

DEPARTMENTAL GRANT APPEALS BOARD

Department of Health and Human Services

SUBJECT: Family Health Program, Inc. DATE: July 31, 1981
Docket No. 78-150
Decision No. 201

DECISION

The Public Health Service (PHS or Agency) is attempting to recover from Family Health Program, Inc. (FHP) interest earned on funds held by predecessors in interest to FHP.

By letter dated November 22, 1978, Family Health Program, Inc. requested review of the October 24, 1978 decision by the Audit Appeals Committee of PHS to uphold the June 16, 1978 decision of the Chief, Grants Management Branch, Health Services Administration, PHS, directing the Utah Family Health Program (UFHP, predecessor in interest to FHP) to return interest in the amount of \$62,170 earned on funds during the period 1971 to 1978. The original Agency decision was based on a report prepared by the HHS (then HEW) Regional Audit Director dated April 25, 1978, captioned Audit Control Number 08-81454.

Our decision is based on FHP's application for review and accompanying briefs, the Agency's response thereto, and submissions by both parties in response to a telephone conference held by the Board on December 30, 1980 and to the Board's Order to Show Cause dated May 15, 1981.

Building Reserve

Neighborhood Health Center (NHC or Grantee), predecessor in interest to UFHP and FHP, accumulated almost exclusively from funds collected in 1972, a building reserve of \$1,069,979 to construct a health services facility. PHS alleges that \$736,498 of the reserve was derived from unspent funding received from Office of Economic Opportunity (OEO) Grant No. 80015. After NHC's health services facility had been constructed (no later than March 31, 1975), the reserve fund had accumulated \$56,558 in interest. Also, on April 1, 1975, with completion of the facility and the subtraction of funds for the building and site, there was a residue in the reserve fund of \$180,477. For reasons that will be explained herein PHS as successor agency to OEO found that the Federal government had an interest in the portion of the building reserve attributable to OEO funds such that PHS should collect (1) \$27,148 of the \$56,558 in interest that had accrued up to March 31, 1975 and (2) \$35,022 of imputed interest on the \$180,477 residue for the period between April 1, 1975 and March 31, 1978.

(1) \$27,148 of Accrued Interest

OEO awarded a Comprehensive Health Services Grant for 1972 to the Community Health Center Foundation (CHCF). As contemplated by the grant award, CHCF contracted with NHC to provide health services to recipients at a rate of of \$33.33 per person served per month up to a maximum of 1,875 persons in a month. The grant budget included a total of \$750,000 for the contract with NHC. The Grant Award statement specifies an extensive list of hospital and out-of-hospital care services that must be provided for "designated enrollees in the NHC Plan who are below poverty guidelines, but not eligible for Title XIX [Medicaid]." The total operations of NHC, however, were by no means limited to OEO grant activities. 1/

During the first half of 1972, NHC determined that it would cost only about \$21.00 per person served per month to provide the required services under the OEO grant. On June 5, 1972 it requested permission of PHS to consider the remaining \$12.33 per person of the OEO money as grant-related income and to accumulate it for the purpose of a building reserve. This request was made in view of PHS' role in administering its own grants to NHC. 2/ NHC indicated that it would be applying the \$21.00 of each \$33.33 in OEO funds received to program expenditures before using any PHS funds. On June 13, 1972 PHS approved the method of accounting for OEO premiums "as outlined in [NHC's] letter of June 5."

PHS now asserts that the \$21.00 per person component of the OEO funds can not be considered to have been spent for providing health services and must instead be imputed to NHC's building reserve and subjected to interest charges. The Agency applies the following analysis in reaching this conclusion.

The Agency found initially that revenues from NHC's operations as a whole exceeded expenditures before counting the OEO grant funds for the period in question. The Agency then determined that the \$21.00 per person component of the OEO grant funds retained its Federal nature. The Agency cited Special Condition 1(b) of the OEO grant as authority for this. Special Condition 1(b) states:

1/ Although the Board has never received a precise breakdown of the other grant projects administered by NHC, or of its privately funded projects, various documents in the record indicate that NHC received funding from PHS and Medicaid for projects larger than the OEO project. There may also have been privately funded projects such as an "Employees Plan." See Attachment E of the opinion by the HHS (then HEW) Office of the General Counsel dated July 8, 1977 submitted to the Board by PHS on February 17, 1981.

2/ The record indicates that the OEO grant project became the responsibility of HEW and thus PHS pursuant to a Memorandum of Understanding in July, 1972. Page 2 of the General Counsel opinion, dated July 8, 1977.

[F]unds received in connection with the operation of the program must be recorded in a separate account in the accounting records and proper support documents must be retained. The account shall be used to meet current operating expenses of the program and the OEO grant funds shall be used for expenses only to the extent that the funds in the account are insufficient.

Having determined that the \$21.00 per person component of the funds remained Federal property under Special Condition 1(b), the Agency then concluded that the funds necessarily became part of NHC's building reserve and that the Federal government should be entitled to any interest that would have accrued up to the point that obligations for building construction were paid. The Agency claimed only interest that would have accrued on the "Federal funds" in the reserve and made no claim on the reserve itself. 3/

In disputing the Agency's position, FHP maintains that all of the funds in the building reserve were non-Federal because (1) NHC was a contractor to whom the special conditions of the grant did not apply, and (2) since NHC's compensation was on a capitation risk basis rather than a cost reimbursement basis, NHC is not accountable to the Federal government for the funds as long as the services provided for under the contract were performed.

The Agency considers NHC a delegate agency of CHCF and therefore subject to the special conditions of the grant. The general conditions governing the Comprehensive Health Services Program under OEO, effective December 1968, state that any condition applying to the grantee shall apply to the delegate agency. Furthermore, the approved grant award uses the term "delegate agency" in a number of sections, including Special Condition 1, indicating that OEO envisioned such an entity participating in the grant. NHC appears to be the only organization involved in the project to which that status could apply and is specifically cited in certain special conditions applicable to the grant. Moreover, NHC rather than CHCF was providing health services to the program beneficiaries. Consequently, FHP's claim that NHC was merely a contractor in this case and therefore not subject to special conditions of the grant is not persuasive.

Even though NHC may be considered to be a delegate agency to which special conditions are applicable, however, the Board concludes that PHS incorrectly applied Special Condition 1(b) to NHC in this instance.

The Agency's disallowance decision interprets Special Condition 1(b) to mean that the grantee may use OEO funds for OEO grant activities only to the extent that excess funds do not exist to pay for these activities

3/ Presumably, since the Agency permitted NHC to consider the \$12.33 component of the original funds to be grant-related income, it has never attempted to collect interest on that component.

from any other source providing revenues to NHC. Thus, PHS concludes that OEO funds must be viewed as "unused" so long as NHC's total operating revenues minus OEO funding exceed NHC's total program expenditures.

We believe that this interpretation of Special Condition 1(b) is unreasonable. First, the interpretation does not comport with the plain meaning of the special condition. When Special Condition 1(b) refers to a separate account for "[f]unds received in connection with the operation of the program," it means funds received specifically for the grant program being funded by OEO. When used elsewhere in the grant award materials, the term "program" is limited to the activities contemplated by the grant award. Indeed, the applicable general conditions governing OEO grants define an "approved program" as "only. . . those activities described in the grant funding request for which funding is approved in the Statement of OEO Grant and its attachments."

Accordingly, under the plain meaning of Special Condition 1(b), the condition only requires separation of funding from other sources when that funding is specifically available for project activities encompassed by the OEO grant. Here, OEO project activities consist solely of providing health care services for designated enrollees who are below poverty guidelines, but not eligible for Title XIX. Thus, the separate account required by Special Condition 1(b) should only contain substitute funding that is specifically available for these enrollees.

Moreover, the plain meaning of the special condition comports with what must have been the purpose behind its adoption by OEO. This purpose is brought to light by General Condition 17, governing all OEO grants made under the Comprehensive Health Services Program (Revised - January 1972), which closely parallels the language of Special Condition 1 and ostensibly was a source for the special condition. 4/

General Condition 17 provides:

INTEGRATION OF FEDERAL, STATE AND LOCAL SOURCES OF FUNDS. Each Comprehensive Health Services program is responsible for making and fully implementing agreements to obtain from public or private agencies which purchase or provide health services or supplies to low-income individuals in a community served by the program all reimbursements available under Federal, state or local law. OEO funds are the last dollar source. Program funds may not be used for health care costs which would otherwise be the

4/ Part (a) of Special Condition (1) provides similar evidence of purpose. For example, Special Condition 1(a) focuses on reimbursements for project services provided by the health center (NHC) that would ordinarily be the responsibility of other agencies. Part (a) begins by indicating that its requirements are "[i]n line with General Condition 17."

responsibility of other agencies unless adequate arrangements for reimbursements on an equitable basis are made. All reimbursements shall be treated as program income. (Emphasis supplied.)

It is likely, then, based on the clear intent of General Condition 17, that Special Condition 1(b) was designed to prevent OEO funds from being used when some other source was available specifically for activities encompassed by the OEO grant. Thus, the special condition prevents the grantee from receiving duplicate funding for particular grant activities and places an affirmative responsibility on the grantee to obtain available alternative funding for health services on behalf of OEO enrollees.

The Agency interpretation goes well beyond these purposes and prevents the grantee from receiving grant funds whenever it has excess revenues from other sources even though the revenues are not specifically intended to cover activities of the OEO grant. The Agency's interpretation greatly limits the grantee's capacity to retain excess revenues from other sources when it receives substantial OEO funding and thereby prevents the grantee from achieving financial stability through the creation of reserves for building funds, emergency contingencies, etc. Indeed, the Agency's interpretation effectively prevents the grantee from knowing whether it can make use of OEO funding for the intended grant activities until it has completed its annual balance sheet for all of its operations.

We also believe that the Agency's interpretation is unreasonable as applied here because OEO did not contemporaneously identify this interpretation of the special condition for NHC and because PHS has been unable, in response to Board questions, to identify OEO policies or guidelines that support the interpretation. Indeed, in administering its own grants to NHC, PHS appears to have approved procedures that conflict with its interpretation of Special Condition 1(b). On June 13, 1972 PHS approved a procedure whereby the \$21.00 of OEO capitation funds would be applied to OEO grant expenditures before any PHS funds. Special Condition 1(b), as here interpreted by PHS, would require OEO funds to be applied after PHS funds. Thus, PHS' approval of procedures relating to its grants on June 13, 1972 conflicts with its current interpretation of OEO Special Condition 1(b).

Finally, we note that the HEW Audit Report that is the basis for the disallowance here sets out three "options" for the Agency in treating the grant funds at issue. These options represent internally inconsistent applications of Special Condition 1(b). PHS has not attempted to rationalize these inconsistencies nor to explain specifically how it reached the interpretation of Special Condition 1(b) reflected in the option it selected. Thus, the selection of the option used by the Agency is tantamount to an arbitrary action.

Accordingly, on the basis of the foregoing analysis the Board is unable to sustain the Agency's charge of accrued interest for the period up to March 31, 1975.

(2) \$35,022 of Imputed Interest from Residue

On March 31, 1975, after the NHC's health services facility had been paid for in full, there was a residue of \$180,477 left in the building reserve. The auditors stated that in light of Special Condition 1(b), the total \$180,477 amount was Federal in nature and so all the interest earned on it between April 1, 1975 and March 31, 1978 should be recovered by the Federal government. The auditors decided that since no records had been kept on the interest earned by those funds, an interest rate of 6% compounded semiannually would be imputed. The interest on \$180,477 at a rate of 6% compounded semiannually yields \$35,022. (See letter dated April 25, 1978 from the Regional Audit Director to the Regional Health Administrator, p. 4.)

FHP does not dispute that 6% interest compounded semiannually is a reasonable rate of interest. However, FHP raises two arguments regarding why it should not owe any interest. First, inasmuch as NHC was paid on a capitation risk basis, the funds lost their Federal nature when NHC received them and accordingly none of the \$180,477 residue could have been Federal. Second, during the period April 1, 1975 through March 31, 1978, FHP and its predecessors in interest suffered losses in their grant funded programs greater than the \$180,477, so that even if the \$180,477 were judged to be Federal it was entirely used to offset losses of grant funded programs. 5/

On the basis of our analysis of the interest charges for the period up March 31, 1975, the Board concludes that Agency's position with respect to the residue is also without support. The residue of the building reserve may only be viewed as Federal in nature if Special Condition 1(b) had been properly applied at the outset with respect to the 1972 OEO grant funds. Since that was not the case, we would be unable to conclude that any funds in the residue retained their Federal character.

5/ The memorandum accompanying the decision by the PHS Audit Appeals Committee indicated that the Committee would have reversed this portion of the disallowance if FHP had provided "conclusive evidence of a loss of funds in operating the program for the period in question." On February 20, 1981, FHP provided to the Board Reports of Revenue and Expenses for the period January 1, 1976 through May 31, 1978 and asserted that grant funded programs suffered losses during a 16-month period beginning January 1, 1976 such that the entire \$180,477 would have been spent for grant funded programs during that period.

Further, even if a portion of OEO funds had remained unused through operation of Special Condition 1(b) for the period before April 1, 1975, FHP and its predecessors appears to have suffered losses in their program operations after that date such that this money would have been "used" during the subsequent period even under the Agency's application of Special Condition 1(b). For this reason too, no interest could properly be imputed on the residue.

Conclusion

For the reasons discussed above, the Board reverses the Agency's decision concerning interest charges on OEO funds received by NHC.

/s/ Norval D. (John) Settle

/s/ Alexander G. Teitz

/s/ Donald F. Garrett, Panel Chair