



May 9, 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 Select Medicare Conditions of Participation and Costs Claimed at Richards Memorial Hospital From October 1, 2004, Through September 30, 2007 (A-05-08-00083)

Attached, for your information, is an advance copy of our final report on select Medicare conditions of participation and costs claimed at Richards Memorial Hospital from October 1, 2004, through September 30, 2007. We will issue this report to Richards Memorial Hospital within 5 business days.

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](mailto:George.Reeb@oig.hhs.gov) or James C. Cox, Regional Inspector General for Audit Services, Region V, at (312) 353-2621 or through email at [James.Cox@oig.hhs.gov](mailto:James.Cox@oig.hhs.gov). Please refer to report number A-05-08-00083.

Attachment



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Office of Audit Services, Region V  
233 North Michigan Avenue  
Suite 1360  
Chicago, IL 60601

May 16, 2011

Report Number: A-05-08-00083

Ms. Peggy S. Borgfeld  
Chief Financial Officer  
Richards Memorial Hospital  
1700 Brazos Avenue  
Rockdale, TX 76567

Dear Ms. Borgfeld:

Enclosed is the U.S. Department of Health & Human Services (HHS), Office of Inspector General (OIG), final report entitled *Review of Select Medicare Conditions of Participation and Costs Claimed at Richards Memorial Hospital From October 1, 2004, Through September 30, 2007*. 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 Jaime Saucedo, Audit Manager, at (312) 353-8693 or through email at [Jaime.Saucedo@oig.hhs.gov](mailto:Jaime.Saucedo@oig.hhs.gov). Please refer to report number A-05-08-00083 in all correspondence.

Sincerely,

/James C. Cox/  
Regional Inspector General  
for Audit Services

Enclosure

**Direct Reply to HHS Action Official:**

Ms. Nanette Foster Reilly  
Consortium Administrator  
Consortium for Financial Management & Fee for Service Operations  
Centers for Medicare & Medicaid Services  
601 East 12<sup>th</sup> Street, Room 235  
Kansas City, MO 64106

Department of Health & Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF SELECT MEDICARE  
CONDITIONS OF PARTICIPATION  
AND COSTS CLAIMED AT  
RICHARDS MEMORIAL HOSPITAL  
FROM OCTOBER 1, 2004,  
THROUGH SEPTEMBER 30, 2007**



Daniel R. Levinson  
Inspector General

May 2011  
A-05-08-00083

# *Office of Inspector General*

<http://oig.hhs.gov>

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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.

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

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

## **EXECUTIVE SUMMARY**

### **BACKGROUND**

Pursuant to Title XVIII of the Social Security Act, the Medicare program provides health insurance for people aged 65 and over and those who are disabled or have permanent kidney disease. The Centers for Medicare & Medicaid Services (CMS) administers the program.

States can establish Medicare Rural Hospital Flexibility Programs and designate certain facilities as Critical Access Hospitals (CAH) (Social Security Act, § 1820, 42 U.S.C. § 1395i-4). CAHs must meet certain Medicare Conditions of Participation (CoP) (42 CFR part 485, subpart F) and guidelines established by CMS.

CAHs, with CMS approval, can have up to 25 inpatient beds used for acute care or swing-bed services (Social Security Act, § 1820(c)(2)(B)(iii), 42 U.S.C. § 1395i-4(c)(2)(B)(iii)). CAHs receive Medicare reimbursement totaling 101 percent of allowable, allocable, and reasonable costs for payments for services furnished during cost-reporting periods beginning on or after January 1, 2004 (Social Security Act, §§ 1814(l), 1834(g)(1), and 1883(a)(3); 42 U.S.C. §§ 1395f(1), 1395m(g)(1), and 1395tt(a)(3)).

Rockdale Blackhawk, LLC, doing business as Richards Memorial Hospital (the hospital), located in Rockdale, Texas, is a wholly owned for-profit subsidiary of KJJO Ltd., doing business as Hospital Management Partners. On October 1, 2004, Texas designated the hospital a CAH providing inpatient and outpatient services. The hospital received Medicare reimbursement totaling \$16.6 million for costs reported in its fiscal years (FY) 2005, 2006, and 2007 Medicare cost reports.

### **OBJECTIVES**

Our objectives were to determine whether the hospital (1) complied with select Medicare CoP and (2) reported costs that were allowable and disclosed in its FYs 2005, 2006, and 2007 Medicare cost reports in accordance with Federal requirements.

### **SUMMARY OF FINDINGS**

The hospital was noncompliant with a Medicare CoP, reported unallowable costs in its Medicare cost reports, and did not properly disclose related-party rental costs. Contrary to Federal regulations, the hospital did not comply with a Medicare CoP because it did not maintain current and active network agreements with other hospitals during our audit period. The hospital also reported \$1,060,512 of unallowable costs in its FYs 2005, 2006, and 2007 Medicare cost reports. Specifically, the hospital reported \$804,426 in unsupported costs, \$197,827 in unallocable costs, and \$58,259 in costs unrelated to patient care. Additionally, the hospital did not properly disclose \$213,228 in related-party rental costs in its Medicare cost reports.

## **RECOMMENDATIONS**

We recommend that the hospital:

- establish and maintain network agreements with other hospitals;
- revise and resubmit its FYs 2005, 2006, and 2007 Medicare cost reports to properly reflect the exclusion of the \$1,060,512 of unallowable costs and the disclosure of \$213,228 of related-party rental costs; and
- ensure that it reports only allowable costs and properly discloses related-party transactions in future Medicare cost reports.

## **AUDITEE COMMENTS**

Regarding our first recommendation, the hospital said that it “has active network agreements in place” and provided a copy of an agreement as part of its comments. Regarding our second recommendation, the hospital said that the fiscal intermediary/CMS had audited all cost reports filed before the end of FY 2008 and had eliminated all expenses that were not allowable or considered related-party transactions. The hospital also stated that it had “taken what was audited in prior years to review current and future allowable expenses.” The hospital concurred with our third recommendation.

The hospital’s comments are included as the Appendix. We excluded the network agreement to protect proprietary information.

## **OFFICE OF INSPECTOR GENERAL RESPONSE**

Nothing in the hospital’s comments caused us to change our findings or recommendations. Regarding the first recommendation, the auditee provided a network agreement that predated the hospital’s designation as a CAH. The hospital should have amended its network agreement or entered into a new agreement after it became a CAH in 2004 to comply with Federal regulations (42 CFR § 485.616(a)). Regarding our second recommendation, although the fiscal intermediary reviewed the hospital’s cost reports, our detailed review revealed both previously unidentified unallowable costs and undisclosed related-party transactions.

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## INTRODUCTION

### BACKGROUND

Pursuant to Title XVIII of the Social Security Act, the Medicare program provides health insurance for people aged 65 and over and those who are disabled or have permanent kidney disease. The Centers for Medicare & Medicaid Services (CMS) administers the program.

#### Critical Access Hospitals

States can establish Medicare Rural Hospital Flexibility Programs and designate certain facilities as Critical Access Hospitals (CAH) (Social Security Act, § 1820; 42 U.S.C. § 1395i-4). CAHs must meet certain Medicare Conditions of Participation (CoP) (42 CFR part 485, subpart F) and guidelines established by CMS.

CAHs, with CMS approval, can have up to 25 inpatient beds used for acute care or swing-bed services (Social Security Act, § 1820(c)(2)(B)(iii); 42 U.S.C. § 1395i-4(c)(2)(B)(iii)).<sup>1</sup> CAHs receive Medicare reimbursement totaling 101 percent of allowable, allocable, and reasonable costs for payments for services furnished during cost-reporting periods beginning on or after January 1, 2004 (Social Security Act, §§ 1814(l), 1834(g)(1), and 1883(a)(3); 42 U.S.C. §§ 1395f(1), 1395m(g)(1), and 1395tt(a)(3)).

#### Rockdale Blackhawk, LLC

Rockdale Blackhawk, LLC, doing business as Richards Memorial Hospital (the hospital), located in Rockdale, Texas, is a wholly owned for-profit subsidiary of KJJO Ltd., doing business as Hospital Management Partners. On November 1, 2006, Blackhawk Healthcare, LLC (Blackhawk), purchased the hospital operations from the Rockdale Hospital District (the District) through a purchase lease assumption agreement.<sup>2</sup> Subsequently, on November 30, 2010, Hospital Management Partners purchased the hospital from Blackhawk.

On October 1, 2004, Texas designated the hospital a necessary provider and a CAH under the provisions of 42 CFR § 485.606. The hospital provides inpatient and outpatient services. The hospital received Medicare reimbursement totaling \$16.6 million for costs reported in its fiscal years (FY) 2005, 2006, and 2007 Medicare cost reports.

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<sup>1</sup> A swing bed can be used interchangeably for inpatient care or skilled nursing care. A patient “swings” or transitions from receiving inpatient services to receiving skilled nursing services.

<sup>2</sup> In 1994, Richards Memorial Hospital filed for bankruptcy. To help the hospital survive and generate additional revenue, the District, a county taxing authority, was created. At that time, the District took over the day-to-day operations of the hospital.

## **OBJECTIVES, SCOPE, AND METHODOLOGY**

### **Objectives**

Our objectives were to determine whether the hospital (1) complied with select Medicare CoP and (2) reported costs that were allowable and disclosed in its FYs 2005, 2006, and 2007 Medicare cost reports in accordance with Federal requirements.

### **Scope**

We reviewed the hospital's compliance with select Medicare CoP and costs reported for the period October 1, 2004, through September 30, 2007, totaling \$16.6 million.<sup>3</sup>

We limited our internal control review to obtaining an overall understanding of the hospital's policies and procedures for complying with the Medicare CoP and reporting costs in its Medicare cost reports.

We performed our fieldwork at the hospital in Rockdale, Texas.

### **Methodology**

To accomplish our objectives, we:

- reviewed applicable Federal CAH requirements, including CMS's *State Operations Manual* and its interpretive guidelines in Appendix W related to Medicare CoP;
- reviewed the hospital's policies and procedures related to compliance with select Medicare CoP and cost-reporting requirements;
- analyzed related-party transactions between the hospital and its affiliated parties;
- analyzed the hospital's financial statements and judgmentally reviewed \$2,948,962 in costs from Medicare cost reports for the audit period and determined whether the costs were allowable;
- analyzed \$1,045,243 of home office costs that Blackhawk allocated to the hospital and that the hospital reported on its FY 2007 Medicare cost report and determined whether the costs were allowable; and
- counted the number of inpatient beds available for use.

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

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<sup>3</sup> The hospital's Medicare cost-reporting period is October 1 through September 30. The hospital became a CAH on October 1, 2004, and Blackhawk purchased the Hospital on November 1, 2006. We reviewed three cost-reporting periods: a 12-month cost-reporting period ended September 30, 2005, a 13-month cost-reporting period ended October 31, 2006, and an 11-month cost-reporting period ended September 30, 2007.

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.

## **FINDINGS AND RECOMMENDATIONS**

The hospital was noncompliant with a Medicare CoP, reported unallowable costs in its Medicare cost reports, and did not properly disclose related-party rental costs. Contrary to Federal regulations, the hospital did not comply with a Medicare CoP because it did not maintain current and active network agreements with other hospitals during our audit period. The hospital also reported \$1,060,512 of unallowable costs in its FYs 2005, 2006, and 2007 Medicare cost reports. Specifically, the hospital reported \$804,426 in unsupported costs, \$197,827 in unallocable costs, and \$58,259 in costs unrelated to patient care. Additionally, the hospital did not properly disclose \$213,228 in related-party rental costs in its Medicare cost reports.

### **NONCOMPLIANCE WITH A CONDITION OF PARTICIPATION**

#### **Federal Regulations**

Federal regulations (42 CFR § 485.616(a)) state that a CAH that is a member of a rural health network must have an agreement with at least one hospital that is a member of the network for purposes of (1) patient referral and transfer, (2) development and use of the network's communications system, and (3) provisions for emergency and nonemergency transportation between the hospitals.

#### **Network Agreements**

Contrary to Federal regulations, the hospital did not comply with a Medicare CoP because it did not maintain current and active network agreements with other hospitals during our audit period. Without proper agreements with other hospitals for patient referral and transfer, communications systems, and transportation, the hospital may not be able to properly serve the community. In December 2008, hospital personnel stated that the hospital was in the process of entering into agreements with other hospitals or a rural health network. However, at the time of our audit, the network agreement did not exist.

### **UNALLOWABLE COSTS**

The hospital reported questioned costs totaling \$1,060,512, as detailed in Table 1, in its FYs 2005, 2006, and 2007 Medicare cost reports.

**Table 1: Total Unallowable Costs**

<b>Category</b>	<b>Unsupported Costs</b>	<b>Unallocable Costs</b>	<b>Costs Unrelated to Patient Care</b>	<b>Total</b>
Business office	\$374,611			\$374,611
Consulting	263,913	\$29,653		293,566
Salaries	159,671	145,796		305,467
Entertainment			\$33,750	33,750
Educational			24,000	24,000
Legal fees		19,997		19,997
Travel	3,955	2,381		6,336
Employee expenses	1,762			1,762
Dues and subscriptions	514			514
Lobbying			509	509
<b>Total Questioned Costs</b>	<b>\$804,426</b>	<b>\$197,827</b>	<b>\$58,259</b>	<b>\$1,060,512</b>

### **Federal Regulations**

Federal regulations (42 CFR § 413.9) and the *Provider Reimbursement Manual* (PRM), publication 15, part 1, chapter 21, §§ 2102.1 and 2102.2, provide that payments to a hospital must be based on the reasonable cost of Medicare services and related to the care of beneficiaries. Both criteria provide that reasonable cost includes all necessary and proper costs (both direct and indirect) incurred in rendering the services. Also, the PRM states, “Costs not related to patient care are costs which are not appropriate or necessary and proper in developing and maintaining the operation of patient care facilities and activities” (part 1, chapter 21, § 2102.3).

### **Unsupported Costs**

Federal regulations require that providers maintain sufficient financial records and statistical data for proper determination of costs payable under the Medicare program (42 CFR § 413.20(a)). Federal regulations also state that providers receiving payment on the basis of reimbursable cost must provide adequate cost data (42 CFR § 413.24(a)). These data must be based on financial and statistical records that must be capable of verification by qualified auditors.

Contrary to Federal regulations, the hospital reported \$804,426 of unsupported costs in its FYs 2005, 2006, and 2007 Medicare cost reports. The hospital did not provide sufficient documentation to support costs related to business office, consulting, salaries, travel, employee expenses, and dues and subscription costs.

### *Business Office*

The hospital did not provide any documentation supporting business office costs totaling \$374,611 in its FY 2006 Medicare cost report.

### *Consulting*

The hospital did not provide sufficient supporting documentation that costs for external consulting services totaling \$263,913 in its FYs 2005, 2006, and 2007 Medicare cost reports were related to patient care.

### *Home Office Salaries*

The hospital did not provide supporting documentation for a journal entry for home office employee salaries totaling \$112,965 sufficient to determine that the salaries were related to patient care. Additionally, the home office employed and allocated salaries to the hospital for two chief financial officers (CFO). The hospital did not provide sufficient documentation to show that costs of \$46,706 for the second CFO were related to patient care. In aggregate, \$159,671 in home office salaries reported by the hospital in its FY 2007 Medicare cost report were unsupported.

### *Travel*

The hospital did not provide sufficient supporting documentation that home office travel costs of \$3,955 that it reported in its FY 2007 Medicare cost report were related to patient care.

### *Employee Expenses*

The hospital did not provide sufficient supporting documentation that home office employee holiday party costs of \$1,762 that it reported in its FY 2007 Medicare cost report were related to patient care.

### *Dues and Subscriptions*

The hospital did not provide sufficient supporting documentation that home office trade association dues costs of \$514 that it reported in its FY 2007 Medicare cost report were related to patient care.

### **Unallocable Costs**

The PRM, part 1, chapter 21, § 2150.3B, states that “[a]llowable costs incurred for the benefit of, or directly attributable to, a specific provider or nonprovider activity must be allocated directly to the chain entity for which they were incurred.”

Contrary to CMS’s requirements, the hospital reported \$197,827 of unallocable costs in its FY 2007 Medicare cost report.

### *Salaries*

Blackhawk allocated \$145,796 of salaries to the hospital in FY 2007. The hospital included these unallocable salaries in its FY 2007 Medicare cost report. These costs included a salary totaling \$94,185 for the director of employee relations for which the hospital did not have documentation to support her efforts and whose unsigned position description outlined duties that did not benefit patient care or the hospital; salaries totaling \$27,883 that were for a period before Blackhawk's purchase of the hospital; annual bonuses totaling \$20,691 that were paid to home office employees in the month of December 2006, a month after the purchase of the hospital; and a portion of salaries totaling \$3,037 that were attributable to Blackhawk's other managed hospital.

### *Consulting*

Blackhawk allocated \$29,653 of professional costs to the hospital in FY 2007. The hospital included these unallocable professional costs in its FY 2007 Medicare cost report. These consulting costs were related to another related entity.

### *Legal Fees*

Blackhawk allocated \$19,997 of home office legal fees to the hospital in FY 2007. The hospital included these unallocable legal fees in its FY 2007 Medicare cost report. The fees related to various legal services unrelated to the hospital and to issues such as the potential purchase of a business and other real estate development ventures.

### *Travel*

Blackhawk allocated \$2,381 of home office travel costs to the hospital in FY 2007. The hospital included these unallocable travel costs in its FY 2007 Medicare cost report. The costs were for a home office employee's travel costs attributable to Blackhawk's other managed hospital.

### **Costs Unrelated to Patient Care**

The PRM states that costs not related to patient care are costs that are not appropriate or necessary (part 1, chapter 21, § 2102.3).

The PRM section titled "Cost of Entertainment" states that costs of entertainment, including tickets to sporting events, alcoholic beverages, golf outings, and other entertainment events, are not allowable in computing reimbursable costs (part 1, chapter 21, § 2105.8).

The PRM section titled "Part-Time Education" states that costs of part-time education for bona fide employees (excluding part-time employees) at properly accredited academic or technical institutions devoted to undergraduate and/or graduate work are allowable costs provided that "[a] direct relationship exists between the recommended training and job responsibilities" (part 1, chapter 4, § 416.3).

The PRM section titled "Political and Lobbying Activities" states, "Provider political and lobbying activities are not related to the care of patients. Therefore, costs incurred for such

activities are unallowable” (part 1, chapter 21, § 2139). Furthermore, the PRM section titled “Organization Dues Related to Lobbying and Political Activities” states, “Trade or other organizations and associations often engage in lobbying and political activities as part of their activities. Therefore ..., the portion of an organization’s dues or other payments related to these activities, including special assessments, is an unallowable cost” (§ 2139.3).

Contrary to CMS’s requirements, the hospital reported \$58,259 for costs unrelated to patient care in its FYs 2005, 2006, and 2007 Medicare cost reports.

#### *Entertainment*

Contrary to CMS’s requirements, the hospital reported unallowable entertainment costs totaling \$33,750 in its FY 2007 Medicare cost report. The costs related to various golf outings, liquor purchases, clothes purchased for the hospital’s inauguration, and gifts to select employees.

#### *Educational*

Contrary to CMS’s requirements, the hospital reported unallowable costs totaling \$24,000 (\$12,000 per year) in its FYs 2005 and 2006 Medicare cost reports related to educational assistance for its chief executive officer to attend law school. A direct relationship did not exist between the education assistance and the employee’s responsibilities.

#### *Lobbying*

Contrary to CMS’s requirements, the hospital reported a total of \$509 for unallowable lobbying costs in its FYs 2005, 2006, and 2007 Medicare cost reports for the lobbying activities portion of association dues payments. The hospital reported lobbying costs of \$450 (\$200 in FY 2005, \$220 in FY 2006, and \$30 in FY 2007) for the hospital and \$59 that was allocated from its home office in FY 2007.

## **DISCLOSURE OF RELATED-PARTY RENTAL COSTS**

### **Federal Requirements**

Federal regulations provide that costs applicable to facilities furnished to the provider by a related organization<sup>4</sup> are allowable “at the cost to the related organization” (42 CFR § 413.17(a)). Moreover, it states that “such cost must not exceed the price of comparable services, facilities, or supplies that could be purchased elsewhere.” Additionally, the PRM states, “Control exists where an individual or an organization has the power, directly or indirectly, significantly to influence or direct the actions or policies of an organization or institution” (part 1, chapter 10, § 1002.3).

CMS’s instructions for preparation of a hospital cost report, Form CMS-2552-96 in the PRM (part 2, chapter 36, § 3614), state that providers must use worksheet A-8-1 to include information for reporting costs of services from related organizations. According to these instructions, part A

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<sup>4</sup> The term “related to the provider” is defined at 42 CFR § 413.17.

of the worksheet should show allowable cost at the cost to the related organizations, with part B showing the relationship to the organizations identified in part A.

### Rental Costs

Contrary to CMS’s instructions, the hospital did not properly disclose \$213,228 for related-party rental costs on Worksheet A-8-1 of its FYs 2005, 2006, and 2007 Medicare cost reports. The hospital did not disclose other related-organization rental transactions it had with the hospital’s contracted physicians and with an external consultant in its FYs 2005, 2006, and 2007 Medicare cost reports, as detailed in Table 2.

**Table 2: Undisclosed Related-Parties Rental Costs**

	<b>FY 2005</b>	<b>FY 2006</b>	<b>FY 2007</b>	<b>Total</b>
Physician A (rural health clinic)	\$47,001	\$50,918	\$58,609	\$156,528
Physician B (provider-based clinic)			42,700	42,700
External consultant (sleep clinic)			14,000	14,000
<b>Total Undisclosed Rental Costs</b>	<b>\$47,001</b>	<b>\$50,918</b>	<b>\$115,309</b>	<b>\$213,228</b>

Physicians and an external consultant who worked for the hospital owned buildings that were leased to the hospital for operating a rural health clinic, a provider-based clinic, and a sleep clinic. In August 2008, hospital officials advised us that these individuals were related parties. However, the hospital did not disclose this fact in its FYs 2005, 2006, and FY 2007 Medicare cost reports.

### RECOMMENDATIONS

We recommend that the hospital:

- establish and maintain network agreements with other hospitals;
- revise and resubmit its FYs 2005, 2006, and 2007 Medicare cost reports to properly reflect the exclusion of the \$1,060,512 of unallowable costs and the disclosure of \$213,228 of related-party rental costs; and
- ensure that it reports only allowable costs and properly discloses related-party transactions in future Medicare cost reports.

### AUDITEE COMMENTS

Regarding our first recommendation, the hospital said that it “has active network agreements in place” and provided a copy of an agreement as part of its comments. Regarding our second recommendation, the hospital said that the fiscal intermediary/CMS had audited all cost reports filed before the end of FY 2008 and had eliminated all expenses that were not allowable or considered related-party transactions. The hospital also stated that it had “taken what was audited in prior years to review current and future allowable expenses.” The hospital concurred with our third recommendation.

The hospital's comments are included as the Appendix. We excluded the network agreement to protect proprietary information.

#### **OFFICE OF INSPECTOR GENERAL RESPONSE**

Nothing in the hospital's comments caused us to change our findings or recommendations. Regarding the first recommendation, the auditee provided a network agreement that predated the hospital's designation as a CAH. The hospital should have amended its network agreement or entered into a new agreement after it became a CAH in 2004 to comply with Federal regulations (42 CFR § 485.616(a)). Regarding our second recommendation, although the fiscal intermediary reviewed the hospital's cost reports, our detailed review revealed both previously unidentified unallowable costs and undisclosed related-party transactions.

# **APPENDIX**

### APPENDIX: AUDITEE COMMENTS



March 3, 2011

James C. Cox  
 Regional Inspector General for Audit Services  
 Office of Audit Services, Region V  
 233 North Michigan Avenue  
 Suite 1360  
 Chicago, IL 60601

Report Number: A-05-08-00083

*Re: Review of Select Medicare Conditions of Participation and Costs Claimed at Richards Memorial Hospital from October 1, 2004, through September 30, 2007.*

Dear Mr. Cox,

We have received the OIG draft report and have reviewed the findings and recommendations. Enclosed are our comments on the Draft Reports recommendations.

- Recommendation: Establish and maintain network agreements with other hospitals.

**Response:**

Richards Memorial Hospital has active network transfer agreements in place and is in compliance with this condition of participation. See attached.\*

- Recommendation: Thoroughly review all expenses in current and future cost reports to ensure proper allowable expense statement as well as note any and all related parties associated with each cost report.

**Response:**

For all cost reports filed before FYE 2008 trailblazer/CMS has already audited these cost reports and therefore kicked out all expenses that were not allowable or considered related party. We have taken what was audited in prior years to review current and future allowable expenses.

- Recommendation: Ensure that it reports only allowable costs and properly discloses related-party transactions in future Medicare cost reports.

Richards Memorial Hospital 1700 Brasco Avenue Rockdale, TX 76567 P: 512.446.4500 F: 512.446.8524	Orthopedic & Rehabilitation Care Center 1701 Pezos Rockdale, TX 76567 P: 512.430.6466 F: 512.430.6470	Family Care Center 1700 Brasco Avenue Rockdale, TX 76567 P: 512.446.4545 F: 512.446.4580	Little River Medical Clinic - Rockdale 602 North Main Rockdale, TX 76567 P: 512.446.4555 F: 512.446.4533	Little River Medical Clinic - Cameron 708 North Crockett Cameron, TX 76520 P: 254.697.6554 F: 254.697.6613
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\*Office of Inspector General Note—We excluded the copy of the network agreement to protect proprietary information.



**Response:**

We concur with the finding that Richards Memorial Hospital claimed unallowable costs and did not properly disclose related-party transactions. Richards Memorial Hospital has taken corrective action by reviewing policies and procedures to ensure that adequate classifications of allowable versus non-allowable transactions are properly accounted for. As part of the annual contract review process, rental agreements are reviewed for related parties.

We appreciate the opportunity to comment on the report submitted.

Sincerely,

A handwritten signature in black ink, appearing to read "Peggy S. Borgfeld".

Peggy S. Borgfeld  
Chief Financial Officer

Richards Memorial Hospital 1700 Brazos Avenue Rockdale, TX 76507 P: 512 446 4500 F: 512 446 6524	Orthopedic & Rehabilitation Care Center 1701 Peacor Rockdale, TX 76507 P: 512 430 6498 F: 512 430 6470	Family Care Center 1700 Brazos Avenue Rockdale, TX 76507 P: 512 446 4545 F: 512 446 4559	Little River Medical Clinic - Rockdale 602 North Main Rockdale, TX 76507 P: 512 446 4555 F: 512 446 4533	Little River Medical Clinic - Cameron 708 North Crockett Cameron, TX 76520 P: 254 897 8554 F: 254 897 8943
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