

Department of Health and Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**NEW YORK DID NOT COMPLY  
WITH FEDERAL GRANT  
REQUIREMENTS FOR  
ALLOCATING AND  
CLAIMING MARKETPLACE  
CONTRACT COSTS**

*Inquiries about this report may be addressed to the Office of Public Affairs at  
[Public.Affairs@oig.hhs.gov](mailto:Public.Affairs@oig.hhs.gov).*



Gloria L. Jarmon  
Deputy Inspector General  
for Audit Services

December 2017  
A-02-15-02008

# *Office of Inspector General*

<https://oig.hhs.gov>

---

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.

## *Office of Evaluation and Inspections*

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.

## *Office of Investigations*

The Office of Investigations (OI) conducts criminal, civil, and administrative investigations of fraud and misconduct related to HHS programs, operations, and beneficiaries. With investigators working in all 50 States and the District of Columbia, OI utilizes its resources by actively coordinating with the Department of Justice and other Federal, State, and local law enforcement authorities. The investigative efforts of OI often lead to criminal convictions, administrative sanctions, and/or civil monetary penalties.

## *Office of Counsel to the Inspector General*

The Office of Counsel to the Inspector General (OCIG) provides general legal services to OIG, rendering advice and opinions on HHS programs and operations and providing all legal support for OIG's internal operations. OCIG represents OIG in all civil and administrative fraud and abuse cases involving HHS programs, including False Claims Act, program exclusion, and civil monetary penalty cases. In connection with these cases, OCIG also negotiates and monitors corporate integrity agreements. OCIG renders advisory opinions, issues compliance program guidance, publishes fraud alerts, and provides other guidance to the health care industry concerning the anti-kickback statute and other OIG enforcement authorities.

# *Notices*

---

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

Section 8M of the Inspector General Act, 5 U.S.C. App., requires that OIG post its publicly available reports on the OIG Web site.

## **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.

## Report in Brief

Date: December 2017

Report No. A-02-15-02008

U.S. DEPARTMENT OF HEALTH & HUMAN SERVICES  
**OFFICE OF INSPECTOR GENERAL**



### Why OIG Did This Review

The Patient Protection and Affordable Care Act provided establishment grants to States for establishing health insurance exchanges (commonly referred to as “marketplaces”) to allow individuals and small businesses to shop for health insurance.

New York contracted with Maximus, Inc., to operate its marketplace customer service center from June 2012 through March 2015. Maximus was contracted to provide assistance to New Yorkers seeking to enroll in a qualified health plan. New York allocated and claimed marketplace customer service center costs to its establishment grants.

This review is related to a prior review of establishment grants awarded to New York.

Our objective was to determine whether New York followed Federal requirements in allocating and claiming Maximus contract costs to its establishment grants.

### How OIG Did This Review

We reviewed \$39.8 million in contract costs for the period October 2014 through March 2015 that New York allocated to the establishment grants. We also reviewed \$17.6 million in profit fees and general and administrative costs for the period June 2012 through April 2014 that New York claimed to the establishment grants.

## New York Did Not Comply With Federal Grant Requirements for Allocating and Claiming Marketplace Contract Costs

### What OIG Found

New York did not always follow Federal requirements for allocating and claiming contract costs to its grants for establishing New York’s marketplace customer service center. Specifically, New York may have misallocated costs totaling nearly \$19.6 million and claimed unallowable profit fees and other costs totaling nearly \$3.8 million.

This occurred because New York did not have written policies that explained how to properly allocate costs when it developed its original cost allocation plan. Further, New York did not establish a basis for the profit fee rate with Maximus at the beginning of the contract, did not require Maximus to always use its final cost rate for general and administrative costs, and did not require Maximus to retroactively adjust the calculation of its profit fee and general and administrative costs by removing project costs that should not have been subject to these charges.

### What OIG Recommends and New York’s Comments

We recommend that New York (1) refund to CMS \$19.6 million that may have been misallocated to the establishment grants or work with CMS to determine the appropriate allocation to the grants, (2) refund to CMS \$797,096 in unallowable profit fees or work with CMS to determine the appropriate amount that should have been claimed to the grants, (3) refund to CMS \$32,083 in unallowable general and administrative costs and related profit fees, and (4) work with CMS to ensure that Maximus contract costs claimed after our audit period are properly allocated.

In written comments on our draft report, New York generally disagreed with our recommendations. Specifically, New York stated that its method for allocating costs to the establishment grants was consistent with CMS-approved methodology and Federal guidance. New York also stated that the fact that different contract terms were negotiated for a subsequent period did not result in unallowable profit fees and general and administrative costs in prior periods.

After reviewing the State agency’s comments, we maintain that our findings and recommendations are valid. The State agency’s allocation formula included certain population groups (such as those enrolled in Medicare) that should not have been expected to use the New York marketplace’s health insurance plan. Also, profit fees and other costs claimed were not allowable.

## TABLE OF CONTENTS

INTRODUCTION .....	1
Why We Did This Review .....	1
Objective .....	1
Background .....	1
Patient Protection and Affordable Care Act .....	1
Federal Requirements Related to Cost Allocation and Contract Costs .....	2
Federal Funding for State-based Marketplaces.....	2
The New York Marketplace.....	2
How We Conducted This Review .....	3
FINDINGS.....	3
The State Agency Used a Cost Allocation Methodology That Included a Material Defect Despite the Availability of Updated Data .....	4
The State Agency Claimed Unallowable Profit Fees .....	6
The State Agency Claimed Unallowable General and Administrative Costs .....	8
RECOMMENDATIONS .....	10
STATE AGENCY COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE .....	11
APPENDICES	
A: Audit Scope and Methodology .....	12
B: State Agency Comments.....	14

## INTRODUCTION

### WHY WE DID THIS REVIEW

The Patient Protection and Affordable Care Act<sup>1</sup> provided grants to States for establishing health insurance exchanges (commonly referred to as “marketplaces”) to allow individuals and small businesses to shop for health insurance.

The New York State Department of Health (State agency) operates the New York State of Health (New York marketplace) and is responsible for complying with applicable establishment grant requirements.

A prior Office of Inspector General (OIG) review of establishment grants awarded to New York found that the State agency did not always follow Federal cost allocation requirements.<sup>2</sup> Specifically, the State agency allocated costs using a methodology that included a material defect and did not adjust its methodology when updated data on marketplace enrollment became available. This review focuses on costs allocated to establishment grants that were incurred by Maximus, Inc., under a contract with the State agency to operate a marketplace customer service center. (We refer to these costs as “contract costs” throughout the report.) We plan to separately review contract costs allocated to Medicaid and the Children’s Health Insurance Program (CHIP).

### OBJECTIVE

Our objective was to determine whether the State agency followed Federal requirements in allocating and claiming contract costs to its establishment grants.

### BACKGROUND

#### Patient Protection and Affordable Care Act

Within the Department of Health and Human Services’ (HHS) Centers for Medicare and Medicaid Services (CMS), the Center for Consumer Information and Insurance Oversight (CCIIO)<sup>3</sup> is responsible for implementing many of the requirements of the ACA, including

---

<sup>1</sup> P.L. No. 111-148 (Mar. 23, 2010), as amended by the Health Care and Education Reconciliation Act of 2010, P.L. No. 111-152 (Mar. 30, 2010), collectively referred to as “ACA.”

<sup>2</sup> *New York Misallocated Costs to Establishment Grants for a Health Insurance Marketplace* (A-02-14-02017, Nov. 21, 2016). Available at: <https://oig.hhs.gov/oas/reports/region2/21402017.asp>.

<sup>3</sup> To implement and oversee the ACA’s marketplace and private health insurance requirements, HHS established the Office of Consumer Information and Insurance Oversight (OCIIO) in April 2010 as part of the HHS Office of the Secretary. In January 2011, OCIIO was transferred to CMS to a new center named CCIIO (76 Fed. Reg. 4703 (Jan. 26, 2011)). In this report, we use “CCIIO” to refer to both OCIIO and CCIIO.

overseeing the implementation of provisions related to the marketplaces and the private health insurance plans offered through the marketplaces. These plans are known as qualified health plans (QHPs). Marketplaces perform many functions, including helping States to coordinate eligibility for enrollment in other State-based public health care programs, such as Medicaid and CHIP.

### **Federal Requirements Related to Cost Allocation and Contract Costs**

CCIO's Establishment Grant Funding Opportunity Announcements and the State agency's Notice of Grant awards terms and conditions require the State agency to allocate shared costs among Medicaid, CHIP, and the New York marketplace consistent with cost principles.<sup>4</sup> CMS provides additional guidance to States that is specific to cost allocation for the marketplaces in *Guidance for Exchange and Medicaid Information Technology (IT) Systems* (version 2.0, May 2011) and *Supplemental Guidance on Cost Allocation for Exchange and Medicaid Information Technology (IT) Systems* (issued Oct. 2012).

The HHS Grants Policy Statement (GPS), incorporated by reference in the terms and conditions of the Notice of Grant awards, says that the State agency is accountable for the appropriate expenditure of establishment grant funds by all parties, including its contractors (HHS GPS, I-37). In addition, 45 CFR § 74.27(a) states that the allowability of costs incurred by commercial organizations is determined in accordance with the provisions of the Federal Acquisition Regulation at 48 CFR part 31.

### **Federal Funding for State-based Marketplaces**

The ACA provided funding to a State for the planning and establishment of a marketplace that incorporates eligibility determination and enrollment functions for all consumers of participating programs, such as Medicaid and private health insurance offered through a marketplace (ACA § 1311).

### **The New York Marketplace**

New York chose to establish and operate its own State-based marketplace. Because the New York marketplace provides eligibility determination and enrollment services for both QHPs and its State-based public health care programs, such as Medicaid, it sought funding from various Federal sources that provided benefits for these programs. Additionally, the State agency developed methodologies for allocating costs related to customer support services to the benefitting programs.

---

<sup>4</sup> Office of Management and Budget (OMB) Circular No. A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, was relocated to 2 CFR part 225 and made applicable by 45 CFR § 92.22(b). After our audit period, OMB consolidated and streamlined its guidance, which is now located at 2 CFR part 200. HHS has codified the guidance in regulations found at 45 CFR part 75.

In June 2012, the State agency amended an existing Maximus contract to expand a centralized State-wide Medicaid and CHIP enrollment center to include marketplace customer services to New Yorkers seeking to enroll in a QHP. The State agency allocated \$141.7 million in customer services contract costs to the establishment grants for the period June 2012 through March 2015.

## **HOW WE CONDUCTED THIS REVIEW**

We reviewed \$39,794,647 in contract costs for the period October 2014 through March 2015 that the State agency allocated to the establishment grants. We also reviewed \$17,644,569 in profit fees<sup>5</sup> and general and administrative (G&A) costs for the period June 2012 through April 2014 that the State agency claimed to the grants.<sup>6</sup>

We limited our review of internal controls to the systems and procedures for allocating and claiming costs to establishment grants and to Medicaid. We obtained an understanding of how the State agency's cost allocation methodologies were developed, used updated data to calculate the amounts that should have been allocated to the establishment grants, and assessed the impact of allocating costs using estimated versus updated data. We recalculated allowable profit fees and G&A costs by applying Maximus' operating profit margin and final G&A rate to allowable project costs.

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 objectives.

Appendix A contains the details of our audit scope and methodology.

## **FINDINGS**

The State agency did not always follow Federal requirements for allocating and claiming contract costs to its establishment grants. Specifically, the State agency:

- may have misallocated contract costs totaling \$19,586,165 using a cost allocation methodology that included a material defect,

---

<sup>5</sup> Profit fees are payments made to a contractor that are in addition to the reimbursement of expenses to allow for a profit.

<sup>6</sup> The Maximus contract contains a clause stating that the contractor will maintain complete and accurate records pertinent to performance under the contract, and authorized entities will have access to those records. The OIG has authority to conduct an examination of these records because the State agency allocated the contract costs to the establishment grants awarded by CMS.

- claimed unallowable profit fees totaling as much as \$3,411,777, and
- claimed unallowable G&A costs and related profit fees totaling \$388,469.

This occurred because the State agency did not have written policies that explained how to develop a Cost Allocation Plan (CAP) based on relative benefits received, did not establish a basis for the profit fee rate with Maximus at the beginning of the contract, and did not require Maximus to always use its final cost rate for G&A costs. Further, the State agency did not require Maximus to retroactively adjust the calculation of its profit fees and G&A costs by removing project costs that should not have been subject to these charges.

### **THE STATE AGENCY USED A COST ALLOCATION METHODOLOGY THAT INCLUDED A MATERIAL DEFECT DESPITE THE AVAILABILITY OF UPDATED DATA**

For a cost to be allowable, it must be allocable to a Federal award (2 CFR part 225, Appendix A, § C.1). A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to that cost objective in accordance with the relative benefits received (2 CFR part 225, Appendix A, § C.3).

CMS guidance published in May 2011 requires that costs be allocated among Medicaid, CHIP, and the marketplace for services or functions that include customer service support. Furthermore, CMS guidance requires prospective adjustments based on updated or better data; however, it is silent on adjusting allocated costs retrospectively when an error was used as the basis for the determination of program cost allocation (CMS's *Guidance for Exchange and Medicaid Information Technology (IT) Systems* (version 2.0)).

States must also establish CAPs that identify, measure, and allocate costs to each State-operated program (45 CFR part 95, subpart E). The Division of Cost Allocation (DCA)<sup>7</sup> provides final approval of the allocation methodology percentages for Medicaid and the establishment grants in the CAP. A State must promptly amend its CAP if there are significant changes in program levels or a material defect is discovered in its CAP (45 CFR §§ 95.509(a)(1) and (2)). The effective date of the required modification is retroactive to the date of the original approval (45 CFR § 95.515). If a State agency fails to submit an amended CAP when a material defect is discovered, the costs improperly claimed will be disallowed (45 CFR § 95.519).

The State agency used a cost allocation methodology that included a material defect. The State agency allocated contract costs totaling \$56,849,496 to the establishment grants and Medicaid for the period October 2014 through March 2015 on the basis of faulty estimates. Specifically, the State agency estimated that 30 percent of the State population would use the marketplace

---

<sup>7</sup> The State is required to submit a CAP to the Director of DCA in the appropriate HHS Regional Office (45 CFR § 95.507(a)). HHS is designated by OMB as the cognizant Federal agency for reviewing and negotiating public assistance CAPs. DCA is currently known as Cost Allocation Services (CAS) and resides within the HHS Program Support Center.

to enroll in Medicaid and that the remaining 70 percent of the State population would use the marketplace to enroll in a QHP. These allocation percentages were identified in the establishment grant applications approved by CMS and subsequently DCA-approved CAP, effective February 2011.

However, as described in our prior review, we found that the State agency's allocation methodology included a material defect. Specifically, we found that the State agency used a population-based methodology that assumed the entire population of New York would use the marketplace to enroll in a health insurance plan. However, the marketplace only made eligibility determinations and enrolled individuals for certain population groups, not the entire population of New York.

We found that the marketplace's enrollment estimates differed significantly from enrollment data available to the State agency. As of April 1, 2014, actual enrollment data showed that 59 percent of enrollees selected Medicaid or CHIP—nearly twice the State agency's initial estimate—while the remaining 41 percent selected a QHP. Further, in December 2014, in conjunction with awarding the State agency a new establishment grant, CCIIO approved a cost allocation methodology that was developed using projected marketplace enrollment data.<sup>8</sup> Under the new cost allocation methodology, Maximus contract costs were to be allocated based on estimates that 70 percent of the enrollment population would enroll in Medicaid or CHIP and 30 percent of the enrollment population would enroll in a QHP. The State agency subsequently submitted to CAS a CAP with this cost allocation methodology for the newly awarded grant. CAS approved the CAP effective January 1, 2015. The State agency did not use this cost allocation methodology to allocate contract costs for establishment grants that were previously awarded because it received instructions from CCIIO to continue to use the original CAP for those grants. However, because the original CAP contained a material defect, the State agency should have amended the CAP and adjusted the allocation of contract costs to these establishment grants.

We re-calculated the allocation of the contract costs to the establishment grants using the updated enrollment data as of April 1, 2014, and the approved cost allocation methodology effective January 1, 2015. We found that the State agency may have misallocated contract costs totaling \$19,586,165 to the establishment grants in accordance with the relative benefits received by the program, as shown in Table 1 (next page). This occurred because the State agency did not have written policies that explained how to properly allocate costs when it developed its original CAP. The State agency based its original allocation methodology (that it continued to use throughout our audit period) on the assumption that the marketplace would potentially provide benefits to all New Yorkers seeking health coverage.

---

<sup>8</sup> The State agency used projected Medicaid, CHIP, and QHP enrollment data, and did not include the entire population of New York. Therefore, this methodology does not contain the material defect noted in the original methodology.

**Table 1: Claimed and Updated Allocation of Contract Costs to Establishment Grants  
(October 2014 Through March 2015)**

Period	Total Costs	State Agency's Claimed Allocation Percentages and Associated Costs		Establishment Grants Updated Allocation Percentages and Associated Costs		State Agency's Potentially Misallocated Costs
		Percentage	Associated Costs	Percentage	Associated Costs	
October – December 2014	\$28,669,398	70	\$20,068,579	41	\$ 11,754,453	\$8,314,126
January – March 2015	28,180,098	70	19,726,068	30	8,454,029	11,272,039
	<b>\$56,849,496</b>		<b>\$39,794,647</b>		<b>\$20,208,482</b>	<b>\$19,586,165</b>

The State agency may seek CMS approval to claim a portion of the \$19,586,165 through Medicaid at Federal fiscal participation rates ranging from 50 percent to 90 percent. Our calculation of potentially misallocated contract costs does not include the impact of the State agency using the cost allocation methodology with the material defect on costs claimed after our audit period ended (March 31, 2015).

**THE STATE AGENCY CLAIMED UNALLOWABLE PROFIT FEES**

A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person in the conduct of competitive business (48 CFR § 31.201-3(a)). What is reasonable depends on a variety of considerations and circumstances, including generally accepted sound business practices and any significant deviations from the contractor's established practices (48 CFR § 31.201-3(b)).

Indirect costs that meet the definition of an "excessive pass-through charge" are unallowable (48 CFR § 31.203(i)). Excessive pass-through charges are charges to the Government for indirect costs or profit on work performed by a contractor that adds no or negligible value to a contract (48 CFR § 52.215-23(a)).

The State agency claimed unallowable profit fees. Specifically, the State agency's contract with Maximus provided for payment of a profit fee calculated by applying a fee percentage to project costs. However, the contract did not specify the fee percentage or the project costs to which the fee should be applied for the period June 2012 through April 2014. During this period, the State agency claimed profit fees to the establishment grants totaling \$10,838,575.<sup>9</sup>

<sup>9</sup> This amount does not include the unallowable profit fees related to the unallowable G&A costs discussed later in this report.

The profit fees were calculated by applying a profit fee rate of 17.65 percent to project costs, including travel and State agency office space costs.<sup>10</sup> However, there was no explanation as to what the profit fee rate was based on or how it was calculated. The State agency subsequently negotiated a profit fee for the period May 2014 through April 2015 based on Maximus' fiscal year profit margin. The State agency and Maximus also agreed that the profit fee rate would not be applied to pass-through costs such as travel and office space costs.

We re-calculated the profit fees for the period June 2012 through April 2014 by applying the appropriate period profit margin reported by Maximus<sup>11</sup> and excluding travel and office space costs, as detailed in Table 2 (next page). We found that the State agency claimed unallowable profit fees totaling as much as \$3,411,777 to the establishment grants. (Our related recommendation reflects that we questioned \$2,614,681 of this amount in our prior report referenced in footnote 2.)<sup>12</sup> This occurred because the State agency did not establish a basis for the profit fee rate or require Maximus to retroactively adjust the calculation of its profit fee charges by removing travel and office space costs, even though Maximus and the State agency subsequently agreed that those project costs should not have been subject to these charges.

---

<sup>10</sup> For the rest of the report, we will refer to these costs as office space costs.

<sup>11</sup> According to its annual report filed with the U.S. Securities and Exchange Commission, Maximus had a profit margin for its Health Services Segment of 13.2 percent for the period October 2010 through September 2011 and 12 percent for the period October 2011 through September 2012.

<sup>12</sup> As of July 2017, the prior audit findings have not been resolved.

**Table 2: OIG Re-calculation of Profit Fee Charges (June 2012 Through April 2014)**

Period	Maximus Calculation of Profit Fee Charges			OIG Re-calculation of Profit Fee Charges			Unallowable Costs (Difference)
	Project Costs Subject to Profit Fees	Profit Fee Rate	Profit Fee Charges	Project Costs Subject to Profit Fees	Profit Margin Percentage	Profit Fee Charges	
June 2012 – August 2013	\$18,920,956	17.65	\$3,339,549	\$18,380,072	13.20	\$2,426,169	\$913,380
September 2013 – April 2014	42,487,403	17.65	7,499,026	41,671,909	12.00	5,000,629	2,498,397
	<b>\$61,408,359</b>		<b>\$10,838,575</b>	<b>\$60,051,981<sup>13</sup></b>		<b>\$7,426,798</b>	<b>\$3,411,777<sup>14</sup></b>

**THE STATE AGENCY CLAIMED UNALLOWABLE GENERAL AND ADMINISTRATIVE COSTS**

Indirect costs that meet the definition of an “excessive pass-through charge” are unallowable (48 CFR § 31.203(i)). Excessive pass-through charges are charges to the Government for indirect costs or profit on work performed by a contractor that adds no or negligible value to a contract (48 CFR § 52.215-23(a)).

A base period for allocating indirect costs is the cost accounting period during which such costs are incurred and accumulated for the allocation of work performed during that period (48 CFR § 31.203(g)). Billing rates and final indirect cost rates shall be used in reimbursing indirect costs under cost-reimbursement contracts (48 CFR § 42.703-1(b)). Within 120 days after settlement of the final annual indirect cost rate, the contractor must submit an invoice or voucher reflecting the settled amounts and rates (48 CFR § 42.705(b)).

The State agency claimed unallowable G&A costs and related profit fees. Specifically, the State agency’s contract with Maximus did not specify the project costs to which the G&A rate should be applied for the period June 2012 through April 2014. Maximus developed G&A rates at the beginning of each fiscal year, which were used for provisional billing. Final G&A rates were developed after the conclusion of each fiscal year. The State agency claimed G&A costs to the establishment grants totaling \$6,747,715 from June 2012 through April 2014. Maximus calculated these costs by applying provisional and final rates to project costs, including travel

<sup>13</sup> The difference of \$1,356,378 between the project costs subject to profit fees calculated by Maximus and the project costs subject to profit fees calculated by the OIG consists of travel and office space costs.

<sup>14</sup> Of this amount, \$3,172,376 was attributed to the use of the operating profit margin to re-calculate the profit fee costs, and \$239,401 was attributed to the removal of the pass-through costs to re-calculate the profit fee costs.

and office space costs. But the State agency and Maximus subsequently agreed that the G&A rate should not be applied to pass-through costs such as travel and office space costs.

We re-calculated the G&A costs for the period June 2012 through April 2014 by applying the appropriate final G&A rate and excluding travel and office space costs, as detailed in Table 3 (next page). We found that the State agency claimed unallowable G&A costs totaling \$330,190 to the establishment grants. The profit fee charges related to these G&A costs totaled \$58,279.<sup>15</sup> Therefore, the unallowable G&A costs and related profit fees claimed to the establishment grants totaled \$388,469.<sup>16</sup> (Our related recommendation reflects that we questioned \$356,386 of this amount in our prior report referenced in footnote 2.)<sup>17</sup> This occurred because the State agency did not require Maximus to always use its final cost rate for G&A costs or require Maximus to retroactively adjust the calculation of its G&A costs by removing travel and office space costs, even though the State agency and Maximus subsequently agreed that these costs should not have been subject to G&A charges.

---

<sup>15</sup> G&A costs are subject to profit fees. Therefore, unallowable G&A costs would have related profit fees. We calculated the related profit fees by applying the profit fee rate of 17.65 percent to the unallowable G&A costs. The profit fees related to the unallowable G&A costs do not duplicate the unallowable profit fees discussed earlier in the report.

<sup>16</sup> Of this amount, \$181,182 is unallowable because Maximus did not use the final G&A rate for the period October 2012 through September 2013. The remaining \$207,287 is unallowable because Maximus did not remove pass-through costs for the period June 2012 through April 2014.

<sup>17</sup> As of July 2017, the prior audit findings have not been resolved.

**Table 3: OIG Re-calculation of General and Administrative Costs Plus Profit Fees  
(June 2012 Through April 2014)**

Period	Maximus Calculation of G&A Costs			OIG Re-calculation of G&A Costs			Unallowable Costs (Difference)
	Project Costs Subject to G&A	Applied G&A Rate	G&A Costs	Project Costs Subject to G&A	Final G&A Rate	G&A Costs	
June 2012 – September 2012	\$346,763	17.19	\$59,608	\$314,160	17.19	\$54,004	\$5,604
October 2012 – September 2013	19,674,965	14.20	2,793,845	19,012,442	13.39	2,545,766	248,079
October 2013 – April 2014	33,658,270	11.57	3,894,262	32,997,018	11.57	3,817,755	76,507
	<b>\$53,679,998</b>		<b>\$6,747,715</b>	<b>\$52,323,620<sup>18</sup></b>		<b>\$6,417,525</b>	<b>\$330,190</b>
<b>Related Unallowable Profit Fees</b>							<b>\$58,279</b>
<b>Total Unallowable G&amp;A and Related Profit Fees</b>							<b>\$388,469</b>

**RECOMMENDATIONS**

We recommend that the State agency:

- refund to CMS \$19,586,165 for costs that may have been misallocated to the establishment grants or work with CMS to determine the appropriate allocation to the grants,
- refund to CMS \$797,096 for unallowable profit fees or work with CMS to determine the appropriate amount that should have been claimed to the grants,
- refund to CMS \$32,083 for unallowable G&A costs and related profit fees, and
- work with CMS to ensure that Maximus contract costs claimed after our audit period are properly allocated.

<sup>18</sup> The difference of \$1,356,378 between the project costs subject to G&A costs calculated by Maximus and the project costs subject to G&A costs calculated by the OIG consists of travel and office space costs.

## **STATE AGENCY COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE**

In written comments on our draft report, the State agency generally disagreed with our recommendations. Specifically, the State agency stated that its method for allocating costs to the establishment grants was consistent with CMS-approved methodology and Federal guidance. The State agency maintained that its cost allocation formula reasonably reflected the distribution of the State population that would benefit from the marketplace.<sup>19</sup> Further, the State agency stated that it complied with CMS instructions to continue using the original cost allocation methodology for previously awarded establishment grants.

The State agency also disagreed with our findings that it claimed unallowable profit fees and G&A costs. The State agency stated that the fact that different contract terms were negotiated for a subsequent period did not result in unallowable costs in prior periods.

After reviewing the State agency's comments, we maintain that our findings and recommendations are valid. The State agency's allocation formula included certain population groups (such as those enrolled in Medicare) that should not have been expected to use the New York marketplace to enroll in a health insurance plan. Therefore, because the original allocation methodology contained a material defect, the State agency should have amended this methodology and adjusted the allocation of contract costs to previously awarded establishment grants.

We maintain that the unallowable profit fees and G&A costs claimed by New York are excessive pass-through charges that are not allowable for Federal reimbursement. Further, the State agency's original contract terms with Maximus did not specify a profit fee rate or what such a rate should be or was based on. Therefore, the State agency has no basis to establish that the profit fee costs were reasonable, as required by Federal regulations. Finally, the final G&A rate was not applied for the period October 2012 through September 2013, as required by Federal regulations.

The State agency's comments are included in their entirety as Appendix B.

---

<sup>19</sup> The State agency maintained throughout its comments that it allocated costs in accordance with the approved methodology, Federal rules, and CMS guidance. In response to our recommendation that it work with CMS to ensure that Maximus contract costs claimed after our audit period are properly allocated (the fourth recommendation), the State agency stated that it will continue to work with CMS to ensure that costs claimed in future periods "are also correctly allocated." We do not believe that this constitutes a concurrence or non-concurrence with the recommendation.

## APPENDIX A: AUDIT SCOPE AND METHODOLOGY

### SCOPE

We reviewed \$39.8 million in contract costs for the period October 2014 through March 2015 that the State agency allocated to the establishment grants. We also reviewed \$17.6 million in profit fees and G&A costs for the period June 2012 through April 2014 that the State agency claimed to the establishment grants. We limited our review of internal controls to the systems and procedures for allocating and claiming costs to establishment grants and to Medicaid.

We conducted our fieldwork at the State agency's offices in Albany, New York, from June 2015 through February 2017.

### METHODOLOGY

To accomplish our objective, we:

- reviewed applicable Federal laws, regulations, and guidance;
- reviewed the State agency's establishment grant application packages and grant award notices;
- reviewed the State agency's policies and procedures for the financial management of the contract;
- reviewed the contract, contract amendments, and task orders to gain an understanding of the contract deliverables, terms and conditions, and costs associated with the contract;
- obtained State agency expenditure general ledger reports for August 2011 through June 2015;
- reconciled the general ledger reports to Federal financial reports submitted by the State agency to CMS to determine whether the general ledger reports were accurate and complete;
- obtained vouchers submitted by Maximus to the State agency for the period June 2012 through March 2015;
- reconciled the voucher amounts to the general ledger reports to verify that the contract costs were allocated and claimed to the establishment grants;

- re-calculated the amounts that should have been allocated to the establishment grants for the period October 2014 through March 2015 using updated data;
- determined the amount that was misallocated to the establishment grants as a result of the State agency not adjusting its allocation methodology and prospectively re-calculating its allocation percentages using updated data;
- reviewed Maximus' methodology for charging profit fees and G&A costs;
- reviewed Maximus' annual report submitted to the U.S. Securities and Exchange Commission to identify the operating profit margins for its Health Services Segment for the years ended September 30, 2012, and 2013;
- re-calculated Maximus' profit fees for the period June 2012 through April 2014 by excluding travel and office space costs and applying the appropriate profit margin;
- determined the amount of unallowable profit fees that were claimed to the establishment grants;
- reviewed Maximus' independent accountant reports for the financial and compliance review of the final G&A rates for the years ended September 30, 2013, 2014, and 2015;
- re-calculated the G&A costs for the period June 2012 through April 2014 by excluding travel and office space costs and applying the final G&A rate;
- determined the amount of unallowable G&A costs and related profit fees claimed to the establishment grants; and
- discussed the results of our review with State agency officials.

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 objectives.

## APPENDIX B: STATE AGENCY COMMENTS



ANDREW M. CUOMO  
Governor

Department  
of Health

HOWARD A. ZUCKER, M.D., J.D.  
Commissioner

SALLY DRESLIN, M.S., R.N.  
Executive Deputy Commissioner

October 19, 2017

Ms. Brenda Tierney  
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-02-15-02008

Dear Ms. Tierney:

Enclosed are the New York State Department of Health's comments on the United States Department of Health and Human Services, Office of Inspector General's Draft Audit Report A-02-15-02008 entitled, "New York Did Not Comply with Federal Grant Requirements for Allocating and Claiming Marketplace Contract Costs."

Thank you for the opportunity to comment.

Sincerely,

*Sally Dreslin*

Sally Dreslin, M.S., R.N.  
Executive Deputy Commissioner

Enclosure

cc: Marybeth Hefner  
Donna Frescatore  
Danielle Holahan  
Jason Helgerson  
Elizabeth Misa  
James Dematteo  
James Cataldo  
Diane Christensen  
Lori Conway  
OHIP Audit SM

---

Empire State Plaza, Corning Tower, Albany, NY 12237 | [health.ny.gov](http://health.ny.gov)

**New York State Department of Health  
Comments on the  
Department of Health and Human Services  
Office of Inspector General  
Draft Audit Report A-02-15-02008 entitled  
“New York Did Not Comply with Federal Grant Requirements for  
Allocating and Claiming Marketplace Contract Costs”**

---

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 (OIG) Draft Audit Report A-02-15-02008 entitled, "New York Did Not Comply with Federal Grant Requirements for Allocating and Claiming Marketplace Contract Costs."

**Recommendation #1:**

Refund to CMS \$19,586,165 for costs that may have been misallocated to the establishment grants or work with CMS to determine the appropriate allocation to the grants.

**Response #1:**

This is a repeat finding of OIG Audit Report A-02-14-02017 which pertained to a different audit period. We disagree with the report's recommendation because it is based on the incorrect conclusion that adjustments to actual enrollment data should have been made earlier.

As stated in our response to OIG Audit Report A-02-14-02017, we continue to disagree that the allocation methodology included a material defect. The allocation formula, which was established in advance of the implementation of the Marketplace, reasonably reflected the distribution of the state population that would benefit from the Marketplace. The method and supporting data was submitted to CMS and approved. As such, no retroactive amendment of the Cost Allocation Plan (CAP) or refund of grant funding to Centers for Medicare and Medicaid Services is required.

Specifically, the method used to allocate \$39,794,647 to exchange grants was consistent with the approved methodology and federal guidance in effect related to the timing of updates to the enrollment projections that are used in the allocation formulas. In September 2014, CMS issued guidance to state-based Marketplaces that requires them to update cost allocation methodologies when seeking additional federal funds using actual enrollment numbers when available (<https://www.cms.gov/CCIIO/Resources/Fact-Sheets-and-FAQs/index.html#Exchange>).

New York complied with this guidance when requesting additional grant funding in October 2014 (HBEIE150208). In addition, on October 22, 2014 coincident with requests to extend the project period for existing grants HBEIE120106, HBEIE120124, and HBEIE130146, New York requested guidance from CMS about cost allocation methodologies:

"Specifically, we need to confirm that grant funding that has been awarded will continue under the previously approved cost allocation methodology, even through no cost extension periods."

In response, on November 4, 2014 CMS confirmed the continued use of the original cost allocation methodology during an extension period:

"Cost allocation is not retrospective; it is prospective with new funding requests. A *no cost* extension is not new funding. It is using existing approved funds to continue to finish up activities that took longer than expected."

Based on this direction, we continued to use the cost allocation formulas as approved by CMS. (Documentation of our October 22, 2014 request and CMS' November 4, 2014 response was provided to the auditors during Audit A-02-14-02017.)

**Recommendation #2:**

Refund to CMS \$797,096 for unallowable profit fees or work with CMS to determine the appropriate amount that should have been claimed to the grants.

**Response #2:**

The Department disagrees that the profit fees claimed are unallowable. The fact that different contract terms were negotiated for a subsequent period does not result in unallowable costs in the previous periods.

**Recommendation #3:**

Refund to CMS \$32,083 for unallowable G&A costs and related profit fees.

**Response #3:**

The Department disagrees that the general and administrative costs and related profit fees claimed are unallowable. The fact that different contract terms were negotiated for a subsequent period does not result in unallowable costs in the previous periods.

**Recommendation #4:**

Work with CMS to ensure that Maximus contract costs claimed after our audit period are properly allocated.

**Response #4:**

The Department maintains that costs for the audit period were correctly allocated and in accordance with the approved methodology, federal rules and CMS guidance. We will continue to work with CMS to ensure that costs claimed in future periods are also correctly allocated in accordance with the approved methodology, federal rules, and CMS guidance.