Department of Health and Human Services

OFFICE OF INSPECTOR GENERAL

HUDSON RIVER HEALTHCARE, INC., CLAIMED UNALLOWABLE FEDERAL GRANT EXPENDITURES

Inquiries about this report may be addressed to the Office of Public Affairs at Public.Affairs@oig.hhs.gov.

James P. Edert
Regional Inspector General

April 2013
A-02-11-02014

Office of Inspector General

https://oig.hhs.gov

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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

The Health Centers Consolidation Act of 1996 (P.L. No. 104-299) consolidated the Health Center Program under section 330 of the Public Health Service Act (42 U.S.C. § 254b). The Health Center Program provides comprehensive primary health care services to medically underserved populations through planning and operating grants to health centers. Within the U.S. Department of Health and Human Services (HHS), the Health Resources and Services Administration (HRSA) administers the program.

Under the American Recovery and Reinvestment Act of 2009, P.L. No. 111-5 (Recovery Act), enacted February 17, 2009, HRSA received $2.5 billion, $2 billion of which was to expand the Health Center Program by serving more patients, stimulating new jobs, and meeting the expected increase in demand for primary health care services among the Nation's uninsured and underserved populations. HRSA awarded a number of grants using Recovery Act funding in support of the Health Center Program, including Capital Improvement Program (CIP) and Increased Demand for Services (IDS) grants.

Hudson River HealthCare, Inc. (Hudson River) is a nonprofit organization that operates a network of 16 health centers throughout southeastern New York State. Hudson River provides primary, preventative, and behavioral health care services and is funded primarily by patient service revenues and Federal grants.

In 2009, HRSA awarded Hudson River approximately $2.9 million in Recovery Act funds, of which Hudson River expended approximately $2.7 million. Approximately $2 million of this amount was awarded under a CIP grant to renovate its existing health centers and enhance its IT and electronic health records infrastructure. Approximately $900,000 was awarded under an IDS grant to sustain its current workforce and hire additional staff.

Hudson River must comply with Federal cost principles in 2 CFR part 230, *Cost Principles for Non-Profit Organizations*, the requirements for health centers in 42 U.S.C. § 254(b), and the financial management system requirements in 45 CFR § 74.21.

OBJECTIVE

Our objective was to determine whether Hudson River's Recovery Act grant expenditures were allowable.

SUMMARY OF FINDINGS

Hudson River claimed Recovery Act grant expenditures totaling $280,558 that were unallowable. Specifically, Hudson River claimed unallowable CIP expenditures totaling $260,586 and unallowable IDS expenditures totaling $19,972. The unallowable claims occurred because Hudson River did not properly comply with its policies and procedures for determining the allowability of costs claimed to Federal grants.

RECOMMENDATIONS

We recommend that HRSA:

- require Hudson River to refund $280,558 to the Federal Government ($260,586 related to the CIP grant and $19,972 related to the IDS grant) and

- ensure that Hudson River follows its policies and procedures for determining the allowability of costs claimed to Federal grants.

HUDSON RIVER HEALTHCARE, INC., COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE

In written comments on our initial draft report, Hudson River disagreed with several of our findings based on its interpretation of Federal regulations and guidance on prior approval that, according to Hudson River, it received from HRSA. After reviewing Hudson River's comments and consulting with HRSA officials, we removed one finding and corresponding recommended disallowance of $25,115 related to cabinetry purchases that Hudson River made under the CIP grant. We maintain that our findings and recommendations in this report are valid. Hudson River's comments appear as the Appendix.

HEALTH RESOURCES AND SERVICES ADMINISTRATION COMMENTS

In written comments on our second draft report—which included Hudson River's written comments on our initial draft report—HRSA concurred with our recommendations. Specifically, HRSA stated that it will work with Hudson River to determine if any CIP or IDS grant funds need to be refunded to the Federal government. HRSA also stated that it will work with Hudson River to ensure that the grantee adheres to its policies and procedures for determining the allowability of costs claimed to Federal grants.

TABLE OF CONTENTS

INTRODUCTION

BACKGROUND

Health Center Program

The Health Centers Consolidation Act of 1996 (P.L. No. 104-299) consolidated the Health Center Program under section 330 of the Public Health Service Act (42 U.S.C. § 254b). The Health Center Program provides comprehensive primary health care services to medically underserved populations through planning and operating grants to health centers. Within the U.S. Department of Health and Human Services (HHS), the Health Resources and Services Administration (HRSA) administers the program.

American Recovery and Reinvestment Act of 2009

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In 2009, HRSA awarded Hudson River approximately $2.9 million in Recovery Act funds, of which Hudson River expended approximately $2.7 million. Approximately $2 million of this amount was awarded under a CIP grant to renovate its existing health centers and enhance its IT and electronic health records infrastructure. Approximately $900,000 was awarded under an IDS grant to sustain its current workforce and hire additional staff.[1]

Federal Requirements for Grantees

Title 45, part 74, of the Code of Federal Regulations establishes uniform administrative requirements governing HHS grants and agreements awarded to nonprofit organizations. As a nonprofit organization in receipt of Federal funds, Hudson River must comply with Federal cost principles in 2 CFR part 230, *Cost Principles for Non-Profit Organizations* (formerly Office of Management and Budget Circular A-122), incorporated by reference at 45 CFR § 74.27(a).

[1] The grant budget periods covered by our audit were: June 29, 2009, through June 30, 2012, for the CIP funds; and March 27, 2009, through March 26, 2011, for the IDS grant funds.

These cost principles require that grant expenditures submitted for Federal reimbursement be reasonable, allowable, and allocable. Hudson River must also comply with the requirements for health centers in 42 U.S.C. § 254(b). The HHS awarding agency may also include additional requirements that are considered necessary to attain the award's objectives.

To help ensure that Federal requirements are met, grantees must maintain financial management systems in accordance with 45 CFR § 74.21. These systems must provide for accurate, current, and complete disclosure of the financial results of each HHS-sponsored project or program (45 CFR § 74.21(b)(1)) and must ensure that accounting records are supported by source documentation (45 CFR § 74.21(b)(7)). Grantees also must have written procedures for determining the reasonableness, allocability, and allowability of expenditures in accordance with applicable Federal cost principles and the terms and conditions of the award (45 CFR § 74.21(b)(6)).

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to determine whether Hudson River's Recovery Act grant expenditures were allowable.

Scope

We reviewed costs totaling $2,744,942 that Hudson River charged to its CIP and IDS grants for the period March 27, 2009, through June 30, 2011.

We performed our fieldwork at Hudson River's administrative office in Peekskill, New York, during September 2011.

Methodology

To accomplish our objective, we:

- reviewed relevant Federal laws, regulations, and guidance;
- reviewed Hudson River's CIP and IDS grant applications and supporting documentation;
- interviewed Hudson River personnel to gain an understanding of Hudson River's accounting system, internal controls over Federal expenditures, and CIP and IDS grant activities;
- reviewed Hudson River's procedures on accounting for Recovery Act funds, time and effort certification, payroll processing, withdrawing Federal funds, and company vehicle use;
- reviewed Hudson River's independent auditor's reports and related financial statements for fiscal years 2008 through 2010; and

- reviewed expenditures claimed on Hudson River's CIP and IDS grants for allowability.

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 findings and conclusions based on our audit objective.

FINDINGS AND RECOMMENDATIONS

Hudson River claimed Recovery Act grant expenditures totaling $280,558 that were unallowable. Specifically, Hudson River claimed unallowable CIP expenditures totaling $260,586 and unallowable IDS expenditures totaling $19,972. The unallowable claims occurred because Hudson River did not properly comply with its policies and procedures for determining the allowability of costs claimed to Federal grants.

UNALLOWABLE EXPENDITURES CLAIMED FOR FEDERAL REIMBURSEMENT

Federal Requirements

Pursuant to 2 CFR part 230, Appendix B, § 15.b, capital expenditures for general purpose equipment, buildings, and land are unallowable as direct charges, except where approved in advance by the awarding agency. In addition, capital expenditures for improvements to land, buildings, or equipment are unallowable as a direct cost except with the prior approval of the awarding agency.

Pursuant to 2 CFR part 230, Appendix B, § 8.h, the portion of the cost of organization-furnished automobiles that relates to personal use by employees (including transportation to and from work) is unallowable as fringe benefits or indirect costs regardless of whether the cost is reported as taxable income to the employees. These costs are allowable as direct costs to sponsored awards when necessary for the performance of the sponsored award and approved by awarding agencies.

Pursuant to 45 CFR § 74.25, recipients are required to report deviations from budget and program plans, and request prior approvals for budget and program plan revisions when there is a change in the scope or the objective of the project or program, even if there is no associated budget revision requiring prior written approval.

Pursuant to 2 CFR part 230, Appendix B, §§ 8.b(2) and 8.m, for salaries and wages to be allowable for Federal reimbursement, grantees must maintain personnel activity reports of the actual activity for each employee working on Federal awards. These reports must be signed by the employee or a supervisory official having firsthand knowledge of the employee's activities, be prepared at least monthly, coincide with one or more pay periods, and account for the total activity of the employee.

Expenditures for the Capital Improvement Program Grant

Hudson River claimed unallowable CIP grant expenditures totaling $260,586. Specifically, Hudson River claimed $92,229 for general purpose equipment purchases that were not approved by HRSA and exceeded its approved budget for certain items by $168,357 without HRSA approval.

Expenditures Not Approved by HRSA

Contrary to 2 CFR part 230, Appendix B, § 15.b, Hudson River made $92,229 in general purpose equipment purchases that were not approved by HRSA (the awarding agency). Specifically, Hudson River purchased a cabling upgrade related to its voice over Internet protocol (VoIP) system ($73,188) and a vehicle, a 2008 Nissan Altima Hybrid ($19,041). These purchases were not in Hudson River's HRSA-approved budget and Hudson River did not receive prior approval from HRSA before making these purchases. Therefore, the $92,229 claimed was not allowable for Federal reimbursement.[2]

These unallowable claims occurred because Hudson River did not properly comply with its policies and procedures for determining the allowability of costs claimed to Federal grants. Hudson River stated that it believed it had HRSA approval for the cabling upgrade related to its VoIP system and did not believe that prior approval was needed for the vehicle purchase.

Expenditures that Exceeded the Approved Budget

Contrary to 45 CFR 74.25 (b), Hudson River exceeded its approved budget by $168,357 without prior approval from HRSA. Specifically, Hudson River exceeded its HRSA-approved budget by $137,678 for a VoIP system, $14,040 for cabinetry at its Beacon site, $8,539 for helpdesk software, and $8,100 for cabinetry at its New Paltz site.

These unallowable claims occurred because Hudson River did not properly comply with its policies and procedures for determining the allowability of costs claimed to Federal grants. Specifically, Hudson River did not know approval was required for budget deviations. Hudson River stated that it was unaware that budget deviations below 25 percent of its budgeted amount required approval from the awarding agency prior to purchase.[3]

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[2] We also noted that the Nissan Altima Hybrid was assigned to the Assistant Vice President of Clinical Operations and Facilities Management and was used for both work and personal reasons, including transportation to and from work. Therefore, the vehicle was also unallowable under 2 CFR pt. 230 App. B § 8.h.

[3] The 25 percent rule that Hudson River referred to is listed in the terms and conditions on pages 15 and 16 of the CIP Notice of Grant Award, dated June 25, 2009, and is an additional requirement that applies to significant rebudgeting of project costs where there are transfers of funds between cost categories exceeding 25 percent or $250,000 (whichever is less) of the total approved budget. If some or all of the rebudgeting reflects a change in scope, prior approval is required, even if the transfers are below the 25-percent or $250,000 threshold (45 CFR § 74.25).

Expenditures for the Increased Demand for Services Grant

Contrary to 2 CFR part 230, Appendix B, §§ 8.b(2) and 8.m, Hudson River did not adequately document $19,972 in salary costs that it charged to the IDS grant; therefore, these costs were unallowable. While Hudson River generally maintained personnel activity reports for its employees, as required by Federal regulations, it failed to charge the IDS grant the correct amount reflected on two employees' activity reports. As a result, Hudson River overcharged its IDS grant a total of $14,115 in salary costs related to the two employees. In addition, Hudson River could not provide supporting documentation for one employee's salary charge of $5,857.

These unallowable claims occurred because Hudson River did not properly comply with its policies and procedures for determining the allowability of costs claimed to Federal grants. Specifically, Hudson River did not follow its procedures for time and effort certification, which required that "supervisors, with firsthand knowledge of employee's activities ... sign each report, attesting after the time is incurred, to the accuracy of the time allocated to each grant, and that 100 percent of the employee's time has been allocated."

RECOMMENDATIONS

We recommend that HRSA:

- require Hudson River to refund $280,558 to the Federal Government ($260,586 related to the CIP grant and $19,972 related to the IDS grant) and

- ensure that Hudson River follows its policies and procedures for determining the allowability of costs claimed to Federal grants.

HUDSON RIVER HEALTHCARE, INC., COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE

In written comments on our initial draft report, Hudson River disagreed with several of our findings based on its interpretation of Federal regulations and guidance on prior approval that, according to Hudson River, it received from HRSA. After reviewing Hudson River's comments and consulting with HRSA officials, we removed one finding and corresponding recommended disallowance of $25,115 related to cabinetry purchases that Hudson River made under the CIP grant. We maintain that our findings and recommendations in this report are valid. Hudson River's comments are included in their entirety as Appendix A.

Capital Improvement Program Grant Expenditures Not Approved by HRSA

Hudson River Comments

Hudson River stated that a cabling upgrade ($73,188) related to its VoIP system was identified as part of its approved award budget. Specifically, Hudson River stated that the budget justification submitted in its CIP application, which it provided under separate cover as part of a package of additional documentation, indicated that it proposed using $75,000 for a VoIP system in addition to separate line items for equipment related to the VoIP system. In addition, Hudson River concurred with our finding regarding the Nissan Altima Hybrid vehicle purchase ($19,041).[4]

Office of Inspector General Response

After reviewing the additional documentation that Hudson River provided with its response and consulting with HRSA officials, we maintain that the cabling upgrade was not in Hudson River's original budget or approved by HRSA.[5] According to Hudson River's CIP application, the proposed budget contained two line items related to the VoIP system, totaling $175,000–the actual VoIP system ($75,000) and handsets for the VoIP system ($100,000). The $73,188 cabling upgrade was in addition to these approved amounts.

Capital Improvement Program Grant Expenditures That Exceeded the Approved Budget

Hudson River Comments

Hudson River stated that prior approval was not required for any of the expenditures that we determined were in excess of its approved budget. Hudson River stated that, according to its interpretation of 45 CFR §§ 74.25(c) and (f), none of the situations requiring prior approval related to the situations described in our findings. Hudson River further stated that no additional Federal funds were used for these expenditures and that prior approval was sought and obtained from HRSA to delete the medical van from the budget and repurpose those funds to other equipment purchases where the costs were over budget. Hudson River provided documentation of these communications with HRSA under separate cover as part of its package of additional documentation.

Office of Inspector General Response

After reviewing the additional documentation that Hudson River provided with its response and consulting with HRSA officials, we maintain that our findings and recommendations are valid. While Hudson River requested approval to repurpose medical van funds on May 18, 2011, in addition to a no-cost extension request, HRSA approved only the no-cost extension on June 24, 2011. HRSA did not require grantees to obtain prior approval for budget revisions of less than 25 percent or $250,000 (whichever is less) as long as the approved scope of work of the project did not change. However, HRSA officials confirmed that the removal of the medical van purchase from the CIP grant project—which supported the increased costs of the purchases listed in our findings described in the "Expenditures that Exceeded the Approved Budget" section of this report (page 4)—would have required prior review and approval because it was a change in the scope of work of the project (45 CFR §§ 74.25(c) and (f)).

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[4] In its comments, Hudson River also stated that cabinetry purchases totaling $25,115, which we questioned in our initial draft report, were approved by HRSA. HRSA officials confirmed that prior approval for the purchases were provided in emails between HRSA and Hudson River; however, we were not aware of these approvals at the time of our fieldwork. Consequently, we removed the finding and corresponding recommended disallowance from our report.

[5] HRSA officials confirmed that the cabling aspect of the VOIP project required prior approval.

Increased Demand for Services Grant Expenditures

Hudson River concurred with our finding regarding the inadequately documented salary costs charged to the IDS grant.

HEALTH RESOURCES AND SERVICES ADMINISTRATION COMMENTS

In written comments on our second draft report—which included Hudson River's written comments on our initial draft report—HRSA concurred with our recommendations. Specifically, HRSA stated that it will work with Hudson River to determine if any CIP or IDS grant funds need to be refunded to the Federal government. HRSA also stated that it will work with Hudson River to ensure that the grantee adheres to its policies and procedures for determining the allowability of costs claimed to Federal grants. HRSA's comments are included in their entirety as Appendix B.

OTHER MATTER: EMPLOYEE SALARIES AND PRESIDENT AND CHIEF EXECUTIVE OFFICER BONUSES

According to its IDS grant application, Hudson River planned to subsidize the salaries of approximately 16 full-time equivalent employees (FTEs) with Recovery Act funds.[6] Of the 16 FTEs, approximately 7 were to be new hires so that Hudson River could expand its services. In its application, Hudson River stated: "Due to the economic crisis, Hudson River has been forced to make some tough decisions around cost savings and has implemented salary reductions and was preparing to lay-off 9 essential health center employees. ... IDS funding will allow Hudson River to retain these 9 positions and preserve our existing successful clinical infrastructure and outreach model."

During our fieldwork we confirmed that Hudson River subsidized the salaries of 16 FTEs with IDS grant funds. We also learned, through discussions with management, that Hudson River was in a very positive cash position and was able to wait several months before drawing down Federal funds to pay for its IDS grant expenditures. As of December 31, 2008—prior to receiving the Recovery Act grants—Hudson River had a cash balance of $664,342, an operating income before depreciation of $443,978, and a net cash flow of $447,152. As of December 31, 2009, Hudson River had a cash balance of approximately $5 million, an operating income before depreciation of approximately $3.9 million, and a net cash flow of approximately $4.3 million. Finally, as of December 31, 2010, Hudson River had a cash balance of approximately $6.4 million, an operating income before depreciation of approximately $3.8 million, and a net cash flow of approximately $1.4 million.

Despite the economic crisis—and the salary reductions Hudson River stated that it implemented—its president and chief executive officer received significant bonuses during 2009 and 2010. In 2009, the first year Recovery Act funds were awarded, she received a bonus

[6] The requirement for reporting jobs is based on a simple calculation used to avoid overstating the number of other than full-time, permanent jobs. The FTE calculation converts part-time or temporary jobs into "full-time equivalent" (FTE) jobs. The number of FTEs is calculated as total hours worked in jobs created or retained divided by the number of hours in a full-time schedule, as defined by the recipient.

totaling $87,816. In 2010, she received a bonus totaling $126,000. We noted that, during 2007 and 2008, she did not receive any bonuses. These bonuses were not paid directly from Recovery Act grant funds; however, rather than using Recovery Act funds to subsidize some of the essential health center employees that it stated would be laid-off due to the economic crisis, Hudson River could have used the bonus money paid to its president and chief executive officer to subsidize these essential employees.

APPENDIXES

APPENDIX A: HUDSON RIVER HEALTHCARE, INC., COMMENTS

communityhealth
Hudson River HealthCare

EXCELLENCE
DEDICATION
COMMUNITY

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August 20, 2012

Mr. James P. Edert
Regional Inspector General for Audit Services
Department of Health and Human Services
Office of Inspector General
Jacob K. Javits Federal Building
26 Federal Plaza, Room 3900
New York, NY 10278

Re: A-02-11-02014

Dear Mr. Edert:

Enclosed please find Hudson River HealthCare, Inc.'s, written response to the U.S. Department of Health and Human Services, Office of Inspector General (OIG) draft report titled Claimed Unallowable Federal Grant Expenditures.

If you have any questions you may contact my office at (914) 734-8747 or anolon@hrhcare.org

Sincerely,

Anne K. Nolon, MPH
President and CEO

Enclosure

Cc: John J. Madigan

Hudson River Healthcare ("HRHCare") is in receipt of the U.S. Department of Health and Human Services, Office of Inspector General's ("OIG's") draft audit report number A-02-11-02014 entitled "Hudson River Healthcare, Inc., Claimed Unallowable Federal Grant Expenditures" dated July 16, 2012.

The subject audit covered two federal awards from the Health Resources and Services Administration ("HRSA") – one under the Capital Improvement Program ("CIP"), and the other under the Increased Demand for Services ("IDS") progam. The CIP award was in the amount of $1,994,540.00 to support improvements to certain HRHCare facilities, upgrades to HRHCare information technology and communications systems, and purchase of a mobile medical unit. The IDS award was in the amount of $917,282.00 to support existing staff compensation and hiring of new staff. The OIG audit reviewed CIP expenditures from June 29, 2009 through June 30, 2012, and IDS expenditures from March 27, 2009 through March 26, 2011.

The draft audit report recommends that HRSA disallow a total of $305,673.00, consisting of $285,701.00 in charges to HRHCare's CIP grant and $19,972.00 in costs under the IDS award. The recommended disallowance of CIP expenditures relates to alleged equipment purchases and costs in excess of the award budget without prior agency approval. The IDS recommendation is in connection with amounts overcharged to the award and lack of documentation to support certain salary charges.

HRHCare responds to the draft report recommendations as follows:

DISCUSSION

I. *Expenditures Not Approved by HRSA*

Finding:

The draft report indicates that HRHCare "purchased a cabling upgrade related to its voice over Internet protocol (VoIP) system ($73,188), cabinetry ($25,115) and a vehicle, a 2008 Nissan Altima Hybrid ($19,041)" without either including those purchases in the approved grant budget or seeking HRSA authorization to incur those expenses. *See* Draft Report at 4. According to the OIG, HRHCare thus violated 2 C.F.R. Part 230, App. B, § 15.b. *Id.* Part 230 of title 2 of the Code of Federal Regulations is the codification of Office of Management and Budget ("OMB") Circular A-122, which sets out the cost principles applicable to awards of financial assistance to not-for-profit organizations. The subsection to which the draft report refers provides that "[c]apital expenditures for general purpose equipment, buildings, and land are unallowable as direct charges, except where approved in advance by the awarding agency." *See* 2 C.F.R. Part 230, App. B, § 15.b.(1).

Response:

As to the VoIP expenses, the OIG is incorrect in asserting that the equipment was not identified as part of an approved award budget.

The budget justification that HRHCare submitted in its application for CIP funds under HRSA Announcement No. HRSA-09-244 clearly shows that HRHCare proposed to use $75,000.00 for "Voice Over Internet Protocol Phone System to create call center and maximize network communications." *See* Att. A. This is in addition to separate line items in the equipment category providing for purchase of other computer hardware and peripherals relating to the VoIP system. *Id.* The "Voice Over IP Telecommunications System" line item in the approved budget would therefore encompass infrastructure improvements (such as cabling upgrades) necessary to the implementation of the VoIP system.

The OIG is similarly mistaken in characterizing the cabinetry costs either as "general purpose equipment" purchases or as unapproved expenditures. The cost principles define "equipment" as "an article of nonexpendable, tangible *personal property* having a useful life of more than one year" and having an acquisition cost above a certain threshold. *See* 2 C.F.R. Part 230, App. B, § 15.a.(2) (emphasis added). Although Part 230 itself contains no definition of "personal property," the uniform administrative requirements applicable to HHS awards to not-for-profit entities state that personal property is "property of any kind except real property." *See* 45 C.F.R. § 74.2. "Real property," in turn, consists of "land, including land improvements, structures and appurtenances thereto, but excludes *movable machinery and equipment*." *Id.* (emphasis added).

Contrary to the statement in the draft report, cabinetry is properly viewed as real property rather than as equipment. This is so because cabinets are fixtures to the structures in which they reside. They are therefore not "movable machinery [or] equipment," but are instead improvements incorporated into HRHCare facilities. Accordingly, any prior approval requirement that might attach to HRHCare's use of grant funds for cabinetry would be under 2 C.F.R. Part 230, App. B, § 15.b.(3), which provides that "[c]apital expenditures for improvements to land, buildings, or equipment which materially increase their value or useful life are unallowable as a direct cost except with the prior approval of the awarding agency."

HRHCare did, in fact, have prior agency approval of the questioned cabinetry costs. HRHCare understands that the $25,115.00 charge to which the draft report refers relates to cabinets installed as part of the renovation of the internal medicine department at HRHCare's Peekskill facility. The revised approved budget for the Peekskill project included $250,000.00 under the "construction" cost category. *See* Att. B. The budget justification provided to HRSA sought general authorization to use CIP funds for improvements to the internal medicine portion of the facility, including "minor renovations required for electrical, plumbing, HVAC, fixed equipment, interior finishes, etc." *Id.* The cost of materials and labor associated with installation of cabinets at the Peekskill site falls within this description of the "construction" cost category in the approved budget. There is therefore no basis on which to conclude that the cabinetry costs lacked any necessary HRSA approval(s).

As to the recommended disallowance of $19,041.00 associated with the purchase of a 2008 Nissan Altima Hybrid, HRHCare agrees with the finding and acknowledges the lack of transportation logs for the vehicle. HRHCare is currently reviewing its motor pool and personal use policies and practices and will take appropriate action(s) upon completion of that review.

II. *Expenditures that Exceeded the Approved Budget*

Finding:

The draft report further states that, "[c]ontrary to 45 CFR 74.25 (b), Hudson River exceeded its approved budget by $168,357 without prior approval from HRSA." *See* Draft Report at 4. The $168,357.00 figure consists of alleged cost overruns in the following amounts: (1) $137,678.00 for the VoIP system; (2) $14,040.00 for cabinetry at HRHCare's Beacon site; (3) $8,539.00 for helpdesk software; and (4) $8,100.00 for cabinetry at HRHCare's New Paltz facility. *Id.* According to the OIG, "[t]hese unallowable claims occurred because Hudson River did not properly comply with its policies and procedures for determining the allowability of costs claimed to federal grants," and, more precisely, because "Hudson River did not know approval was required for budget deviations." *Id.*

Response:

This finding is without merit.

No prior approval requirement of the breadth described by the OIG exists. The portion of the uniform administrative requirements cited in the draft report, 45 C.F.R. § 74.25(b), provides that awardees "are required to report deviations from budget and program plans, and request prior approvals for budget and program plan revisions, *in accordance with this section.*" 45 C.F.R. § 74.25(b) (emphasis added).

The "in accordance with this section" qualification refers, in the case of non-construction awards, to the eight circumstances enumerated under 45 C.F.R. § 74.25(c). For construction awards, a grantee must obtain prior agency approval where one or more of the three conditions listed in 45 C.F.R. § 74.25(f) are met. Unless a rebudgeting gives rise to one of the situations under 45 C.F.R. § 74.25(c) or (f), an awardee is free to implement that rebudgeting without first obtaining approval from the grantor agency.

None of the relevant conditions is present here, and HRHCare's expenditure of the questioned $168,357.00 is therefore proper. Only two of those conditions – changes in project scope or objective, and need for additional federal funding – have any conceivable bearing given the nature of the OIG's concerns, but not even those two conditions apply in this matter. The extent to which HRHCare exceeded the budgeted amounts under any of the line items identified by the OIG did not create a need for more federal funds, nor did it entail a transfer of funds among cost categories that would comprise a change in project scope. HRHCare consulted with HRSA regarding whether it needed to obtain prior approval in order to reallocate CIP dollars from one funded project to another. *See* Att. C. Consistent with the HHS Grants Policy Statement, HRSA advised HRHCare that agency approvals for such budget actions were necessary only if the cumulative changes exceeded 25% of the total award budget. *Id.*

What is more, in the one instance where HRHCare eliminated a relatively high value budget line item and moved those funds to another project, HRHCare sought and obtained HRSA approval. HRHCare budgeted $175,000.00 for the VoIP project and $65,000.00 in federal funds (out of a budgeted $250,000.00) for a medical van. *See* Att. A. However, the anticipated matching funds for the mobile medical unit project did not materialize, while other line items in the "equipment" category for the communications/information technology project proved to be more expensive than HRHCare had budgeted. HRHCare therefore sought a no cost extension from HRSA that would allow HRHCare to delete the medical van from the budget and to repurpose those funds to the other equipment purchases where the costs were over budget. *See* Att. D. The request was approved. *See* Att. E.

In light of the above, the questioned costs are allowable.

III. *Expenditures for the Increased Demand for Services Grant*

Finding:

The draft report indicates that "Hudson River did not adequately document $19,972 in salary costs that it charged to the IDS grant; therefore, these costs were unallowable." *See* Draft Report at 5. Of that $19,972.00, $14,115.00 related to charges for compensation to two employees that were in excess of what the employees' personnel activity reports reflected. *Id.* The remaining $5,857.00 related to salary costs for which there was no supporting documentation. *Id.*

Response:

HRHCare has a comprehensive policy for tracking and documenting time and effort of employees. HRHCare endeavors to ensure 100% compliance with its existing policy. The time and effort process is regularly reviewed by grant funders and HRHCare auditors. HRHCare acknowledges the errors cited by the OIG report and does not dispute this finding.

IV. *Other Matter: Employee Salaries and President and Chief Executive Officer Bonuses*

This portion of the draft report contains no findings or recommendations, but instead consists of various observations concerning (1) HRHCare's financial position immediately prior to and during the IDS award period, and (2) bonus compensation to HRHCare's chief executive officer ("CEO") in 2009 and 2010. *See* Draft Report at 5-6.

Because this discussion has no bearing on the findings and recommendations elsewhere in the draft report, and otherwise lacks any independent relevance, it warrants no response and HRHCare respectfully requests that it be removed from the final audit report.

That said, HRHCare maintains that compensation paid to its CEO during the relevant time period – and, for that matter, all time periods – was in keeping with HRHCare's duly approved and legally sound policies and procedures.

CONCLUSION

HRHCare appreciates the opportunity to provide the above responses to the OIG's draft audit report. Should the OIG have any questions, comments, or concerns regarding these responses, we stand ready to provide any additional information that the OIG may require.

APPENDIX B: HEALTH RESOURCES AND SERVICES ADMINISTRATION COMMENTS

DEPARTMENT OF HEALTH & HUMAN SERVICES

Health Resources and Services Administration

Rockville, MD 20857

TO: Inspector General

FROM: Administrator

SUBJECT: OIG Draft Report: "Hudson River HealthCare, Inc., Claimed Unallowable Federal Grant Expenditures" (A-02-11-02014)

Attached is the Health Resources and Services Administration's (HRSA) response to the OIG's draft report, "Hudson River HealthCare, Inc., Claimed Unallowable Federal Grant Expenditures" (A-02-11-02014). If you have any questions, please contact Sandy Seaton in HRSA's Office of Federal Assistance Management at (301) 443-2432.

Mary K. Wakefield, Ph.D., R.N.

Attachment

Health Resources and Services Administration's Comments on the OIG Draft Report – "Hudson River HealthCare, Inc. Claimed Unallowable Federal Grant Expenditures" (A-02-11-02014)

The Health Resources and Services Administration (HRSA) appreciates the opportunity to respond to the above draft report. HRSA's response to the Office of Inspector General (OIG) recommendations are as follows:

OIG Recommendation:

We recommend that HRSA ensure that Hudson River refunds $280,558 to the Federal Government ($260,586 related to the CIP grant and $19,972 related to the IDS grant).

HRSA Response:

HRSA concurs with OIG's recommendation. HRSA will work with Hudson River HealthCare, Inc., (Hudson River) to determine if any Capital Improvement Program or Increased Demand for Services grant funds need to be refunded to the federal government.

OIG Recommendation:

We recommend that HRSA ensure that Hudson River follows its policies and procedures for determining the allowability of costs claimed to Federal grants.

HRSA Response:

HRSA concurs with OIG's recommendation. HRSA will work with Hudson River to ensure that the grantee adheres to its policies and procedures for determining the allowability of costs claimed to federal grants.