



April 15, 2011

TO: Donald M. Berwick, M.D.
Administrator
Centers for Medicare & Medicaid Services

FROM: /George M. Reeb/
Acting Deputy Inspector General for Audit Services

SUBJECT: Review of Medicaid Reimbursement Rates for School-Based Services in West Virginia (A-03-05-00203)

Attached, for your information, is an advance copy of our final report on our review of Medicaid reimbursement rates for school-based services in West Virginia. We will issue this report to the West Virginia Department of Health and Human Resources within 5 business days. We conducted this review at the request of the Centers for Medicare & Medicaid Services' regional office in Philadelphia.

If you have any questions or comments about this report, please do not hesitate to contact me at (410) 786-7104 or through email at George.Reeb@oig.hhs.gov or Stephen Virbitsky, Regional Inspector General for Audit Services, Region III, at (215) 861-4470 or through email at Stephen.Virbitsky@oig.hhs.gov. Please refer to report number A-03-05-00203.

Attachment



Office of Audit Services, Region III
Public Ledger Building, Suite 316
150 S. Independence Mall West
Philadelphia, PA 19106-3499

April 21, 2011

Report Number: A-03-05-00203

Mr. Warren D. Keefer
Deputy Secretary for Administration
West Virginia Department of Health and Human Resources
1 Davis Square, Suite 300
Charleston, WV 25301

Dear Mr. Keefer:

Enclosed is the U.S. Department of Health & Human Services (HHS), Office of Inspector General (OIG), final report entitled *Review of Medicaid Reimbursement Rates for School-Based Services in West Virginia*. 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.

Section 8L of the Inspector General Act, 5 U.S.C. App., requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at <http://oig.hhs.gov>.

If you have any questions or comments about this report, please do not hesitate to call me, or contact Robert Baiocco, Audit Manager, at (215) 861-4486 or through email at Robert.Baiocco@oig.hhs.gov. Please refer to report number A-03-05-00203 in all correspondence.

Sincerely,

/Stephen Virbitsky/
Regional Inspector General
for Audit Services

Enclosure

Direct Reply to HHS Action Official:

Ms. Jackie Garner
Consortium Administrator
Consortium for Medicaid and Children's Health Operations
Centers for Medicare & Medicaid Services
233 North Michigan Avenue, Suite 600
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Department of Health & Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REVIEW OF MEDICAID REIMBURSEMENT
RATES FOR SCHOOL-BASED SERVICES IN
WEST VIRGINIA**



Daniel R. Levinson
Inspector General

April 2011
A-03-05-00203

Office of Inspector General

<http://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

The Medicaid Program

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.

Section 1903(c) of the Act permits Medicaid payment for medical services provided through a child's individualized education plan under the Individuals with Disabilities Education Act (originally enacted as P.L. No. 91-230 in 1970). Pursuant to 42 CFR § 430.10, to receive Federal funding a State must claim the cost of medical assistance in accordance with its approved State plan.

West Virginia's School-Based Program

In West Virginia, the Department of Health and Human Resources' Bureau for Medical Services (the State agency) administers the Medicaid program. In 2000, the State agency created rates for seven Medicaid school-based health services (school-based services) provided by local education agencies. The State agency used State fiscal year (FY) 1999 salaries and fringe benefits of local education agency employees who provided school-based services to calculate the rates. The State agency received \$33.6 million (Federal share) for local education agency services provided for State FYs 2001 through 2003.

In 2002, the State agency contracted with a consulting firm, Public Consulting Group, Inc. (PCG), on a contingency fee basis. PCG proposed to add two new cost components to the rates for school-based services, operating and indirect costs, and to update those rates by using State FY 2001 data for salaries and fringe benefits. PCG recommended that the State agency submit a retroactive claim for these costs for FYs 2001 through 2003. The State agency submitted a retroactive claim in September 2003. In June 2005, the State agency made further adjustments to its calculations and submitted a second retroactive claim.

The State agency received an additional \$39.4 million (Federal share) for these two retroactive claims. The total amount claimed for State FYs 2001 through 2003 for school-based services was \$73 million (Federal share). The State agency paid PCG a contingency fee of \$2.4 million but did not claim the fee as a Federal reimbursable expense. Another report (A-03-06-00201) determined that \$2.3 million (Federal share) of the retroactive claim for September 2003 fell outside the required 2-year filing limit. We excluded the \$2.3 million from this report and based the effect of any findings on the total payments of \$70.7 million (Federal share) in school-based services claimed for State FYs 2001 through 2003.

CMS requested that we determine the allowability of the cost components of the rates used to claim the seven school-based services.

OBJECTIVE

Our objective was to determine whether the State agency complied with the approved State plan when it calculated the rates for school-based services.

SUMMARY OF FINDINGS

The State agency did not fully comply with the approved State plan. The State agency included costs in the calculation of its rates for school-based services that were not included in the reimbursement methodology described in the approved State plan.

These errors occurred because the State agency did not provide adequate oversight of PCG during the rate calculation process. We deducted the unallowable costs and recalculated the rates based on the reimbursement methodology described in the State agency's approved State plan. The State agency received reimbursements totaling \$70,713,963 (Federal share). Using our recalculated rates, we allowed \$47,907,733 (Federal share) of the total payments. The \$22,806,230 (Federal share) difference represents an overpayment.

RECOMMENDATIONS

We recommend that the State agency:

- refund \$22,806,230 to the Federal Government for unallowable costs included in reimbursement for school-based services for claims for State FYs 2001 through 2003,
- work with CMS to determine the unallowable costs included in reimbursement rates for State FYs 2004 to the present and make the appropriate refund, and
- work with CMS in developing more accurate school-based service rates and make necessary revisions to the State plan.

STATE AGENCY COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE

In written comments on our draft report, the State agency did not concur with our findings and recommendations. In response to the first recommendation, the State agency said that it "believes that operating and indirect costs were claimed in accordance with the State plan." In response to the second recommendation, the State agency said it has tried to work with CMS to determine the allowability of specific cost items but that CMS never responded. The State agency's comments appear in their entirety as Appendix D.

Nothing in the State agency's comments has made us change our recommendations or our conclusion that the State agency included costs in the calculation of its rates for school-based

services that were not included in the reimbursement methodology described in the approved State plan.

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INTRODUCTION

BACKGROUND

The Medicaid Program and Applicable Federal Requirements

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.

Pursuant to 42 CFR § 430.10, to receive Federal funding, a State must claim the cost of medical assistance in accordance with its approved State plan.

Medicaid Coverage of School-Based Services

Section 1903(c) of the Act permits Medicaid payment for medical services provided through a child's individualized education plan under the Individuals with Disabilities Education Act (originally enacted as P.L. No. 91-230 in 1970). Under the Act, States are permitted to claim Federal Medicaid reimbursement for health-related services and administrative costs for school-based activities. CMS's *Medicaid and School Health: A Technical Assistance Guide* (August 1997) (CMS's Technical Guide) states that school health-related services included in a child's individualized education plan may be covered if all relevant statutory and regulatory requirements are met. In establishing payment rates, States may use the rates already established or develop unique payment rates for school-based providers using statistically accurate and valid data to justify the rate amounts.

West Virginia's School-Based Program

In West Virginia, the Department of Health and Human Resources' Bureau for Medical Services (the State agency) administers the Medicaid program. West Virginia's Federal medical assistance percentage is approximately 75 percent. Based on its memorandum of understanding with the State agency, the State Department of Education (Department of Education) provides school-based health services through each of its 57 local education agencies, which are primarily county boards of education.

The State plan distinguishes between therapy services, including speech, occupational, and physical therapy, that are provided by individual practitioners and school-based health and related services (school-based services) that are provided by local education agencies.

The State Agency's Reimbursement Methodology

In 2000, the State agency submitted to CMS¹ State plan amendment (SPA) 00-01 describing a reimbursement methodology to claim six school-based services. The State plan described a fee-for-service reimbursement methodology, which paid providers interim rates and stated that “[c]osts [are] not to exceed actual, reasonable costs and must be cost settled on an annual basis.” To calculate rates using the reimbursement methodology, the State agency used State fiscal year (FY) 1999 data that was based solely on contractual salaries and fringe benefits of eight occupational categories of local education agency employees who provided school-based services. After consulting with State officials, CMS approved SPA 00-01 effective January 1, 2000. The State agency subsequently separated the costs for personal aides for full-time and part-time services, which increased the number of Medicaid school-based rates to seven:

- W3080: Individualized Education Plan (IEP)—Initial/Triennial Development
- W3081: Individualized Education Plan—Annual Update
- W3084: Personal Care Aide—Full Day
- W3085: Personal Care Aide—Half Day
- W3086: Specialized Transportation—Vehicle
- W3087: Specialized Transportation—Aide
- W3089: Care Coordination

From July 1, 2000, through June 30, 2003, the State agency received \$33,599,094 (Federal share) based on claims paid in accordance with the approved reimbursement methodology described in SPA 00-01.

The State Agency's Use of a Consultant To Increase Rates

In 2002, the State agency contracted with a consulting firm, Public Consulting Group, Inc. (PCG), on a contingency fee basis. PCG proposed to update the seven rates for school-based services by adding two new cost components: operating and indirect costs. (See Appendixes A and B.) These costs did not represent salary and fringe benefit costs historically used to calculate the State agency's rates for school-based services under the approved reimbursement methodology. PCG also proposed to update the rates by using State FY 2001 data in support of salaries and fringe benefit costs. PCG recommended that the State agency submit a retroactive claim to recoup these costs for State FYs 2001 through 2003.

The State agency accepted PCG's proposal and submitted a retroactive claim in September 2003. In June 2005, the State agency made further adjustments to its calculations and submitted a second retroactive claim. The State agency received an additional \$39,413,198 (Federal share) for these two retroactive claims. The total amount claimed for State FYs 2001 through 2003 for school-based services was \$73,012,292 (Federal share). The State agency paid PCG a contingency fee of \$2,414,297 but did not claim the fee as a federally reimbursable expense.

¹ Before June 2001, CMS was known as the Health Care Financing Administration.

CMS requested that we determine the allowability of the cost components of the rates used to claim the seven school-based services.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to determine whether the State agency complied with the approved State plan when it calculated the rates for school-based services.

Scope

We reviewed the State agency's seven school-based rates used to claim total payments of \$73,012,292 (Federal share) for State FYs 2001 through 2003 (July 1, 2000, through June 30, 2003). Another report determined that \$2,298,329 (Federal share) of the retroactive claims for State FY 2001 fell outside the required 2-year filing limit.² Therefore, we excluded the \$2,298,329 (Federal share) from this report and based the effect of any findings on the total payments of \$70,713,963 (Federal share).

To calculate the State agency's seven school-based rates, PCG used local education agency cost data. We segregated the local education agency cost data of \$3,848,527,723 for State FYs 2001 through 2003 into four categories—operating costs, indirect costs, salaries, and fringe benefits—and applied the State agency's approved reimbursement methodology as described in SPA 00-01.

We did not review the overall internal control structure of the State agency or the Medicaid program. We limited our review to those controls related to the State agency's methodology for calculating the rates and determining subsequent reimbursement.

We performed our fieldwork at the State agency offices in Charleston, West Virginia.

Methodology

To accomplish our objective, we:

- reviewed the applicable Federal and State Medicaid laws, regulations and guidance;
- reviewed relevant sections of the Medicaid State plan, PCG's contract with the State agency, the State agency's memorandum of understanding with the Department of Education, and other relevant State documentation related to school-based services;
- held discussions with CMS officials about the State agency's methodology in relation to the State plan, as well as their concerns with the rates the State agency used to claim Medicaid reimbursement;

² *Review of Timeliness of West Virginia's Retroactive Claims for Medicaid School-Based Services*, A-03-06-00201, issued April 14, 2009.

- interviewed State agency and Department of Education officials to gain an understanding of the State’s school-based program and how the State agency processed Medicaid claims for school-based services;
- analyzed and compared PCG’s revised reimbursement methodology to the State Agency’s reimbursement methodology approved by CMS in SPA 00-01;
- reviewed the Medicaid paid claims database consisting of 1,366,379 school-based service units for the State agency’s retroactive claims for State FYs 2001 through 2003;
- analyzed \$3,848,527,723 in local education agency costs to determine if they complied with the approved State plan and Federal requirements;
- removed unallowable local education agency costs from the rate calculation identified in our analysis of PCG’s reimbursement methodology and recalculated the seven school-based service rates in accordance with the State agency’s approved State plan; and
- applied our recalculated rates to the school-based service units claimed for State FYs 2001 through 2003.

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

The State agency did not fully comply with the approved State plan. The State agency included costs in the calculation of its rates for school-based services that were not included in the reimbursement methodology described in the approved State plan.

These errors occurred because the State agency did not provide adequate oversight of PCG during the rate calculation process. We deducted the unallowable costs and recalculated rates based on the reimbursement methodology described in the State agency’s approved State plan. The State agency received reimbursements totaling \$70,713,963 (Federal share). Using our recalculated rates, we allowed \$47,907,733 (Federal share) of the total payments. The \$22,806,230 (Federal share) difference represents an overpayment.

STATE DID NOT COMPLY WITH STATE PLAN

Federal and State Plan Requirements

Pursuant to 42 CFR § 430.10, States may claim Federal funding for the cost of medical assistance only in accordance with their approved State plans.

West Virginia's SPA 00-01, Attachment 4.19-B, which CMS approved on May 12, 2000, amended the State plan to define the reimbursement methodology for school-based services.

SPA 00-01 provided that reimbursement for personal care, assessment and treatment planning, and care coordination services "shall be fee-for-service. Reimbursement for interim rates are based on statewide historical costs." The SPA further limits reimbursement to "[c]osts not to exceed actual, reasonable costs and must be settled on an annual basis."

Costs Not in State Plan Included in the Rate Calculations

The State agency included costs in the calculation of its rates for school-based services that were not included in the reimbursement methodology described in the approved State plan. For 3 years, from July 1, 2000, through June 30, 2003, the State agency received Federal funding based on claims submitted using reimbursement rates based solely on salaries and fringe benefits of local education agency employees in eight occupational categories that the State agency identified as providing benefit to the program.³

In September 2003, the State agency submitted a retroactive claim for school-based services based on a rate-setting methodology proposed by the State agency's new consultant, PCG.⁴ The revised rates added two new cost categories, operating and indirect costs, to the rate calculations. For our audit period, operating costs and indirect costs totaled \$2,044,377,965. Historically, the State agency's interpretation of the reimbursement methodology described in the State plan did not include operating or indirect costs. Accordingly, inclusion of these costs in the reimbursement methodology was in violation of the State plan as interpreted by the State and approved by CMS.

Operating Costs

For our audit period, operating costs included in the calculations of the revised reimbursement rate totaled \$1,234,998,063. These costs included supplies, rental costs, maintenance and repair costs, and related capital and debt service costs. PCG used these costs to calculate an operating rate by dividing each local education agency's total operating costs by the local education agency's total salaries and fringe benefit costs. We identified the operating rate for all occupational categories reported by each local education agency and excluded the resulting operating costs from our rate calculations because they did not conform with the State plan as originally interpreted by the State agency.

³ The eight occupational categories included individualized education plan coordinator (also referred to as a Student Assistance/IEP leader), special education teacher, psychologist, nurse, speech/language pathologist, personal care aide, bus driver, and bus aide.

⁴ In a previous report (A-02-06-00201), we disallowed the portion of the claim that exceeded the 2-year limit for filing claims.

Indirect Costs

For our audit period, indirect costs, including general school administration and support functions such as business services and facility operations, totaled \$809,379,902. The indirect cost rates, approved by the Department of Education, were calculated by each local education agency by dividing its indirect costs by total local education agency costs. PCG applied the indirect cost rates to the average annual salaries, fringe benefits, and operating costs of each occupational category for each local education agency. We excluded the resulting indirect costs from our rate calculations because they did not conform with the State plan as originally interpreted by the State agency.

OFFICE OF INSPECTOR GENERAL CALCULATED OVERPAYMENTS

The State agency did not provide adequate oversight of PCG during the rate calculation process. As a result, the school-based rates included operating costs and indirect costs that were not included in the reimbursement methodology described in the approved State plan.

Of the \$3,848,527,723 in local education agency costs, we identified and excluded \$2,044,377,965 in unallowable costs in the rate components: \$1,234,998,063 in operating costs and \$809,379,902 in indirect costs. We applied the State agency's methodology to the allowable local education agency costs of \$1,804,149,758 to recalculate the rates for the seven school-based services and the appropriate Federal share for State FYs 2001 through 2003.

Based on our audited rates (listed in Appendix C), the State agency received overpayments totaling \$22,806,230 (Federal share). The table summarizes these overpayments.

Payments (Federal Share) Not Questioned and Questioned

| State FY | Units Paid | Total Payments | Payments Not Questioned | Payments Questioned |
|---------------------|-----------------------|---------------------------|--|--------------------------------|
| 2001 | 354,209 | \$16,137,951 | \$13,168,437 | \$2,969,514 |
| 2002 | 516,655 | 26,850,016 | 17,016,134 | 9,833,882 |
| 2003 | 495,515 | 27,725,996 | 17,723,162 | 10,002,834 |
| Total | 1,366,379 | \$70,713,963 | \$47,907,733 | \$22,806,230 |

RECOMMENDATIONS

We recommend that the State agency:

- refund \$22,806,230 to the Federal Government for unallowable costs included in reimbursement for school-based services for claims for State FYs 2001 through 2003,
- work with CMS to determine the unallowable costs included in reimbursement rates for State FYs 2004 to the present and make the appropriate refund, and

- work with CMS in developing more accurate school-based service rates and make necessary revisions to the State plan.

STATE AGENCY COMMENTS

In written comments on our draft report, the State agency did not concur with our findings and recommendations. In response to the first recommendation, the State agency said that it “believes that operating and indirect costs are actual and reasonable costs incurred by the State in providing the services in question and therefore were claimed in accordance with the State plan.” In response to the second recommendation, the State agency said it has tried to work with CMS to determine the allowability of specific cost items but that CMS never responded.

The State agency’s comments appear in its entirety as Appendix D.

OFFICE OF INSPECTOR GENERAL RESPONSE

Nothing in the State agency’s comments has made us change our recommendations or our conclusion that the State agency included costs in the calculation of its rates for school-based services that were not included in the reimbursement methodology described in the approved State plan.

APPENDIXES

**APPENDIX A: EXAMPLE OF REIMBURSEMENT METHODOLOGY FOR
SCHOOL-BASED SERVICES—PROCEDURE CODE W3080**

Procedure code W3080: Individualized Education Plan—Initial/Triennial Development includes the services of an Individualized Education Plan coordinator, a special education teacher, a psychologist, a nurse, and a speech/language therapist. The following example illustrates the Public Consulting Group, Inc. (PCG), hourly rate calculation for an Individualized Education Plan (IEP) coordinator (coordinator) for the Berkeley County local education agency and the subsequent calculation of the school-based service rate for State fiscal year (FY) 2001:

- PCG calculated that the local education agency paid \$4,003,957 to all its coordinators. Based on 112.8 full-time equivalent employees, the average annual salary totaled \$35,496.
- PCG applied a fringe benefit rate of 32.43 percent to the average annual salary of \$35,496, adding \$11,512 in fringe benefit costs. The salary and fringe benefits totaled \$47,008.
- PCG applied an operating rate of 27.12 percent to the \$47,008 salary and fringe benefits, adding \$12,748 in operating costs. The salary, fringe benefits, and operating costs totaled \$59,756.
- PCG applied an indirect cost rate of 10.17 percent to the total salary, fringe benefits, and operating costs of \$59,756, adding \$6,077 in indirect costs. The average annual salary, fringe benefits, operating costs, and indirect costs for the coordinator totaled \$65,833. PCG called this the “annual fully loaded individual cost.”
- PCG divided the annual fully loaded individual cost of \$65,833 by 1,400 hours (per school year) to calculate a fully loaded hourly rate of \$47.02.
- PCG multiplied the fully loaded hourly rate of \$47.02 by 6.02 percent¹ to calculate a weighted hourly fully loaded rate of \$2.83 for the Berkeley County local education agency.
- PCG added the weighted hourly rate for an individualized education plan coordinator in Berkeley County (\$2.83) to the weighted hourly rates for all other local education agencies that provided data to calculate a statewide hourly rate of \$45.70.
- PCG repeated this process for those local education agencies that provided data for all occupational categories included in code W3080. PCG multiplied the statewide hourly rate of \$45.70 by the 3.63 estimated hours used to calculate the individualized education plan coordinator’s cost of \$165.89.

¹ For the local education agencies that provided data to the State agency for State FY 2001, 6.02 percent of special education students were from Berkeley County.

- PCG made similar calculations for each of the other four occupational categories participating in the individualized education plan development for a total cost of \$657.94 per unit of service.

W3080: Individualized Education Plan—Initial/Triennial Development

| Occupational Category | A Weighted Average Hourly Rate | B Average Hours SAT² Process | C Average Hours Evaluations | D Average Hours IEP³ Meeting | E Total Staff Hours (B+C+D) | F Total Dollars per IEP (A×E) |
|---|---|--|--|--|--|--|
| IEP Coordinator Special Education Teacher | \$45.70 | 1.63 | 0 | 2.00 | 3.63 | \$165.89 |
| Psychologist | 46.03 | 1.13 | 1.67 | 1.50 | 4.30 | 197.95 ⁴ |
| Nurse | 58.34 | 1.38 | 2.25 | 0 | 3.63 | 211.78 ⁵ |
| Speech/Language Therapist | 45.86 | 1.00 | 0 | 0 | 1.00 | 45.86 |
| | 48.63 | 0 | 0.75 | 0 | 0.75 | 36.47 |
| Total | | | | | | \$657.94⁶ |

² The Student Assistance Team (SAT) process includes the IEP coordinator (e.g., principal), special education teacher, psychologist, and nurse.

³ The IEP meeting, or IEP development, includes the IEP coordinator and special education teacher.

⁴ The \$197.95 is a correct amount; the difference of \$0.02 is due to rounding.

⁵ The \$211.78 is a correct amount; the difference of \$0.01 is due to rounding.

⁶ The \$657.94 is a correct amount; the difference of \$0.01 is due to rounding.

APPENDIX B: REIMBURSEMENT METHODOLOGY FOR SCHOOL-BASED SERVICES—TRANSPORTATION RATES

To create rates for the two transportation services, W3086 (Specialized Transportation—Vehicle) and W3087 (Specialized Transportation—Aide), PCG gathered cost information for (1) salaries and fringe benefits of the bus drivers and aides and (2) operating and indirect costs. PCG divided these costs by the number of students transported to compute the cost per student per year. PCG multiplied this annual cost by the county's percentage of special education students and divided the total by 180, the number of days in the school year, to compute a weighted average cost per daily round trip. For example, in State FY 2001, every day that a Medicaid beneficiary received specialized transportation in Berkeley County, the State agency reimbursed the local education agency \$24.76. If the beneficiary receiving specialized transportation also required the services of an aide, the local education agency received an additional \$19.83.

APPENDIX C: COMPARISON BETWEEN CLAIMED AND AUDITED RATES

The approved reimbursement methodology was similar to PCG’s proposed methodology except that it did not include operating or indirect costs.

| <u>Procedure Code</u> | <u>State FY</u> | <u>Claimed Rate</u> | <u>Audited Rate</u> | <u>Difference</u> |
|--|-----------------|---------------------|---------------------|-------------------|
| W3080 IEP— Initial/Triennial Development | 2001 | \$657.94 | \$456.22 | \$201.72 |
| | 2002 | 703.66 | 475.01 | 228.65 |
| | 2003 | 703.50 | 475.19 | 228.31 |
| W3081 IEP— Annual Update | 2001 | 160.45 | 111.90 | 48.55 |
| | 2002 | 171.97 | 116.55 | 55.42 |
| | 2003 | 171.73 | 116.40 | 55.33 |
| W3084 Personal Care Aide— Full Day | 2001 | 172.60 | 119.83 | 52.77 |
| | 2002 | 192.68 | 130.63 | 62.05 |
| | 2003 | 192.34 | 130.49 | 61.85 |
| W3085 Personal Care Aide— Half Day | 2001 | 86.30 | 59.91 | 26.39 |
| | 2002 | 96.34 | 65.32 | 31.02 |
| | 2003 | 96.17 | 65.24 | 30.93 |
| W3086 Specialized Transportation— Vehicle | 2001 | 24.76 | 21.67 | 3.09 |
| | 2002 | 26.77 | 14.04 | 12.73 |
| | 2003 | 26.32 | 13.79 | 12.53 |
| W3087 Specialized Transportation— Aide | 2001 | 19.83 | 17.17 | 2.66 |
| | 2002 | 22.86 | 12.49 | 10.37 |
| | 2003 | 22.90 | 12.48 | 10.42 |
| W3089 Care Coordination | 2001 | 91.85 | 63.97 | 27.88 |
| | 2002 | 98.41 | 66.60 | 31.81 |
| | 2003 | 98.25 | 66.51 | 31.74 |

APPENDIX D: STATE AGENCY COMMENTS



STATE OF WEST VIRGINIA
DEPARTMENT OF HEALTH AND HUMAN RESOURCES

Chief Financial Officer

Earl R. Tomblin
Governor

1 Davis Square
Suite 300
Charleston, WV 25301
Telephone Number (304) 558-5208 Fax: (304) 558-1003

Patsy A. Hardy, FACHE, MSN, MBA
Cabinet Secretary

November 15, 2010

Mr. Stephen Virbitsky
Regional Inspector General for Audit Services
Department of Health & Human Services
Office of Inspector General
150 S. Independence Mall West, Suite 316
Philadelphia, PA 19106-3499

Report Number: A-03-05-00203

Dear Mr. Virbitsky:

The West Virginia Department of Health and Human Resources (WVDHHR) has reviewed the Draft Report of the U.S. Department of Health & Human Services (DHHS), Office of Inspector General (OIG), entitled "Review of Medicaid Reimbursement Rates for School-Based Services in West Virginia", dated October 14, 2010.

Based on our analyses of the Draft, we do not concur with the finding and recommendations. Specifically, the Department believes that operating and indirect costs are actual and reasonable costs incurred by the State in providing the services in question and therefore were claimed in accordance with the State plan. Per discussions with you, the recommended refund leaves only salary and fringe benefits in the rates rather than actual, reasonable costs stated in the approved State Plan.

With respect to the second recommendation, the Department has tried to work with CMS to determine the allowability of specific cost items, as set forth in the attached letter seeking guidance from CMS dated February 14, 2005, to which CMS has never responded. In addition, in response to CMS's request, we have already agreed to work with it to amend our state plan to include a more thorough description of how actual, reasonable costs are determined for school based health services, as set forth in the attached letter dated August 10, 2010.

If you have any questions concerning the information contained in this letter, please contact Tara Buckner, Chief Financial Officer at (304) 558-5208.

Sincerely,

A handwritten signature in black ink, appearing to read "Warren B. Keefer".

Warren B. Keefer
Deputy Secretary for Administration

c Patsy A. Hardy, Secretary
Nancy V. Atkins, Commissioner



STATE OF WEST VIRGINIA
DEPARTMENT OF HEALTH AND HUMAN RESOURCES

Joe Manchin III
Governor

Martha Yeager Walker
Secretary

February 14, 2006

Ms. Susan Cuerdon
Associate Regional Administrator
Division of Medicaid and Children's Health
Public Ledger Building, Suite 216
150 South Independence Mall West
Philadelphia, PA 19106

Dear Ms. Cuerdon:

We appreciated the opportunity to discuss our current School Health Services (SHS) issues with Ted Gallagher, Fran McCullough, John Whalen and yourself during our conference call on February 2, 2006. In adherence to our understanding of the information we are to provide you, the purpose of this letter is to provide that information and address certain actions requiring immediate attention, including:

- 1) Adjustments to CMS-64 claiming for the July-September 2005 and October-December quarters to offset the impacts of incorrect data in SHS rate calculations.
- 2) Adjustments required to address potential errors in rate development for previous periods.
- 3) Resolution of specific issues of consistency in the application of the State's interpretation of the cost finding methodology described in its approved State Plan for SHS.

We appreciate your assurance of an expeditious review and response to these matters, so that we may proactively utilize your technical assistance to avoid major financial disruptions within our provider community.

Introduction – Incorrect Costs:

As discussed in our conference call regarding the Department of Health and Human Resources' (DHHR) retroactive adjustment for SHS, we identified certain costs that had been incorrectly included in the rates developed for the school health services, both at the settlement of the 2001-2003 fiscal years, and in the subsequent interim payments. DHHR and its consultants discovered the incorrect inclusion of these costs while reviewing and collecting documentation for the current SHS Audit being performed by the Department of Human

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Services (DHHS), Office of Inspector General (OIG). As per professional practice under Title XIX regulatory guidelines, DHHR disclosed these errors and made known its intent to voluntarily adjust prior claims for the corrected payment amounts, and to adjust current rates accordingly.

This direct disclosure led to our conference call on February 2. Based on understandings reached at that time, we agreed to adjust the most recently filed CMS-64 (quarter ending September 30, 2005) and the CMS-64 for the current quarter (quarter ending December 31, 2005) based on the revision of the SHS rates paid to schools to reflect costs net of those incorrectly included previously. Those amounts are \$620,686.11 and \$586,24.64 respectively (see Exhibit 1). It is our understanding that this voluntary adjustment, based on timely and open disclosure of identified cost errors, will preclude any deferral action at this time.

During the conference call, we also discussed DHHR's responsibility and intent to further adjust SHS rates, as well as to address any prior claims errors, based on consistent application and correct interpretation of our approved State Plan (SPA). Given the major budgetary and economic impact of both public education and Medicaid within our State, it is imperative that DHHR react proactively in addressing errors or changes in service funding mechanisms so as to avoid any potential catastrophic disruptions throughout the state-wide delivery system. Also, we are aware that the OIG has inferred that an alternative cost accounting technique may have been more appropriate in determining the Operating Rate component. For all of these reasons, we sought technical guidance from CMS, so that we may proactively identify and address any potential adjustments that must be made.

Specifically, we are requesting CMS guidance regarding which of two identified cost finding techniques better represent how DHHR should identify actual costs related to the Operating Rate component. This follows the "benefiting principles" concept under OMB A-87, Medicare Cost Principles, and Medicaid regulations. We have consistently maintained that our intent, as per the SPA, is to reimburse costs. Originally, DHHR utilized, as a conservative calculation, an "organizational-wide" cost finding approach for the Operating Rate. The OIG auditors have begun, on an item-by-item basis, to question each individual item utilized in the calculation, and to infer that a more "Individual Education Plan (IEP)-direct" calculation may be more appropriate. As will be noted below, this does NOT entail any change in methodology, but rather in the definition and application of the "benefiting principles" for cost finding/cost determination within the same rate methodology. Consequently, we seek your guidance as to how best to proceed at this point.

Brief History:

In July 2002, DHHR examined the Medicaid rates for SHS and determined that the interim rates were understated and not reflective of county school-board actual costs incurred in providing specific Medicaid services. The approved Medicaid State Plan (Section 9 – Attachment 4.19-B), details the reimbursement methodology for school health services (see

Exhibit 2). Under this approved State Plan, the cost-based reimbursement rate is calculated as a fee-for-service, such that:

"Reimbursement interim rates are based on statewide historical costs... Costs not to exceed actual, reasonable costs and must be cost settled on an annual basis".

Specifically, this SPA identified DHHR's direct intent, which has been demonstrated to incorporate the following:

- 1) Interim rates will be calculated based on historical costs, as identified, in accordance with Medicare Principles of Reimbursement.
- 2) The interim rates will be paid out as a "fee-for-service", as opposed to a percent of charges, per diem, etc., but in full accordance with Medicare Principles of Reimbursement.
- 3) The intent is to identify and pay actual costs, settling on an annual basis as per Medicare Principles of Reimbursement, with cost determination based on OMB A-87 allowable cost.
- 4) As per Medicaid regulatory practice, the "test of reasonableness" is contained within the methodology. Rather than identifying and settling the actual costs of each of the 55 providers (county school boards), the cost-based methodology determines a state-wide average rate per covered service.

The initial interim rates paid during the 2001-2003 fiscal years were based on SFY1999 data and omitted certain allowable costs (materials and supplies, interest on long-term debt, and other indirect costs, among others) permitted under OMB A-87 and Medicaid regulations. In significant part, these omissions were attributable to insufficient cost identification prior to the initial rate establishment due to limited history, as well as intentions to maintain a conservative (underestimated) approach prior to initial settlements. Because Medicaid reimbursement for these services is based on actual costs, the exclusion of these allowable expenditures understated considerably the true cost of providing services. A claim was made in September 2003 in the amount of \$32,567,351.85 based on the results of DHHR's examination of the SHS. This amount included a settlement for SFY2001 and interim adjustments to SFY2002 and SFY2003 rates for SHS. The files supporting these amounts have been supplied to the OIG and are available for CMS review. Transition issues with UNISYS have delayed subsequent settlements.

In March 2005, DHHR received notification that the DHHS OIG would be conducting an audit to determine if the methodology used to develop the school health services rates "was reasonable and in accordance with Federal regulations". The OIG began their review of the rate setting methodology in April 2005.

In May 2005, DHHR completed the settlements for SFY2002 and SFY2003 and made interim payments for SFY2004 in the amount of \$9,748,545.23. To date, SFY2004 through SFY2006 have not been cost settled.

Today, the OIG is still conducting its review of DHHR's methodology, cost finding techniques, and supporting documentation. The State is working hard to satisfy their requests for additional information including working directly with the county school boards to access source documentation supporting the cost settlements and rate calculations.

Cost Methodology:

As demonstrated by DHHR's SPA, it is our intent to reimburse the identified school health services on "actual, reasonable costs." In accordance with Medicare Principles and our consistent historical practice, the intent is to pay an interim rate based on historical costs, and to settle those costs on an annual basis. The test of reasonableness is applied through a state-wide weighted average used in determining the single reimbursement rate for each covered service, both on an interim and on a final basis. Consequently, all tests of reasonableness and upper limits requirements will be met.

As local government entities with multiple reporting and functional layers, costs are identified and segmented in three non-overlapping components for rate setting. These are:

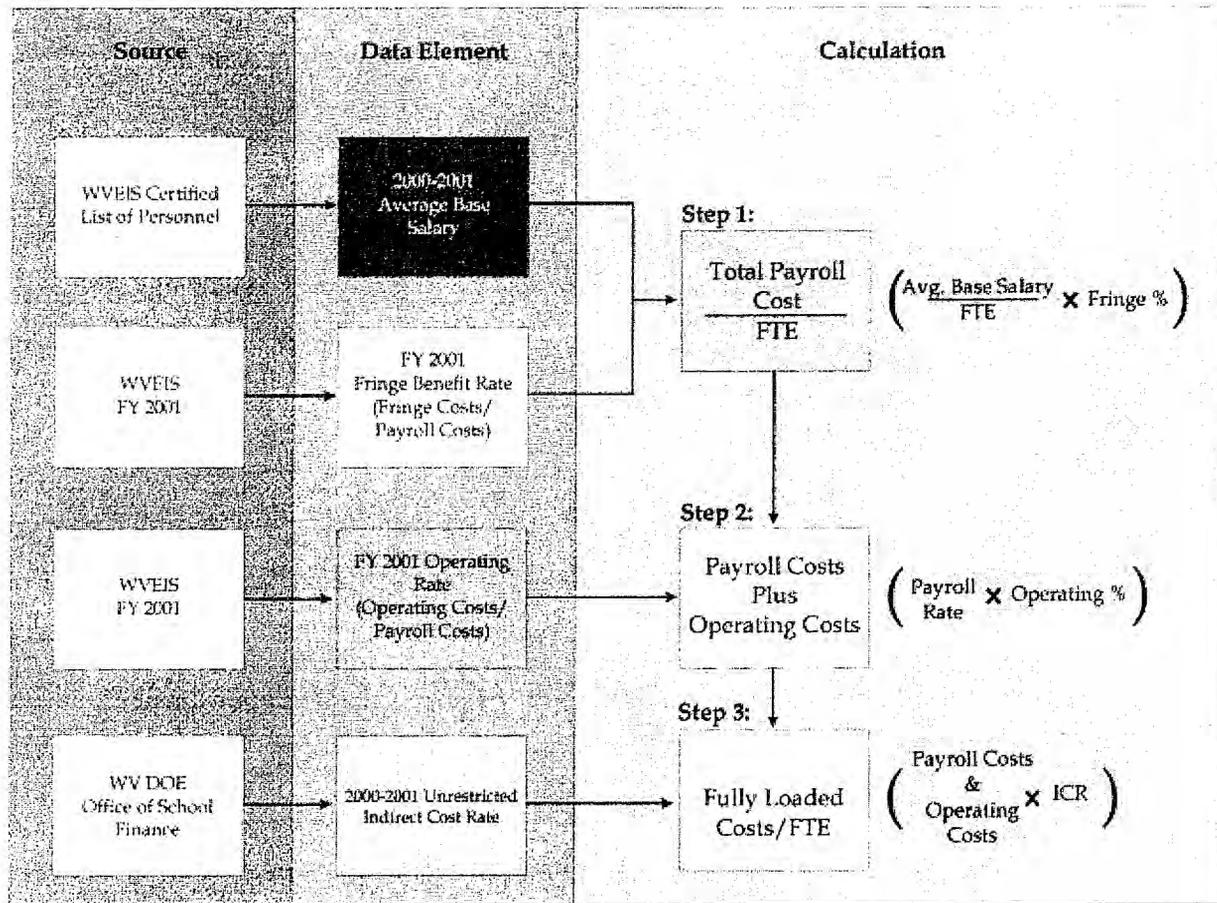
- Direct costs – the direct costs, primarily personnel, associated with delivery of the specific services.
- Indirect costs – based on the Indirect Cost Rate (ICR) computed by the West Virginia Department of Education (WVDOE) and approved by the cognizant agency United States Department of Education (USDE) for each provider (county school board), and applied as a percentage.
- Operating Rate – the allocable portion of allowable materials and supplies, as per OMB A-87, and NOT included in the cognizant agency's approved ICR. This is a normal requirement for local government agencies.

The current questions for which DHHR seeks guidance are in the area of the determination of the Operating Rate noted above.

Explanation of SHS Operating Rate:

The Operating Rate (Step 2 in the diagram below) is an essential component of the formula used for rate setting and cost settlement.

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The Operating Rate reflects the percentage (%) of allowable materials, supplies and other OMB A-87 allowable costs not included in the indirect cost rate (ICR) computed by WVDOE and approved by the federal USDE as the cognizant agency. The DHHR was careful to ensure that the Operating Rate costs are not duplicative of costs included in the indirect cost rate formula and we have consistently demonstrated the separate, non-overlapping nature of these expenditures to OIG.

As noted previously, the calculation methodology under the SPA is not in question. The methodology for deriving the Operating Rate is:

$$\text{O.R.} = (\text{Direct Expenditures} + \text{Administrative Expenditures}) / \text{Direct Expenditures}$$

What has been questioned is the benefiting principle used and encompassed in this methodology to determine the allowable actual costs as per OMB A-87.

Organizational Wide Approach - The current Operating Rate formula uses an organizational wide approach to benefiting principles to determine the allowable percentage (%) of object code 300 and above operating costs for each county provider. This approach results in an equitable

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distribution of all county school board costs between regular education and special education. The rate is calculated by including non-federal expenditures from the West Virginia Education Information System (WVEIS) for object codes 300 and above (excluding transportation and contracted medical services) in the numerator and dividing by the non-federal expenditures for object codes 100 (Personnel Service - Salaries) and 200 (Employee Benefits) in the denominator (*refer to Exhibit 3 – Map Detailing Organizational Wide Operating Rate*). DHHR believes strongly that this approach is consistent with the intent of our Medicaid State Plan and is an acceptable method for determining Medicaid allowable operating costs.

IEP Specific Approach - Feedback received from the OIG indicates that an IEP-specific approach to benefiting principles in the calculation of the Operating Rate is preferable, since only expenditures related to IEP services are then used in the calculation of the rate. For example, rather than include all (i.e. organizational wide) program and object codes in the percentage calculation, only those codes related to the provision of IEP services are used. All non-federal program and object codes that are considered unrelated to the provision of IEP services, as well as those unallowable per OMB A-87, are excluded in this approach. Examples of program codes that are unrelated to the IEP may include Program/Function 1111X – Regular Instruction, Program/Function 313XX – Vocational Education, and Object Code 64X – Classroom Supplies. Examples of unallowable object codes may include 56X – Tuition, 82X – Judgements, and 93X – Interfund Transfers Out (*refer to Exhibit 4 – Map Detailing IEP Specific Operating Rate*).

Similar to the organization-wide approach, the IEP-Specific approach also removes all costs included in the WVDOE Unrestricted Indirect Cost Rate to avoid double-counting. A pro-rata share of school board costs such as payment of interest on long-term debt and other school administration costs are also included in the numerator of the IEP Specific Operating Rate calculation since they are not included in the indirect cost rate but are allowable per OMB A-87 regulations.

Next Steps:

Based on the foregoing discussion, DHHR respectfully requests CMS assistance in determining the most appropriate approach for correcting SHS rates for SFY 2001 and subsequent years. Both the organization-wide and IEP-specific approaches to actual cost identification with the Operating Rate are compliant with the current approved State Plan language specifying that reimbursement shall be based on actual, reasonable costs. However, we understand that the OIG recommends that the approach be directly reconciled to expenditures incurred for the provision of IEP services.

In determining the proper approach to take, we note the following questions:

- 1) Does the OIG audit constitute an “opening” of the settled years, SFY 2001 - SFY 2003?

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- 2) Can an adjusted cost accounting technique, within the existing methodology, which is held to provide a more accurate reflection of actual costs, be applied?
- 3) Given the myriad of DHHS DAB rulings (e.g., 934, 1328, and 1542) which hold that a state has the right to interpret its own State Plan in its own way, and the requirement of consistency in that application, won't the same accepted (and acceptable) costing technique necessarily have to apply to all periods, even those previously settled?

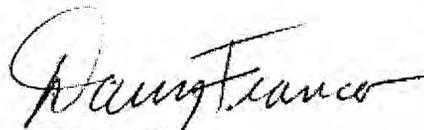
The answers to these questions will directly impact how DHHR proceeds in identifying and addressing any necessary rate revisions, claims adjustments, or operating practices necessary to ensure a viable financial position for these vital state programs.

The table below summarizes the present and proposed cost finding techniques for determining allowable operating costs.

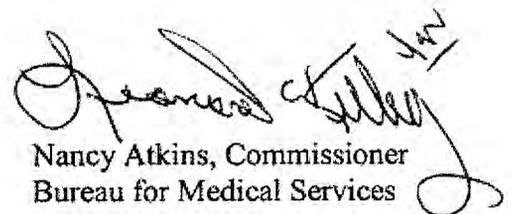
| West Virginia SHS Operating Rate | | | |
|----------------------------------|--------------|---------------------|--------------------|
| | Cost Settled | Present Approach | Corrected Approach |
| SFY 2001 | Y | Organizational Wide | IEP Specific |
| SFY 2002 | Y | Organizational Wide | IEP Specific |
| SFY 2003 | Y | Organizational Wide | IEP Specific |
| SFY 2004 | N | Organizational Wide | IEP Specific |
| SFY 2005 | N | Organizational Wide | IEP Specific |
| SFY 2006 | N | Organizational Wide | IEP Specific |

Your kind consideration and prompt response is greatly appreciated.

Sincerely,



Danny Franco
 Deputy Secretary for Administration



Nancy Atkins, Commissioner
 Bureau for Medical Services

DF/NA/eaw

Attachments

- c Martha Yeager Walker
- Gary Knight
- Ted Gallagher
- Fran McCullough
- John Whalen