DEPARTMENTAL GRANT APPEALS BOARD

Department of Health and Human Services

SUBJECT: New Mexico Department of Human Services DATE: August 31, 1981
Docket No. 78-154-NM-SS
Decision No. 211

DECISION

The New Mexico Department of Human Services (Grantee) filed an application for review of a November 14, 1978 decision by the Commissioner of Social Security. In that decision, the Commissioner affirmed the decision of the Regional Commissioner, Region VI, Social and Rehabilitation Service (SRS) to disallow $781,149 in Federal financial participation (FFP) claimed for costs to operate the Grantee's food assistance program for the period July 1, 1968 through June 30, 1973. 1/

There are no material issues of fact in dispute. We have, therefore, determined to proceed to decision based on the written record, which consists of: the reconsideration record developed pursuant to 45 CFR 201.14, the Grantee's application for review, the relevant Audit Report (Audit Control No. 06-50021), pertinent correspondence between the parties, the Grantee's response to an Order to Show Cause issued by the Board Chair, and the parties' responses to the Board's request for additional information. For the reasons stated below, we conclude that the decision of the Commissioner should be upheld.

Statement of the Case

Auditors assigned to the Department of Health, Education, and Welfare (now HHS) Region VI Audit Agency conducted an audit of the Indirect Cost Proposal (ICP) submitted by the Grantee for the fiscal year ended June 30, 1973. The purpose of the audit was to determine if the costs included in the ICP were allowable under the criteria set forth in Office of Management and Budget Circular No. A-87 (effective July 1, 1969) and if the methodology and procedures followed in accumulating and distributing the costs were in accordance with sound accounting principles.

1/ The Social Security Administration (Agency) is the successor agency to the Social and Rehabilitation Service (SRS) for purposes of cash assistance programs previously administered by SRS.

During the review of the Income Maintenance account included in the ICP, the auditors determined that the Grantee had incorrectly charged public assistance programs under the Social Security Act with certain unallowable direct and indirect costs of its food assistance program. These costs included charges related to the certification of households in which no members were public assistance recipients, the distribution of food, and other services provided to recipients of the food assistance programs. Due to the significance of the amount alleged to be incorrectly charged, the review was expanded to include the period July 1, 1968 through June 30, 1972. The Audit Report dated May 1, 1975 concluded that the total unallowable cost amounted to $781,149 for this expanded period of time.

The Grantee made a financial adjustment in Quarter II FY '74 of $112,760 leaving a balance due of $668,389, but continues to dispute the entire $781,149 disallowance.

Authority

The Grantee and HHS jointly fund public assistance programs; however, the extent of HHS's financial participation in the food assistance programs is limited. The allowability of these costs was set out in Part V of the Handbook of Public Assistance Administration (HPA), effective July 28, 1965. 2/

Handbook of Public Assistance Administration, (HPA), Part V, §4810:

> Federal Financial Participation
>
> For the purpose of this section, the term, "public assistance recipients," means applicants for or recipients of assistance under the federally aided State public assistance programs, including medical assistance for the aged.

2/ The Acting Commissioner of Social Security's November 14, 1978 decision to uphold the disallowance determination includes as "conclusions of law" that, although HPA provisions are not regulations, they have the force and effect of regulations, citing King v. Smith, 392 U.S. 309, 317 (1968). The Grantee questioned the continuing validity of the HPA in its application for review, but did not present any supporting arguments in response to the Board's Order to Show Cause which tentatively found the HPA binding on the parties.

A. Federal financial participation is available for matching State and local welfare agency expenditures for the initial certification and recertification of households as eligible (1) to obtain coupon allotments under the food stamp program or (2) to receive foods under the direct distribution program of the Agriculture Marketing Service, when one or more members of the household are public assistance recipients.

B. Federal financial participation is not available for matching State or local welfare agency expenditures for the certification of households in which no members are public assistance recipients.

C. Federal financial participation is not available for matching the State and local welfare agency expenditures for costs incident to the acceptance, storage, protection, issuance of, and accountability for, food coupons; nor for the costs of storage, packaging, and distribution of foods under the surplus food program. (emphasis added)

HPA, Part V, §4820:

> Cost Allocation Plan
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> If the State agency and/or one or more local agencies makes expenditures of the kind described in V-4810, items A, B, and C, above, the cost allocation plan must indicate how such costs are to be handled in making the Federal claim... The cost allocation plan must be amended, if necessary, to give effect to this intent and to exclude from the Federal claim all costs identified under V-4810, items B and C. (emphasis added)

Discussion

Issue #1. Whether the Limitations on Reimbursement in HPA §4810 Are Contrary to the Social Security Act

Grantee contends that HHS is authorized to pay for not only the costs of certification and recertification of public assistance households as eligible for food coupons, but also other associated costs of the food assistance programs. Grantee's Memorandum, May 11, 1981, p. 2. Grantee argues that the food assistance activities stem from the same legislative provision and, therefore, any distinction by HHS between these costs in providing FFP under HPA §4810 is "purely artificial." Id. at p. 3.

In support of its argument, the Grantee argues that HHS's authorization to participate in the costs of administering the food stamp program comes not from the Food Stamp Act, but from the Social Security Act and, therefore, any restrictions on that participation must be found in the Social Security Act. Grantee cites as statutory authority for HPA §4810 sections 1, 401, 1001, 1401, and 1601 of the Social Security Act. Grantee notes that the following language is contained in each of those sections:

> For the purpose of enabling each State to furnish financial assistance, as far as practicable under the conditions in such State... to furnish rehabilitation and other services... there is hereby authorized to be appropriated for each fiscal year a sum sufficient to carry out the purposes of this part.

Grantee agrees that each of the titles provides for the provision of services to individuals who meet certain eligibility requirements. Grantee further argues that certification and recertification is only one step in the provision of the service, and that it must necessarily include the costs of receiving, storing, distributing and accounting for food coupons. Therefore, since all these activities stem from the same legislative provision, any distinction made under HPA §4810 becomes "arbitrary and capricious." Id.

The Agency argues that HPA §4810 is authorized by the "Appropriation" sections of Titles I, IV, X, and XIV of the Social Security Act. Agency's Memorandum, May 8, 1981, p. 1. The Agency contends, however, that the justification for paying the costs of certification and recertification of a public assistance applicant's eligibility for food stamps cannot be extended to include the costs at issue here. The Agency argues that the determination of eligibility for the food assistance program for these households is "inextricably enmeshed" in the determination of eligibility for the public assistance program so that few, if any, additional costs result. Id. at p. 2. The Agency states further that the fact that the food assistance statutes do not authorize the United States Department of Agriculture (USDA) to match the costs of certifying public assistance households, there is an implied recognition "that certification could be accomplished without additional cost in the determination of public assistance eligibility." Id. For these reasons the Agency can provide FFP for these activities.

The Agency argues that the food assistance costs are not intermingled in public assistance programs, but are separate. Therefore, the Agency asserts that "[u]nlike the costs associated with certification and recertification of public assistance households, there is no justification for matching these food assistance program costs." Id. at p. 3.

The Board rejects the Grantee's argument that HHS is authorized to pay for all the costs of the food assistance program. Sections 1, 401, 1001, 1401, and 1601 of the Social Security Act authorized appropriations only for the public assistance titles. Costs incurred in the administration of programs other than the public assistance programs are not subject to FFP under the public assistance titles of the Act. See, California Department of Benefit Payments, Decision No. 160, March 31, 1981.

The Secretary of HHS determined that FFP was available under the public assistance titles for the initial certification and recertification of public assistance households as eligible for food coupons. HPA §4810A. In light of the Secretary's duty under the public assistance titles to furnish assistance and other services consistent with the provisions of the individual titles, it was not unreasonable for the Secretary to have determined that FFP would be available in the limited situations prescribed in HPA §4810A. See, Connecticut Department of Social Services, Decision No. 183, May 29, 1981. Such a provision recognizes that certification under the prescribed circumstances benefits the public assistance programs while incurring little, if any, additional costs for either the food assistance or public assistance programs. The provision is not inconsistent with the relevant sections of the Social Security Act and furthers the efficient administration of the functions with which the Secretary is charged under the Act. Section 1102 of the Act.

The disallowed costs in this case were direct and indirect costs associated with certifying non-public assistance recipients for the food stamp program, distributing food, and other services provided to non-public assistance recipients of the food assistance program. These costs were incurred in the administration of food programs and are outside the scope of the public assistance programs. Congress established these food programs in legislation apart from the public assistance titles of the Social Security Act and provided for their administration at the Federal level by the USDA, and not HHS which administers the public assistance titles. Therefore, there is no justification for HHS's participation in the payment of the costs incurred solely in the administration of those food programs.

Issue #2. Whether the Disallowance Constitutes a Retroactive Disapproval of the State's Cost Allocation Plan.

The Grantee argues that HHS had the opportunity to review and approve the ICP's for the fiscal years 1969-1973 and did eventually approve them, thus causing the Grantee to rely on the approval and to proceed with what is now termed an unallowable practice.

The identical page, page 16, was included in the Grantee's ICP to describe the cost allocation in the Food Assistance section for the years 1969 through 1972. Page 16 contained the following language:

> 4. Food Assistance Section: Direct expenses with allocated State Office administrative costs will be distributed to the Food Distribution Program, the Food Stamp Program and the Federal Food Distribution Program on the percentage distribution of employees in these programs at the end of each quarter.
>
> Costs chargeable to the Food Distribution Program and the Food Stamp Program will be distributed to the Public Assistance Program AABD and AFDC and to non-financial assistance food program (categories 29 and 39) based on participation data compiled by the Statistical Analysis Section. 50% Federal Financial Participation will be claimed on costs charged to AABD and AFDC.

Grantee in its March 16, 1981 Memorandum in Response to the Order to Show Cause disputes the tentative finding of the Board that the disallowance constitutes a disapproval of costs rather than a retroactive disapproval of the Cost Allocation Plan (CAP). While the Grantee tentatively agrees with the Board's assessment of the second paragraph cited above,3/ Grantee contends that the fair import of the first cited paragraph has been overlooked by both the Board, in the Order to Show Cause, and the Agency on four separate occasions, November 15, 1968, January 7, 1970, April 19, 1971, August 2, 1972, when the Grantee submitted its ICP to HHS's Division of Grants Administration Policy. Exhibit 12 of the Reconsideration Record. Grantee argues that this paragraph "states in a straightforward manner that direct expenses will be allocated to the various food programs," thereby sufficiently putting the Agency on notice of the Grantee's practice of charging indirect food assistance costs to the public assistance Income Maintenance account. Grantee's Memorandum, March 16, 1981, p. 2.

The Agency, in its May 8, 1981 response to the Board's Request for Additional Information, contends that there was no actual Agency approval of the Grantee's ICPs for 1969-1972 upon which the Grantee could rely.

3/ The Board found tentatively in the Order to Show Cause that the second paragraph appeared "to describe a general method of allocation and not a description of individual costs to be charged."

Although the Agency agrees with the Grantee's claim that the ICPs were submitted on four separate occasions, the Agency argues that the ICPs were not approved following those submissions. In addition, the Agency asserts that there was no tacit approval of the Grantee's unallowable practice. The Agency agrees with the Grantee that the first full paragraph on Page 16 "states in a straightforward manner that direct expenses will be allocated to the various food programs." Grantee's Memorandum, March 16, 1981, p. 1-2. The Agency contends, however, that such a statement "cannot be construed as giving the Agency notice that the State would be charging unallowable food assistance costs to the Income Maintenance account for public assistance." Agency's Memorandum, May 8, 1981, p. 2.

The Agency argues further that if the Grantee had followed the provisions of its CAP the food assistance costs would be directly charged to the proper program or set aside as unallowable before the allocation process was initiated. Therefore, the CAP was read by the Agency as assuring that the State was charging only allowable costs.

The Board concludes, based on the evidence in the record, that the Grantee has not shown that the Agency actually or tacitly approved the charging of unallowable food assistance costs to the public assistance Income Maintenance account.

Grantee argues that the ICPs were submitted annually for the years 1969-1973 and the Agency had the opportunity to review and approve the plans and eventually did so. However, Grantee has submitted no evidence indicating when the plans were eventually approved. 4/ The record does show that the revised ICPs for 1969-1972 were submitted for retroactive approval on August 2, 1972. Exhibit 12 of the Reconsideration Record. In this context, the Board finds that the Grantee has presented no evidence of actual approval by the Agency upon which it could rely for charging these unallowable food assistance costs to the public assistance programs.

Further, the Grantee's argument that approval for charging the unallowable food assistance costs to the public assistance programs could be inferred, because the Agency did not question the treatment of these costs, incorrectly implies that the ICPs for the years 1969-1973 clearly indicate that these costs would be treated in this fashion. In reading the two paragraphs, the Board finds that neither can be interpreted as describing a practice

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4/ The Agency states that it has been unable to locate any evidence of such approval in its records. Agency's Memorandum, May 8, 1981, p. 4.

of charging unallowable costs. The first paragraph simply states that direct expenses will be allocated to the various food programs. The second paragraph, as the Board has previously stated and the Grantee has agreed (Grantee's Memorandum, March 16, 1981, p. 1) is a description of a general method of allocation, and not a description of individual costs to be charged. Neither paragraph contains language which would have put the Agency on notice of the Grantee's unallowable practice. This is especially so when the paragraphs are read in light of other provisions of the CAP describing treatment of direct charges (section 5320.1) and certification that indirect costs are in accordance with statutory restrictions. Certification page of CAP. It was, therefore, reasonable for the Agency to have assumed that the Grantee, in participating in the public assistance program, was complying with the provisions of the HPA. Accordingly, the fact that these improper costs were not detected by the Agency does not constitute a tacit approval of Grantee's practice of charging the public assistance program with food assistance program costs. Therefore, we conclude that the Agency was not on notice of, and did not approve by silence, Grantee's practice of charging food assistance costs to the public assistance programs. Such a finding would be particularly unreasonable in light of the HPA provision requiring Grantee to identify how it will handle these types of food assistance costs. HPA §4820.

In view of the Board's findings above, the Grantee's second argument of retroactive disapproval is not persuasive. The above-quoted portion on page 16 of the Grantee's CAP was not being disapproved; only the improper charges were disapproved. Costs of certification and recertification of households as eligible for food stamps, allowable under the HPA, are properly chargeable under this section of the ICP, but other costs of food coupons, as set forth in §4810(C) of the HPA, are not.

Issue #3. Whether the Indirect Costs are Allowable

The Grantee argues that all of the "indirect cost FFP" ($169,096) represented in the $781,149 disallowance was properly chargeable to HHS. Grantee alleges that the Federal auditors did not completely follow the CAP, which provided for the distribution of indirect costs on a "step down basis", to the final step but instead disallowed the costs at the food program level. The Board stated in its November 26, 1980 Order to Show Cause that the Grantee's argument, if documented and accepted, might require an adjustment to some of the disallowed costs.

The Grantee submitted a Justification Paper dated January 26, 1981 which purports to explain the disallowed indirect costs. The Grantee states that:

> [T]he disallowed indirect costs benefited the Financial Assistance Programs OAA, AFDC, ANB and AOTD and were distributed based on commodity certification and Food Stamp Participation... In our view, the above disallowed indirect costs were necessary and reasonable for the proper and efficient administration of the Financial Assistance programs and are proper charges as allowed under Section 4810(A) of the HPA.

The Agency has argued that it is irrelevant whether the indirect costs were necessary and reasonable; they are unallowable under the HPA except for certification and recertification costs. In addition, the Agency contends that its auditors followed the Grantee's ICP completely and that the step-down process did not eliminate unallowable costs.

The Board concludes that the Agency was reasonable in requiring the State to eliminate from the pool unallowable food assistance costs because the Grantee has not shown that its step-down method of allocating costs excluded the unallowable costs from claims for FFP.

It is a basic principle of grants law that to be allowable under a grant program, costs must be necessary and reasonable for proper and efficient administration of the grant program, be allocable to that program, and conform to any limitation or exclusion set forth in federal laws or other governing limitations as to types or amounts of cost items. A cost is allocable to a particular cost objective to the extent of benefits received by such objective. See, e.g., Office of Management and Budget (OMB) Circular No. A-87, Attachment A, Section C.1 and 2.

The HPA specifically requires that the Grantee's cost allocation plans indicate how the unallowable food assistance costs are to be handled in making a federal claim, and directs that the plans be amended, if necessary, to insure that these costs are excluded from federal claims. See, HPA § 4810, 4820.

While the Grantee claims that its allocation formula "pulled out" the unallowable food assistance costs and charged them to an account which does not receive federal funds, the Grantee has not presented any persuasive evidence to support this position. Since the HPA required

the Grantee to ensure that no FFP was claimed for these costs, and there is no relationship in this instance between the necessity and reasonableness of the costs and the allowability of the costs under the HPA, the Grantee has the burden of showing that its method of allocation did not result in improper claims for FFP. See, California Department of Benefit Payments, Decision No. 160, March 31, 1981. The Grantee has not shown how its method of allocation excluded the unallowable food assistance costs from claims to the public assistance programs.

Issues #4. Whether Time Limitations Precluded the Auditing of this Period

The Grantee has argued that HHS is precluded from auditing any records dating prior to three years preceding the audit pursuant to 45 CFR Part 74 and 45 CFR 205.145. Grantee asserts that these regulations operate as a three year statute of limitations on federal government review of Grantee records, thus prohibiting an audit of program years 1968 and 1969.

The Grantee states that 45 CFR 205.145 was revised "to bring it into compliance with Office of Management and Budget Circular A-102 dated October 19, 1971 which directed that no later than July 1, 1972 all federal agencies reduce the record retention period to three years unless there were unresolved audit findings." Grantee's Memorandum, March 16, 1981, p. 4. The Grantee contends that although the effective date of the amendment is July 1, 1972, "[n]o place in the regulation is there a statement to the effect that it is inapplicable to periods prior to July 1, 1972." Id.

The normal rule is for legislation and regulations to be applied prospectively to events and agreements which occur later. See, e.g., Greene v. United States, 376 U.S. 149, 159-160 (1964). Since there is no clear intention that these regulations should operate retrospectively, the Board will follow the normal rule and apply them prospectively. This is especially true here where a retrospective application of the regulations would effectively cut off substantive rights of the Agency which it had at the time the grants were awarded.

The regulations relied on by the Grantee were not in effect until 1972 for Part 205 and 1974 for Part 74. They, therefore, do not apply to the program years 1968 and 1969.

During the period in question, the retention of record provision in effect was contained in the HPA at §3411.1(6). It provided that:

> All records relating to the State's accountability for expenditures made pursuant to Titles I, IV, X XIV and XVI of the Social Security Act must be kept for a sufficient period of time to permit examination by the administration through the Federal fiscal audit, the administrative review, and the personnel review, or for 3 years, whichever is later.... (emphasis added)

Although this provision was superceded in 1971 by SRS Program Regulation 10-11, later to become 45 CFR 205.60, it is controlling for the relevant time period.

It is apparent from a reading of this provision that the burden was on the Grantee to retain the records for a minimum of three years or until the federal government has had an opportunity to audit them, as is the situation in the present case. There is no corresponding duty placed on the Agency to conduct the audit within a specified time. Therefore, the Grantee's argument is without merit.

Conclusion

For the reasons stated above, we sustain the disallowance of FFP in the full amount of $781,149.

/s/ Norval D. (John) Settle

/s/ Alexander G. Teitz

/s/ Donald F. Garrett, Panel Chair