PROVIDER REIMBURSEMENT REVIEW BOARD DECISION

2005-D25

PROVIDER –
Brady Home Health Care Services, Inc.
Brady, Texas

Provider No.: 67-7455

vs.

INTERMEDIARY –
BlueCross BlueShield Association/
Palmetto Government Benefits Administrators

DATE OF HEARING –
June 2, 2004

Cost Reporting Period Ended -
December 31, 1996

CASE NO.: 99-1213

INDEX

ISSUES:

1. Whether the Intermediary's adjustment to remove accrued salaries for owners due to payment not being properly liquidated within 75 days after the close of the cost reporting period was correct.

2. Whether it was proper for the Intermediary to disallow the portion of the accrued owner's compensation expenses attributable to the employees' share of Federal and State withholding taxes.

STATEMENT OF THE CASE AND STATUTORY AND REGULATORY BACKGROUND:

This is a dispute over the amount of Medicare payments to a health care provider.

The Medicare program provides health insurance to aged and disabled persons. 42 U.S.C. §§1395-1395cc. The Secretary of the Department of Health and Human Services is authorized to promulgate regulations prescribing the health care services covered by the program and the methods of determining payments for those services. The Centers for Medicare & Medicaid Services (CMS), formerly the Health Care Financing Administration (HCFA), is the operating component of the Department of Health and Human Services charged with the program's administration. CMS has entered into contracts with insurance companies known as fiscal intermediaries to maintain the program's payment and audit functions. Intermediaries determine payment amounts due providers of health care services (e.g., hospitals, skilled nursing facilities, and home health agencies) under Medicare law and under interpretative guidelines issued by CMS.

At the close of its fiscal year, each provider submits a cost report to its intermediary showing the costs it incurred during the period and the portion of those costs to be allocated to Medicare. 42 C.F.R. §413.20. The intermediary reviews the cost report and determines the total amount of Medicare reimbursement due the provider, and notifies the provider in a Notice of Program Reimbursement (NPR). 42 C.F.R §405.1803. A provider dissatisfied with the intermediary's determination may file an appeal with the Provider Reimbursement Review Board (Board) within 180 days of the NPR. 42 U.S.C. §1395oo; 42 C.F.R. §405.1835.

Brady Home Health Care Services, Inc. (Provider) is a home health agency located in Brady, Texas. At the close of its cost reporting period ended December 31, 1996, the Provider had accrued salaries payable amounting to $23,456. This amount consisted of $11,418 payable to the Provider's two owners and $12,038 representing the State and Federal withholding taxes related to those salaries.

On March 14, 1997, the Provider issued checks to its owners for the $11,418; however, the checks were not cashed and did not clear the bank until April 2, 1997, and April 4, 1997, respectively. Palmetto Government Benefit Administrators (Intermediary) reviewed the Provider's cost report and disallowed the entire amount of $23,456 which the Provider had expensed. The Intermediary indicated that the disallowances (adjustments) were necessary because the accruals had not been properly liquidated within 75 days after the close of the cost reporting period. Although the Provider had issued checks within the 75-day period, an actual transfer of the Provider's assets did not occur until the checks had cleared the bank, which exceeded 75 days.

Regulations at 42 C.F.R. §413.100(c)(2)(iv) state:

> *Compensation of owners.* Accrued liability related to compensation of owners other than sole proprietors and partners must be liquidated within 75 days after the close of the cost reporting period in which the liability occurs. (Emphasis added).

Program rules addressing this matter at Provider Reimbursement Manual, Part I (HCFA Pub. 15-1) §906.4, were amended in February 1996 (Transmittal No. 391). In pertinent part the manual instructions state that effective with cost reporting periods beginning on or after October 1, 1995:

> [t]he compensation of stockholder-employees and individuals described in §901 (other than sole proprietors and partners) is included for a cost reporting period if earned within the period, even if not paid until after the close of the period. However, payment must be made (whether by check or other negotiable instrument, cash or legal transfer of assets such as stocks, bonds, real property, etc.) within 75 days after the close of the period. Where payment is made by check or other negotiable instrument (e.g., a promissory note), these forms of payment must be liquidated through an actual transfer of the provider's assets within 75 days after the close of the period in order to meet the requirements of this section. If payment, including the liquidation of negotiable instruments, is not made within the cost reporting period, or within 75 days thereafter, the unpaid compensation is not includable in allowable costs either in the period when earned or in the period when actually paid. (Emphasis added).

The Provider appealed the Intermediary's adjustments to the Board pursuant to 42 C.F.R. §§405.1835-1841 and met the jurisdictional requirements of those regulations. The amount of Medicare funds in controversy is approximately $21,500.

The Provider was represented by John W. Jansak, Esq., of Harriman, Jansak & Wylie. The Intermediary was represented by James R. Grimes, Esq., Associate Counsel, Blue Cross Blue Shield Association.

PARTIES' CONTENTIONS:

The Provider contends that it is improper to apply the provisions of Transmittal No. 391 to its accrued owners' compensation of $11,418 since that would represent retroactive rule making. Transmittal No. 391 was issued in February 1996, which is after the start of the subject cost reporting period. Prior to the transmittal's issuance, CMS allowed providers and intermediaries more than 75 days to liquidate accrued owners' compensation before disallowing the costs.[1]

The Provider also contends that the requirement in Transmittal No. 391 that an actual transfer of assets be made within 75 days after the close of a cost reporting period (in order for accrued compensation to be an allowable cost) is illegal. This requirement is inconsistent with the controlling authority of 42 C.F.R. §413.100(c)(2)(iv) which only requires "liquidation" to occur within 75 days. The transfer of assets provision is a significant change requiring an amendment to the regulation in accordance with the Administrative Procedure Act. Moreover, the term "liquidation" is defined as payment of a debt. Under certain circumstances a debt is considered liquidated as of the date of issuance of a check. Brady on Bank Checks, Revised edition at ¶4.06, Harbor v. K & W Trucking Company, 725 Fed.2nd 1065, Parnell v. Johnson, 503 U.S. 393 (1992).

With respect to the $12,038 withholding tax adjustment, the Provider contends that employment-related taxes are an allowable cost pursuant to HCFA Pub. 15-1 §2122.3.[2] These taxes must be paid to the respective government entities regardless of whether or not Medicare recognizes the related salaries as an allowable cost. In accordance with IRS rules, these taxes were withheld and recorded on March 14, 1997 when the related compensation checks were issued. These withholdings are not part of the checks written to the Provider's owners and are not subject to the 75-day rule.

The Intermediary contends that Transmittal No. 391 was issued one month after the start of the Provider's cost reporting period. Therefore, the Provider was given sufficient time to comply with the transmittal's instructions. Also, the issuance of Transmittal No. 391 does not represent retroactive rule making; the case cited by the Provider, Bowen v. Georgetown University Hospital, 488 U.S. 204 (1988), pertained to the retroactive application of cost limits, not to the clarification or issuance of new manual instructions.

Regarding the $12,038 portion of the disallowance, the Intermediary contends that the tax liability at issue is that of the Provider's owners and not that of the Provider. The Provider was merely holding the funds until they were properly deposited with the appropriate government agency. The Provider did, however, expense the gross amount of the salaries, $23,456, which is properly at issue and should be disallowed.

FINDINGS OF FACT, CONCLUSIONS OF LAW AND DISCUSSION:

The Board, after consideration of Medicare law and guidelines, parties' contentions, and evidence presented, finds that the Intermediary properly disallowed the owners' compensation expense accrued by the Provider at the end of its Medicare cost reporting period. Although the Provider had issued checks within 75 days after the end of the reporting period to liquidate the accruals pursuant to 42 C.F.R. §413.100(c)(2)(iv), the

[1] Provider's Final Position Paper at 6. Provider's Supplemental Position Paper at 3.
[2] Provider's Draft Position Paper at 5.

checks had not cleared the Provider's bank within that period. Accordingly, the accrued expenses are unallowable pursuant to HCFA Pub. 15-1 §906.4 which, as amended by Transmittal No. 391, requires accrued compensation to be liquidated through an actual transfer of the Provider's assets within the 75-day period.

The Board disagrees with the Provider's argument that applying the transfer of assets requirement of Transmittal No. 391 to the subject cost reporting period represents retroactive rule making. The Board finds that Transmittal No. 391 was issued only one month after the start of the Provider's cost reporting period, thus, affording the Provider ample time to comply with its requirements. Also, the transfer of assets requirement contained in Transmittal No. 391 does not represent a significant change in program rules that would have warranted a regulatory change, including publication in the Federal Register prior to implementation. At one time, regulations at 42 C.F.R. §405.426(d) required accrued owners' compensation to be liquidated within 75 days after the close of a provider's cost reporting period for the accrued compensation to be included in allowable costs. Then, in 1983, HCFA stated that this requirement did not need to be incorporated in the regulations, and that program instructions at HCFA Pub. 15-1 §2305 were sufficient to safeguard against abuse. 48 Fed. Reg. 39752, 39753 (Sept. 1, 1983). Notably, HCFA Pub. 15-1 §2305, which pertains to short-term liabilities, requires that where liquidation is made by check or other negotiable instrument, payment must be made "through an actual transfer of the provider's assets within the time limits specified." Accordingly, Transmittal No. 391 essentially reiterated existing policy.

The Board also disagrees with the Provider's argument that accrued expenses should be considered liquidated when a check for payment has been issued. The issuance of a check does not represent an actual transfer of assets, as a check may never be cashed or there may be insufficient funds in the account upon which the check was drawn to allow the check to be cashed. There is no transfer of assets until the amount of the check has been withdrawn from the Provider's bank account.

Finally, the Board disagrees with the Provider's argument that the Federal and State withholding tax portions of the Intermediary's adjustments are improper since they are not associated with the checks issued to its owners and, therefore, not subject to Medicare's 75-day rule. The Board finds that the program's rules regarding accrued owners' compensation apply to the total salary expense included in a provider's cost report. This expense (compensation) includes the gross amount earned by the owners and claimed for program reimbursement rather than the amount paid net of payroll withholding taxes. The Provider is responsible for withholding all applicable payroll taxes and remitting them to the proper government agencies.

DECISION AND ORDER:

The Intermediary's adjustment disallowing accrued owners' compensation expense that was not liquidated within 75 days after the close of the Provider's cost reporting period was proper. The adjustment properly included the portion of the accrued owners' compensation expenses attributable to the individuals' share of Federal and State employment taxes. The Intermediary's adjustment is affirmed.

Board Members Participating:

Suzanne Cochran, Esq.
Dr. Gary B. Blodgett
Martin W. Hoover, Jr., Esq.
Elaine Crews Powell, C.P.A
Anjali Mulchandani-West

FOR THE BOARD:

DATE: February 11, 2005

Suzanne Cochran, Esq.
Chairman