NEW YORK STATE OF OPPORTUNITY. Department of Health

KATHY HOCHUL
Governor

MARY T. BASSETT, M.D., M.P.H.
Commissioner

KRISTIN M. PROUD
Acting Executive Deputy Commissioner

May 31, 2022

CERTIFIED MAIL/RETURN RECEIPT

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RE: In the Matter of Wesley Gardens Corporation

Dear Parties:

Enclosed please find the Decision After Hearing in the above referenced matter.

If the appellant did not win this hearing, the appellant may appeal to the courts pursuant to the provisions of Article 78 of the Civil Practice Law and Rules. If the appellant wishes to appeal this decision, the appellant may wish to seek advice from the legal resources available (e.g. the appellant's attorney, the County Bar Association, Legal Aid, OEO groups, etc.). Such an appeal must be commenced within four (4) months after the determination to be reviewed becomes final and binding.

Sincerely,

Dawn MacKillop-Soller

Dawn MacKillop-Soller
Acting Chief Administrative Law Judge
Bureau of Adjudication

DXM: cmg
Enclosure

STATE OF NEW YORK
DEPARTMENT OF HEALTH

COPY

In the Matter of

WESLEY GARDENS CORPORATION
Provider ID: 00365893

Appellant,

from a determination by the NYS Office of the Medicaid Inspector General (OMIG) to recover Medicaid Program overpayments.

DECISION
Audit No. #16-3383

Before: Jean T. Carney
Administrative Law Judge

Held at: Via WebEx Videoconference

Hearing Date: May 12, 2021

Parties: New York State Office of the Medicaid Inspector General
800 North Pearl Street
Albany, New York 12204
By: Kathleen Dix, Esq.

Wesley Gardens Corporation
3 Upton Park, Floor 1
Rochester, New York 14607
By: Ross P. Lanzafame, Esq.
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JURISDICTION

The New York State Department of Health (Department or DOH) acts as the single state agency to supervise the administration of the Medical Assistance (Medicaid) Program in New York. (Public Health Law [PHL] § 201[1][v]; Social Services Law [SSL] § 363-a). The New York State Office of the Medicaid Inspector General (OMIG), an independent office within the DOH, is authorized to investigate and pursue civil and administrative enforcement actions to recover improperly expended Medicaid funds. (PHL §§ 31-32). The OMIG determined to recover Medicaid Program overpayments from Wesley Gardens Corporation (Appellant) for the rate period from January 1, 2012 through December 31, 2015. The Appellant requested a hearing pursuant to SSL § 22, and Department of Social Services (DSS) regulations at 18 NYCRR § 519.4 to review the OMIG's determination.

HEARING RECORD

The OMIG presented the audit file with supporting documents (OMIG Exhs 1-21); and the testimony of Sujata Stratton, C.P.A., Audit Supervisor for OMIG's Rate Audit Unit. The Appellant presented documents (Appellant Exhs A-H); and the testimony of Robert W. Jones, III, Appellant's former President and Chief Executive Officer (CEO); Barry Palatas, Appellant's Chief Financial Officer (CFO); and [redacted] C.P.A., Partner at the Bonadio Group. A stenographic transcript of the proceedings was made (pages 1-224). The parties submitted post-hearing briefs, and the record closed on August 13, 2021.

APPLICABLE LAW

Residential health care facilities are eligible for payment of a Medicaid daily rate billable for resident beds occupied by Medicaid recipients. (10 NYCRR § 86-2.10). The Department's Bureau of Long-Term Care Reimbursement (BLTCR) sets rates for each residential health care facility by using the information that the facility submits annually in a cost report form RHCF-4. (10 NYCRR § 86-2.2). A facility's basic rate is comprised of

four separate and distinct cost components: (a) direct; (b) indirect; (c) noncomparable; and (d) capital. (10 NYCRR § 86-2.10[b][1][i]). The capital component is facility specific, and includes "costs reported in the depreciation, leases and rentals, interest on capital debt and/or major movable equipment depreciation cost centers, as well as costs reported in any other cost center under the major natural classification of depreciation, leases and rentals on the facilities annual cost report (RHCF-4)." (10 NYCRR § 86-2.10[a][9]).

A facility's rate of payment is provisional and subject to audit. The Department may adjust a payment rate retroactively if an audit determines that such an adjustment is warranted. (SSL § 368-c; 10 NYCRR § 86-2.7; 18 NYCRR § 517.3). Upon completion of an audit, the OMIG may require the repayment of any amounts not authorized to be paid by the Medicaid Program. (18 NYCRR § 518.1).

A Medicaid provider is entitled to a hearing to review the OMIG's final determination requiring repayment of any overpayments. (18 NYCRR § 519.4). The burden lies with the Appellant to prove by substantial evidence that the OMIG's determination is incorrect. (18 NYCRR § 519.18[d] and 18 NYCRR § 519.18[h]; New York State Administrative Act (SAPA) § 306[1]). Substantial evidence means such relevant proof as a reasonable mind may accept as adequate to support a conclusion or fact; less than preponderance of evidence, but more than mere surmise, conjecture, or speculation, and constituting a rational basis for decision. (*Stoker v. Tarantino*, 101 A.D.2d 651, 475 N.Y.S.2d 562 [3rd Dept. 1984], *appeal dismissed* 63 N.Y.2d 649 [1984]).

ISSUES

Has the Appellant shown that the OMIG erred in disallowing replacement of a portion of the heating system as a capital cost?

Has the Appellant shown that the OMIG erred in disallowing, as a capital cost, the undepreciated amount of the heating system equipment that was disposed of two years after being installed?

Has the Appellant shown that the OMIG erred in disallowing abandoned project planning costs as capital costs?

FACTS

Citations in parentheses refer to testimony (T) and exhibits (Exh) found persuasive in arriving at a particular finding. Conflicting evidence, if any, was rejected in favor of cited evidence.

1. The Appellant is a residential health care facility (RHCF) licensed under Article 28 of the PHL, and is enrolled as a Medicaid provider. (Exh 6).

2. Medicaid reimburses the Appellant for a portion of its costs associated with providing care to its residents who are Medicaid recipients. The daily rate of reimbursement is set by the DOH Bureau of Residential Health Care Reimbursement (BRHCR, formerly known as the BLTCR). (T Stratton at p. 20-21).

3. The OMIG conducted an audit of the Medicaid rates paid to the Appellant from January 1, 2012 through December 31, 2015. The audit consisted of a review of the Appellant's records supporting the capital portion of its RHCF-4s for the calendar years of January 1, 2010 through December 31, 2013. (Exhs 4 and 6; T at p. 23).

4. On January 16, 2019, the OMIG issued a draft audit report detailing its preliminary findings and calculating an estimated Medicaid overpayment of $302,472.00. (Exh 4).

5. On February 19, 2019, The Appellant submitted its response to the draft audit report, objecting to three of OMIG's findings. Specifically, the Appellant objected to:

> 1(d) - "The Provider incorrectly capitalized costs that should have been expensed as operating costs because they were for repairs;"
>
> 1(e) - "The asset on which the repairs were made [in adjustment #1(d)] was disposed of in the following year and the Provider reported the undepreciated amount of the repair costs as a loss on disposal of

equipment. These expenditures for the repairs should have been expensed, rather than capitalized;" and

2 - "Costs not related to patient care are costs that are not appropriate or necessary and proper in developing and maintaining the operation of patient care facilities and activities. Only costs that are properly chargeable to patient care are allowable. The Provider reported planning costs related to an expansion project that was abandoned. Since the project was abandoned prior to completion, it was never used for patient care. In addition, planning costs for an abandoned project are an operating expenditure rather than a capital related cost." (Exhs 4 and 5).

6. After reviewing the Appellant's submission, the OMIG issued its final audit report on June 5, 2019, making no changes to the overpayments identified in the draft audit report. (Exh 6).

Heating System

7. In 2011, the Appellant's heating system consisted of three cast-iron boilers, distributing steam through a heat exchanger to heat the facility. The boilers had been operating since approximately 1998, and in the autumn of 2011 the number two boiler failed prematurely. The Appellant considered repairing the boiler, but determined that option was too risky. The Appellant ultimately decided to remove and replace the failed boiler with a new boiler, new control systems, bypass damper, condensate pumps, and heat exchangers. (T at pp 75-82, Exh D).

8. When a fixed or capital asset is purchased, it is assigned a useful life value based on the American Hospital Association guidelines, and depreciated over that useful life. The new boiler was assigned a useful life of 15 years. The other components were assigned useful lives after consultation with the vendor, broken down by individual cost. The piping was assigned a useful life of 20 years, the automation and glycol systems were assigned a useful life of 15 years, and the pumps were given a useful life of five years.

The Appellant's cost reports included the new boiler and other components as capital costs. (Exhs 5 and 17; T at pp. 57-58, 62, 135-138).

9. In 2013, boilers one and three showed signs of scale build-up and were at risk of failing. The Appellant decided to replace the entire heating system, including the boiler that was installed in 2011, with a more energy efficient hot water heating system. The Appellant was able to keep the existing air handlers and piping from the 2011 project. (T at pp 84-86, 91-92).

Abandoned Project

10. In 2003, the Appellant submitted a Certificate of Need (CON) to the DOH, seeking approval to renovate and expand the facility by adding a tower to the south side of the building and creating a parking lot. The Appellant obtained survey drawings and plans; but never started construction. The facility is located in a historic district, and the Appellant needed approval from the preservation board. In 2011, the Appellant abandoned the project because the preservation board would not approve it. (T at pp. 95-98, 99-100; Exh 17).

11. Medicaid regulations are silent regarding whether planning costs for abandoned projects may be reimbursed. Medicare regulations allow such costs to be reimbursed as operating expenses. (10 NYCRR 86-2.17[a]; T at pp. 50-51).

12. The Appellant accrued $95,285 in planning costs associated with the abandoned project. The Appellant wrote off the entire amount of $95,285 and included it in its 2013 cost reports. The Appellant also requested to amortize the planning costs over three years, and included the amortized portions in their 2014 and 2015 cost reports, resulting in duplicate write-offs. (Exh 5 at p. 12; Exh 18 at p. 86; Exh 6 at p. 20).

13. In its response to the draft audit report, the Appellant referenced an open appeal with BRHCR regarding the abandoned project costs. In 2020, BRHCR told the Appellant that the abandoned project costs would be allowed once the Appellant

provided documentation to support the reason for abandonment being the preservation board's refusal to approve the project. (Exhs 5 and A; T at pp. 163-168).

DISCUSSION

The Appellant failed to meet its burden of proving that the OMIG erred in disallowing depreciation for the new boiler as a capital cost in Finding #1(d); and in disallowing the loss on disposal as a capital cost in Finding #1(e). The Appellant also failed to show the OMIG erred in disallowing the abandoned project costs in Finding #2.

Heating System Disallowances

The OMIG disallowed depreciation costs reported by the Appellant for installing a new boiler in their heating system in 2011. In making this determination, the OMIG viewed the heating system as a whole, with three boilers working together to provide heat to the facility. The OMIG determined that pursuant to Department regulations applicable to residential health care faciities, this constituted a repair, not a capitalizable expenditure. Repairs are defined as the "restoration of a capital asset to full capacity, or a contribution thereto, after damage, accident, or prolonged use, without increase in its previously estimated service life or productive capacity." (10 NYCRR § 451.230[a]). The record reflects that the heating system used by the facility was installed in or by 1998. By 2011, boiler two was failing due to scale build up, caused in part by flooding during previous years. Additionally, the boiler was leaking. The failing boiler was broken up, and a crane hoisted the new boiler into place. New control systems, bypass damper, and heat exchangers were also installed. Replacing boiler two restored the heating system to full capacity after being used approximately 13 years, while suffering damage from flooding. The record is silent regarding the useful life of the other components of this heating system, so it is unclear whether replacing boiler two increased the estimated service life or productive capacity of the heating system.

The Appellant argued that the new boiler was a capital expenditure, and from an accounting perspective, it was appropriate to treat it as a depreciable asset until the

decision was made to dispose of it. Capital expenditures are "generally restricted to expenditures that add fixed-asset units or that have the effect of increasing the capacity, efficiency, life span or economy of an existing fixed asset." (10 NYCRR 451.46). Here, replacing boiler two neither added to, nor increased the capacity of the heating system. Rather, it restored the heating system to its former, full capacity. The 2011 project did increase the overall efficiency of the heating system, but there was no evidence to support the contention that it increased the system's service life or productive capacity, particularly in light of the fact that the entire heating system was replaced in 2014. Therefore, the OMIG's determination to disallow depreciation for the new boiler as a capital cost was reasonable.

When the old heating system was replaced in 2014, the Appellant reported it as a loss on disposal of a depreciable asset. Having affirmed the OMIG's determination that the new boiler was a repair, and not a depreciable asset, it follows that the loss on disposal was also reasonably disallowed.

Abandoned Project Costs

The Appellant claimed costs related to a construction project it abandoned because the preservation board would not approve the project. The Medicaid regulations are silent as to whether planning costs are allowable, so the OMIG turned to Medicare regulations for guidance. (10 NYCRR § 86-2.17[a]). The relevant Medicare regulations allow abandoned project costs, as operating costs, if the project was intended to expand or renovate the nursing home. (Exh 18 at pp. 13-14; T at p. 51). Here, the project included building an addition to the nursing home that would allow the facility to reconfigure the number of beds on each floor. Therefore, those planning costs are allowable under the operating component of the Appellant's rate; not under the capital component.

The Appellant argued that if the BRHCR granted their rate appeal and adjusted the Appellant's rates to allow the abandoned project costs, then the OMIG should not disallow them on audit. However, any rate set by the BRHCR is considered provisional

until audited by the OMIG. (10 NYCRR § 86-2.7; T at pp. 45-46). Therefore, the Appellant has not shown that the OMIG erred in disallowing the abandoned project costs.

DECISION

The OMIG's determination under finding #1(d) in the final audit report to disallow depreciation expenses applicable to the replacement of a boiler is affirmed.

The OMIG's determination under finding #1(e) in the final audit report to disallow loss on disposal of the boiler is affirmed.

The OMIG's determination under finding #2 in the final audit report to disallow abandoned project costs is affirmed.

This Decision is made pursuant to the designation by the Commissioner of Health of the State of New York to render final decisions in hearings involving Medicaid provider audits.

DATED: May 31, 2022
Albany, New York

JEAN T. CARNEY
Administrative Law Judge