DEPARTMENTAL GRANT APPEALS BOARD

Department of Health and Human Services

SUBJECT: Michigan Department of Social Services DATE: October 29, 1981
Docket No. 79-216-MI-HC
Decision No. 224

DECISION

This case involves an October 15, 1979 determination by the Health Care Financing Administration (HCFA, Agency) to disallow $12,706,662 in Federal financial participation (FFP) claimed by the State of Michigan Department of Social Services (MDSS or State). The State appealed only part of the disallowance in the amount of $5,659,300, which represents the federal share of administrative costs under Section 1903(a)(6), presently Section 1903(a)(7), of the Social Security Act for the period January 1, 1973 to September 30, 1975. The issue in dispute is whether the State claimed administrative costs attributable to Title XIX in accordance with its approved cost allocation plan.

The record on which this decision is based includes the State's application for review, the Agency response to the application, an Order to Show Cause issued by the Board, the Grantee's response to the Order, the Agency response submitted in accordance with the Board's request during a telephone conference call held July 29, 1981, the transcript of the hearing held in this matter on August 19, 1981, the Agency's post-hearing briefing submitted in accordance with the presiding Board member's request made at the hearing, and the State's response to the Agency's post-hearing briefing.

We conclude that the Agency's determination cannot be sustained, for reasons set forth below.

Relevant Regulatory Provisions

The Agency, in its notice of disallowance dated October 15, 1979, cited the following provision as the basis for its disallowance:

> As a condition for receipt of Federal financial participation in administration services (excluding purchased services) and training for any quarterly period, a State's claim for such expenditures must be in accord with a cost allocation plan on file with and approved by the Regional Commissioner for that period. 45 CFR 205.150(b)(1) (1976).

The above-cited provision was published March 31, 1976 at 41 FR 13584, and was to become effective 90 days after the publication or earlier at State option. Since the disallowance period ends September 30, 1975, the provision cited by the Agency is not applicable here.

During the period for which the disallowance was taken, two versions of 45 CFR 205.150 were in effect. The first, which was in effect from February 27, 1971 until November 26, 1973, is as follows:

> §205.150 Cost allocation.
>
> State plan requirements: A State plan under title I, IV-A, X, XIV, XVI, or XIX of the Social Security Act must provide that the State agency will establish and maintain methods and procedures for properly charging the costs of activities under the plan to the program in accordance with Federal requirements (Bureau of the Budget Circular A-87 and Department and Social and Rehabilitation Service regulations and instructions). Such methods and procedures and revisions of them are subject to approval by the Department; revisions must be submitted promptly and in no case later than 12 months following the effective date of the change. The State's methods and procedures must include a description of the method for:
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> (a) Allocating all administrative costs of the State department in which the State agency is located between Federal and non-Federal programs;
> (b) Identifying, of the costs applicable to more than one of the Federal programs, those applicable to each of the separate programs, in accordance with program classifications specified by the Secretary; and
> (c) Segregating costs in paragraph (b) of this section by service and income maintenance functions, where applicable, and such other classifications as are found necessary by the Secretary.

The second version of 45 CFR 205.150 was in effect from November 26, 1973 to June 29, 1976. The NPRM for the second version, published June 15, 1973 at 38 FR 15738, states that the reason for the revision is to "implement an administrative determination that State public assistance and medical assistance agencies must submit cost allocation plans when requested by the Regional Commissioner. This will permit review and updating of costing methods and provide information on the significance of costs in relation to the allocation base." The final rule, published September 26, 1973 at 38 FR 26804 effective November 26, 1973, is as follows:

(a) State plan requirements. A State plan under title I, IV-A, IV-B, X, XIV, XVI, or XIX of the Social Security Act must provide that the single State agency will establish and maintain methods and procedures for properly charging the costs of administration...under the plan in accordance with Federal requirements (Office of Management and Budget Circular No. A-87 and Department and Social and Rehabilitation Service regulations and instructions). Such methods and procedures must include those for:

> [Subparagraphs (1), (2), and (3) have been deleted here. They are the same as subparagraphs (a), (b), and (c) of the 1971 regulation, quoted above.]

(b) Federal financial participation. As a condition for receipt of Federal financial participation, a State must submit for approval a revised cost allocation plan within 3 months after being requested by the SRS Regional Commissioner ....

> [Subsection (b) proceeds to detail when such requests will be made, the content of the CAP, and the effect on FFP of the submission of a revised plan.]

Background

The Agency's October 15, 1979 notification of disallowance stated that the Agency's auditors determined that the allocation base for administrative costs was incorrect and, therefore, costs charged to Title XIX were overstated. The auditors claimed the basis used should have been all medical assistance (MA) eligibles receiving assistance as stated in the approved cost allocation plan (CAP), rather than those eligible to receive assistance. The disallowance cites Section IX, B, 4 of the approved State CAP which provided that:

> All income maintenance costs will be allocated to programs in proportion to the number of cases receiving assistance under AFDC, MA, GA, and the Non-public assistance segment of the Food Stamp program.

The notification of disallowance concluded that the claim for expenditures was contrary to the State's approved CAP, and, therefore, was not in accordance with 45 CFR 205.150(b)(1) - citing the 1976 inapplicable provision - and Section 1903(a)(6) (presently Section 1903(a)(7)) of the Social Security Act. The latter provision provides that the Secretary shall pay to each State which has an approved State plan an amount equal to 50 percent of the amounts expended as found necessary by the Secretary for the proper and efficient administration of the State plan.

Discussion

Requirement of claiming costs in accordance with the State CAP.

The Agency based its disallowance here on the fact that the State claimed administrative costs for medical assistance on a basis other than that specified in its approved CAP for the period and, according to 45 CFR 205.150(b)(1) (1976), as a condition for FFP, a State's claim for expenditures must be in accordance with its CAP. This regulation with its specific language was not published until March 31, 1976. During the period in question here, January 1, 1973 through September 30, 1975, applicable regulations did not specify that as a condition for the receipt of FFP, a State's claim must be in accordance with its approved CAP. Therefore, the State argued that since the requirement contained in the disallowance letter was not a validly promulgated regulation prior to the audit period, the requirement cannot now be imposed on the State and the disallowance is not valid.

Both regulations in effect during the period, however, do specify that the State establish and maintain methods and procedures for charging the costs of activities "in accordance with Federal requirements (Bureau of the Budget Circular A-87 and Department and Social and Rehabilitation Service regulations and instructions)." The Bureau of the Budget Circular A-87 provides principles and standards for determining costs applicable to grants and contracts with State government agencies. The Department of Health, Education, and Welfare (now Department of Health and Human Services) in 1969 published a brochure entitled "A Guide for State Government Agencies," OASC-6, intended to implement the Bureau of the Budget Circular A-87. The purpose of the brochure was to provide "guidance on the procedures to be followed by State governments in seeking to recover the costs of [central support] services ...and the indirect costs of grantee State departments." (OASC-6, March, 1969, p. iii). The brochure was sent to State Administrators and established the Department's instructions concerning cost allocation plans and indirect costs. (SRS Program Regulation 1-1, from the SRS Commissioner dated April 18, 1969). The Agency cited this brochure in its post-hearing response for the proposition that the State must claim costs in accordance with its CAP. (Supplemental Response of HCFA dated September 1, 1981, p. 4). The State has not contested that this brochure was binding on it. (Supplemental Response of the State of Michigan Department of Social Services, dated September 4, 1981, p. 2).

This brochure states that in order for a State to recover indirect costs, a CAP must be submitted to the Federal Government annually. These plans "form the basis for agreements between the State and the Federal Government setting forth the indirect costs which may be charged to Federally supported programs," and "these agreements constitute authority

to Federal agencies making awards to States to reimburse indirect costs under their programs...." (OASC-6, p. 2). Although the Agency's disallowance was based on the "regulatory requirement [45 CFR 205.150(a) and (b) (1976)] that FFP in administrative costs is available only if provided in accordance with an approved CAP filed with HEW," and although the regulations in effect during the period of the disallowance do not contain this specific language, the regulations do impose on the State a legal requirement to establish methods and procedures on charging costs in accordance with Federal requirements, specifically Bureau of the Budget Circular A-87 and the Department's instructions pertaining to methods and procedures of charging costs.

Despite the fact that the Agency in its disallowance letter miscited the legal basis for the Agency's actions, there still was an independent requirement on the State to claim costs in accordance with its CAP. Therefore, we conclude that the State was required to claim costs in accordance with its CAP in order to receive FFP.

Interpretation of Provision in State CAP

Although we have determined that the State was required to claim costs in accordance with its CAP, the question remains whether the State, by its interpretation of the term "receiving assistance," did in fact claim costs in conformance with its CAP.

The dispute here revolves around Section IX, B, 4 of the approved CAP and the meaning of "receiving assistance" as contained in that section. The Agency interprets "receiving assistance" as cases actually receiving medical services. The Agency admits that the State had an approved CAP for the period in question and that, but for this provision in the CAP (as the Agency interprets it), the claimed costs here are otherwise allowable. (Response of HCFA to Petitioner's Application for Review, pp. 9 and 10; Transcript of August 19, 1981 hearing, pp. 12 and 14).

The State's argument throughout this proceeding has been that although the phrase "receiving assistance" was used, the State has always interpreted it, for the MA programs, to mean all persons eligible to receive assistance. The State indicated through written submissions and oral testimony that it consistently claimed costs on this basis until the Agency, by letter dated March 31, 1978, (State Exhibit 3) informed the State that the initial review of the State's CAP submitted for the fiscal year ending (FYE) September 30, 1978 indicated an inconsistency as to the allocation base used. (Application for Review; State Response to Order to Show Cause, p. 8; Transcript, pp. 24-27, 34-41). In response to the Agency, the State by letter dated May 19, 1978 (State Exhibit 4), indicated that in accordance with the Agency's review, the CAP for FYE September 30, 1978 had been corrected to read "the number of cases eligible for assistance" rather than "number of cases receiving assistance."

The section of the CAP in question also referred to the allocation of administrative costs for three other programs besides the MA program under Title XIX. These programs are cash assistance programs, which means a determination of eligibility entitles the recipient to receive cash assistance immediately. The MA program is the only program unlike this. (Transcript, pp. 30-31, 56-58). It is not a cash assistance program but a vendor program, meaning a recipient may be determined as medically needy but may not receive medical services from a provider until some time later. (Transcript, pp. 30-31, 56-58). If one would interpret "receiving assistance" as the receipt of medical services, it is entirely possible that the person determined eligible may not have received assistance, i.e. medical services, until a later date. Therefore, the MA program is unlike the other programs in that a determination of eligibility does not mean that the person eligible receives some kind of medical service or cash assistance upon the making of that determination.

The State indicated that it grouped these programs together in this section not knowing that the wording of this section was ambiguous as to the meaning of "receiving assistance." (Transcript, p. 56). The State argued that its intent was and its practice has always been to claim these costs on the basis of persons eligible. (Transcript, pp. 56-57). The State also explained that when the State makes a determination of eligibility under the MA program, it incurs costs for establishing and maintaining the file, issuing a card to the recipient and other administrative costs of determining eligibility which are legitimate and allowable costs. (Transcript, p. 56). The Agency in rebuttal argues that the CAP states "receiving assistance" and that this provision means "receiving medical assistance." (Response of HCFA to Petitioner's Application for Review, pp. 4-8; Supplemental Response of HCFA, pp. 5-6).

The Agency, in closing argument at the hearing, claimed the State did make a distinction between those persons eligible to receive medical assistance and those persons eligible who are actually receiving medical assistance. (Transcript, p. 102). The Agency contends that it has the right to rely on the plan inasmuch as the document should speak for itself. (Transcript, p. 102).

The Agency has not shown why the phrase "receiving assistance" should be interpreted for Title XIX as meaning "receiving medical assistance." This phrase is susceptible to more than one reasonable interpretation. Where ambiguous language exists, the general principle is to ascertain and determine the intent and meaning of the parties. 17 Am Jur 2d Contracts, §224.

The regulations in effect during the period in question, 45 CFR 205.150 (1971) and (1973), provide that the methods and procedures for charging costs to federal programs are subject to approval by the Agency and method and procedures for charging costs under the plan must be in accordance with SRS regulations and instructions. The "Financial Review Guide" published January, 1974 by the Social and Rehabilitation Service (the predecessor of HCFA) relating to administrative costs and cost allocation states that the purpose of the section on cost allocation plans and methods in this guide is to determine whether the methods utilized for allocating costs are consistent with the approved State cost allocation plan. The Guide provides that the Agency review the State CAP and the State's methods for allocating costs. Upon completion of the review of the actual allocation methods in comparison with the approved department allocation procedures, the Agency shall issue a final report which includes recommendations for improvement if discrepancies between the approved department cost allocation plan and actual cost allocation methods are found. (Financial Review Guide, January, 1974, pp. 8 and 43).

The Agency admitted that for the period in question, January 1, 1973, to September 30, 1975, cost allocation plans for the fiscal years involved were approved by the Agency. (Transcript, p. 14). Evidence indicates that the Agency did not communicate to the State that there was any discrepancy between the State's actual cost allocation method and the approved cost allocation plan even though the State was claiming costs based on "eligibles." (Transcript, pp. 39-42). In fact, the first evidence in the record of notice to the State that the Agency believed there was any discrepancy between the method and plan was the audit report issued December 21, 1977. Furthermore, the State indicates that it changed its plan for the FYE September, 1978 only after the Agency notified the State of the discrepancy and indicated that a correction was necessary in order to receive approval of the CAP for the FYE September, 1978. (Transcript, pp. 33-42 and p. 65).

The record also indicates that the State always claimed administrative costs for the MA program based on the number of cases eligible to receive assistance. (Transcript, p. 25). The State has also shown that by making an eligibility determination that a recipient is "medically needy," a recipient receives certain "assistance"; a file is set up and maintained and a medical assistance card is issued each month. (Transcript, pp. 46-48 and 56).

The uncontroverted evidence is that the State has consistently interpreted its CAP as including all persons eligible to receive assistance. The only costs the State is attempting to allocate are the administrative costs of determining eligibility. The Agency has admitted that these costs are otherwise allowable.

Given the State's consistent interpretation of a phrase that the State itself put in its own CAP and the fact that determination of eligibility results in allowable costs to the State, we cannot concur in an overly technical interpretation by the Agency of the State's plan. The State has shown that the plan as interpreted does not result in an inequitable distribution of costs. Furthermore, the Bureau of the Budget Circular A-87, which establishes uniform Government-wide guidelines for identifying costs under grants to states, was designed to provide that "Federally assisted programs bear their fair share of costs." This circular provides that unless otherwise restricted, "all indirect costs of the grantee State department are allowable providing they are necessary for the efficient conduct of the grant program." (OASC-6, p. 1).

We emphasize that we are not deciding that a State is not bound by the provisions of its CAP. Rather, we conclude that in the circumstances of this case, where there is an ambiguous phrase in the CAP susceptible of two interpretations, and circumstances indicate that the phrase was consistently and reasonably interpreted to mean "all persons eligible to receive assistance," and the costs are otherwise allowable, that the State, by its interpretation of "receiving assistance," claimed costs in conformance with its CAP.

Conclusion

For the reasons stated above, the Agency's disallowance is reversed.

/s/ Cecilia Sparks Ford

/s/ Alexander G. Teitz

/s/ Norval D. (John) Settle, Panel Chair