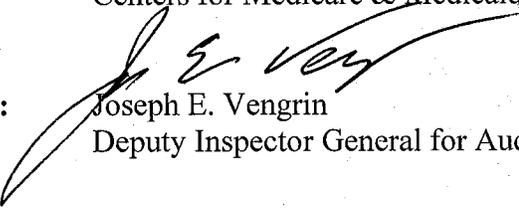




MAR 17 2009

**TO:** Charlene Frizzera  
Acting Administrator  
Centers for Medicare & Medicaid Services

**FROM:**   
Joseph E. Vengrin  
Deputy Inspector General for Audit Services

**SUBJECT:** Review of Medicaid Indirect Costs Submitted by the New York State Department of Health on Behalf of the Office of Mental Retardation and Developmental Disabilities (A-02-06-01028)

Attached is an advance copy of our final report on our review of Federal Medicaid reimbursement of indirect administrative costs submitted by the New York State Department of Health (DOH) on behalf of the Office of Mental Retardation and Developmental Disabilities (OMRDD). We will issue this report to New York State DOH within 5 business days.

In New York State, OMRDD provides services to individuals—both Medicaid and non-Medicaid beneficiaries—with mental retardation and developmental disabilities under a cooperative agreement with DOH, which administers the State’s Medicaid program. On a quarterly basis, OMRDD submits to DOH a report of both direct and indirect costs incurred in supporting administration of the State Medicaid plan. DOH reports the total of OMRDD’s direct and indirect Medicaid administration costs for Federal Medicaid reimbursement on the Form CMS-64, “Quarterly Medicaid Statement of Expenditures for the Medical Assistance Program.”

Our objective was to determine whether DOH properly claimed Federal Medicaid reimbursement of indirect administrative costs submitted by OMRDD.

OMRDD did not maintain documentation to support its indirect cost rate calculations. In addition, DOH did not review OMRDD’s administrative costs before claiming them on the CMS Form-64. As a result, \$8,097,591 (\$4,048,795 Federal share) of the \$9,683,556 (\$4,841,778 Federal share) in indirect administrative costs that DOH claimed from January 1, 2003, through June 30, 2006, was unallowable.

We recommend that DOH:

- refund \$4,048,795 to the Federal Government and

- verify that Medicaid indirect costs billed by OMRDD are adequately supported.

In its comments on our draft report, DOH concurred with our finding and recommendations.

Pursuant to the Freedom of Information Act, 5 U.S.C. § 552, Office of Inspector General reports generally are made available to the public to the extent that information in the report is not subject to exemptions in the Act. Accordingly, this report will be posted on the Internet at <http://oig.hhs.gov>.

Please send us your final management decision, including any action plan, as appropriate, within 60 days. If you have any questions or comments about this report, please do not hesitate to call me, or your staff may contact George M. Reeb, Assistant Inspector General for the Centers for Medicare & Medicaid Audits, at (410) 786-7104 or through e-mail at [George.Reeb@oig.hhs.gov](mailto:George.Reeb@oig.hhs.gov) or James P. Edert, Regional Inspector General for Audit Services, Region II, at (212) 264-4620 or through e-mail at [James.Edert@oig.hhs.gov](mailto:James.Edert@oig.hhs.gov). Please refer to report number A-02-06-01028.

Attachment



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office Of Inspector General  
Office Of Audit Services

MAR 19 2009

Region II  
Jacob K. Javits Federal Building  
26 Federal Plaza  
New York, NY 10278

Report Number: A-02-06-01028

Richard F. Daines, M.D.  
Commissioner  
New York State Department of Health  
14<sup>th</sup> Floor, Corning Tower  
Empire State Plaza  
Albany, New York 12237

Dear Dr. Daines:

Enclosed is the U.S. Department of Health and Human Services, Office of Inspector General (OIG), final report entitled "Review of Medicaid Indirect Costs Submitted by the New York State Department of Health on Behalf of the Office of Mental Retardation and Developmental Disabilities." We will forward a copy of this report to the HHS action official noted on the following page for review and any action deemed necessary.

The HHS action official will make final determination as to actions taken on all matters reported. We request that you respond to this official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

Pursuant to the Freedom of Information Act, 5 U.S.C. § 552, OIG reports generally are made available to the public to the extent that information in the report is not subject to exemptions in the Act. Accordingly, this report will be posted on the Internet at <http://oig.hhs.gov>.

If you have any questions or comments about this report, please do not hesitate to call me, or contact James Cox, Audit Manager, at (518) 437-9390, extension 222, or through e-mail at [James.Cox@oig.hhs.gov](mailto:James.Cox@oig.hhs.gov). Please refer to report number A-02-06-01028 in all correspondence.

Sincerely,

A handwritten signature in black ink that reads "James P. Edert".

James P. Edert  
Regional Inspector General  
for Audit Services

Enclosure

**Direct Reply to HHS Action Official:**

Ms. Jackie Garner  
Consortium Administrator  
Consortium for Medicaid & Children's Health Operations  
Centers for Medicare & Medicaid Services  
233 North Michigan Avenue, Suite 600  
Chicago, Illinois 60601

Department of Health and Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF MEDICAID INDIRECT  
COSTS SUBMITTED BY THE NEW  
YORK STATE DEPARTMENT OF  
HEALTH ON BEHALF OF THE  
OFFICE OF MENTAL  
RETARDATION AND  
DEVELOPMENTAL DISABILITIES**



Daniel R. Levinson  
Inspector General

March 2009  
A-02-06-01028

# ***Office of Inspector General***

<http://oig.hhs.gov>

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The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health and Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

## ***Office of Audit Services***

The Office of Audit Services (OAS) provides auditing services for HHS, either by conducting audits with its own audit resources or by overseeing audit work done by others. Audits examine the performance of HHS programs and/or its grantees and contractors in carrying out their respective responsibilities and are intended to provide independent assessments of HHS programs and operations. These assessments help reduce waste, abuse, and mismanagement and promote economy and efficiency throughout HHS.

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The Office of Evaluation and Inspections (OEI) conducts national evaluations to provide HHS, Congress, and the public with timely, useful, and reliable information on significant issues. These evaluations focus on preventing fraud, waste, or abuse and promoting economy, efficiency, and effectiveness of departmental programs. To promote impact, OEI reports also present practical recommendations for improving program operations.

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# *Notices*

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**THIS REPORT IS AVAILABLE TO THE PUBLIC**  
at <http://oig.hhs.gov>

Pursuant to the Freedom of Information Act, 5 U.S.C. § 552, Office of Inspector General reports generally are made available to the public to the extent that information in the report is not subject to exemptions in the Act.

## **OFFICE OF AUDIT SERVICES FINDINGS AND OPINIONS**

The designation of financial or management practices as questionable, a recommendation for the disallowance of costs incurred or claimed, and any other conclusions and recommendations in this report represent the findings and opinions of OAS. Authorized officials of the HHS operating divisions will make final determination on these matters.

## **EXECUTIVE SUMMARY**

### **BACKGROUND**

Pursuant to Title XIX of the Social Security Act, the Medicaid program provides medical assistance to low-income individuals and individuals with disabilities. The Federal and State Governments jointly fund and administer the Medicaid program. At the Federal level, the Centers for Medicare & Medicaid Services (CMS) administers the program. Each State administers its Medicaid program in accordance with a CMS-approved State plan. Although the State has considerable flexibility in designing and operating its Medicaid program, it must comply with applicable Federal requirements.

In New York State, the Office of Mental Retardation and Developmental Disabilities (OMRDD) provides services to individuals—both Medicaid and non-Medicaid beneficiaries—with mental retardation and developmental disabilities under a cooperative agreement with the Department of Health (DOH), which administers the State’s Medicaid program. On a quarterly basis, OMRDD submits to DOH a report of both direct and indirect costs incurred in supporting administration of the State Medicaid plan. Direct Medicaid administration costs include such activities as budgeting, rate development, and fiscal oversight. OMRDD applies an indirect cost rate to salaries it claims as direct costs of Medicaid administration. DOH reports the total of OMRDD’s direct and indirect Medicaid administration costs for Federal Medicaid reimbursement on the Form CMS-64, “Quarterly Medicaid Statement of Expenditures for the Medical Assistance Program.”

Pursuant to the Office of Management and Budget (OMB) Circular A-87, “Cost Principles for State, Local, and Indian Tribal Governments” (2 CFR part 225), Att. A §C.1, allowable costs must be necessary and reasonable for proper and efficient administration of the program, be allocable to Federal awards, and be adequately documented. Pursuant to OMB Circular A-87, Att. E § D.1.a, State agencies claiming indirect costs under Federal awards must prepare and retain an indirect cost rate proposal and related documentation to support those costs. Pursuant to the cooperative agreement between the Department of Social Services (DOH’s predecessor) and OMRDD, OMRDD agreed to maintain all records necessary for the proper and efficient operation of the Medicaid program and to comply with requirements for any indirect costs claimed for Federal reimbursement.

### **OBJECTIVE**

Our objective was to determine whether DOH properly claimed Federal Medicaid reimbursement of indirect administrative costs submitted by OMRDD for the period January 1, 2003, through June 30, 2006.

### **SUMMARY OF FINDING**

DOH improperly claimed Federal Medicaid reimbursement of indirect administrative costs submitted by OMRDD. Contrary to Federal regulations and its cooperative agreement with

DOH, OMRDD did not maintain documentation to support its indirect cost rate calculations. In addition, DOH did not review OMRDD's administrative costs before claiming them on the Form CMS-64. As a result, \$8,097,591 (\$4,048,795 Federal share) of the \$9,683,556 (\$4,841,778 Federal share) in indirect administrative costs that DOH claimed from January 1, 2003, through June 30, 2006, was unallowable. The remaining \$1,585,965 (\$792,983 Federal share) in indirect administrative costs represents the amount that could have been claimed based on the State's approved indirect cost rate for central service units.

## **RECOMMENDATIONS**

We recommend that DOH:

- refund \$4,048,795 to the Federal Government and
- verify that Medicaid indirect costs billed by OMRDD are adequately supported.

## **DEPARTMENT OF HEALTH COMMENTS**

In its comments on our draft report, DOH concurred with our finding and recommendations. DOH's comments are included as the Appendix.

**TABLE OF CONTENTS**

	<b><u>Page</u></b>
<b>INTRODUCTION</b> .....	1
<b>BACKGROUND</b> .....	1
Office of Mental Retardation and Developmental Disabilities.....	1
Federal Requirements .....	1
State Requirements .....	2
<b>OBJECTIVE, SCOPE, AND METHODOLOGY</b> .....	2
Objective .....	2
Scope.....	3
Methodology .....	3
<b>FINDING AND RECOMMENDATIONS</b> .....	3
<b>LACK OF DOCUMENTATION</b> .....	4
<b>CALCULATION OF THE UNALLOWABLE AMOUNT</b> .....	4
<b>RECOMMENDATIONS</b> .....	5
<b>DEPARTMENT OF HEALTH COMMENTS</b> .....	5
<b>APPENDIX</b>	
<b>DEPARTMENT OF HEALTH COMMENTS</b>	

## INTRODUCTION

### BACKGROUND

Pursuant to Title XIX of the Social Security Act (the Act), the Medicaid program provides medical assistance to low-income individuals and individuals with disabilities. The Federal and State Governments jointly fund and administer the Medicaid program. At the Federal level, the Centers for Medicare & Medicaid Services (CMS) administers the program. Each State administers its Medicaid program in accordance with a CMS-approved State plan. Although the State has considerable flexibility in designing and operating its Medicaid program, it must comply with applicable Federal requirements.

### Office of Mental Retardation and Developmental Disabilities

The Office of Mental Retardation and Developmental Disabilities (OMRDD) provides services to individuals—both Medicaid and non-Medicaid beneficiaries—with mental retardation and developmental disabilities under a cooperative agreement with the Department of Health (DOH), which administers the State’s Medicaid program. On a quarterly basis, OMRDD submits to DOH a report of both direct and indirect costs incurred in supporting administration of the State Medicaid plan. Direct Medicaid administration costs include such activities as budgeting, rate development, and fiscal oversight.<sup>1</sup> OMRDD applies an indirect cost rate to salaries it claims as direct costs of Medicaid administration.

On a quarterly basis, DOH submits to CMS a Form CMS-64, “Quarterly Medicaid Statement of Expenditures for the Medical Assistance Program,” to summarize, by category of service, Medicaid expenditures for Federal reimbursement incurred by all State agencies, including OMRDD. For the period January 1, 2003, through June 30, 2006, DOH’s claims for Federal Medicaid reimbursement of administrative costs included \$9,683,556 (\$4,841,778 Federal share) for indirect administrative costs reported by OMRDD.

### Federal Requirements

Pursuant to Office of Management and Budget (OMB) Circular A-87, “Cost Principles for State, Local, and Indian Tribal Governments” (2 CFR part 225), Att. E § A.2, indirect costs include “the indirect costs originating in each department or agency of the governmental unit carrying out Federal awards and the costs of central governmental services distributed through the central service cost allocation plan . . . and not otherwise treated as direct costs.” These costs are normally charged to Federal awards through an indirect cost rate.

Pursuant to OMB Circular A-87, Att. A §C.1, allowable costs must be necessary and reasonable for proper and efficient administration of the program, be allocable to Federal awards, and be adequately documented. Medicaid regulations at 42 CFR § 433.34 provide that administrative costs are eligible for Federal reimbursement only to the extent that they are allocated to Medicaid

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<sup>1</sup>OMRDD’s quarterly reports include direct costs of Medicaid administration activities at OMRDD’s central office and regional office, as well as direct costs allocated from the New York State Commission on Quality of Care and Advocacy for Persons With Disabilities, which provides independent oversight of State mental hygiene programs.

pursuant to an approved cost allocation plan. Pursuant to OMB Circular A-87, Att. E § D.1.a, State agencies claiming indirect costs must prepare an indirect cost rate proposal and related documentation to support those costs, including certification that the indirect costs will be allowable in accordance with the OMB circular.<sup>2</sup>

Pursuant to section 2500(A)(1) of the CMS “State Medicaid Manual,” amounts reported on the Form CMS-64 must be actual expenditures for which all supporting documentation, in readily reviewable form, has been compiled and is available immediately at the time the claim is filed. In addition, section 2500.5 of the “State Medicaid Manual” states that, pursuant to §1903(a)(7) of the Act, expenditures may be claimed only for the proper and efficient administration of the State Medicaid plan and must be in accordance with an approved cost allocation plan.

## **State Requirements**

Pursuant to a cooperative agreement signed in 1993 by the Department of Social Services<sup>3</sup> and OMRDD, OMRDD agreed to:

- maintain a cost allocation plan that complies with applicable rules and regulations for any indirect costs claimed that are subject to Federal reimbursement;
- bill DOH only at rates, fees, or schedules approved by the New York State Division of the Budget;<sup>4</sup> and
- maintain all records necessary for the proper and efficient operation of the agreement and the State Medicaid program.

## **OBJECTIVE, SCOPE, AND METHODOLOGY**

### **Objective**

Our objective was to determine whether DOH properly claimed Federal Medicaid reimbursement of indirect administrative costs submitted by OMRDD for the period January 1, 2003, through June 30, 2006.

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<sup>2</sup>The certification requires that all costs included in the proposal be properly allocable to Federal awards on the basis of a beneficial or causal relationship between the expenses incurred and the agreements to which they are allocated in accordance with applicable requirements.

<sup>3</sup>In 1997, the Department of Social Services was dissolved, and its Medicaid functions were distributed within DOH.

<sup>4</sup>On an annual basis, the State Division of the Budget establishes an indirect cost rate to allocate statewide central services costs to each receiving State agency, including OMRDD, under a federally approved statewide cost allocation plan. State agencies also incur their own indirect costs, such as personnel administration and other supporting functions. The Division of the Budget suggests that agencies allocate, claim, and recover their own indirect costs, in addition to recovering central services costs imposed by the State (Division of the Budget, Budget Bulletin B-1141 (1993)). The Division of the Budget does not review or track rates developed by individual agencies to recover their own indirect costs.

## Scope

Our audit period covered January 1, 2003, through June 30, 2006, during which time DOH claimed Medicaid reimbursement of \$9,683,556 (\$4,841,778 Federal share) for indirect administrative costs submitted by OMRDD. We did not review the overall internal control structure of DOH, OMRDD, or the Medicaid program. Rather, we reviewed only the internal controls that pertained directly to our objective.

We performed fieldwork at DOH's and OMRDD's offices in Albany, New York.

## Methodology

To accomplish our objective, we:

- reviewed relevant Federal laws and regulations and the State Medicaid plan;
- held discussions with officials of CMS, DOH, OMRDD, and the State Division of the Budget to identify State policies, procedures, and guidance;
- reconciled indirect costs submitted by OMRDD with the Form CMS-64 submitted by DOH for the fourth quarter of State fiscal year 2004 (January through March 2005); and
- sought documentation from DOH and OMRDD related to OMRDD's indirect administrative cost rate proposal and related calculations.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objective.

## FINDING AND RECOMMENDATIONS

DOH improperly claimed Federal Medicaid reimbursement of indirect administrative costs submitted by OMRDD. Contrary to Federal regulations and its cooperative agreement with DOH, OMRDD did not maintain a cost allocation plan for indirect costs or documentation to support its indirect cost rate calculations. In addition, DOH did not review OMRDD's administrative costs before claiming them on the Form CMS-64. As a result, \$8,097,591 (\$4,048,795 Federal share) of the \$9,683,556 (\$4,841,778 Federal share) in indirect administrative costs that DOH claimed from January 1, 2003, through June 30, 2006, was unallowable. The remaining \$1,585,965 (\$792,983 Federal share) in indirect administrative costs represents the amount that could have been claimed based on the State's approved indirect cost rate for central service units.

## **LACK OF DOCUMENTATION**

Pursuant to OMB Circular A-87, Att. A §C.1, allowable costs must be allocable to Medicaid and must be adequately documented. Medicaid regulations at 42 CFR § 433.34 provide that administrative costs are eligible for Federal reimbursement only to the extent that they are allocated to Medicaid pursuant to an approved cost allocation plan. Pursuant to a 1993 cooperative agreement with DOH, OMRDD agreed to maintain a cost allocation plan and the records and reports necessary for proper and efficient administration of the State Medicaid program. Pursuant to Att. E § D.1.a, State agencies claiming indirect costs must prepare an indirect cost rate proposal and maintain supporting documentation.

OMRDD used an indirect cost rate of 10.43 percent from January 1, 2003, through March 31, 2004, and a rate of 10.42 percent from April 1, 2004, through September 30, 2005, to calculate its indirect Medicaid administrative costs.<sup>5</sup> OMRDD submitted these costs to DOH, which claimed Federal Medicaid reimbursement for the costs on the Form CMS-64. However, contrary to Federal regulations and its cooperative agreement with DOH, OMRDD did not maintain documentation to support its indirect cost rate calculations. In addition, OMRDD officials were unable to explain the calculations. DOH did not review OMRDD's indirect administrative costs before submitting them on the Form CMS-64.

## **CALCULATION OF THE UNALLOWABLE AMOUNT**

During our audit period, OMRDD's statewide indirect cost rate for central service units, as calculated by the Division of the Budget, ranged from 0.82 percent to 1.51 percent.<sup>6</sup> Because the State allocated central services costs based on a federally approved methodology, the amount allocated through the statewide indirect cost rate could be allowable for Medicaid reimbursement. However, OMRDD could not provide support for any other agency-specific Medicaid-related indirect costs. To determine the unallowable amount, we calculated the difference between the indirect cost rate that OMRDD used and the State's approved indirect cost rate for central service units. We then multiplied the difference in those rates by OMRDD's indirect cost base.

Based on our calculations, \$8,097,591 (\$4,048,795 Federal share) of the \$9,683,556 (\$4,841,778 Federal share) in indirect administrative costs that DOH claimed for Medicaid reimbursement during the audit period was unsupported and unallowable. The remaining \$1,585,965 (\$792,983 Federal share) in indirect administrative costs represents the amount that could have been claimed based on the State's approved indirect cost rate for central service units.

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<sup>5</sup>OMRDD did not report indirect Medicaid administrative costs to DOH from October 1, 2005, through June 30, 2006. OMRDD officials stated that they did not report these costs after they learned that they had been using an incorrect indirect cost rate.

<sup>6</sup>The U.S. Department of Health and Human Services, Division of Cost Allocation, reviewed and approved New York's methodology for calculating its statewide indirect cost rate for each agency.

## **RECOMMENDATIONS**

We recommend that DOH:

- refund \$4,048,795 to the Federal Government and
- verify that Medicaid indirect costs billed by OMRDD are adequately supported.

## **DEPARTMENT OF HEALTH COMMENTS**

In its comments on our draft report, DOH concurred with our finding and recommendations. DOH's comments are included as the Appendix.

# **APPENDIX**



Corning Tower The Governor Nelson A. Rockefeller Empire State Plaza Albany, New York 12237

Richard F. Daines, M.D.  
Commissioner

Wendy E. Saunders  
Executive Deputy Commissioner

February 11, 2009

James P. Edert  
Regional Inspector General for Audit Services  
Department of Health and Human Services  
Region II  
Jacob Javitz Federal Building  
26 Federal Plaza  
New York, New York 10278

Ref. No. A-02-06-01028

Dear Mr. Edert:

Enclosed are the New York State Department of Health's comments on the Department of Health and Human Services, Office of Inspector General's draft audit report A-02-06-01028 on "Review of Medicaid Indirect Costs Submitted by the New York State Department of Health on Behalf of the Office of Mental Retardation and Developmental Disabilities."

Thank you for the opportunity to comment.

Sincerely,

A handwritten signature in black ink that reads "Wendy Saunders". The signature is written in a cursive, flowing style.

Wendy E. Saunders  
Executive Deputy Commissioner

Enclosure

cc: Diana Jones Ritter - OMRDD  
Robert W. Reed  
Deborah Bachrach  
James Sheehan  
Nicholas Meister  
Stephen Abbott  
Irene Myron  
Ronald Farrell  
Gail Kerker

**New York State Department of Health's  
Comments on the  
Department of Health and Human Services  
Office of Inspector General's  
Draft Audit Report A-02-06-01028 on  
"Review of Medicaid Indirect Costs Submitted by the New  
York State Department of Health on Behalf of the Office of  
Mental Retardation and Developmental Disabilities"**

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The following are the New York State Department of Health's (Department) comments in response to the Department of Health and Human Services, Office of Inspector General's (OIG) draft audit report A-02-06-01028 on "Review of Medicaid Indirect Costs Submitted by the New York State Department of Health on behalf of the Office of Mental Retardation and Developmental Disabilities."

**Recommendation #1:**

The Department should refund \$4,048,795 to the Federal Government.

**Response #1:**

The Department agrees to refund \$4,048,795 to the Federal Government.

**Recommendation #2:**

The Department should verify that Medicaid indirect costs billed by the Office of Mental Retardation and Developmental Disabilities (OMRDD) are adequately supported.

**Response #2:**

The Department will periodically verify that claims for OMRDD indirect costs incurred in supporting administration of the Medicaid State Plan utilize the indirect cost rate for central service units established by the New York State Division of the Budget.