid from two different payrolls. The Provider contends that the Intermediary determined (incorrectly) that condition (a), "separate organization," was not met and then failed to evaluate the other exception criteria outlined above.

With regard to janitorial services, HHCM does not offer itself to the general public as such but its involvement with its sister company, the appealing Provider, is only incidental to serving itself. The Provider obtained bids for janitorial service from area suppliers and decided that services from HHCM would be far less expensive. It therefore engaged HHCM for that service, thereby saving the Medicare program the cost of obtaining such services from an outside janitorial supplier.

With regard to staff relief services, HHCM has contracts with non-related providers and suppliers of service in the area and its involvement with the appealing Provider is incidental. The combined involvement of HHCM for both janitorial and staff relief services to the appealing Provider represents less than 1% of its business revenue. Thus, the Provider believes that it meets the criterion for an exception to the related party principles in that a substantial part of the supplying organizations business is carried on with organizations not related to the Provider and supplier by common ownership or control.

The Provider has submitted its financial statements for HHCM[7] as well as a detailed work paper calculating the cost of services supplied by HHCM to the Provider.[8]

Finally, the Provider contends that even if the Board determines that the exception does not apply, the Intermediary's calculation of cost is understated. The Provider asserts that the costs as determined by audit should be increased to agree with the Provider's calculations.

INTERMEDIARY'S CONTENTIONS:

The Intermediary contends that the Provider and HHCM are not bona fide separate organizations and, therefore, do not meet the first exception criterion for the following reasons:

1. The owner of both the Provider and HHCM serves as the Executive Director and sole board member of both companies. The two companies also share a Director of Human Resources and a Branch Manager which prevent the Provider from conducting arms length transactions. Additionally, the Provider shares a total of 63 employees with HHCM.

2. Two HHCM employees attended the Provider's Executive Management Planning Conference[9]. Therefore, the planning functions of the two companies appear to be performed jointly.

3. Office supplies are purchased at bulk rates by the Provider for HHCM.

4. The Provider and HHCM share a commercial insurance package and split the cost 70/30.[10]

5. Among the 63 shared employees are three employees who perform

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[7] Provider Exhibit P-7.

[8] Provider Exhibit P-8.

[9] Intermediary Exhibit I-3.

[10] Intermediary Exhibit I-5.

> the janitorial services purchased from HHCM.[11] Therefore, the Provider has purchased the services of its own employees from a related organization at a marked up rate.

The Intermediary also contends that the Provider did not meet the second exception criteria of HCFA Pub. 15-1 § 1010. This section requires that a substantial part of the supplying organization's business activity of the type carried on with the provider is to be transacted with other organizations. HHCM does not provide janitorial services to any clients other than the Provider. Thus, the second exception has not been met.

Finally, the Intermediary contends that it was not required to evaluate the third and fourth criteria, in that the Provider does not meet the first two.

Issue 3 - Allocation of Cost Shared with the Related Company:

Facts

The Provider received certain management services from HHCM. On its Medicare cost report, the Provider determined the cost of such management services and claimed that amount in its as filed cost report. The Intermediary determined that the Provider's methodolgy for determining the cost of management services should be replaced. The Intermediary adjustment established a home office cost report for these two providers and allocated costs using the pooled cost method.

PROVIDER'S CONTENTIONS:

The Provider contends that its original cost report adequately computed the cost of care giver and administrative services provided by employees that worked for both the Provider and HHCM.

The Provider received both care giver and administrative services from HHCM during the period in question. All personnel serving both the Provider and HHCM were separately employed by each entity, received separate pay checks specifically reflecting their services to each, were maintained on separate payroll registers according to the services they performed, and were reported on separate payroll tax forms submitted by each entity to state and federal authorities. The Intermediary's own work papers listing employees of the Provider[12] and HHCM[13] support the fact that all employees that were found to be working for both the Provider and HHCM were issued separate IRS Forms W-2.

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[11] Intermediary Exhibit I-4.

[12] Provider Exhibit P-9.

[13] Provider Exhibit P-10.

As indicated on these work papers prepared by the Intermediary, all compensation amounts claimed by these dually-employed individuals were traceable to specific IRS Forms W-2, without exception.

The Intermediary at first rejected and later accepted this documentation for purposes of delineating care giver services. The Provider contends that the same documentation should be equally probative with regard to the determination of administrative cost represented by such dually employed individuals. The Provider contends that, absent a specific finding that such individuals were not being paid by these entities in direct proportion to the work performed, such an adjustment is not in keeping with the Medicare regulations regarding cost reimbursement at 42 C.F.R. §413.5.[14]

That regulation is aimed at reimbursing providers for the actual direct and indirect cost incurred, inpatient care, assuming appropriate accounting support is maintained. The Provider submits that the existence of two separately-incorporated business entities, and the maintenance of two separate sets of financial records including two separate payroll registers provide evidence of accounting support of the highest and most credible order.

As to the individuals listed in Exhibits P-9 and P-10, the Provider contends the issue is not to determine whether a particular time study or time-keeping mechanism adequately differentiates a shared employee's time between two or more divisions of the same company. Instead, the task is to determine whether separate payrolls should be discarded and the most general allocation mechanism substituted in their stead. The Provider contends that the individuals listed in Exhibits P-9 and P-10 are not shared employees, but dually-employed individuals. As such, they work for distinctly different supervisors and business entities as much as they would if they held two jobs at different companies that did not happen to be owned by the same individual.

The Provider also contends that its Executive Director maintained detailed time records supporting her oversight of the Provider. The Provider further notes that the very same type and format of continuous time records were maintained in previous periods, and served as the basis for the resolution of a prior year appeal before the Board.

The Provider does not dispute that its Executive Director owned both the Provider and its sister company, HHCM. The Provider submits, however, that the Intermediary was furnished with detailed time records supporting the Executive Director's oversight of the Provider. The Intermediary, according to its work papers and adjustment reports, apparently dismissed such documentation out of hand. The Provider notes that its sister company, HHCM, itself a Medicare-certified home health provider, had its own administrator, its own supervisors and its own care giver staff in compliance with relevant state regulations and with the Medicare program's Conditions of Participation. Only a small portion of its care giver and administrative staff was dually employed by HHCM and the provider. Dually-employed staff did not include the administrator of HHCM.

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[14] Provider Exhibit P-11.

While the Provider does not claim that its continuous time records maintained by the Executive Director are infallible, the Provider strongly believes that they are significantly more reliable than the Intermediary's alternative.

The Provider contends that the rules on home office cost allocation[15] basically allow for three general methods: 1.direct cost assignment, 2.allocation of components based upon functional statistics, and 3.the least sophisticated general allocation based upon a ratio of "cost-to cost". In making its adjustment, the Intermediary ignored the first two and went directly to the least sophisticated method. The Provider believes that the existing rules allow for a second look at that decision, i.e. for direct allocation. Specifically, the instructions in HCFA Pub. 15-1 § 2150 et. seq. state:

> B. Costs Directly Allocable to Components. --The initial step in the allocation of allowable home office costs to components in the chain is the direct allocation of certain costs. Directly allocate allowable costs incurred for the benefit of, or directly attributable to, a specific provider or non-provider activity to the chain entity for which they were incurred. For example, when such costs are paid by the home office, interest expense is allocated to the facility for which the loan was made. Salaries are allocated, to the facility to whose employees they apply. Rent is allocated when the home office rents space for a specific provider, etc. Home offices may simplify the allocation of costs to the chain components in the cost finding process by transferring the costs which are directly allocable to the components through the intercompany accounts. The transfers must be made at the time the costs are incurred and for functional allocation.
>
> C. Costs of Home Office Operations.--Allocate among the provider the allowable costs not directly allocable on a basis designed to equitably allocate the costs over the chain components or activities receiving the benefits of the costs and in a manner reasonably related to the services received by the entities in the chain. Chain home offices may provide certain centralized services, e. g., central payroll or central purchasing, to the chain components. Where practical and the amounts are material, allocate these costs on a functional basis. For example, costs of a central payroll operation could be allocated to the chain components based on the number of checks

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[15] Provider Exhibit P-12.

> issued. The costs of a central purchasing function could be allocated based on purchases made or requisitions handled. Otherwise, these costs may be appropriately included in the pooled costs and allocated as described in subsection D. The functions or cost centers used to allocate, home office costs and the unit bases used to allocate the costs) (including, those for, the pooled costs described in subsection D) must be used consistently from one home office accounting period to another.

Id.

The Provider contends that the above guidelines could serve as an alternative to the position taken in the adjustment. Each component should either be directly assigned to one entity or another or they should be grouped into functionally similar components for allocation based upon an available, auditable statistic.

INTERMEDIARY'S CONTENTIONS:

The Intermediary asserts that during its review of the Provider's administrative costs the following situations were noted:

1 . The Provider and HHCM shared 63 employees, including the Executive Director, Director of Human Services and Branch Manager. Time records were not maintained to support the split of the shared employees' salaries,

2. The Provider's owner served as the Executive Director and sole board member of both the Provider and HHCM. Her entire salary was recorded on the books of the Provider.

3. The Provider purchased supplies for both companies. The cost of these supplies remained on the books and submitted cost report of the Provider.

4. The Provider shared a commercial insurance policy with HHCM and the cost was split 70/30.

As the Provider had not properly allocated these costs shared with HHCM, the Intermediary determined that a home office cost statement was needed to perform the allocation. This was developed in accordance with HCFA Pub. 15-2 § 3100 which states:

> [F]or Medicare and/or Medicaid purposes, a chain organization consists of a group of two or more health care facilities or at least one health care facility and any other business or entity owned, leased, or, through any other device, controlled by one organization. Chain

> organizations include, but are not limited to, chains operated by proprietary organizations and chains operated by various religious, charitable, and governmental organizations. A chain organization may also include business organizations engaged in other activities not directly related to health care. (See HCFA Pub. 15-1, chapter 10 for definitions of common ownership and control).

The Intermediary's adjustment reclassified the shared administrative employees' salaries, office supplies expense and insurance expense to the home office cost report to be allocated to the chain providers using the pooled cost method. The Intermediary accepted the submitted allocation of shared care giver salaries as the allocation was appropriately based on visits performed.

The Provider has proposed that the Executive Director's time records be used to allocate her salary, although, the Provider admits that these records are not "infallible". The Intermediary believes that the majority of the Executive Director’s time must benefit both companies due to the number of employees shared and other shared administrative items such as office supplies and insurance.

The Intermediary contends that a direct allocation of the office supplies expense and the insurance expense is not possible. In order to directly assign office supplies expense, the Provider must be able to document each specific chain provider's usage of supplies expensed during the 12/31/94 fiscal year. Even if these records had been maintained and were available, the pooled method of allocation would be the only appropriate method to use for office supplies related to shared employees. Additionally, the insurance policy was written for both companies combined as one entity, therefore, it is not possible to determine the portion of this expense specifically related to each entity. The Provider has made no specific suggestions as to what functional allocation basis may be used for office supplies or insurance expense. The Intermediary knows of no statistics maintained by the Provider reasonably related to the consumption of office supplies or insurance expense. It appears unlikely that any such statistics are available.

The Intermediary has determined that no direct or functional allocation basis is appropriate for the shared employees' salaries, office supplies and insurance expense. These are residual costs incurred for general management or administrative services that should be allocated using the pooled cost basis.

CITATION OF LAW, REGULATIONS AND PROGRAM INSTRUCTIONS:

1. Law - 42 U.S.C.:

§§ 405.1835-.1841	-	Board Jurisdiction
§ 413.5	-	Cost Reimbursement- General
§ 413.17	-	Cost to Related Organizations

2. Program Instructions - Provider Reimbursement Manual, Part I (HCFA Pub. 15-1):

§ 1000	-	Principle
§ 1010	-	Exception to the Related Organization Principle
§ 2115	-	Treatment of Medical Supply Costs in HHAs
§ 2150 et seq.	-	Allocation of Home Office Costs to Components in Chains
§ 2221	-	Apportionment of Home Health gency Medical Supply Costs
§ 2304	-	Adequacy of Cost Information
§ 2307	-	Direct Assignment of General Service Costs

Provider Reimbursement Manual, Part II, (HCFA Pub. 15-2):

§ 1704	-	Instructions-HCFA Form 1728-86
§ 3100	-	Home Office Costs- Chain Operations
§ 3104	-	Allocation of Home Office Costs
§ 3206	-	Worksheet A- Reclassification and Adjustments of Trial Balance of Expenses

FINDINGS OF FACT, CONCLUSIONS OF LAW AND DISCUSSION:

The Board after considering the facts of the case, parties' contentions, and evidence submitted, finds and concludes as follows:

Issue 1 - Reclassification of Supplies' Salaries to the Administrative and General Cost Center

The Board notes that the Provider included the entire salary paid to one individual and 50% of the salary paid to two other individuals as a direct cost of billable medical supplies. These amounts were reclassified by the Intermediary to the A&G cost center.

The Board finds that the employee job descriptions represent the best evidence available. However, upon review the Board noted that the job descriptions reflected duties in addition to those relating to billable medical supplies. The Board also finds that there is no additional evidence in the record to support the 50% allocation for two of the employees.

The Board does not concur with the alternative approach offered by the Provider. Specifically, the Provider suggested that salaries could be allocated using the total direct cost of billable and non-billable medical supplies. The Board finds this suggested approach to be flawed in that the cost of supplies does not directly relate to the time spent handling those supplies.

The Board also notes that HCFA Pub. 15-1 § 2307 states that: [t]he basis for assigning directly allocable costs of a general service cost center to the benefiting cost center must be on a factual and auditable basis. This precludes the use of averages, estimates or statistical surrogates such as square feet.

The Board finds that since the Provider does not have supplemental time records to support the actual amount of time spent, the most accurate methodology is to include the supplies' salaries in the A&G cost center.

Issue 2 - Disallowance of Costs Paid to a Related Organization

The Board notes that the Provider included the costs paid to a related entity for janitorial and staff relief services in its Medicare cost report. The Board recognizes that 42 C.F.R. § 413.17 states that if a Medicare provider purchases services from a related organization, those costs will only be reimbursed to the provider at the cost of the related organization. Section 413.17 also contains an exception provision which allows a provider to be reimbursed to the extent of supplier charges, provided four specific criteria are met. Medicare program instructions in HCFA Pub. 15-1 § 1000 and § 1010 serve to clarify the Cost to Related Organizations regulation and the exceptions thereto.

The Board finds, in the instant case, that the Provider is not entitled to the exception noted above. First, the evidence indicates that the Provider's owner served as the Executive Director and sole board member of the Provider and the related organization, HHCM. The two companies also share a Director of Human resources and a branch manager. The evidence also indicates that three of the 63 shared employees performed the janitorial services purchased from HHCM. This resulted in the Provider purchasing services rendered by its own employees from a related organization. Secondly, the record indicates that HHCM does not provide janitorial services to any clients other than the

Provider. In addition, there was no evidence in the file which related to the provision of staff relief services.

The Board therefore finds that the Provider did not meet the first or second exception criteria as set forth in 42 C.F.R. § 413.17 and HCFA Pub. 15-1 §§ 1000 and 1010.

Issue 3- Reallocation of Shared Costs Using the Pooled Cost Method

The Board notes that the Provider filed its Medicare cost report using a direct costing methodology. However, the record indicates there is no information to supplement the W-2 statements which only reflect total dollars expended. Thus, there is no documentation to support how the employees time and salaries were assigned to the two different companies.

The Board finds that in view of the determination that the Provider is a related organization, the Intermediary is correct in determining that a home office cost statement is required to properly allocate costs. See HCFA Pub. 15-2 Section 3100- Home Office Costs.

The Board also finds there is no evidence in the record to support the Provider's request for a functional allocation. While the Board agrees with the rationale behind the Provider's contention, there is simply no evidence to support a more sophisticated allocation methodology. Therefore, the Board finds that the Intermediary's use of a pooled method (as discussed in HCFA Pub. 15-2 section 3104) was reasonable in this situation, as it was the only remaining alternative.

DECISION AND ORDER:

Issue 1 - Reclassification of the Supplies Salaries to the Administrative and General Cost Center:

The Intermediary's determination that the Provider does not have sufficient documentation to support the actual amount of time spent by employees handling billable and non-billable medical supplies, as well as other duties is correct. The Intermediary' s adjustment to reclassify salaries from the supplies cost center to the administrative and general cost center is affirmed.

Issue 2 - Disallowance of Costs Paid to a Related Organization:

The Intermediary's determination that the Provider did not meet the criteria for an exception to the Cost To Related Organizations regulation is correct. The Intermediary's adjustment to reduce the related organizations charge to actual cost is affirmed.

Issue 3 - Reallocation of Shared Costs Using the Pooled Cost Method:

The Intermediary's determination that no direct or functional allocation basis is appropriate for the shared employees' salaries, office supplies and insurance is correct. The Intermediary's adjustment to allocate shared cost with a related entity using the pooled cost basis on a home office cost report is affirmed.

Board Members Participating:

Irvin W. Kues
James G. Sleep
Henry C. Wessman, Esquire
Martin W. Hoover Jr., Esquire
Charles R. Barker

Date of Decision: February 7, 2000

FOR THE BOARD:

Irvin W. Kues
Chairman