



DEPARTMENT OF HEALTH AND HUMAN SERVICES

OFFICE OF INSPECTOR GENERAL

WASHINGTON, DC 20201



May 4, 2012

TO: Marilyn Tavenner
Acting Administrator
Centers for Medicare & Medicaid Services

FROM: /Kay L. Daly/ for
Gloria L. Jarmon
Deputy Inspector General for Audit Services

SUBJECT: Southern California Renal Disease Council, Inc., Claimed Unallowable and Unsupported Costs Under Medicare Contract Number HHSM-500-2006-018C (A-09-11-02044)

Attached, for your information, is an advance copy of our final report on costs claimed by Southern California Renal Disease Council, Inc. (Council), to administer the end-stage renal disease Network Organization Program as a Federal contractor. We will issue this report to the Council within 5 business days. The Centers for Medicare & Medicaid Services, Office of Acquisition and Grants Management, requested that we conduct this contract closeout audit.

If you have any questions or comments about this report, please do not hesitate to call me, or your staff may contact Brian P. Ritchie, Assistant Inspector General for the Centers for Medicare & Medicaid Audits, at (410) 786-7104 or through email at Brian.Ritchie@oig.hhs.gov or Lori A. Ahlstrand, Regional Inspector General for Audit Services, Region IX, at (415) 437-8360 or through email at Lori.Ahlstrand@oig.hhs.gov. Please refer to report number A-09-11-02044.

Attachment



DEPARTMENT OF HEALTH AND HUMAN SERVICES

OFFICE OF INSPECTOR GENERAL



OFFICE OF AUDIT SERVICES, REGION IX
90 - 7TH STREET, SUITE 3-650
SAN FRANCISCO, CA 94103

May 7, 2012

Report Number: A-09-11-02044

Ms. Harriet L. Edwards
Executive Director
Southern California Renal Disease Council, Inc.
6255 Sunset Boulevard, Suite 2211
Los Angeles, CA 90028

Dear Ms. Edwards:

Enclosed is the U.S. Department of Health and Human Services (HHS), Office of Inspector General (OIG), final report entitled *Southern California Renal Disease Council, Inc., Claimed Unallowable and Unsupported Costs Under Medicare Contract Number HHSM-500-2006-018C*. 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 Jessica Kim, Audit Manager, at (323) 261-7218, extension 702, or through email at Yun.Kim@oig.hhs.gov. Please refer to report number A-09-11-02044 in all correspondence.

Sincerely,

/Lori A. Ahlstrand/
Regional Inspector General
for Audit Services

Enclosure

Direct Reply to HHS Action Official:

Mr. Daniel F. Kane
Director
Office of Acquisition and Grants Management
Centers for Medicare & Medicaid Services
Mail Stop C2-21-15
7500 Security Boulevard
Baltimore, MD 21244-1850

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**SOUTHERN CALIFORNIA RENAL
DISEASE COUNCIL, INC.,
CLAIMED UNALLOWABLE AND
UNSUPPORTED COSTS UNDER
MEDICARE CONTRACT NUMBER
HHSM-500-2006-018C**



Daniel R. Levinson
Inspector General

May 2012
A-09-11-02044

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

BACKGROUND

The Social Security Amendments of 1972, P.L. No. 92-603, extended Medicare coverage to individuals with end-stage renal disease (ESRD) who require dialysis or kidney transplantation. The ESRD Amendments of 1978, P.L. No. 95-292, authorized the formation of ESRD network areas and the establishment of the Network Organization Program (program) to ensure the effective and efficient administration of program benefits.

The Centers for Medicare & Medicaid Services (CMS) contracts with 18 ESRD Network Organizations (network) to administer the program. According to CMS's *Medicare ESRD Network Organizations Manual*, the networks are responsible for "conducting activities in the areas of quality improvement, community information and resources, administration, and information management."

Southern California Renal Disease Council, Inc. (Council), a nonprofit organization, is one of the 18 networks. The Council administers the program for an area covering 13 California counties. As a nonprofit organization that was awarded a Federal contract, the Council must follow the cost principles in the Office of Management and Budget Circular A-122.

We reviewed \$5,454,108 of the \$6,680,140 that the Council claimed under Medicare contract number HHSM-500-2006-018C, which is a cost-reimbursable contract for the period July 1, 2006, through September 29, 2010. In accordance with our agreement with the contracting officer, we did not review subcontract costs of \$913,695. We also did not review fixed fees of \$312,337.

CMS requested that we conduct this contract closeout audit. The Council used provisional rates based on estimated costs to calculate fringe benefits and indirect costs that it claimed for reimbursement. CMS asked us to calculate the Council's fringe benefit and indirect cost rates using actual costs. CMS might use those rates when negotiating and settling with the Council during the contract closing process.

OBJECTIVES

Our objectives were to (1) determine whether the costs that the Council claimed were allowable under the terms of the contract and pursuant to applicable Federal regulations and (2) calculate the fringe benefit and indirect cost rates based on actual costs.

SUMMARY OF FINDINGS

Of the \$5,454,108 of costs we reviewed, \$2,601,054 was allowable under the terms of the contract and pursuant to applicable Federal regulations. The remaining \$2,853,054 consisted of \$112,670 in other direct costs that we determined were unallowable and \$2,740,384 that we set aside for CMS resolution because the Council did not maintain supporting documentation for

review. The Council claimed unallowable or unsupported costs because it did not have adequate controls to account for costs claimed under Federal contracts.

We calculated fringe benefit and indirect cost rates based on actual costs.

RECOMMENDATIONS

We recommend that the Council:

- refund to the Federal Government \$112,670 for unallowable costs,
- work with CMS to determine the allowability of \$2,740,384 that we set aside and refund to the Federal Government any amount that is determined to be unallowable, and
- strengthen its controls to account for costs claimed under Federal contracts.

AUDITEE COMMENTS

In its written comments on our draft report, the Council concurred with our first and second recommendations and provided information on actions that it had taken or planned to take to address our third recommendation. The Council's comments are included in their entirety as Appendix B.

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INTRODUCTION

BACKGROUND

End-Stage Renal Disease Network Organization Program

The Social Security Amendments of 1972, P.L. No. 92-603, extended Medicare coverage to individuals with end-stage renal disease (ESRD) who require dialysis or kidney transplantation. The ESRD Amendments of 1978, P.L. No. 95-292, authorized the formation of ESRD network areas and the establishment of the Network Organization Program (program), consistent with criteria that the Secretary of Health and Human Services determined would ensure the effective and efficient administration of program benefits.

The Centers for Medicare & Medicaid Services (CMS) contracts with 18 ESRD Network Organizations (network) to administer the program for each State, each territory, and the District of Columbia. According to CMS's *Medicare ESRD Network Organizations Manual*, the networks are responsible for "conducting activities in the areas of quality improvement, community information and resources, administration, and information management." The networks work with consumers, ESRD facilities, and other providers of ESRD services to refine care delivery systems to ensure that ESRD patients get the right care at the right time.

Southern California Renal Disease Council, Inc.

Southern California Renal Disease Council, Inc. (Council), a nonprofit organization, is one of the 18 networks that serves as a Federal contractor to administer the program. The Council's area covers 13 California counties from the Mexico and Arizona/Nevada borders to the central California coastal area and inland. There are 297 member dialysis facilities and 17 renal transplant centers in the area that provide treatment to more than 30,000 dialysis patients and 12,000 transplant recipients.

Under Medicare contract number HHSM-500-2006-018C, which is a cost-reimbursable contract, the Council claimed \$6,680,140 for administering the program. Of this amount, \$1,141,453 was for fringe benefits and \$706,601 was for indirect costs that the Council claimed using provisional rates based on estimated costs. The purpose of this contract was "to meet the requirements of [Federal directives] related to improving the quality of care provided to patients with ESRD through to end of life." The contract was for the period July 1, 2006, through September 29, 2010.¹ During this period, this contract was the Council's primary source of revenue.² In this report, we refer to contract number HHSM-500-2006-018C as "the contract."

¹ As of September 30, 2010, CMS had awarded the Council a fixed-price contract.

² The Council had another cost-reimbursable contract with CMS to provide centralized support for the program for the period September 30, 2002, through September 28, 2006. We issued a separate report for that contract on April 23, 2012 (A-09-11-02005, *Southern California Renal Disease Council, Inc., Claimed Unallowable and Unsupported Costs Under Medicare Contract Number 500-02-NW18CH*).

The contract required the Council to comply with the Office of Management and Budget (OMB) Circular A-122, *Cost Principles for Non-Profit Organizations*, and applicable sections of the Federal Acquisition Regulation (FAR). In addition, the contract stated that a contract closeout audit would be performed to determine whether the Council complied with the contract, OMB Circular A-122's cost principles for nonprofit organizations receiving Federal awards, the FAR, and other relevant guidelines.

CMS requested that we conduct this contract closeout audit. FAR § 52.216-7 requires CMS to negotiate and settle with the Council the total claimed costs, including the final fringe benefits and indirect costs. The Council used provisional rates based on estimated costs to calculate fringe benefits and indirect costs. CMS asked us to calculate the Council's fringe benefit and indirect cost rates using actual costs. CMS might use those rates during the contract closing process.

OBJECTIVES, SCOPE, AND METHODOLOGY

Objectives

Our objectives were to (1) determine whether the costs that the Council claimed were allowable under the terms of the contract and pursuant to applicable Federal regulations and (2) calculate the fringe benefit and indirect cost rates based on actual costs.

Scope

We reviewed \$5,454,108 of the \$6,680,140 that the Council claimed under Medicare contract number HHSM-500-2006-018C for the period July 1, 2006, through September 29, 2010. In accordance with our agreement with the contracting officer, we did not review subcontract costs of \$913,695. We also did not review fixed fees of \$312,337.

We did not conduct a full-scope audit addressing the Council's performance. Also, we did not review the overall internal control structure of the Council. We limited our review of the Council's internal controls to those that were significant to the objectives of our audit.

We conducted our audit from May to October 2011 and performed fieldwork at the Council's office in Los Angeles, California.

Methodology

To accomplish our objectives, we:

- reviewed applicable Federal laws and regulations;
- reviewed the terms of the contract and modifications that CMS made;
- reviewed minutes of board of directors' meetings;

- reviewed the Council’s policies and/or procedures on the allocation of costs, property management, payroll, and travel;
- interviewed Council officials to gain an understanding of the Council’s accounting procedures;
- reviewed the Council’s financial statements for the periods July 1, 2006, through June 30, 2007; July 1, 2007, through June 30, 2008; and July 1, 2008, through June 30, 2009;³
- reconciled the expenses recorded in the Council’s general ledger with expenses claimed under the contract;
- reviewed consultant agreements for nine consultants paid over \$1,000;
- reconciled the claimed costs for salaries and wages with the Council’s payroll distribution records;
- analyzed the general ledger to identify large, unusual, and/or recurring transactions and judgmentally selected transactions for claimed costs (direct and indirect costs and fringe benefits) to determine their allowability;⁴
- reviewed costs claimed to determine whether fringe benefits and indirect costs were treated consistently in like circumstances; and
- calculated the fringe benefit and indirect cost rates for each contract year based on the actual costs recorded in the general ledger and the paid-time-off records.

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.

³ The financial statements for 2007–2008 were audited. The financial statements for 2006–2007 and 2008–2009 were unaudited.

⁴ When errors were identified for a particular element of cost from the judgmentally selected transactions, we expanded our review to determine the extent of the errors. We determined that the number, dollar amount, and type of transactions selected were sufficient based on the adequacy of supporting documentation.

FINDINGS AND RECOMMENDATIONS

Of the \$5,454,108 of costs we reviewed, \$2,601,054 was allowable under the terms of the contract and pursuant to applicable Federal regulations. The remaining \$2,853,054 consisted of \$112,670 in other direct costs that we determined were unallowable and \$2,740,384 that we set aside for CMS resolution because the Council did not maintain supporting documentation for review. The Council claimed unallowable or unsupported costs because it did not have adequate controls to account for costs claimed under Federal contracts. See Appendix A for a schedule of the costs claimed by the Council and the results of our audit, i.e., allowable, unallowable, and set-aside amounts.

We calculated fringe benefit and indirect cost rates based on actual costs. See Tables 1 and 2 for the provisional fringe benefit and indirect cost rates that the Council used and our revised rates.

SALARIES AND WAGES

OMB Circular A-122, Attachment B, subparagraph 8.m, states:

(1) Charges to awards for salaries and wages, whether treated as direct costs or indirect costs, will be based on documented payrolls approved by a responsible official(s) of the organization. The distribution of salaries and wages to awards must be supported by personnel activity reports

(2) Reports reflecting the distribution of activity of each employee must be maintained for all staff members (professionals and nonprofessionals) whose compensation is charged, in whole or in part, directly to awards. In addition, in order to support the allocation of indirect costs, such reports must also be maintained for other employees whose work involves two or more functions or activities if a distribution of their compensation between such functions or activities is needed in the determination of the organization's indirect cost rate(s)

Of the \$2,610,436 claimed for salaries and wages, \$1,016,693 was allowable.⁵ We set aside the remaining \$1,593,743 for CMS resolution because the Council did not maintain for review supporting documentation, such as personnel activity reports, that reflected the distribution of activity for each employee. Based on our review of the Council's payroll records, we were able to determine that the Council incurred these costs for salaries and wages. However, without personnel activity reports, we could not determine the amount of salaries and wages allocable to the contract.

⁵ The \$1,016,693 of allowable salaries and wages was for employees for which the Council maintained supporting documentation, such as payroll distribution records and personnel activity reports.

FRINGE BENEFITS

OMB Circular A-122, Attachment B, subparagraph 8.g.(2), states that fringe benefits can be treated as direct or indirect costs. Further, Attachment A, subparagraph C.1., states: “Indirect costs are those that have been incurred for common or joint objectives and cannot be readily identified with a particular final cost objective.”

FAR § 52.216-7(b)(1) states:

For the purpose of reimbursing allowable costs ... the term “costs” includes only— (i) Those recorded costs that, at the time of the request for reimbursement, the Contractor has paid by cash, check, or other form of actual payment for items or services purchased directly for the contract; (ii) When the Contractor is not delinquent in paying costs of contract performance in the ordinary course of business, costs incurred, but not necessarily paid for— ... (F) Properly allocable and allowable indirect costs

Of the \$1,141,453 claimed for fringe benefits,⁶ \$444,574 was allowable. We calculated the \$444,574 of fringe benefit costs by applying the revised fringe benefit rates based on actual costs (discussed below) to the allowable salaries and wages discussed in the previous section. We set aside for CMS resolution the remaining \$696,879 because it related to the \$1,593,743 in unsupported salaries and wages.

Table 1 illustrates the fringe benefit rates that the Council used to claim fringe benefits using provisional rates based on estimated costs, the fringe benefits claimed by the Council, our revised rates based on actual costs, and the fringe benefits calculated by applying the revised rates to the salaries and wages claimed by the Council. The fringe benefit costs claimed by the Council using provisional rates were less than costs calculated using our revised rates, except for the contract years ended June 30, 2007, and June 30, 2010.

⁶ The Council treated fringe benefits as indirect costs, except for fringe benefits claimed as direct costs (discussed in the section “Other Direct Costs”).

Table 1: Fringe Benefit Rates and Costs

Contract Year	Council Rate(s)⁷ (Percentage)	Costs Claimed Using the Council Rate	Revised Rate (Percentage)	Costs Calculated Using the Revised Rate
7/1/2006– 6/30/2007	47.0	\$269,007	43.17	\$247,075
7/1/2007– 6/30/2008	47.0 and 50.35	303,686	44.26	307,500
7/1/2008– 6/30/2009	47.39 and 47.49	284,714	49.53	317,696
7/1/2009– 6/30/2010	40.47	227,245	40.19	225,944
7/1/2010– 9/29/2010	40.47	56,801	44.91	63,039

INDIRECT COSTS

OMB Circular A-122, Attachment A, subparagraph E.1.d., states: “Final rate means an indirect cost rate applicable to a specified past period which is based on the actual costs of the period. A final rate is not subject to adjustment.”

FAR § 52.216-7(d)(2) states: “(i) The Contractor shall submit an adequate final indirect cost rate proposal to the Contracting Officer ... and auditor The Contractor shall support its proposal with adequate supporting data. (ii) The proposed rates shall be based on the Contractor’s actual cost experience for that period.” Further, FAR § 52.216-7(g) states: “At any time or times before final payment, the Contracting Officer may have the Contractor’s invoices or vouchers and statements of cost audited.”

Of the \$706,601 claimed for indirect costs, \$280,404 was allowable. We calculated the \$280,404 of indirect costs by applying the revised indirect cost rates based on actual costs (discussed below) to the allowable salaries and wages and fringe benefits discussed in previous sections. We set aside the remaining \$426,197 for CMS resolution because it related to the \$1,593,743 in unsupported salaries and wages and \$696,879 in fringe benefits applicable to the unsupported salaries and wages.

⁷ The Council used two different rates in 2007–2008 and 2008–2009. According to a Council official, the provisional rates were revised during each contract year based on the annual budget.

Table 2 illustrates the indirect cost rates that the Council used to claim indirect costs using provisional rates⁸ based on estimated costs, the indirect costs claimed by the Council, our revised rates based on actual costs, and the indirect costs calculated by applying the revised rates to the salaries and wages claimed by the Council and the applicable fringe benefits. The indirect costs claimed by the Council using provisional rates were less than costs calculated using our revised rates, except for the contract year ended June 30, 2010.

Table 2: Indirect Cost Rates and Indirect Costs

Contract Year	Council Rate(s)⁹ (Percentage)	Costs Claimed Using the Council Rate	Revised Rate (Percentage)	Costs Calculated Using the Revised Rate
7/1/2006– 6/30/2007	38.63 and 17.29	\$178,170	24.92	\$204,199
7/1/2007– 6/30/2008	17.29 and 18.36	166,076	21.77	218,160
7/1/2008– 6/30/2009	19.31 and 19.23	170,200	19.55	187,506
7/1/2009– 6/30/2010	19.49	153,729	18.61	146,516
7/1/2010– 9/29/2010	19.49	38,426	20.68	42,057

CONSULTANTS

OMB Circular A-122, Attachment A, subparagraph A.2., states that to be allowable under an award, costs must be reasonable for the performance of the award and adequately documented. Further, Attachment B, subparagraph 37(b), lists factors that are relevant in determining the allowability of consultant costs, including but not limited to the nature and scope of the service

⁸ The Council claimed the indirect costs by using provisional rates calculated as a ratio of the indirect cost pool (i.e., numerator) and the base (i.e., denominator). The indirect cost pool included estimated total facilities and administration costs, and the base included estimated total salaries and wages plus fringe benefits. We revised the indirect cost rates using actual costs.

⁹ The Council used two different rates in 2006–2007, 2007–2008, and 2008–2009. According to a Council official, the provisional rates were revised during each contract year based on the annual budget.

provided in relation to the service required, the necessity of contracting for the service, and the adequacy of the contractual agreement for the service (e.g., description of the service, estimate of time required, rate of compensation, and termination provisions).

Of the \$91,234 claimed for consultant costs, \$67,669 was allowable. We set aside the remaining \$23,565 for CMS resolution because the Council did not maintain for review consultant agreements that reflected the nature and scope of the services provided, the necessity of contracting for the services, or the adequacy of the contractual agreements. According to a Council official, the Council's previous executive director hired consultants without written agreements. Based on our review of the Council's invoices for consultants, we were able to determine that the Council incurred these consultant costs. However, without consultant agreements, we could not determine the reasonableness of the consultant costs.

OTHER DIRECT COSTS

OMB Circular A-122, Attachment A, subparagraph A.2., states that to be allowable under an award, costs must be reasonable for the performance of the award and adequately documented. Subparagraph B.1. states: "Direct costs are those that can be identified specifically with a particular final cost objective" Subparagraph C.1. states: "Indirect costs are those that have been incurred for common or joint objectives and cannot be readily identified with a particular final cost objective."

OMB Circular A-122, Attachment A, subparagraph D.3.b(4), states that in developing the indirect cost pool for general administration and general expenses, "special care should be exercised to ensure that costs incurred for the same purpose in like circumstances are treated consistently as either direct or indirect costs."

Of the \$781,017 claimed for other direct costs,¹⁰ \$668,347 was allowable. The remaining \$112,670 was unallowable and consisted of \$10,550 claimed incorrectly because of clerical errors and \$102,120 that the Council claimed as direct costs but should have included in the fringe benefit and indirect cost pools:

- The \$10,550 in unallowable costs was for direct costs incorrectly claimed on two public vouchers because of clerical errors.¹¹ The supporting transactions were less than the total costs claimed for other direct costs on the two public vouchers. The Council could not provide an explanation of why the total amount of the transactions was less than the total costs claimed.
- The \$102,120 in unallowable costs was for certain types of fringe benefits and indirect costs that the Council claimed as direct costs but should have included in the fringe benefit and indirect cost pools, respectively. The \$102,120 consisted of \$45,557 in fringe

¹⁰ Other direct costs included furniture and equipment, supplies, legal fees, meeting and conference expenses, postage fees, printing fees, recruiting fees, and telephone expenses.

¹¹ To claim costs for reimbursement, the Council submitted to CMS the Standard Form 1034, Public Voucher for Purchases and Services Other Than Personal.

benefits, such as health insurance and pension expenses, and \$56,563 in indirect costs, such as office supply expenses and dues and subscriptions. The Council did not ensure that these types of costs incurred for the same purpose in like circumstances were treated consistently as either fringe benefits or indirect costs. To be consistent with the requirements of OMB Circular A-122, we included the \$102,120 when calculating the revised fringe benefit and indirect cost rates.

LACK OF ADEQUATE CONTROLS

The Council did not have adequate controls to ensure that the costs claimed under the contract were allowable under the terms of the contract and pursuant to applicable Federal regulations. The Council did not maintain supporting documentation as required by Federal regulations, and the person who was responsible for the Council's accounting was not familiar with the requirement to treat costs consistently in like circumstances. Further, the Council did not have policies and procedures for documenting contractual agreements for consultant services. A Council official stated that many of the consultants had provided services to the Council for many years and that the Council's former executive director handled the procurement of consultant services during our audit period.

RECOMMENDATIONS

We recommend that the Council:

- refund to the Federal Government \$112,670 for unallowable costs,
- work with CMS to determine the allowability of \$2,740,384 that we set aside and refund to the Federal Government any amount that is determined to be unallowable, and
- strengthen its controls to account for costs claimed under Federal contracts.

AUDITEE COMMENTS

In its written comments on our draft report, the Council concurred with our first and second recommendations and provided information on actions that it had taken or planned to take to address our third recommendation. The Council's comments are included in their entirety as Appendix B.

OTHER MATTERS

REQUIRED ANNUAL SINGLE AUDIT

OMB Circular A-133 (*Audits of States, Local Governments, and Non-Profit Organizations*), subpart B, §__200(a), states: "Non-Federal entities that expend \$300,000 (\$500,000 for fiscal years ending after December 31, 2003) or more in a year in Federal awards shall have a single or program-specific audit conducted for that year"

OMB Circular A-133, subpart E, §__505, states that the auditor’s report must identify that the audit was conducted in accordance with this part and include a report on internal controls related to financial statements and major programs. This report must describe the scope of testing of internal controls and the results of the tests and, where applicable, refer to the separate schedule of findings and questioned costs described in paragraph (d) of this section.

The Council did not have single audits conducted for each year of our audit period, even though it expended more than \$500,000 in Federal awards in each of those years. The Council had its financial statements for the year ended June 30, 2008, audited by an independent auditor, but the audit report did not identify that the audit was conducted in accordance with OMB Circular A-133. Further, the audit report did not include a report on the internal controls related to financial statements and major programs as required by Federal regulations.

PROCUREMENT POLICIES AND PROCEDURES

OMB Circular A-110 (*Uniform Administrative Requirements for Grants and Agreements With Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations*), section __.43, requires that all procurement transactions be conducted in a manner to provide open and free competition. Section __.44(a) requires that all recipients establish written procurement procedures. Section __.45 states: “Some form of cost or price analysis shall be made and documented in the procurement files in connection with every procurement action.”

The Council did not establish written procurement procedures and did not have documentation to support that the procurement of consultants and equipment provided open and free competition or that a cost or price analysis was performed in procuring consultants and equipment.

APPENDIXES

**APPENDIX A: SCHEDULE OF COSTS CLAIMED AND RESULTS OF AUDIT
FOR THE PERIOD JULY 1, 2006, THROUGH SEPTEMBER 29, 2010**

Element of Cost	Claimed	Allowable	Unallowable	Set Aside
Salaries and Wages	\$2,610,436	\$1,016,693	\$0	\$1,593,743
Fringe Benefits	1,141,453	444,574	0	696,879
Indirect Costs	706,601	280,404	0	426,197
Consultants	91,234	67,669	0	23,565
Other Direct Costs	781,017	668,347	112,670	0
Travel	123,367	123,367	0	0
Total Costs	\$5,454,108	\$2,601,054	\$112,670	\$2,740,384

APPENDIX B: AUDITEE COMMENTS



Southern California
Renal Disease Council
INCORPORATED
ESRD NETWORK 18

April 2, 2012

Lori A. Ahlstrand
Regional Inspector General for Audit Services
Office of Audit Services, Region IX
90- 7th Street, Suite 3-650
San Francisco, CA. 94103

Re: Report Number: A-09-11-02044

Dear Ms. Ahlstrand:

Please find this letter in response to the U.S. Department of Health and Human Services, Office of Inspector General (OIG), and draft report entitled Southern California Renal Disease, Inc. Claimed and Unallowable and Unsupported Costs under Medicare Contract Number HHSM-500-2006-018C dated March 5, 2012.

According to the Summary of Finding, your audit team reviewed \$5,454,108 of costs of which \$2,601,054 were allowable, allocable and reasonable under the terms of the contract; The remaining \$2,853,054 consisted of \$112,670 in other direct costs that were determined to be unallowable; and \$2,740,384 that your audit team set aside for CMS resolution.

The recommendations issued by the audit team are as follows:

- Refund to the Federal Government \$112,607* for unallowable other direct costs,
- Work with CMS to determine the allowability of \$2,740,384 of the set aside funds and refund the amount determined by CMS to be unallowable,
- Strengthen its controls to account for costs claimed under Federal contracts.

Southern California Renal Disease Council, Inc. is presenting the following statements of concurrence for the above recommendations made by the OIG.

- SCRDC, Inc. concurs with the recommendation of refunding the \$112,607 to CMS for unallowable other direct costs.
- SCRDC, Inc. concurs with the recommendation of working with CMS to determine the allowability of the set aside amount of \$2,740,384.
- SCRDC, Inc. has begun implementing policies and procedures that strengthen and improve the control to accounts for costs claimed under Federal contracts.

Mission Statement

To provide leadership and assistance to renal dialysis and transplant facilities in a manner that supports continuous improvement in patient care, outcomes, safety and satisfaction.

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* **Office of Inspector General Note:** According to the auditee, the \$112,607 was intended to be \$112,670. The auditee concurred with the recommended refund of \$112,670.

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Southern California Renal Disease Council appreciates the opportunity to respond to the recommendations offered by the OIG; and would also like to include the following information:

1. The Contract Awards which were audited during this audit period were Cost Reimbursement Contracts rather than being a Fixed Contract.
2. The previous Executive Director during the audited contract years was replaced on December 28, 2008.
3. It has been brought to my attention that correspondence was sent to the Contracting Officer during the contracts: a) rates for indirect costs; b) and asking when the audit was to be scheduled. Please note that CMS audits for the Council had not been completed since the Contract Year 2001.
4. Current Administration has implemented policies and procedures that will bring the Council into compliance with the Office of Management and Budget (OMB) Circular 122-A, as well as the applicable sections of the Federal Acquisition Regulations (FAR). These implemented policies and procedures include but are not limited to:
 - a. **Salaries and Wages**
 - i. Employee activity reports (including timesheets) have been implemented to provide documentation for charging their compensation to the award.
 - ii. Payroll records are now maintained according to State and Federal laws.
 - iii. Employees dealing with wages, salaries and contract awards have been given the pertinent information from OMB Circular A-122 and FAR.
 - iv. Employee activity reports, timesheets and payroll records will be kept four years after CMS has performed the final audit of contract.
 - b. **Fringe Benefits Cost/Rate**
 - i. In order to calculate the fringe rate, policies and procedures have been implemented for cost contracts to utilized actual fringe costs in accordance with OMB Circular A-122 and FAR, and once approved by CMS, used throughout the contract period.
 - ii. Documents will be maintained four years after CMS has audited contract.
 - c. **Indirect Costs**
 - i. Policies and procedures are in place that will prevent the misallocation of indirect costs to direct costs and vice versa.
 - ii. The Council will submit an adequate final indirect cost rate proposal to the Contracting Officer and this final indirect rate will be supported by adequate supporting data. This indirect rate will be based on the Council's actual cost experience.
 - iii. Documents will be maintained four years after CMS has audited contract.
 - d. **Consultants**
 - i. Implemented policy directed at complying with the procurement of consultants according to the OMB Circular A-122 Attachment A, subparagraph A.2 and Attachment B, subparagraph 37(b); including creating a form for documenting the procurement of consultants and establishing a consultant agreement/contract which delineates the description of services, estimate of time required, rate of compensation and termination provisions.
 - ii. Any and all consultant selection will be conducted in such a manner as to provide open and free competition.
 - e. **Other Direct Costs**
 - i. Policies and procedures are in place that will prevent the misallocation of direct costs to Indirect costs and vice versa.
 - ii. The Council will identify and adequately record direct cost to appropriate accounts, along with maintain adequate supporting data.

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iii. Documents will be maintained four years after CMS has audited contract.

f. Required Annual Single Audit

i. This required Single Audit was implemented by the new Executive Director in 2010 as part of the increased fiscal awareness and effort to comply with contract requirements (OMB Circular A-133).

g. Lack of Adequate Internal Controls

i. Policies and procedures have been implemented, reviewed, or replaced to insure strict adherence to the Circular A-122 and FAR.

h. Procurement Policies and Procedures

i. Procurement Policies and procedures have been implemented to require that all procurement transactions be conducted in a manner to provide open and free competition, in adherence to the Circular A-110.

ii. Supporting documents will be maintained four years after CMS has audited contract.

Thank you for allowing us to review and respond to these audit finding.

Sincerely,

/Harriet L. Edwards/

Harriet L. Edwards, MSW/MSG
Executive Director