

PROVIDER REIMBURSEMENT REVIEW BOARD HEARING DECISION

2002-D41

PROVIDER –
Mercer Street Friends Center
Trenton, NJ

Provider No. 31-7062

vs.

INTERMEDIARY – Blue Cross and
Blue Shield Association/United
Government Services, LLC

DATE OF HEARING-

Cost Reporting Period Ended
June 30, 1996

CASE NO. 99-0286R

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ISSUE:

Was the interest paid on working capital loans from the Friend Center Fund and commercial banks necessary and allowable?

STATEMENT OF THE CASE AND PROCEDURAL HISTORY:

Mercer Street Friends (Provider) is a home health agency (HHA) located in Trenton, New Jersey. On June 29, 2000, the Provider Reimbursement Review Board (Board) issued Mercer Street Friends v. Blue Cross and Blue Shield Association/United Government Services, PRRB Case No. 2000-D68, June 29, 2000, Medicare & Medicaid Guide (CCH) Transfer Binder ¶ 80, 514 (Mercer) which stated that working capital interest expense is allowed on one-month's average operating expenses. The Intermediary's adjustment which disallowed all working capital interest was modified. The then Health Care Financing Administration (now Centers for Medicare and Medicaid Services (CMS)) Administrator declined to review the decision pursuant to 42 C.F.R. § 405.1875, and the Board decision became final. The Provider exercised its right to judicial review pursuant to 42 C.F.R. § 405.1877 by filing an action in the United States District Court for the District of New Jersey.

In a consent order dated March 26, 2001, the case was remanded to CMS, the Board and parties for further proceedings. The following was the Court Order.

Court Order

The above captioned case shall be remanded to the Department of Health and Human Services for additional proceedings including: (1) a supplemental hearing before the Provider Reimbursement Review Board ("PRRB") for the purpose of allowing the parties to present evidence regarding the applicability of the "donor restricted funds" exception to Medicare's related party rule, 42 C.F.R. § 413.153(c)(2), to this case, if any; and (2) the issuance of a new decision by the PRRB.

The Parties presented additional arguments and evidence in response to the Court's requirements. They chose to have a hearing on the submitted record. The Provider's representative, John W. Jansak, Esquire, of Harriman, Jansak and Wylie and the Intermediary's representative, Bernard M. Talbert, Esquire, of Blue Cross and Blue Shield Association submitted joint contentions relating to their agreed upon conclusion that payments of interest paid by the Provider to the Friends Center Fund meets the donor restricted funds exception in 42 C.F.R. § 413.153(c)(2).

JOINT CONTENTIONS OF PROVIDER AND INTERMEDIARY:

The Provider and Intermediary jointly contend that there is a conflict or inconsistency between a stipulation agreed to by the parties at the hearing and the Board's analysis supporting its decision. The transcript of the original hearing at page 6, line 8 through 14, reflects the following stipulation:

MR. JANSACK: There was also a stipulation reframing one of the issues, merging two of the issues together and indicating that it is agreed that the issue, shall pay to a related party meets the donor restricted fund exception of 42 C.F.R. § 413.153(c)(2).

CHAIRMAN KUES: Mr. Talbert, do you agree with that?

MR. TALBERT: Yes, sir.

CHAIRMAN KUES: That is associated with our issue number one, correct?

MR. JANSACK: Yes.

Regarding the Board's decision, the parties jointly contend that the Board apparently either overlooked the stipulation or affirmatively rejected it, without stating why. The third full paragraph in the DECISION, FINDINGS OF FACT, CONCLUSIONS OF LAW AND DISCUSSION should be considered in the context of the remand:

The Board notes that the Provider claimed \$113,000 in interest expense that the Intermediary disallowed. This included \$43,000 to commercial banks and \$70,000 to the Friends Center Fund. The Board finds that the \$29,090 it is allowing for working capital interest relates to the commercial lending interest. The Friends Center Fund interest is not allowed. The Board finds that the Provider and the Friends Center Fund are related parties under Medicare regulations at 42 CFR § 413.17. The parties in their joint stipulation agree that the various corporate entities and fund are related under Medicare principles. The Board finds that 42 C.F.R. § 413.153 does not allow loans from a related party. That section does allow certain exceptions to related party interest such as interest paid on loans from-donor-restricted funds and motherhouse interest. The Board finds neither of these two exceptions applicable in this case. There is no evidence to support the fact that the Friends Center Fund was a donor-restricted fund. In addition, the facts do not support an exception based on a "motherhouse" loan. The organizations existing are not religious institutions in and of themselves. They are non-profit care corporations, not religious orders. (Emphasis added).

Mercer at 201,641.

The parties contend that the purpose of their original stipulation was to eliminate the agreed upon conclusion that the appealing Provider and Friends Center Fund were related as a sole basis for the disallowance. A borrowing from an entity related to the provider, which uses restricted funds as the source of the loan, removes the related party taints under the regulatory definition of “proper.”

The Provider and the Intermediary state that they were not in agreement over the significance of the stipulation. However, they did agree that it was appropriate to characterize the Friends Center Fund as a restricted fund that could not be spent on routine operating expenses.

The parties contend that the Court remand has given them cause to revisit the stipulation. Based upon a review of documents in the original appeal record as well as evidence submitted with the joint contentions, the parties still believe that the fund is restricted to the extent that it cannot be used for working capital. A document supporting the stipulation is the Restated Certification of Incorporation of Friends Center Fund.¹ The key provision is at the beginning of Article II:

Second: The purposes for which the corporation is organized are:

To provide financial and other resources to support the mission, programs, expansion, continued existence and needs other than routine operating expenses of the Mercer Street Friends Center, a community oriented, multi-service, tax-exempt, charitable non-profit corporation based in Trenton, New Jersey.

Also, considered as evidence to support the parties position is Provider Exhibit 3 from the remand record. That is an affidavit from Ms. Judith Trachtenberg that describes the history of the Friends Center Fund, Inc. and sources of its funding. In addition, a declaration of Mr. Stephen Kitts² supplements Ms. Trachtenberg’s affidavit and the Restated Certificate of Incorporation. The September 26, 2001 affidavit states that Mr. Kitt was personally involved in soliciting almost all the donations to the fund. He advised all potential donors that the fund was a separate entity from the Mercer Street Friends Center, and that the funds would not be used for routine operating expenses of the Mercer Street Friends Center. All of the funds would be used to support the mission of the Mercer Street Friends.³ Mr. Kitt also attested to the fact that the donors understood that the Fund was restricted, and that the donations were intended to be restricted.

The parties contend that the only question remaining is whether this is a donor-restricted fund that is within the purview of the regulations at 42 C.F.R. § 413.153(c)(2). The answer

¹ Provider Exhibit 5 in the record of the remanded case.

² See Joint Stipulation Exhibit A

³ Provider Case: Exhibit 16, in the record of the remanded case.

is yes. The Friends Center Fund does meet the donor-restricted requirements of that regulation because of a long-standing legal principle:

. . . [w]here a testator devises or bequeaths property to a charitable corporation to be applied to a particular charity or purpose, it is to be inferred that the application of the property to the designated purpose is the Testator's primary intent. . . .

Scott on Trust, 3rd Edition, ¶ 397.3.

This means that all the donations to Friends Center Fund, including those when it was set up, as well as any made after such time to this date, were meant by the testator to be restricted to the particular charitable purposes of the Mercer Street Friends Center. Since the Friends Center Fund was restricted, any donations were meant to be so restricted.

CITATION OF LAW, REGULATIONS AND PROGRAM INSTRUCTIONS:

1. Regulations – 42 C.F.R.:

§ 405.1875	-	Administrator's Review
§ 405.1877	-	Judicial Review
§ 413.153 <u>et seq.</u>	-	Interest Expense

2. Cases:

Mercer Street Friends v. Blue cross and Blue Shield Association/United Government Services, PRRB Case No. 2000-D68, June 29, 2000, Medicare & Medicaid Guide (CCH) Transfer Binder ¶ 80,514 (Mercer), HCFA Administration declined review, August 23, 2000.

3. Other:

Scott's on Trust, 3rd Edition, ¶ 397.3

FINDINGS OF FACT, CONCLUSIONS OF LAW AND DISCUSSION:

The Board, after considering the Medicare law, regulations, program instructions, facts, parties' contentions, and evidence submitted, finds and concludes that the Friends Center Fund is a donor-restricted fund as defined by 42 C.F.R. § 413.153. The Board, however, finds that the primary issue still before it is whether the interest expense incurred on working capital loans is reasonable and necessary. The Board addressed this issue in its

Mercer, supra, (Issue 1). The Board found that only \$29,280 out of \$113,000 of interest expense incurred by the Provider was allowable. Since the Provider incurred \$43,000 in interest on loans with commercial banks, the Board concluded that all allowable interest expense related to the commercial loans. It, in effect, disallowed the remaining \$70,000 interest expense incurred from borrowings with the Friends Center Fund.

The Board found the latter fund to be non-donor-restricted because of the lack of evidence to support a finding that the fund was donor-restricted. As a result of the Court order, the Board has re-examined the evidence presented by the Parties along with their joint statement of contentions. It finds that, based on this information, the Friends Center Fund is in fact a donor-restricted fund whose interest expense could be allowed under the related party interest expense exception in 42 C.F.R. § 413.153. However, as noted in the original decision, all allowable interest expense permitted by the Board on its deemed necessary borrowing was absorbed by the commercial bank interest expense. As such, the question of whether the Friends Center Fund was donor-restricted or not is moot since none of the interest paid to that fund would have been allowed. In effect, the Board's original decision resulted in stating that all funds borrowed from the Friends Center Fund were unnecessary and excessive. As such, any interest expense incurred, even if the borrowing to which it relates meets the regulatory exception of donor-restricted, would be disallowed as unnecessary interest expense.

The Board concludes that its original decision on working capital interest was correct and that none of the interest on the donor-restricted Friends Center Fund is allowable.

DECISION AND ORDER:

The Friends Center Fund is a donor-restricted fund whose interest expense would satisfy the Medicare regulatory exception in 42 C.F.R. § 413.153. However, the Provider's incurred interest expense on this borrowing was unnecessary and not allowable. The Board's original decision is sustained.

BOARD MEMBERS PARTICIPATING:

Irvin W. Kues
Henry C. Wessman, Esquire
Stanley J. Sokolove
Dr. Gary B. Blodgett
Suzanne Cochran, Esquire

Date of Decision: September 19, 2002

FOR THE BOARD:

Irvin W. Kues
Chairman