

Department of Health and Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**VIRGINIA DID NOT CLAIM SOME  
MEDICAID ADMINISTRATIVE COSTS  
FOR ITS MEDALLION 3.0 WAIVER  
PROGRAM IN ACCORDANCE WITH  
FEDERAL REQUIREMENTS**

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Deputy Inspector General  
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**June 2018  
A-03-17-00200**

# *Office of Inspector General*

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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.

## Report in Brief

Date: June 2018

Report No. A-03-17-00200

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



### Why OIG Did This Review

Previous OIG reviews of Medicaid administrative costs found that several States did not always claim administrative costs according to Federal requirements. As part of a Medicaid risk assessment, we noted that Virginia claimed \$342.6 million (\$220 million Federal share) for Medicaid administrative costs associated with Virginia's Medicaid Managed Care Medallion 3.0 waiver program for State fiscal years (SFYs) 2016 and 2017. We conducted this audit because of the significant amount that Virginia claimed and because of our previous findings related to Medicaid administrative costs.

Our objective was to determine whether Virginia claimed Medicaid administrative costs for its waiver program for SFYs 2016 and 2017 in accordance with Federal requirements.

### How OIG Did This Review

We reviewed Virginia's supporting documentation to determine whether the administrative costs claimed for the waiver program were identified in Virginia's Cost Allocation Plan (CAP), whether the administrative costs claimed were directly related to the administration of the waiver program, and whether the administrative costs claimed were allocated according to the approved CAP methodology.

## Virginia Did Not Claim Some Medicaid Administrative Costs for Its Medallion 3.0 Waiver Program In Accordance With Federal Requirements

### What OIG Found

Of the \$342.6 million (\$220 million Federal share) in administrative costs claimed for Virginia's waiver program in SFYs 2016 and 2017, Virginia correctly claimed \$324.9 million (\$211.2 million Federal share). However, we found that Virginia claimed \$15.3 million (\$7.7 million Federal share) in unallowable waiver program administrative costs not identified in the CAP. In addition, Virginia incorrectly claimed \$2.3 million (\$1.2 million Federal share) in administrative costs that were misclassified as waiver program administrative costs. The misclassified expenditures did not directly benefit the waiver program but directly benefited a separate public welfare program, Virginia's Children's Health Insurance Program (CHIP).

### What OIG Recommends and Virginia Comments

We recommend that Virginia (1) refund to the Federal Government \$7.7 million for administrative costs that were not identified in the CAP and (2) reclassify \$2.3 million (\$1.2 million Federal share) in administrative costs that directly benefited Virginia's CHIP program and not the waiver program. In written comments on our draft report, the State agency agreed to reclassify administrative costs that directly benefited the State's CHIP program and not the waiver program. The State agency did not concur with our recommendation that it refund \$7,674,910 in questioned costs. The State agency stated that only one section of its CAP contained cost centers, and that the section addressed personnel costs only. The State agency contended that only personnel-related cost centers (i.e., cost centers 018, 041, 068, and 090C) should have been included in the CAP. The State agency stated that any disallowance should be limited to personnel-related costs allocated to these omitted cost centers, reducing the potential disallowance to \$607,529. In addition, the State agency contended that no disallowance is required because Federal law allows retroactive approval of corrections for a deficient CAP. The State agency requested a retroactive revision of its CAP on November 17, 2017; as of March 30, 2018, the revision had not been approved. After reviewing the State agency's comments, we maintain that our disallowance recommendation is valid. The DAB and Federal regulations require State agencies to include all of their program administrative costs, not just personnel costs, in their CAPs. However, the costs associated with the remaining missing cost centers we identified in our findings were not included anywhere in the CAP. We acknowledge that some costs might be allowable if the State agency receives retroactive approval of amendments to its CAP. However, the State has not received such approval.

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## INTRODUCTION

### WHY WE DID THIS REVIEW

Previous Department of Health and Human Services (HHS) Office of Inspector General (OIG) reviews of Medicaid administrative costs found that several States did not always claim administrative costs according to Federal requirements.<sup>1</sup> As part of a Medicaid risk assessment, we noted that the Commonwealth of Virginia Department of Medical Assistance (State agency) claimed \$342,629,185 (\$220,002,038 Federal share) for Medicaid administrative costs associated with Virginia's Medallion 3.0 Waiver (waiver) program for State fiscal years (SFYs) 2016 and 2017. The amount the State agency claimed for these SFYs was significantly higher than the amounts claimed by other States in the region during the same period. We conducted this audit because of the significant amount that the State agency claimed and because of our previous findings related to Medicaid administrative costs.

### OBJECTIVE

Our objective was to determine whether the State agency claimed Medicaid administrative costs for its waiver program for SFYs 2016 and 2017 in accordance with Federal requirements.

### BACKGROUND

#### Medicaid Program

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 Medicaid State plan. Although each State has considerable flexibility in designing and operating its Medicaid program, it must comply with Federal requirements. In Virginia, the State agency administers the Medicaid program.

Section 1903(a) of the Social Security Act (the Act) permits States to claim Federal reimbursement for Medicaid administrative costs. Most administrative costs "for the proper and efficient administration" of the Medicaid program are reimbursed at a 50-percent rate (the Act § 1903(a)(7)). However, States can receive enhanced Federal funding for some administrative costs. States claim administrative costs on Form CMS-64, Quarterly Medicaid Statement of Expenditures for the Medical Assistance Program.

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<sup>1</sup> See Appendix B for a list of related OIG reports on Medicaid administrative costs.

## **Virginia's Medallion 3.0 Waiver Program**

Virginia's waiver program is a State-wide Medicaid managed care program that provides its members with access to preventive and coordinated care.<sup>2</sup> The waiver program is a capitated, risk-based, and mandatory managed care program for Medicaid beneficiaries in Virginia. Through the waiver program, the State agency contracts State-wide with six Medicaid managed care organizations (MCOs) for the provision of most Medicaid covered services. Contracted MCOs receive a per member per month capitation payment that covers a comprehensive set of services.<sup>3</sup> The initial waiver program was effective April 1, 2005. CMS approved a renewal effective July 1, 2015, with an expiration date of June 30, 2017. The waiver program currently operates under a further renewal that became effective July 1, 2017.

### **Cost Allocation Plans**

Subpart E of 45 CFR part 95 requires State agencies to allocate administrative and training costs to programs in accordance with public assistance cost allocation plans (CAPs). A State's CAP describes how the State agency identifies, measures, and allocates costs to each Medicaid program. To be allowable, administrative costs must be included in the CAP. When claiming administrative costs, States must comply with cost principles found at 45 CFR part 75. These cost principles specify that State agencies may claim administrative costs for each program only in proportion to the benefits received by the program. Only costs allocable to a particular program are allowable for that program, and costs must be reasonable and necessary for proper administration of the program (45 CFR § 75.403).

Appendix C contains Federal requirements related to the waiver program and Medicaid administrative costs.

### **HOW WE CONDUCTED THIS REVIEW**

Our review covered the \$342,629,185 (\$220,002,038 Federal share) in administrative costs for the waiver program that the State agency claimed for SFYs 2016 and 2017. We reviewed the State agency's supporting documentation to determine whether the administrative costs claimed for the waiver program were identified in the State agency's CAP, whether the administrative costs claimed were directly related to the administration of the waiver program, and whether the administrative costs claimed were allocated according to the approved CAP methodology.

We did not review the overall internal control structure of the State agency. We limited our review to those controls related to the State agency's methodology for claiming administrative costs for the waiver program. We performed our review between April and October 2017.

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<sup>2</sup> The waiver program is authorized under sections 1915(b)(1) and 1915(b)(4) of the Act.

<sup>3</sup> Virginia Administrative Code, title 12, section 30-120-370, provides Virginia's enrollment standards for its Medicaid MCOs.

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

Of the \$342,629,185 (\$220,002,038 Federal share) in administrative costs claimed for Virginia's waiver program in SFYs 2016 and 2017, the State agency correctly claimed \$324,947,461 (\$211,161,177 Federal share). However, we found that the State agency claimed \$15,349,822 (\$7,674,910 Federal share) in unallowable waiver program administrative costs not identified in the CAP. In addition, the State agency incorrectly claimed \$2,331,902 (\$1,165,951 Federal share) in administrative costs that were misclassified as waiver program administrative costs. The misclassified expenditures did not directly benefit the waiver program but directly benefited a separate public welfare program, Virginia's Children's Health Insurance Program (CHIP).<sup>4</sup>

### **SOME ADMINISTRATIVE COSTS WERE NOT IDENTIFIED IN THE STATE AGENCY'S COST ALLOCATION PLAN**

Federal regulations require the CAP to contain sufficient detailed information for Federal officials to reach an informed judgment about the correctness and fairness of the methods employed by the State for identifying, measuring, and allocating all costs to each of the programs operated by the State agency (45 CFR § 95.507). Recent Departmental Appeals Board (DAB) decisions<sup>5</sup> have ruled that "regulations expressly require that a State claim 'FFP [Federal financial participation] for costs associated with a program **only** in accordance with its approved'" CAP (DAB No. 2653, quoting 45 CFR § 95.517 (emphasis added by the DAB)). Costs not claimed in accordance with the CAP will be disallowed (45 CFR § 95.519).

The State agency claimed \$15,349,822 (\$7,674,910 Federal share) in waiver program administrative costs that were not identified in the State agency's CAP as required in Federal regulations. This total includes \$6,895,224 (\$3,447,611 Federal share) in waiver program administrative costs allocated in SFY 2016 that were not identified in the CAP and \$8,454,598 (\$4,227,299 Federal share) allocated in SFY 2017 that were not identified in the CAP.

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<sup>4</sup> Authorized under Title XXI of the Act, CHIP is a program that provides Federal matching funds to States for health insurance to eligible children. The program was designed to cover uninsured children in families with incomes that are modest but too high to qualify for Medicaid.

<sup>5</sup> *Pennsylvania Department of Human Services*, DAB No. 2710 (2016), *Pennsylvania Department of Public Welfare*, DAB No. 2669 (2015), and *Pennsylvania Department of Public Welfare*, DAB No. 2653 (2015).

The State agency stated that these missing costs “were in the original 15-02 CAP, however, they appear to have been inadvertently omitted during subsequent edits.”<sup>6</sup> However, these missing costs were not included in the 15-02 CAP. The July 1, 2017, CAP amendment includes the missing costs. Therefore, these costs would be allowable in SFY 2018 but not in previous years.

A list of the missing CAP costs and their associated expenditure data for SFY 2016 is included as Appendix D. Appendix E contains a list of the missing CAP costs and their associated expenditure data for SFY 2017.

### **SOME CLAIMED ADMINISTRATIVE COSTS WERE NOT RELATED TO THE MEDALLION 3.0 WAIVER PROGRAM**

Subpart E of 45 CFR part 95 requires State agencies to allocate administrative costs to programs in accordance with the State agency’s CAP. Further, costs must be allocated to a particular program in accordance with relative benefits received (45 CFR § 75.405(a)).

The State agency claimed \$2,331,902 (\$1,165,951 Federal share) in CHIP administrative costs as waiver program administrative costs contrary to the State agency’s CAP, which requires these costs to be directly charged to the CHIP program. These costs were directly related to the administration of the State’s CHIP program and should have been claimed as CHIP administrative costs rather than as waiver program administrative costs.

### **RECOMMENDATIONS**

We recommend that the State agency:

- refund to the Federal Government \$7,674,910 for administrative costs that were not identified in the CAP and
- reclassify \$2,331,902 (\$1,165,951 Federal share) in administrative costs that directly benefited the State’s CHIP program and not the waiver program.

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

In written comments on our draft report, the State agency agreed to reclassify administrative costs that directly benefited the State’s CHIP program and not the waiver program. The State agency did not concur with our recommendation that it refund \$7,674,910 in questioned costs. The State agency stated that only one section of its CAP contained cost centers,<sup>7</sup> and that the section addressed personnel costs only. The State agency contended that only personnel-

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<sup>6</sup> The Commonwealth of Virginia Department of Medical Assistance Services Public Assistance Cost Allocation Plan Amendment 15-02 (15-02 CAP) was effective January 1, 2015, and was the version of the CAP in effect during our audit period.

<sup>7</sup> The CAP groups each program’s administrative costs into categories known as cost centers. To be allowable, administrative costs must be identified in the CAP.

related cost centers (i.e., cost centers 018, 041, 068, and 090C) should have been included in the CAP. The State agency stated that any disallowance should be limited to personnel-related costs allocated to these omitted cost centers, reducing the potential disallowance to \$607,529. In addition, the State agency contended that no disallowance is required because Federal law<sup>8</sup> allows retroactive approval of corrections for a deficient CAP. The State agency requested a retroactive revision of its CAP on November 17, 2017; as of March 30, 2018, the revision had not been approved.

After reviewing the State agency's comments, we maintain that our disallowance recommendation is valid. The DAB and Federal regulations require State agencies to include all of their program administrative costs, not just personnel costs, in their CAPs. However, the costs associated with the remaining missing cost centers we identified in our findings were not included anywhere in the CAP. We acknowledge that some costs might be allowable if the State agency receives retroactive approval of amendments to its CAP. However, the State has not received such approval.

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

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<sup>8</sup> 45 CFR § 95.509 and 45 CFR § 95.515.

## APPENDIX A: AUDIT SCOPE AND METHODOLOGY

### SCOPE

From July 1, 2015, through June 30, 2017, the State agency claimed \$342,629,185 (\$220,002,038 Federal share) in Medicaid costs for the administration of its waiver program. The costs were allocated to 36 cost centers in SFY 2016 and 39 cost centers in SFY 2017. We reviewed the State agency's supporting documentation to determine whether the administrative costs claimed for the waiver program were allocated to cost centers identified in the State agency's CAP, whether the administrative costs claimed were directly related to the administration of the waiver program, and whether the administrative costs claimed were allocated according to approved CAP methodology.

We did not review the overall internal control structure of the State agency or the Medicaid program. Rather, we reviewed only those internal controls related to our objective. We limited our review to determining whether the State agency's claims for Medicaid administrative costs were made in accordance with Federal requirements.

We conducted our audit from April through October 2017.

### METHODOLOGY

To accomplish our objective, we:

- reviewed applicable laws, regulations, and guidelines;
- interviewed State agency officials regarding their CAPs, related policies and procedures, and process for claiming Medicaid administrative costs;
- reviewed the State agency's CAP to determine acceptable processes for claiming Medicaid administrative costs;
- reviewed other Virginia State agencies' CAPs for administrative costs claimed through interagency agreements;<sup>9</sup>

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<sup>9</sup> Other State agencies, including the Virginia Department of Social Services and the Virginia Department for Aging and Rehabilitative Services, may incur administrative costs on behalf of the Medicaid program, and the State agency's CAP specifies that the State agency may claim these administrative costs according to interagency agreements. The State agency bills the costs in accordance with each agency's individual CAP, the State agency's CAP, and the corresponding interagency agreement.

- reconciled the Medicaid administrative costs claimed on Form CMS-64 to the State agency's Form CMS-64 accounting records and the State agency's CAP detail reports;<sup>10</sup>
- organized the claimed administrative costs by CAP cost center number;
- determined whether the cost centers to which the claimed costs were allocated were included in the CAP, whether the cost centers were directly related to the administration of the waiver program, and whether the costs in the cost centers were allocated according to the approved CAP methodology; and
- discussed our findings with CMS and 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.

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<sup>10</sup> The State agency's CAP system has a Cost Allocation Plan Detail real-time report that displays the results of the cost allocation process and allows for verification, analysis, and updates. It indicates the details of beginning costs and how the costs are distributed first to allocation categories and finally to the benefiting programs.

**APPENDIX B: RELATED OFFICE OF INSPECTOR GENERAL REPORTS**

<b>Report Title</b>	<b>Report Number</b>	<b>Date Issued</b>
<i>Texas Did Not Always Comply With Federal Requirements and Its Public Assistance Cost Allocation Plan When It Claimed Medicaid Administrative Costs</i>	<a href="#"><u>A-06-15-00038</u></a>	8/1/2016
<i>Florida Claimed Some Medicaid Administrative Costs That Did Not Comply With Program Requirements</i>	<a href="#"><u>A-04-10-00076</u></a>	3/7/2013
<i>Pennsylvania Claimed Unallowable Medicaid Administrative Costs for the Regional Housing Coordinator Initiative</i>	<a href="#"><u>A-03-11-00210</u></a>	12/17/2012
<i>Maryland Claimed Medicaid Administrative Costs for Unallowable Remedial and Training Services for the Maryland Poison Center</i>	<a href="#"><u>A-03-12-00204</u></a>	9/27/2012
<i>Pennsylvania Claimed Medicaid Administrative Costs for Provider Training Under Its Restraint Reduction Initiative</i>	<a href="#"><u>A-03-11-00209</u></a>	7/24/2012
<i>Review of Medicaid Administrative Costs Claimed by New Jersey for State Fiscal Year 2007</i>	<a href="#"><u>A-02-07-01050</u></a>	11/4/2011
<i>Review of Administrative Costs Claimed for Pennsylvania's Home and Community-Based Waiver for Individuals Aged 60 and Over</i>	<a href="#"><u>A-03-10-00202</u></a>	6/28/2011

## APPENDIX C: FEDERAL REQUIREMENTS

### Section 1915(b) Waivers

Section 1915(b) of the Act gives the HHS Secretary the discretion to waive a broad range of requirements included in section 1902 of the Act as necessary to enable a State to implement alternative delivery mechanisms for its Medicaid program. However, the Secretary may only exercise that discretion if the alternative delivery mechanism is found to be cost-effective, efficient, and not inconsistent with the purposes of Title XIX of the Act. The approval period for a State's 1915(b) waiver program is limited to 2 years. There are four possible waiver features under section 1915(b):

- (b)(1) restricts Medicaid enrollees to receive services within the managed care network,
- (b)(2) utilizes a “central broker to assist beneficiaries in making coverage choices,”
- (b)(3) uses cost savings to provide additional services to beneficiaries, and
- (b)(4) restricts the provider from whom the Medicaid eligible may obtain services.

The Medallion 3.0 waiver program operates under sections (b)(1) and (b)(4).

### Cost Allocation Plans

Section 1903(a) of the Act permits States to claim Federal reimbursement for Medicaid administrative costs. Subpart E of 45 CFR part 95 requires State agencies to allocate administrative costs to programs in accordance with a public assistance CAP that describes the costs claimed and the methodology for allocating the costs to the programs. When claiming administrative costs, States must comply with cost principles found at 45 CFR part 75<sup>11</sup> (45 CFR § 95.507).

For administrative costs to be allowable, they must be necessary and reasonable for the proper and efficient administration of the Medicaid program, be allocable to Federal awards, and be adequately documented (45 CFR § 75.403). 45 CFR section 75.405(a) specifies that “a cost is allocable to a particular Federal award or other cost objective if the goods or services involved are chargeable or assignable to that Federal award or cost objective in accordance with relative benefits received.” These cost principles specify that State agencies may claim administrative costs for each program only in proportion to the benefits received by the program. Only costs allocated to a particular program are allowable for that program, and costs must be reasonable and necessary for proper administration of the program (45 CFR § 75.403).

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<sup>11</sup> Before our audit period, Office of Management and Budget (OMB) Circular A-87, Cost Principles for State, Local, and Indian Tribal Governments, was consolidated with other OMB guidance and codified at 2 CFR part 200. HHS adopted this guidance and codified the text, with HHS-specific amendments, at 45 CFR part 75.

HHS Cost Allocation Services (CAS)<sup>12</sup> approves States' CAPs after CMS reviews and comments on the fairness of the cost allocation methodologies. State agencies must adhere to their approved CAPs in computing claims for the Federal share of administrative costs (45 CFR § 95.517) and must update the plans by submitting amendments when the CAPs become outdated or other changes occur that make the approved CAPs invalid (45 CFR § 95.509). States may claim costs based on proposed CAPs or plan amendments; however, States must make retroactive adjustments to their claims, if necessary, to conform to the subsequently approved CAPs (45 CFR § 95.517). If costs are not claimed in accordance with an approved CAP, and State agencies have not submitted amendments as specified in 45 CFR section 95.509, the improperly claimed costs will be disallowed (45 CFR § 95.519).

### **CMS Letter to State Medicaid Directors**

CMS guidance issued in a December 1994 letter to State Medicaid directors (Letter No. 122094) clarified its policy concerning State claims for Medicaid administrative costs. CMS, then called the Health Care Financing Administration, stated, "We have consistently held that allowable claims under this authority must be directly related to the administration of the Medicaid program." CMS's letter also provided a list of allowable administrative activities, but it was not all-inclusive. CMS stated that an allowable administrative cost must be directly related to Medicaid State plan or waiver program services. The letter also stated that claims for administrative costs "cannot reflect the cost of providing a direct medical or remedial service, such as immunizations or psychological counseling." In addition, CMS's letter stated that States "may not include funding for a portion of general public health initiatives that are made available to all persons, such as public health education campaigns . . ." and "may not include the overhead costs of operating a provider facility, such as the supervision and training of providers."

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<sup>12</sup> CAS is part of the Office of the Deputy Secretary for Program Support.

**APPENDIX D: ADMINISTRATIVE COSTS NOT IDENTIFIED IN THE STATE AGENCY'S PUBLIC ASSISTANCE COST ALLOCATION PLAN FOR STATE FISCAL YEAR 2016**

<b>Cost Center Number</b>	<b>Cost Center Name</b>	<b>Total Costs</b>	<b>Federal Share</b>
018	Provider Reimbursement Division <sup>13</sup>	\$2,965,745	\$1,482,872
020	Health Care Services' Pharmacy Unit – Pharmacy Management Services	1,278,855	639,428
021	Long Term Care Division – Civil Monetary Penalties <sup>14</sup>	47,295	23,648
041	Provider Reimbursement Division	2,309,144	1,154,572
044B	Information Management Division – Virginia Medicaid Management Information System	(833,849)	(416,925)
050 052	Commonwealth Central Services – Mailing Services & Library Subscription Services	772,269	386,135
068	State Agency Director's Office – Justice Unit	98,429	49,214
069	Procurement and Contract Management <sup>15</sup>	161	80
080	Marketing and Enrollment Services – Cover Virginia Call Center <sup>16</sup>	257,175	128,587
<b>Total</b>		<b>\$6,895,224</b>	<b>\$3,447,611</b>

<sup>13</sup> Cost Centers 018 and 041 both represent expenditures in the State agency's Provider Reimbursement Division. Cost Center 018 includes salary costs, non-salary division costs, and contractual costs for actuarial and rate-setting services. Cost Center 041 only includes non-salary costs. The non-salary costs are accumulated in an indirect cost pool and allocated based on each employee's role and function in the organization.

<sup>14</sup> Under 42 CFR section 438.704, civil monetary penalties may be assessed against MCOs for failure to comply with a series of operational requirements.

<sup>15</sup> Cost Center 069, Procurement and Contract Management, was not in the SFY 2016 CAP but was included for SFY 2017.

<sup>16</sup> The Cover Virginia Call Center was established in October 2013 as a result of the Patient Protection and Affordable Care Act to accept phone applications for Medicaid and Family Access to Medical Insurance Security (FAMIS) services. FAMIS is Virginia's CHIP services program. The Cover Virginia Call Center is operated by private contractors.

**APPENDIX E: ADMINISTRATIVE COSTS NOT IDENTIFIED IN THE STATE AGENCY'S PUBLIC ASSISTANCE COST ALLOCATION PLAN FOR STATE FISCAL YEAR 2017**

<b>Cost Center Number</b>	<b>Cost Center Name</b>	<b>Total Costs</b>	<b>Federal Share</b>
010	Dental Services	\$1,172,606	\$586,303
018	Provider Reimbursement Division	4,486,906	2,243,453
020	Health Care Services' Pharmacy Unit – Pharmacy Management Services	1,349,076	674,538
021	Long Term Care Division – Civil Monetary Penalties	80,448	40,224
041	Provider Reimbursement Division	2,452,622	1,226,311
044B	Information Management Division – Virginia Medicaid Management Information System	(66,297)	(33,148)
050 052	Commonwealth Mailing Services Library Subscription Services	734,304	367,152
068	State Agency Director's Office – Justice Unit	83,917	41,958
070A	Fiscal FFP Adjustments	(2,008,021)	(1,004,011)
078	Developmental Disabilities and Behavioral Health	77,555	38,778
080	Marketing and Enrollment Services – Cover Virginia Call Center	92,386	46,193
090C	Rehab Service - Eligibility Determinations	(904)	(452)
<b>Total</b>		<b>\$8,454,598</b>	<b>\$4,227,299</b>

## APPENDIX F: STATE AGENCY COMMENTS



### COMMONWEALTH of VIRGINIA *Department of Medical Assistance Services*

JENNIFER S. LEE, M.D.  
DIRECTOR

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March 30, 2018

Ms. Nicole Freda, Acting Regional Inspector General for Audit Services  
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Office of Inspector General  
Office of Audit Services, Region III  
Public Ledger Building, Suite 316  
150 South Independence Mall West  
Philadelphia, PA 19106-3499

Re: Report Number, A-03-17-00200

Dear Ms. Freda:

This is the Virginia Department of Medical Assistance's ("DMAS") response to the Office of the Inspector General's ("OIG") draft report dated March 9, 2018, entitled "Virginia Did Not Claim Some Medicaid Administrative Costs for its Medallion 3.0 Waiver Program In Accordance With Federal Requirements."<sup>1</sup> The report states that the OIG reviewed \$342.6 million (\$220 million Federal share) in costs claimed for DMAS' Medallion waiver in SFYs 2016 and 2017, and found that DMAS properly claimed \$324.9 million (\$211.2 million Federal share). (DR, p. 3).

The report also states that the OIG found that DMAS improperly: (a) claimed \$15.3 million (\$7.7 million Federal share) in administrative costs not identified in the Cost Allocation Plan ("CAP"); and (b) misclassified \$2.3 million (\$1.2 million Federal share) in administrative costs to the Medallion waiver rather than to DMAS' Children's Health Insurance Program ("CHIP"). (DR, p. 3). The OIG recommends that DMAS refund the Federal Government \$7.7 million and reclassify the \$2.3 million (\$1.2 million Federal share) in costs to CHIP. (DR, p. 4).

DMAS agrees to reclassify the \$2.3 million (\$1.2 million Federal share) in administrative costs to CHIP. DMAS will submit a waiver-only adjustment with the CMS-64 report for the certified quarter ending in March 31, 2018.

DMAS respectfully disagrees with the recommendation that it should refund the Federal Government \$7.7 million on the basis that it improperly claimed \$15.3 million (\$7.7 million Federal share) in costs not identified in the CAP. For the reasons explained below, DMAS submits that, even if the OIG's position were accepted: (a) the potential disallowance amount is \$607,529;

<sup>1</sup> Citations will be made to specific pages in the draft report in the following format: (DR, [page number]).

and (b) federal law authorizes retroactive amendment of the CAP as an alternative to disallowance.<sup>2</sup>

#### **I. Summary of DMAS' position**

The report states that, from July 1, 2015 to June 30, 2017, DMAS claimed \$342,629,185 (\$220,002,038 Federal share) in administration costs for the Medallion waiver. The report states that these costs were allocated to 36 cost centers in SFY 2016 and 39 cost centers in SFY 2017. (DR, p. 5).

Describing its audit methodology, the OIG states that it reconciled the costs claimed on DMAS' CMS-64 reports with the CMS-64 accounting records and the CAP, and organized the claimed costs by cost center number. (DR, p. 5). The OIG also states that it reviewed whether the cost centers to which claimed costs had been allocated were included in the CAP, whether the cost centers were directly related to administration of the Medallion waiver, and whether the costs in the cost centers were allocated according to the approved CAP methodology. (DR, p. 5).

The OIG compared the cost centers in the waiver worksheets used for CMS-64 reporting to the cost centers in the CAP applicable to SFYs 2016 and 2017. The OIG determined that some cost centers were in the worksheets but not in the CAP. The OIG identified the "unlisted" cost centers in Appendix D (SFY 2016) and Appendix E (SFY 2017) and now proposes to disallow any costs allocated to those cost centers. (DR, pp. 7-8).

Respectfully, the audit methodology fails to account for a crucial fact. As explained below, cost centers are listed in Section VIII of the CAP (entitled "Personnel Cost Allocations") and are used to allocate personnel costs only and, more specifically, only those personnel costs related to a single line item in DMAS' time-reporting system (TAL).

By contrast, each cost center in the worksheets were only used to group related costs, some (but not all) of which are personnel costs. In fact, several cost centers in the worksheets do not have any personnel costs allocated to them. Thus, those cost centers would not (and should not) be applicable to Section VIII of the CAP, as that section addresses only personnel costs.

Even if one accepts the premise that all cost centers in the worksheets should also have been in Section VIII of the CAP, no disallowance is required as Federal law allows retroactive approval of corrections for a deficient CAP.

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<sup>2</sup> By letter sent to the Division of Cost Allocation on November 9, 2017, DMAS submitted a request for this remedy to be approved. The letter's receipt was confirmed and, as of the date of this response, the request is still pending. A copy of DMAS' November 9, 2017, request is attached to this response as Exhibit A.

**II. Cost centers in the CAP are listed in Section VIII, which addresses the allocation of personnel costs only, and these cost centers were used to allocate personnel costs related to one category in DMAS' time-reporting system**

Cost centers are found in only one section of the CAP for all applicable Amendments in the audit period. This is Section VIII, which is entitled, "Personnel Cost Allocations," and, as is evident from its title, this section addresses personnel costs only. The allocation of non-personnel costs is addressed in a different section of the CAP: Section IX, which is entitled, "Non-Personnel Cost Allocations."

Section VIII of the CAP explains that the term "cost center" refers, generally, to an organizational unit, often an overhead or program service department. Each cost center's name and designated number are identified in the second of two tables in Section VIII. This second table describes how personnel costs are to be allocated to a single category (known as "Default Medicaid") in DMAS' time reporting system, TAL. As that table pertained only to personnel costs, it would not have included any cost centers that DMAS used solely for allocating non-personnel expenses.

**III. Only four cost centers listed in Appendices D and E of the draft report (018, 041, 068 and 090C) were used to allocate personnel costs, and therefore only those cost centers should have listed in Section VIII of the CAP**

The OIG's audit methodology involved comparing the list of cost centers in Section VIII of the CAP (which addressed personnel costs only) with the cost centers listed in the CMS-64 report worksheets. DMAS has explained that cost centers in the CAP were used to allocate personnel costs to a specific category in DMAS' time-reporting system.

In the CMS-64 report worksheets, each cost center represents an individual group to classify related costs together. Only four of the cost centers used in the worksheets, and identified in Appendices D and E of the draft report, involved allocation of personnel costs. These four cost centers are: 018, 041, 068 and 090C. (DR, pp. 10-11). DMAS agrees with the OIG that those four cost centers should have been in Section VIII of the CAP. All the other cost centers in Appendices D and E involve costs not applicable to waiver personnel, and therefore those cost centers would not (and should not) have been listed in a section of the CAP (Section VIII) that was used to describe the allocation of personnel costs.

Having agreed with the OIG that cost centers 018, 041, 068 and 090C were omitted (which DMAS submits was done inadvertently<sup>3</sup>), DMAS wishes to clarify that only some of the costs that

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<sup>3</sup> The draft report, page 4, states that DMAS "stated that these missing costs 'were in the original 15-02 CAP, however, they appear to have been inadvertently omitted during subsequent edits.' However, these missing costs were not included in the 15-02 CAP." This portion of the draft report requires clarification because it infers that DMAS previously acknowledged that *all* of the cost centers identified by CMS in Appendix D and Appendix E should have been listed in the 15-02 CAP. The full quote from DMAS was "Cost Centers referenced in the CAP on page 30 are payroll related with the allocation method indicated for Default time. Other cost centers not indicated do not include

were allocated to these omitted cost centers were personnel-related. DMAS submits that any disallowance should be limited to the personnel costs allocated to these omitted cost centers. DMAS has prepared two tables, attached as Exhibit A, which identify the personnel costs allocated to cost centers 018, 041, 068 and 090C for SFYs 2016 and 2017. As reflected in those tables, the total amount of any potential disallowance should be \$607,529. However, as discussed below, the disallowance should be rejected in favor of a federally created remedy which, given our facts, is appropriate to redress the OIG-identified deficiencies in the CAP.

#### **IV. Federal law authorizes a remedy in lieu of disallowance**

Federal law affords DMAS a remedy that would avoid any disallowance in this case. That remedy is to allow for an amendment to the CAP, with the effective date of the amended CAP being made retroactive. Not only does our case warrant application of this remedy, but the OIG has also approved its application to address situations similar to ours.

Federal regulations require that a state must promptly amend its CAP whenever events occur which affect the validity of the approved cost allocation procedures. Furthermore, federal regulations state that the effective date of a CAP amendment is the first day of the calendar quarter following the date of the event that required the amendment, but that there can be exceptions to this general rule under certain circumstances.<sup>4</sup> In cases where either (a) an earlier date is needed to avoid a significant inequity to either the state or the Federal Government; or (b) the information provided by the state which was used to approve a previous plan or plan amendment is later found to be materially incomplete or inaccurate, or the previously approved plan is later found to violate a Federal statute or regulation. Under either scenario, the effective date of a required modification to the plan would be the same as the effective date of the plan or plan amendment that contained the defect.<sup>5</sup>

By letter dated November 9, 2017, and addressed to the Division of Cost Allocation, Virginia requested that CAP Amendment 17-04 (effective 7/1/17) that included the missing cost centers, be made retroactive to the effective date of CAP Amendment 15-02. If the request is approved (it is still pending as of the date of this response), then no disallowance would be required.

DMAS submits that application of retroactive amendment is appropriate in our case. First, refusing to approve the remedy would be inequitable, denying a substantial amount of funds to which DMAS is otherwise entitled. Based on the OIG's findings, the sole reason for disallowance is that the cost centers in the CAP do not match the cost centers in the CMS-64 report worksheets.

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any payroll except for several indicated below. *These exceptions were in the original 15-02 CAP...* [emphasis added]. DMAS was referring to the cost centers with personnel costs as the "exceptions." This is consistent with the explanation in this response that only cost centers with personnel costs were intended to be in Section VIII of the 15-02 CAP. Further, the statement that the exceptions were originally included in the CAP refers to DMAS' initial internal draft, with the removal inadvertently occurring during subsequent internal edits by DMAS.

<sup>4</sup> 45 C.F.R. §95.509

<sup>5</sup> 45 C.F.R. §95.515

Respectfully, DMAS has addressed why the audit methodology applied in our case should be reconsidered. First, DMAS explained how cost centers were used in Section VIII of the CAP to allocate personnel costs only. Second, DMAS explained that only four of the cost centers identified by the OIG as the basis for the disallowance involved personnel costs. Finally, DMAS has agreed with the OIG's finding that those four cost centers (*i.e.*, 018, 041, 068 and 090C) should have been listed in Section VIII of the CAP and were omitted (inadvertently, in DMAS' view).

In considering whether the remedy of retroactive amendment should be allowed, it is appropriate to note the absence of certain findings. For example, there were no findings that the costs to be disallowed were unreasonable for any reason. Nor were there any findings that those costs were based on estimates rather than on actual expenses that were properly documented and verified through adequate supporting documentation. Finally, there were no findings that those costs were not necessary to the administration of the Medallion waiver.<sup>6</sup>

In addition to the technical nature of the cited deficiencies, there is a second reason favoring application of retroactive amendment in our case. Before DMAS received the OIG's report, it was informed by CMS of the "omitted" cost centers. This was the first time that CMS took the position that this omission rendered the CAP materially incomplete or inaccurate. After seeking additional guidance from CMS, DMAS took action to address CMS' concerns by filing CAP Amendment 17-04 and requesting retroactive application. DMAS submits that it acted promptly, as soon as the alleged deficiency in the CAP was brought to its attention, and that its actions, undertaken in good faith and after consultation with CMS, are deserving of the remedy of retroactive amendment.

As a final note, the OIG has recognized the viability of retroactive amendment in published reports issued to Vermont (September 2016, A-01-15-02500) and to New York (November 2016, A-02-14-02017). In both cases, the OIG affirmed that a state is obligated to amend its CAP upon discovery of a material defect and acknowledged that the effective date of a required modification is retroactive to the date of the original approval. In fact, in the report issued to Vermont, the OIG stated that a retroactive amendment request was made and granted.

## **V. Conclusion**

The proposed disallowance of \$7.7 million is based on the OIG's finding that all cost centers listed in DMAS' CMS-64 report worksheets should also have been listed in Section VIII of CAP. DMAS respectfully disagrees with the amount of the proposed disallowance and with the need for any disallowance to be assessed.

First, the cost centers in Section VIII of the CAP involved only personnel costs. Only four of the cost centers which the OIG identifies as subject to disallowance included personnel costs: 018, 041, 068 and 090C. The remaining cost centers identified by the OIG carried non-personnel

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<sup>6</sup> This statement does not apply to the costs which DMAS has agreed should be reclassified to CHIP, as stated earlier, but does apply to all of the other costs which the OIG proposes to disallow.

Ms. Nicole Freda, Acting Regional Inspector General for Audit Services  
March 30, 2018  
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costs, and therefore would not (and should not) have been included in Section VIII of the CAP. In Exhibit A, DMAS identified the potential total disallowance as \$607,529, which represents the personnel costs allocated to cost centers 018, 041, 068 and 090C.

Second, federal law authorizes a remedy in lieu of any disallowance. This remedy is retroactive amendment and applies in two circumstances. The first is where refusing the remedy would create a significant inequity to either the state or the Federal Government. The second is where the information that is provided by the state, and which is used to approve a CAP or amendment, is later found to be materially incomplete or inaccurate.

DMAS has already submitted a request for retroactive amendment by letter dated November 9, 2017. The request is currently being reviewed by the Division of Cost Allocation. As noted in its request, DMAS believes that this remedy is appropriate and warranted in this case. No finding was made that the disallowed costs were unreasonable, were not based on actual costs, or were unnecessary to administration of the Medallion waiver. Moreover, DMAS took immediate steps, to correct the deficiencies raised by CMS regarding the "omitted" cost centers, by filing an amended CAP and requesting retroactive application.

Thank you for considering these comments.

Sincerely,



Jennifer S. Lee, M.D., Director  
Department of Medical Assistance Services

Enc.  
cc: Scott Crawford, DMAS  
Lanette Walker, DMAS  
Karen Stephenson, DMAS

**COST CENTERS NOT IDENTIFIED IN THE STATE AGENCY PUBLIC ASSISTANCE COST ALLOCATION PLAN  
STATE FISCAL YEAR 2016**

Cost Center Number	Cost Center Name	ORG		VA Non-Concurrence			VA Concurrence		
		Total Claim	Federal Share	Non-personnel costs		Statement	Personnel costs		Statement
				Total Claim	Federal Share		Total Claim	Federal Share	
018	Provider Reimbursement Division 10	\$2,965,745	\$1,482,872	\$2,674,079	\$1,337,039	Not applicable to CAP Section VIII. Non-personnel cost	\$291,666	\$145,833	Cost Centers not in the CAP with applicable personnel cost
020	Health Care Services' Pharmacy Unit - Pharmacy Management Services	\$1,278,835	\$639,428	\$1,278,835	\$639,428	Not applicable to CAP Section VIII. Non-personnel cost	\$0	\$0	
021	Long Term Care Division - Civil Monetary Penalties 11	\$47,296	\$23,648	\$47,296	\$23,648	Not applicable to CAP Section VIII. Non-personnel cost	\$0	\$0	
041	Provider Reimbursement Division	\$2,309,144	\$1,154,572	\$2,309,144	\$1,154,572	Not applicable to CAP Section VIII. Non-personnel cost	\$0	\$0	
04B	Information Management Division - Virginia MDMS12	(\$833,849)	(\$416,925)	(\$833,849)	(\$416,925)	Not applicable to CAP Section VIII. Non-personnel cost	\$0	\$0	
050 032	Commonwealth Central Services - Mailing Services & Library Subscription Services	\$772,269	\$386,135	\$772,269	\$386,135	Not applicable to CAP Section VIII. Non-personnel cost	\$0	\$0	
068	State Agency Director's Office - Justice Unit	\$98,429	\$49,214	\$0	\$0		\$98,429	\$49,214	Cost Centers not in the CAP with applicable personnel cost
069	Procurement and Contract Management 13	\$161	\$80	\$161	\$80	Not applicable to CAP Section VIII. Non-personnel cost	\$0	\$0	
080	Marketing and Enrollment Services - Cover Virginia Call Center 14	\$257,175	\$128,587	\$257,175	\$128,587	Not applicable to CAP Section VIII. Non-personnel cost	\$0	\$0	
<b>Total</b>		<b>\$6,895,225</b>	<b>\$3,447,611</b>	<b>\$6,595,130</b>	<b>\$3,252,564</b>		<b>\$390,095</b>	<b>\$195,047</b>	

COST CENTERS NOT IDENTIFIED IN THE STATE AGENCY PUBLIC ASSISTANCE COST ALLOCATION PLAN  
STATE FISCAL YEAR 2017

Cost Center Number	Cost Center Name	OIG		VA Non-Concurrence			VA Concurrence		
		Total Claim	Federal Share	Non personnel costs		Statement	Personnel costs		Statement
				Total Claim	Federal Share		Total Claim	Federal Share	
10	Dental Services	\$1,172,606	\$386,303	\$1,172,606	\$386,303	Not applicable to CAP Section VIII Non-personnel cost	\$0	\$0	
018	Provider Reimbursement Division10	\$4,486,906	\$2,243,453	\$3,815,217	\$1,907,609	Not applicable to CAP Section VIII Non-personnel cost	\$671,689	\$335,844	Cost Centers not in the CAP with applicable personnel cost
020	Health Care Services Pharmacy Unit - Pharmacy Management Services	\$1,349,075	\$674,538	\$1,349,076	\$674,538	Not applicable to CAP Section VIII Non-personnel cost	\$0	\$0	
021	Long Term Care Division - Civil/Monetary Penalties11	\$80,448	\$40,224	\$80,448	\$40,224	Not applicable to CAP Section VIII Non-personnel cost	\$0	\$0	
041	Provider Reimbursement Division	\$2,452,622	\$1,226,311	\$2,382,360	\$1,191,180	Not applicable to CAP Section VIII Non-personnel cost	\$70,262	\$35,131	Cost Centers not in the CAP with applicable personnel cost
044B	Information Management Division - Virginia DMIS12	(\$66,297)	(\$33,148)	(\$66,297)	(\$33,148)	Not applicable to CAP Section VIII Non-personnel cost	\$0	\$0	
050 052	Commonwealth Central Services - Mailing Services & Library Subscription Services	\$734,304	\$367,152	\$734,304	\$367,152	Not applicable to CAP Section VIII Non-personnel cost	\$0	\$0	
068	State Agency Director's Office - Justice Unit	\$83,917	\$41,958	\$0	\$0		\$83,917	\$41,958	Cost Centers not in the CAP with applicable personnel cost
070A	Fiscal FFP Adjustments	(\$2,008,021)	(\$1,004,011)	(\$2,008,021)	(\$1,004,011)	Not applicable to CAP Section VIII Non-personnel cost	\$0	\$0	
78	Developmental Disabilities and Behavioral Health	\$77,555	\$38,778	\$77,555	\$38,777	Not applicable to CAP Section VIII Non-personnel cost	\$0	\$0	
080	Marketing and Enrollment Services - Cover Virginia Call Center14	\$92,386	\$46,193	\$92,386	\$46,193	Not applicable to CAP Section VIII Non-personnel cost	\$0	\$0	
090C	Rehab Service- Eligibility Determinations	(\$804)	(\$402)	\$0	\$0		(\$804)	(\$402)	Cost Centers not in the CAP with applicable personnel cost
<b>Total</b>		<b>\$8,454,597</b>	<b>\$4,227,299</b>	<b>\$7,639,634</b>	<b>\$3,814,817</b>		<b>\$824,963</b>	<b>\$412,482</b>	