STATE OF NEW YORK
OFFICE OF THE MEDICAID INSPECTOR GENERAL
800 North Pearl Street
Albany, New York 12204

ANDREW M. CUOMO
GOVERNOR

JAMES C. COX
MEDICAID INSPECTOR GENERAL

May 28, 2013

[redacted]
St. Johnland Nursing Center
395 Sunken Meadow Rd.
Kings Park, New York 11754

Re: Medicaid Rate Audit #09-4255
NPI Number: [redacted]
Provider Number: [redacted]

Dear [redacted]:

Enclosed is the final audit report of the Office of the Medicaid Inspector General's (the "OMIG") audit of St. Johnland Nursing Center's (the "Facility") Medicaid rates for the rate period January 1, 2005 through December 31, 2008. In accordance with 18 NYCRR Section 517.6, this report represents the OMIG's final determination on issues raised in the draft audit report.

In response to the draft audit report dated December 18, 2012, you identified specific audit findings with which you disagreed. Your comments have been considered (see Attachment A) and the report has been either revised accordingly and/or amended to address your comments (see Attachment B). Consideration of your comments resulted in an overall reduction of $56,474 to the total Medicaid overpayment shown in the draft audit report. As previously stated in the draft audit report, the Medicare Part B and D offsets were not within the scope of the review and may be examined as part of a future audit. Based on the enclosed audited rates calculated by the Bureau of Long Term Care Reimbursement, the Medicaid overpayment currently due is $1,127,495. This overpayment is subject to Department of Health (the "DOH") and Division of Budget (the "DOB") final approval. While not anticipated, any difference between the calculated overpayment and the final DOH and DOB approved amount will be resolved with the Facility by the OMIG Bureau of Collections Management.

The overpayment does not reflect the impact on rates subsequent to December 31, 2008 that utilized the July 1, 2005 through June 30, 2006 base period for operating expense. Any overpayment resulting from operating expense disallowances in the July 1, 2005 through June 30, 2006 base period report for rates subsequent to December 31, 2008 will be addressed in the future.

In accordance with 18 NYCRR Part 518 which regulates the collection of overpayments, your repayment options are described below.

OPTION #1: Make full payment by check or money order within 20 days of the date of the final audit report. The check should be made payable to the New York State Department of Health and be sent with the attached Remittance Advice to:

[redacted]
New York State Department of Health
Medicaid Financial Management
GNARESP Corning Tower, Room 2739
File #09-4255
Albany, New York 12237-0048

OPTION #2: Enter into a repayment agreement with the Office of the Medicaid Inspector General. If your repayment terms exceed 90 days from the date of the final audit report, recoveries of amounts due are subject to interest charges at the prime rate plus 2%. If the process of establishing the repayment agreement exceeds 20 days from the date of the final audit report, the OMIG will impose a 15% withhold after 20 days until the agreement is established. The OMIG may require financial information from you to establish the terms of the repayment agreement. If additional information is requested, the OMIG must receive the information within 30 days of the request or a 50% withhold will be imposed. OMIG acceptance of the repayment agreement is based on your repaying the Medicaid overpayment as agreed. The OMIG will adjust the rate of recovery, or require payment in full, if your unpaid balance is not being repaid as agreed. The OMIG will notify you no later than 5 days after initiating such action. If you wish to enter into a repayment agreement, you must forward your written request within 20 days to the following:

Bureau of Collections Management
New York State Office of the Medicaid Inspector General
800 North Pearl Street
Albany, New York 12204
[redacted]

If within 20 days, you fail to make full payment or contact the OMIG to make repayment arrangements, the OMIG will establish a withhold equal to 50% of your Medicaid billings to secure payment and liquidate the overpayment amount, interest and/or penalty, not barring any other remedy allowed by law. The OMIG will provide notice to you no later than 5 days after the withholding of any funds.

In addition, if you receive an adjustment in your favor while you owe funds to the State, such adjustment will be applied against the amount owed.

You have the right to challenge this action and determination by requesting an administrative hearing within sixty (60) days of the date of this notice. You may not request a hearing to raise issues related to rate setting or rate setting methodology. In addition, you may not raise any issue that was raised or could have been raised at a rate appeal with your rate setting agency. You may only request a hearing to challenge specific audit adjustments which you challenged in a response to the draft audit report.

If you wish to request a hearing, the request must be submitted in writing to:

General Counsel
Office of Counsel
New York State Office of the Medicaid Inspector General
800 North Pearl Street
Albany, New York 12204

Questions regarding the request for a hearing should be directed to [redacted] of the Office of Counsel at [redacted]

If a hearing is held, you may have a person represent you or you may represent yourself. If you choose to be represented by someone other than an attorney, you must supply a signed authorization permitting that person to represent you along with your hearing request. At the hearing, you may call witnesses and present documentary evidence on your behalf.

Should you have any questions, please call [redacted] at [redacted] or through email at [redacted] Please refer to audit number 09-4255 in all correspondence.

Sincerely,

[redacted]
Bureau of Rate Audit
Division of Medicaid Audit
Office of the Medicaid Inspector General

Attachments:

Attachment A - Facility Draft Report Comments and OMIG Response
Attachment B - Summary of Changes from Draft Report to Final Report
EXHIBIT I - Summary of Per Diem Impact and Medicaid Overpayment
EXHIBIT II - Summary of Medicaid Rates Audited
EXHIBIT III - Operating Expense Disallowances/(Allowances)
EXHIBIT IV - Property Expense Disallowances/(Allowances) For Nursing Facility
EXHIBIT V - Property Expense Disallowances/(Allowances) For TBI Unit

CERTIFIED MAIL # [redacted]
RETURN RECEIPT REQUESTED
Ver-16.0

NEW YORK STATE
OFFICE OF THE MEDICAID INSPECTOR GENERAL
REMITTANCE ADVICE

NAME AND ADDRESS OF AUDITEE ST. JOHNLAND NURSING CENTER 395 SUNKEN MEADOW RD. KINGS PARK, NEW YORK 11754	NPI [redacted] PROVIDER [redacted]
	AUDIT #09-4255
AMOUNT DUE: $1,127,495	AUDIT TYPE: [ ] PROVIDER [X] RATE [ ] PART B [ ] OTHER:

CHECKLIST

1. To ensure proper credit, please enclose this form with your check.

2. Make checks payable to: *New York State Department of Health*

3. Record the Audit Number on your check.

4. Mail check to:

[redacted]
New York State Department of Health
Medicaid Financial Management
GNARESP Corning Tower, Room 2739
File #09-4255
Albany, New York 12237-0048

5. If the provider number shown above is incorrect, please enter the correct number below.

CORRECT PROVIDER NUMBER

ST. JOHNLAND NURSING CENTER - AUDIT #09-4255
FACILITY DRAFT REPORT COMMENTS AND OMIG RESPONSE

All OMIG adjustments were accepted by the Facility except for those shown below. The following details the disposition of final report adjustments after consideration of the Facility's draft audit report response comments. See Attachment B for adjustment changes included in the final audit report.

EXHIBIT III COMMENTS

Operating Adjustment #1 – Utilities Expense Disallowance

Facility Comment

St. Johnland takes exception to the proposed audit disallowance. This expense of $3,720 relates to the base year cost reported as fuel oil. The audit disallowance cites lack of adequate documentation. Attached please find invoices substantiating the reported fuel oil expense.

OMIG Response

The Facility is reimbursed for the Fuel Oil #4 cost listed on schedule 6 of the base year cost report. Using the crosswalk, the OMIG determined that the cost of $3,720 is made up of 3 different accounts [redacted]). The Facility provided us with invoices for the account [redacted] which is not one of the accounts listed above. Since the Facility could not provide documentation for the accounts in question, the OMIG disallowance will remain the same

Disposition: The draft report disallowance remains the same.

Operating Adjustment #2 – Utilities Expense Disallowance

Facility Comment

St. Johnland also takes exception to the proposed audit disallowance. This expense of $5,722 relates to the base year cost reported as water and sewer expense. Attached please find invoices and an allocation worksheet in support of the total water and sewer expense ($100,965) reported in our base year cost report.

OMIG Response

The Facility was able to provide documentation for the expenses reported. Therefore the OMIG disallowance will be eliminated.

Disposition: The draft report is changed to show the elimination of operating adjustment #2.

Operating Adjustment #3 – Reclassification of Utilization Review Expense

Facility Comment

St. Johnland objects to the proposed audit disallowance. St. Johnland has located the job descriptions and has attached copies for the auditors' review. Accordingly, there is no basis for the reclassification on the ground cited in the Report.

We note that the MDS Coordinators perform an integral role in the facility's utilization review functions. The MDS Coordinators are experienced registered nurses who report directly to the facility's Director of Nursing ("DON"). The MDS staff are present at all Interdisciplinary meetings held daily at the facility, Monday through Friday. Other medical professional staff regularly attending these meetings are the facility's DON and Medical Director. As part of the utilization review functions, the MDS Coordinators participate in reviewing the admissions and discharges to the facility, residents' level of care, and the appropriateness of placement of residents in the facility.

The MDS Coordinators are also responsible for performing in-depth reviews of residents to identify proper placement and discharge plans, if appropriate, on a weekly basis. MDS personnel are part of quality improvement teams at the facility, addressing falls, pressure ulcers and length of stay.

Other responsibilities of the MDS Coordinator include:

- Participating in discharge planning process
    - ensures that residents are appropriately discharged to lower level of care when care plan goals are met and resident no longer requires skilled level of care
    - ensures that resident is appropriately placed in nursing home as needed
- Interviewing staff, residents and families to confirm that needed resources are provided
- Making rounds on the facility's units as needed to observe care being provided
- Conducting quality assurance audits, providing feedback to interdisciplinary team and facility administration, and revising systems and protocols as needed.
- Assisting the MDS Coordinators in carrying out their duties are administrative staff within the MDS Department.

Accordingly, St. Johnland requests that this proposed adjustment be eliminated from the final audit report.

OMIG Response

The job descriptions the Facility was able to provide were for the current period and not for the base year period. Furthermore, the job descriptions provided in the Facility response do not fit the description needed for the expense to fall under utilization review, as the MDS coordinator reports to the Director of Nursing. Therefore, the disallowance will remain the same.

Disposition: The draft report disallowance remains the same.

EXHIBIT IV COMMENTS

Property Adjustment #2 – Equipment Rental Expense Disallowances

Facility Comment

St. Johnland objects to this proposed disallowance. St. Johnland has located documentation, including invoices, supporting reported various equipment lease expenses, and has attached copies for the auditors' review. Accordingly, there is no basis for the disallowance on the ground cited in the report.

OMIG Response

The Facility was able to provide substantiation for some of the rental items disallowed in the draft report. The Facility provided $4,744 of invoices for CPM machines that were part of Rent G. $4,744 of the disallowance for Rent G will be eliminated. However, the Facility did not substantiate the amounts disallowed for Rent B ($3,430), Rent F ($2,401), or the remainder of Rent G ($15,193). Therefore, the disallowance for those items will remain the same.

Disposition: The draft report is changed to show the partial elimination of property adjustment #2

Property Adjustment #4 – Mortgage Expense Amortization

Facility Comment

St. Johnland objects only to the proposed disallowance in subparagraph (b) of this item. The report proposes to disallow $17,619 of mortgage expense amortization, citing lack of documentation. This adjustment is made for rate year 2008/cost year 2006. Please note that the mortgage expense amortization relates to 2004 mortgage refinancing ($266,688) and the society loan of February 2005 ($7,750).

These costs are being amortized over the respective lives of the loans in accordance with generally accepted accounting principles and therefore the mortgage amortization expense should be recognized as an allowable cost for Medicaid reimbursement purposes. Attached is a copy of the invoice from GMAC Commercial Mortgage related to the 2004 mortgage refinancing in support of costs associated there with.

We respectfully request the audit report reflect appropriate amortization of these costs in the annual amount of $14,163 ($224,255/190 months).

OMIG Response

The documentation provided by the Facility was sufficient enough to partially eliminate the disallowance in the draft report. The Facility was able to provide documentation to support $14,163 of expenses a year. The original disallowance was $17,619. Therefore, there will still be a disallowance of $3,456 for adjustment #4b.

Disposition: The draft report is changed to reflect the partial elimination of property adjustment #4b.

Property Adjustment #5 – Working Capital Interest Disallowances

Facility Comment

St. Johnland objects to the proposed disallowance in subparagraph (a) only of this item. St. Johnland takes exception to the proposed audit disallowance in rate years 2005, 2006 (1/1-3/31/06) and 2007.

The audit work papers state that "(late fees are not an allowable expense". We disagree with this comment, as there is no regulatory provision stating that late fees are not allowable costs, with the exception of late fees, interest and penalties resulting from governmental obligations (10 N.Y.C.R.R. § 86-2.17(g) or violation of Federal, State or local laws (PRM Sections 2102.3 and 2105.10). Also, there is no mention in the Report that these costs were not in fact incurred.

The Report also refers to 10 N.Y.C.R.R. § 86-2.17(a) and (d) and PRM-2103. However, these provisions relate broadly to costs necessary to patient care or to the efficient production of services and do not address the treatment of late fees. Moreover, in computing the capital component of the St. Johnland's annual Medicaid rate, the Department of Health (DOH) was aware of the nature of the costs reported by St. Johnland on the cost report and allowed such costs, subject to the appropriate working capital threshold. It is significant to note that the reported costs for 2003/rate year 2005 were less than the applicable threshold. Consequently, the DOH determination was appropriate, especially considering the financial position of St. Johnland during this period, as indicated below:

Calendar Year Ended 12/31	2002	2003	2004	2005
Current Assets	$9,532,338	$9,219,857	$9,143,045	$11,350,146
Current Liabilities	$11,366,744	$11,692,224	$13,075,433	$11,992,157
Working Capital	$(1,834,406)	$(2,472,367)	$(3,932,388)	$(642,011)
Unrestricted Cash & Investments	$27,665	$63,688	$2,882	$12,283
Calendar Year Ended 12/31	2002	2003	2004	2005
Income from operations	$(844,751)	$(1,242,831)	$(1,137616)	$(814,969)
Non- Operating Revenues	$312,434	$289,953	$203,982	$214,508
Extraordinary(Loss)/Gain	$(1,963,233)	$-	$1,005,092	$-
Excess Income/(Expenses)	$(2,495,550)	$(952,878)	$71,458	$(600,461)

We further submit that OMIG on audit is bound by DOH rate determinations, and lacks the authority to retroactively change a level of reimbursement approved by the rate setters. See Livingston Cty. Health Related Facility v. Perales, 124 A.D.2d 289, 291 (3d Dep't 1986); see also Rossi v. Axelrod, 178 A.D.2d 813, 814 (3d Dep't 1991) (auditors must "faithfully adhere to the methodology which DOH established and employed in calculating [the facility's] original rights").

Moreover, the facts refute then the auditors' assumption that St. Johnland acted imprudently in delaying the loan payments that resulted in late fees. Clearly, St. Johnland was experiencing financial difficulty, with substantial operating losses, razor-thin unrestricted cash balances and significant negative working capital in each of the audited years and had limited, if any, ability to access additional loans for working capital purposes. Rather than incur a short term debt to increase cash balances and to overcome substantial negative working capital positions, St. Johnland managed its limited cash resources and incurred cost far less than it would have incurred had it had borrowed the prior years' ending negative working capital position for a one year period at an interest rate equal to the interest rate utilized in the applicable rate year working capital threshold calculation, as shown below:

	2003	2004	2005
Loan Amount	$1,834,400	$2,472,000	$3,932,000
Interest Rate	6.25%	6.00%	7.25%
Term-Years	1	1	1
Total Payments	$1,897,000	$2,553,000	$4,088,000
Interest Expense	$62,600	$81,000	$156,000
Schedule 8d Expense	$31,156	$38,945	$64,986

Application of the "prudent buyer" principle to determine whether a provider incurred costs in line with the going rate for a given service or product requires consideration of any extenuating circumstances in which the provider was operating at the time it entered into the transaction being reviewed. PRM-1 Section 2013[B]. As indicated above, contrary to the audit summary, the facts and circumstances demonstrate that St. Johnland did act as a prudent and cost conscious buyer, by avoiding more costly borrowings, and that the DOH came to the same conclusion when allowing the costs subject to the working capital threshold.

In sum, St. Johnland submits that the proposed audit disallowances are inappropriate and requests that they be eliminated prior to the issuance of the final audit report.

OMIG Response

Reimbursement regulations states that the buyer of service should refuse to pay more than the going price of an item/service and seek to economize by minimizing cost. By incurring late fees, the Facility was in conflict with the above regulations. Therefore, the disallowance will remain in the report.

Disposition: The draft report disallowance remains the same.

Property Adjustment #6 – Moveable Equipment Depreciation Disallowances

Facility Comment

St. Johnland objects only to the proposed disallowance in subparagraph (b) of this item. The Report proposes to disallow moveable equipment depreciation expense in rate years 2006, 2007 and 2008 relating to an automobile utilized by the facility's administrator.

As the administrator, I can attest that the vehicle in question, a Jeep Cherokee, is not a luxury vehicle, and I do not utilize the vehicle for my personal use. In fact, I maintain my own private vehicle, at my own expense, for personal use. I utilize the Jeep Cherokee in day to day operations, to travel to and from meetings outside of the facility as well as to and from the facility. The administrator is on call during off hours and is required to travel to the facility at all hours on an emergency or as needed basis. Moreover, the facility is not accessible from my residence via public transportation. The administrator is also the facility's primary representative at external meetings and conferences related to the operation of the facility, and I use the Jeep Cherokee on those occasions as well.

In light of the administrator's responsibilities and my use of the Jeep for business purposes, the depreciation expenses associated with the vehicle in question should be allowed as related to patient care. Consequently, we request that the proposed disallowance be eliminated prior to the issuance of the final audit report.

OMIG Response

Other than the attestation by the administrator, the Facility cannot provide any substantiation to support its claim. The Facility could not provide the OMIG with a log for the automobile in question. Consequently, the disallowance remains the same.

Disposition: The draft report disallowance remains the same.

Property Adjustment #7 –Investment Income Recovery

Facility Comment

St. Johnland objects to the disallowances in subparagraphs (a) and (b) of this item.

Income Offset Regulations:

The regulation governing the propriety of the proposed income offsets included in this item is 10 NYCRR Section 86-2.20(c). Section 86-2.20(c)(1) states:

> Interest expense shall be reduced by investment income with the exception of income from funded depreciation, qualified pension funds, trusteed malpractice insurance funds, or in instances where income from gifts or grants is restricted by donors. Interest on funds borrowed from a donor-restricted fund or funded depreciation is an allowable expense. Investment income shall be defined as the aggregate net amount realized from dividends, interest, rental income, interest earned on temporary investment of withholding taxes, as well as all gains and losses. If the aggregate net amount realized is a loss, the loss is not allowable.

Section 86-2.20(c)(3) states:

> For rate years beginning on or after January 1, 1994, for all residential health care facilities, investment income reported for the same year used to compute capital cost reimbursement for a facility's rate shall reduce the interest expense allowed for reimbursement.

Subparagraph (a).

Background:

St. Johnland's refinancing was completed in furtherance of the Department of Health (DOH) refinancing initiative provided for under Public Health Law (PHL) Section 2808(20), and in accord with guidelines established in the DOH letter of July 11, 2003 (copy attached). The refinancing fulfilled the statute's aim, providing substantial savings to the Medicaid program. The monthly mortgage debt service requirement reduced from $95,826 to $82,104, without any increase in mortgage principal amount nor extension of the mortgage maturity date. The primary beneficiary of those interest rate savings is the State Medicaid Program: based on historical census we estimate the Medicaid interest expense savings net of the cost of closing the refinance transaction at approximately $1,750,000 over the life of the refinanced mortgage.

Discussion:

With respect to the refinancing, we reference the 2004 certified financial statements, more specifically Note E of the Notes to Financial Statements, which provides the summary breakdown of the use of the reported Gain on Refinancing. As noted, the gain of $1,005,092 was utilized as follows:

Mortgage Reduction------------------------ $104,141
Payment of Mortgage Closing Costs---- $266,688
Cash Proceeds--------------------------------$634,263

At the outset, we object to the proposed offset of *2004* "investment income" against *2006* rate year interest expense as contrary to DOH reimbursement methodology. Applying the applicable regulations, the DOH methodology is to reimburse mortgage interest expense on a current year basis. We note that the audit adjustments proposed in Property Expense Disallowances item #2 Mortgage Interest Expense Adjustments recognizes the DOH methodology. Accordingly, the cited regulatory provision requires that investment income be offset to mortgage interest expense on a current year basis. The offset of 2004 "investment income" against 2006 mortgage interest expense is inappropriate, and St. Johnland requests that it be eliminated prior to the issuance of the final audit report.

In any event, to now penalize St. Johnland by offsetting a gain on refinancing against the reduced interest expense is inequitable and actually detrimental to the Medicaid program going forward, as providers in similar situations may not refinance when faced with the prospect of reduced interest expense reimbursement beyond the savings provided by the refinancing. Furthermore, in seeking to arrogate to the State the defeased funds - in addition to savings on mortgage interest reimbursement - the auditors are exceeding their authority, and the reach of Public Health Law 2808(20), by recouping monies beyond the financial benefits intended to inure to the Medicaid program.

What is more, since the mortgage balance at time of refinancing was partially reduced by application of gain proceeds and the mortgage amount was not further increased by the amount of closing costs, those elements of the gain should not be subject to investment income offset. Please see the standard formula described in the July 11, 2003 letter, whereby the program provides for the use of excess debt service reserve funds to reduce the mortgage amount and for the transaction costs related to the refinancing to be reflected in the approved mortgage amount.

Thus, even if an offset were appropriate (and it is not), the amount of the proposed offset ($705,236) is overstated as it does not recognize the additional benefits provided to the Medicaid program from the reduction in mortgage amount and the payment of refinancing transaction costs without increasing the mortgage amount as allowable consistent with the standard formula as supported by statute. The appropriate basis of investment income recovery, if any, should be the net cash proceeds to St. Johnland or $634,263.

Summary:

St. Johnland's refinancing was completed in concert with the DOH refinance initiative under PHL Section 2808(20) and provided substantial savings to the Medicaid program. Also, St. Johnland's refinancing reduced the amount of the mortgage debt and offset the transaction cost related to the refinanced mortgage by utilizing funds from the gain on refinancing. Accordingly, we request that the proposed offset be eliminated in the final audit report. In any event, the amount of the gain to be offset, if any, is overstated and is being inappropriately applied to rate year 2006 in violation of the applicable regulations.

Subparagraph (b).

Background:

The Report proposes an investment income offset in rate years 2005 through 2008, without recognition that the majority of the investment income was related to restricted fund accounts, more specifically the HUD restricted reserve for replacements and mortgage sinking fund accounts.

A yearly summary of the earnings on these accounts is provided below. We are again providing copies of the activity reports for these accounts substantiating the investment income by year:

HUD Restricted Account Fund Earnings

	2003	2004	2005	2006
Reserve for Replacements	5,296	4,347	6,287	8,488
Mtg. Sinking Fund	3,899	3,019	4,149	5,356
Total	9,155	7,366	10,436	13,844

Please note that the aggregate restricted fund earnings, by year, support the amount of restricted fund earnings as reported in the respective cost reports (Exhibit E) filed with DOH.

Discussion:

There is no question but that funds deposited into a HUD-restricted sinking or reserve fund qualify as funded depreciation under DOH regulations and should be exempt from any income offset in accordance with 10NYCRR Section 2-20(c)(I).

10 NYCRR Section 86-2.19(b), relating to funded depreciation, refers to such funds as essentially restricted for a capital-related purpose. The regulation states in relevant part:

> ... In instances where funding [of depreciation] is required, such fund may be use d only for capital expenditures with approval as required or for the amortization of capital indebtedness. Funding for plant and fixed equipment shall mean that the transfer of monies to the funded accounts shall occur by the end of the fiscal period in which the depreciation is recorded. Board-designated funds and the accrual of liabilities to the funded depreciation accounts (due to/from accounts) shall not be recognized as funding of depreciation. Deposits to the funded depreciation accounts must remain in such accounts to be considered as valid funding transactions unless expended for the purpose for which it was funded. (Emphasis added.)

Similarly, 10 NYCRR Section 451.235 defines restricted funds as " funds designated by the donors, governmental units and endowments for special non-operating purposes". The descriptions of the HUD Replacement Reserve and Sinking Fund accounts, attached hereto, outline the restricted purposes for the use of funds from those accounts. Those purposes mirror the purpose of the funded depreciation account and should be treated as such. Indeed, prior to the elimination of mandated depreciation funding, the Department of Health viewed the deposits to the HUD reserve and sinking fund accounts as elements of meeting annual funded depreciation requirements.

Finally, we note that Section 86-2.20(c)(1) indicates that income offset is net of gains and losses. The 2005 adjustment fails to take into account the investment loss as reported in the facility's certified financial statements of 2003. Consequently, we request that the final audit report reflect the reported restricted fund earnings and 2003 investment loss.

OMIG Response

BLTCR regulations state that gains are offset against interest expense on a two year lag. That means a gain due to refinancing occurring in 2004 would be offset against 2006 rate year interest. Regulations also state that the entire gain from refinancing is subject to offsetting, not just the cash proceeds received. Therefore, there is no change to adjustment 7a.

The Facility was able to provide backup documentation that showed that the remaining investment income was in fact restricted. The accounts were reserve for replacement and a mortgage sinking fund. These accounts were specifically HUD reserve accounts, which qualify as restricted income. Therefore, disallowance 7b will be eliminated.

Disposition: Adjustment #7b is eliminated from the draft report. Adjustment #7a remains the same.

EXHIBIT V COMMENTS

Property Adjustment #2 – Equipment Rental Expense Disallowances

Facility Comment

St. Johnland objects to this proposed disallowance. St. Johnland has located documentation, including invoices, supporting reported various equipment lease expenses, and has attached copies for the auditors' review. Accordingly, there is no basis for the disallowance on the ground cited in the Report.

OMIG Response

The Facility was able to provide substantiation for only some of the rental items disallowed in the draft report. However, the Facility was only able to provide substantiation for items listed under Rent G, which does not apply to the TBI unit. Therefore, no adjustment was made to the disallowances listed in Exhibit V

Disposition: The draft report disallowance remains the same.

Property Adjustment #4 – Mortgage Expense Amortization

Facility Comment

St. Johnland objects only to the proposed disallowance in subparagraph (b) of this item. The report proposes to disallowance $17,619 of mortgage expense amortization, citing lack of documentation. This adjustment is made for rate year 2008/cost year 2006. Please note that the mortgage expense amortization relates to 2004 mortgage refinancing ($266,688) and the society loan of February 2005 ($7,750).

These costs are being amortized over the respective lives of the loans in accordance with generally accepted accounting principles and therefore the mortgage amortization expense should be recognized as an allowable cost for Medicaid reimbursement purposes. Attached is a copy of the invoice from GMAC Commercial Mortgage related to the 2004 mortgage refinancing in support of costs associated there with.

We respectfully request the audit report reflect appropriate amortization of these costs in the annual amount of $14,163 ($224,255/190 months).

OMIG Response

The documentation provided by the Facility was sufficient enough to partially eliminate the disallowance in the draft report. The Facility was able to provide documentation to support $14,163 of expenses a year. The original disallowance was $17,619. Therefore, there will still be a disallowance of $3,456 for adjustment #4b.

Disposition: The draft report is changed to reflect the partial elimination of property adjustment #4b.

Property Adjustment #5 – Working Capital Interest Disallowances

Facility Comment

St. Johnland objects to the proposed disallowance in subparagraph (a) only of this item. St. Johnland takes exception to the proposed audit disallowance in rate years 2005, 2006 (1/1-3/31/06) and 2007.

The audit work papers state that "(late fees are not an allowable expense". We disagree with this comment, as there is no regulatory provision stating that late fees are not allowable costs, with the exception of late fees, interest and penalties resulting from governmental obligations (10 N.Y.C.R.R. § 86-2.17(g)) or violation of Federal, State or local laws (PRM Sections 2102.3 and 2105.10). Also, there is no mention in the Report that these costs were not in fact incurred.

The Report also refers to 10 N.Y.C.R.R. § 86-2.17(a) and (d) and PRM-2103. However, these provisions relate broadly to costs necessary to patient care or to the efficient production of services and do not address the treatment of late fees. Moreover, in computing the capital component of the St. Johnland's annual Medicaid rate, the Department of Health (DOH) was aware of the nature of the costs reported by St. Johnland on the cost report and allowed such costs, subject to the appropriate working capital threshold. It is significant to note that the reported costs for 2003/rate year 2005 were less than the applicable threshold. Consequently, the DOH determination was appropriate, especially considering the financial position of St. Johnland during this period, as indicated below:

Calendar Year Ended 12/31	2002	2003	2004	2005
Current Assets	$9,532,338	$9,219,857	$9,143,045	$11,350,146
Current Liabilities	$11,366,744	$11,692,224	$13,075,433	$11,992,157
Working Capital	$(1,834,406)	$(2,472,367)	$(3,932,388)	$(642,011)
Unrestricted Cash & Investments	$27,665	$63,688	$2,882	$12,283

Calendar Year Ended 12/31	2002	2003	2004	2005
Income from operations	$(844,751)	$(1,242,831)	$(1,137616)	$(814,969)
Non-Operating Revenues	$312,434	$289,953	$203,982	$214,508
Extraordinary(Loss)/Gain	$(1,963,233)	$-	$1,005,092	$-
Excess Income/(Expenses)	$(2,495,550)	$(952,878)	$71,458	$(600,461)

We further submit that OMIG on audit is bound by DOH rate determinations, and lacks the authority to retroactively change a level of reimbursement approved by the rate setters. See Livingston Cty. Health Related Facility v. Perales, 124 A.D.2d 289, 291 (3d Dep't 1986); see also Rossi v. Axelrod, 178 A.D.2d 813, 814 (3d Dep't 1991) (auditors must "faithfully adhere to the methodology which DOH established and employed in calculating [the facility's] original rights").

Moreover, the facts refute then the auditors' assumption that St. Johnland acted imprudently in delaying the loan payments that resulted in late fees. Clearly, St. Johnland was experiencing financial difficulty, with substantial operating losses, razor-thin unrestricted cash balances and significant negative working capital in each of the audited years and had limited, if any, ability to access additional loans for working capital purposes. Rather than incur a short term debt to increase cash balances and to overcome substantial negative working capital positions, St. Johnland managed its limited cash resources and incurred cost far less than it would have incurred had it had borrowed the prior years' ending negative working capital position for a one year period at an interest rate equal to the interest rate utilized in the applicable rate year working capital threshold calculation, as shown below:

	2003	2004	2005
Loan Amount	$1,834,400	$2,472,000	$3,932,000
Interest Rate	6.25%	%6.00	7.25%
Term-Years	1	1	1
Total Payments	$1,897,000	$2,553,000	$4,088,000
Interest Expense	$62,600	$81,000	$156,000
Schedule 8d Expense	$31,156	$38,945	$64,986

Application of the "prudent buyer" principle to determine whether a provider incurred costs in line with the going rate for a given service or product requires consideration of any extenuating circumstances in which the provider was operating at the time it entered into the transaction being reviewed. PRM-1 Section 2013[B]. As indicated above, contrary to the audit summary, the facts and circumstances demonstrate that St. Johnland did act as a prudent and cost conscious buyer, by avoiding more costly borrowings, and that the DOH came to the same conclusion when allowing the costs subject to the working capital threshold.

In sum, St. Johnland submits that the proposed audit disallowances are inappropriate and requests that they be eliminated prior to the issuance of the final audit report.

OMIG Response

Reimbursement regulations states that the buyer of service should refuse to pay more than the going price of an item/service and seek to economize by minimizing cost. By incurring late fees, the Facility was in conflict with the above regulations. Therefore, the disallowance will remain in the report.

Disposition: The draft report disallowance remains the same.

Property Adjustment #6 – Moveable Equipment Depreciation Disallowances

Facility Comment

St. Johnland objects only to the proposed disallowance in subparagraph (b) of this item. The Report proposes to disallow moveable equipment depreciation expense in rate years 2006, 2007 and 2008 relating to an automobile utilized by the facility's administrator.

As the administrator, I can attest that the vehicle in question, a Jeep Cherokee, is not a luxury vehicle, and I do not utilize the vehicle for my personal use. In fact, I maintain my own private vehicle, at my own expense, for personal use. I utilize the Jeep Cherokee in day to day operations, to travel to and from meetings outside of the facility as well as to and from the facility. The administrator is on call during off hours and is required to travel to the facility at all hours on an emergency or as needed basis. Moreover, the facility is not accessible from my residence via public transportation. The administrator is also the facility's primary representative at external meetings and conferences related to the operation of the facility, and I use the Jeep Cherokee on those occasions as well.

In light of the administrator's responsibilities and my use of the Jeep for business purposes, the depreciation expenses associated with the vehicle in question should be allowed as related to patient care. Consequently, we request that the proposed disallowance be eliminated prior to the issuance of the final audit report.

OMIG Response

Other than the attestation by the administrator, the Facility cannot provide any substantiation to support their claim. The Facility could not provide the OMIG with a log for the automobile in question. Consequently, the disallowance remains the same.

Disposition: The draft report disallowance remains the same.

Property Adjustment #7 –Investment Income Recovery

Facility Comment

St. Johnland objects to the disallowances in subparagraphs (a) and (b) ofthis item.

Income Offset Regulations:

The regulation governing the propriety of the proposed income offsets included in this item is 10 NYCRR Section 86-2.20(c). Section 86-2.20(c)(1) states:

> Interest expense shall be reduced by investment income with the exception of income from funded depreciation, qualified pension funds, trusteed malpractice insurance funds, or in instances where income from gifts or grants is restricted by donors. Interest on funds borrowed from a donor-restricted fund or funded depreciation is an allowable expense. Investment income shall be defined as the aggregate net amount realized from dividends, interest, rental income, interest earned on temporary investment of withholding taxes, as well as all gains and losses. If the aggregate net amount realized is a loss, the loss is not allowable.

Section 86-2.20(c)(3) states:

> For rate years beginning on or after January 1, 1994, for all residential health care facilities, investment income reported for the same year used to compute capital cost reimbursement for a facility's rate shall reduce the interest expense allowed for reimbursement.

Subparagraph (a).

Background:

St. Johnland's refinancing was completed in furtherance of the Department of Health (DOH) refinancing initiative provided for under Public Health Law (PHL) Section 2808(20), and in accord with guidelines established in the DOH letter of July 11, 2003 (copy attached). The refinancing fulfilled the statute's aim, providing substantial savings to the Medicaid program. The monthly mortgage debt service requirement reduced from $95,826 to $82,104, without any increase in mortgage principal amount nor extension of the mortgage maturity date. The primary beneficiary of those interest rate savings is the State Medicaid Program: based on historical census we estimate the Medicaid interest expense savings net of the cost of closing the refinance transaction at approximately $1,750,000 over the life of the refinanced mortgage.

Discussion:

With respect to the refinancing, we reference the 2004 certified financial statements, more specifically Note E of the Notes To Financial Statements, which provides the summary breakdown of the use of the reported Gain on Refinancing. As noted, the gain of $1,005,092 was utilized as follows:

Mortgage Reduction------------------------ $104,141
Payment of Mortgage Closing Costs---- $266,688
Cash Proceeds------------------------------$634,263

At the outset, we object to the proposed offset of *2004* "investment income" against *2006* rate year interest expense as contrary to DOH reimbursement methodology. Applying the applicable regulations, the DOH methodology is to reimburse mortgage interest expense on a current year basis. We note that the audit adjustments proposed in Property Expense Disallowances item #2 Mortgage Interest Expense Adjustments recognizes the DOH methodology. Accordingly, the cited regulatory provision requires that investment income be offset to mortgage interest expense on a current year basis. The offset of 2004 "investment income" against 2006 mortgage interest expense is inappropriate, and St. Johnland requests that it be eliminated prior to the issuance of the final audit report.

In any event, to now penalize St. Johnland by offsetting a gain on refinancing against the reduced interest expense is inequitable and actually detrimental to the Medicaid program going forward, as providers in similar situations may not refinance when faced with the prospect of reduced interest expense reimbursement beyond the savings provided by the refinancing. Furthermore, in seeking to arrogate to the State the defeased funds - in addition to savings on mortgage interest reimbursement - the auditors are exceeding their authority, and the reach of Public Health Law 2808(20), by recouping monies beyond the financial benefits intended to inure to the Medicaid program.

What is more, since the mortgage balance at time of refinancing was partially reduced by application of gain proceeds and the mortgage amount was not further increased by the amount of closing costs, those elements of the gain should not be subject to investment income offset. Please see the standard formula described in the July 11, 2003 letter, whereby the program provides for the use of excess debt service reserve funds to reduce the mortgage amount and for the transaction costs related to the refinancing to be reflected in the approved mortgage amount.

Thus, even if an offset were appropriate (and it is not), the amount of the proposed offset ($705,236) is overstated as it does not recognize the additional benefits provided to the Medicaid program from the reduction in mortgage amount and the payment of refinancing transaction costs without increasing the mortgage amount as allowable consistent with the standard formula as supported by statute. The appropriate basis of investment income recovery, if any, should be the net cash proceeds to St. Johnland or $634,263.

Summary:

St. Johnland's refinancing was completed in concert with the DOH refinance initiative under PHL Section 2808(20) and provided substantial savings to the Medicaid program. Also, St. Johnland's refinancing reduced the amount of the mortgage debt and offset the transaction cost related to the refinanced mortgage by utilizing funds from the gain on refinancing. Accordingly, we request that the proposed offset be eliminated in the final audit report. In any event, the amount of the gain to be offset, if any, is overstated and is being inappropriately applied to rate year 2006 in violation of the applicable regulations.

Subparagraph (b).

Background:

The Report proposes an investment income offset in rate years 2005 through 2008, without recognition that the majority of the investment income was related to restricted fund accounts, more specifically the HUD restricted reserve for replacements and mortgage sinking fund accounts.

A yearly summary of the earnings on these accounts is provided below. We are again providing copies of the activity reports for these accounts substantiating the investment income by year:

HUD Restricted Account Fund Earnings

	2003	2004	2005	2006
Res. for Replacements	5,296	4,347	6,287	8,488
Mtg. Sinking Fund	3,899	3,019	4,149	5,356
Total	9,155	7,366	10,436	13,844

Please note that the aggregate restricted fund earnings, by year, support the amount of restricted fund earnings as reported in the respective cost reports (Exhibit E) filed with DOH.

Discussion:

There is no question but that funds deposited into a HUD-restricted sinking or reserve fund qualify as funded depreciation under DOH regulations and should be exempt from any income offset in accordance with 10NYCRR Section 2-20(c)(I).

10 NYCRR Section 86-2.19(b), relating to funded depreciation, refers to such funds as essentially restricted for a capital-related purpose. The regulation states in relevant part:

> ... In instances where funding [of depreciation] is required, such fund may be use d only for capital expenditures with approval as required or for the amortization of capital indebtedness. Funding for plant and fixed equipment shall mean that the transfer of

> monies to the funded accounts shall occur by the end of the fiscal period in which the depreciation is recorded. Board-designated funds and the accrual of liabilities to the funded depreciation accounts (due to/from accounts) shall not be recognized as funding of depreciation. Deposits to the funded depreciation accounts must remain in such accounts to be considered as valid funding transactions unless expended for the purpose for which it was funded. (Emphasis added.)

Similarly, 10 NYCRR Section 451.235 defines restricted funds as " funds designated by the donors, governmental units and endowments for special non-operating purposes". The descriptions of the HUD Replacement Reserve and Sinking Fund accounts, attached hereto, outline the restricted purposes for the use of funds from those accounts. Those purposes mirror the purpose of the funded depreciation account and should be treated as such. Indeed, prior to the elimination of mandated depreciation funding, the Department of Health viewed the deposits to the HUD reserve and sinking fund accounts as elements of meeting annual funded depreciation requirements.

Finally, we note that Section 86-2.20(c)(1) indicates that income offset is net of gains and losses. The 2005 adjustment fails to take into account the investment loss as reported in the facility's certified financial statements of2003. Consequently, we request that the final audit report reflect the reported restricted fund earnings and 2003 investment loss.

OMIG Response

BLTCR regulations state that gains are offset against interest expense on a two year lag. That means a gain due to refinancing occurring in 2004 would be offset against 2006 rate year interest. Regulations also state that the entire gain from refinancing is subject to offsetting, not just the cash proceeds received. Therefore there is no change to adjustment 7a. The Facility was able to provide backup documentation that showed that the remaining investment income was in fact restricted. The accounts were reserve for replacement and a mortgage sinking fund. These accounts were specifically HUD reserve accounts, which qualify as restricted income. Therefore, disallowance 7b will be eliminated.

Disposition: Adjustment #7b is eliminated from the draft report. Adjustment #7a remains the same.

ATTACHMENT B

ST. JOHNLAND NURSING CENTER - AUDIT #09-4255
SUMMARY OF CHANGES FROM DRAFT REPORT TO FINAL REPORT

		Rate Period	Draft Disallowance (Allowance)	Change	Final Disallowance (Allowance)
EXHIBIT III - OPERATING EXPENSE DISALLOWANCES/(ALLOWANCES)					
1.	UTILITIES EXPENSE DISALLOWANCE	7/1/05-6/30/06	$ 3,720	$ -	$ 3,720
2.	UTILITIES EXPENSE DISALLOWANCE	7/1/05-6/30/06	5,722	(5,722)	
3.	RECLASSIFICATION OF UTILIZATION EXPENSE	7/1/05-6/30/06	110,962	-	110,962
EXHIBIT IV - PROPERTY EXPENSE DISALLOWANCES/(ALLOWANCES) FOR NURSING FACILITY					
2.	EQUIPMENT RENTAL EXPENSE DISALLOWANCES				
	RENT E	2005	438	-	438
	RENT F	2005	600	-	600
	RENT J	2005	4,995	-	4,995
	RENT E	2006	4,771	-	4,771
	RENT F	2007	23,595	-	23,595
	RENT B	2008	3,430	-	3,430
	RENT F	2008	2,401	-	2,401
	RENT G	2008	19,937	(4,744)	15,193
4(b).	MORTGAGE EXPENSE AMORTIZATION	2008	17,619	(14,163)	3,456
5(a).	WORKING CAPITAL INTEREST EXPENSE DISALLOWANCES	2005	24,894	-	24,894
		2006	26,733	-	26,733
		2007	31,225	-	31,225
				-	
6(b).	MOVEABLE EQUIPMENT DEPRECIATION DISALLOWANCES	2006	3,191	-	3,191
		2007	7,375	-	7,375
		2008	7,375	-	7,375
7.	INVESTMENT INCOME RECOVERY	2005	7,541	(7,541)	
		2005	3,196	(3,196)	
		2006	705,236	-	705,236
		2006	7,017	(7,017)	
		2007	9,080	(9,080)	
		2007	9,556	(9,556)	
		2008	12,854	(12,854)	
EXHIBIT V - PROPERTY EXPENSE DISALLOWANCES/(ALLOWANCES) FOR TBI UNIT					
2.	EQUIPMENT RENTAL EXPENSE DISALLOWANCES			-	
	RENT E	2005	438	-	438
	RENT E	2006	4,771	-	4,771
	RENT F	2007	23,595	-	23,595
	RENT B	2008	3,430	-	3,430
	RENT F	2008	2,401	-	2,401
4(b).	MORTGAGE EXPENSE AMORTIZATION	2008	17,619	(14,163)	3,456
5(a).	WORKING CAPITAL INTEREST EXPENSE DISALLOWANCES	2005	24,894	-	24,894
		2006	26,733	-	26,733
		2007	31,225	-	31,225
				-	
6(b).	MOVEABLE EQUIPMENT DEPRECIATION DISALLOWANCES	2006	3,191	-	3,191
		2007	7,375	-	7,375
		2008	7,375	-	7,375
7.	INVESTMENT INCOME RECOVERY	2005	7,541	(7,541)	
		2005	3,196	(3,196)	
		2006	705,236	-	705,236
		2006	7,017	(7,017)	
		2007	9,080	(9,080)	
		2007	9,556	(9,556)	
		2008	12,854	(12,854)	

EXHIBIT I

ST. JOHNLAND NURSING CENTER- AUDIT #09-4255
RATE PERIODS JANUARY 1, 2005 THROUGH DECEMBER 31, 2008
SUMMARY OF PER DIEM IMPACT AND MEDICAID OVERPAYMENT

RATE PERIOD NURSING FACILITY		ISSUED PART B & D NON-ELIGIBLE RATES*	FINAL PART B & D NON-ELIGIBLE RATES	RATE DECREASE (INCREASE)	MEDICAID DAYS	MEDICAID OVERPAYMENT
01/01/05 -	03/31/05	$199.67	$198.14	$1.53	16,138	$ 24,691
04/01/05 -	06/30/05	199.55	198.02	1.53	16,089	24,616
07/01/05 -	09/30/05	246.40	243.71	2.69	15,918	42,819
10/01/05 -	12/31/05	246.45	243.75	2.70	15,573	42,047
01/01/06 -	03/31/06	259.11	247.31	11.80	15,197	179,325
04/01/06 -	06/30/06	259.02	247.17	11.85	15,568	184,481
07/01/06 -	09/30/06	258.75	246.90	11.85	15,170	179,765
10/01/06 -	12/31/06	257.07	245.22	11.85	15,608	184,955
01/01/07 -	03/31/07	262.17	260.23	1.94	15,690	30,439
04/01/07 -	06/30/07	260.80	258.86	1.94	15,696	30,450
07/01/07 -	08/31/07	254.65	252.71	1.94	10,655	20,671
09/01/07 -	12/31/07	254.65	252.71	1.94	21,340	41,400
01/01/08 -	03/31/08	259.43	257.72	1.71	15,299	26,161
04/01/08 -	06/30/08	257.61	255.91	1.70	15,238	25,905
07/01/08 -	12/31/08	264.60	259.92	1.70	32,003	54,405
MEDICAID OVERPAYMENT - NURSING FACILITY						**$ 1,092,130**
TBI UNIT						
01/01/05 -	03/31/05	$557.87	$554.66	$3.21	99	$ 318
04/01/05 -	06/30/05	573.86	570.65	3.21	153	491
07/01/05 -	09/30/05	572.61	567.18	5.43	72	391
10/01/05 -	12/31/05	569.76	564.33	5.43	166	901
01/01/06 -	03/31/06	596.21	576.90	19.31	178	3,437
04/01/06 -	06/30/06	596.35	576.89	19.46	350	6,811
07/01/06 -	09/30/06	591.22	571.76	19.46	255	4,962
10/01/06 -	12/31/06	588.90	569.44	19.46	373	7,259
01/01/07 -	03/31/07	594.04	590.13	3.91	293	1,146
04/01/07 -	06/30/07	590.72	586.82	3.90	439	1,712
07/01/07 -	08/31/07	590.72	586.82	3.90	384	1,498
09/01/07 -	12/31/07	590.72	586.82	3.90	644	2,512
01/01/08 -	03/31/08	599.26	596.39	2.87	403	1,157
04/01/08 -	12/31/08	594.86	592.01	2.85	972	2,770
MEDICAID OVERPAYMENT - TBI						**$ 35,365**
TOTAL MEDICAID OVERPAYMENT						**$ 1,127,495**

* Any differences between these rates and the rates listed in Exhibit II of this report represent rate changes made subsequent to OMIG's audit. These changes remain open to future audit by the OMIG. For the purpose of this Exhibit, the Medicare Part B and D rates are not shown. The rate decrease/(increase) for those rates is the same as shown for the Medicare Part B and D non-eligible rates above.

ST. JOHNLAND NURSING CENTER- AUDIT #09-4255
RATE PERIODS JANUARY 1, 2005 THROUGH DECEMBER 31, 2008
SUMMARY OF MEDICAID RATES AUDITED

The Facility's Medicaid utilization was approximately 73 percent for the nursing facility and 20 percent for the TBI unit for the period under audit and the Medicaid per diem rates audited are shown below. Any differences between these rates and the "Issued Rates" listed in Exhibit I of this report represent rate changes made subsequent to our audit. These changes remain open to future audit by the OMIG.

RATE PERIOD	Issued Medicare Part B & D Non-Eligible Rates *
NURSING FACILITY	
01/01/05 - 03/31/05	$200.06
04/01/05 - 06/30/05	199.94
07/01/05 - 09/30/05	240.46
10/01/05 - 12/31/05	246.45
01/01/06 - 03/31/06	259.11
04/01/06 - 06/30/06	259.02
07/01/06 - 09/30/06	258.75
10/01/06 - 12/31/06	257.07
01/01/07 - 03/31/07	262.17
04/01/07 - 06/30/07	260.80
07/01/07 - 08/31/07	254.65
09/01/07 - 12/31/07	254.65
01/01/08 - 03/31/08	254.79
04/01/08 - 06/30/08	252.97
07/01/08 - 12/31/08	259.96
TBI UNIT	
01/01/05 - 03/31/05	$557.87
04/01/05 - 06/30/05	573.86
07/01/05 - 09/30/05	572.61
10/01/05 - 12/31/05	569.76
01/01/06 - 03/31/06	596.21
04/01/06 - 06/30/06	596.35
07/01/06 - 09/30/06	591.22
10/01/06 - 12/31/06	588.90
01/01/07 - 03/31/07	594.04
04/01/07 - 06/30/07	590.72
07/01/07 - 08/31/07	590.72
09/01/07 - 12/31/07	590.72
01/01/08 - 03/31/08	599.26
04/01/08 - 12/31/08	594.86

* The Medicare Part B and D rates are not shown for the purpose of this Exhibit. The Medicare Part B and D offsets were not within the scope of this audit and may be examined as part of a future audit.

EXHIBIT III

ST. JOHNLAND NURSING CENTER- AUDIT #09-4255
RATE PERIODS JANUARY 1, 2005 THROUGH DECEMBER 31, 2008
OPERATING EXPENSE DISALLOWANCES/(ALLOWANCES)

	DESCRIPTION	COST CTR.	DISALLOWED (ALLOWED)	NF TRACE-BACK %	TBI TRACE-BACK %	OPERATING EXPENSE COMPONENT: NF DIRECT	TBI DIRECT	NF INDIRECT	TBI INDIRECT	NF NON-COMP.	TBI NON-COMP.
Operating Expense Allowed per HE-12B						$ 13,364,728	$ 2,742,826	$ 5,974,503	$ 614,241	$ 1,299,697	$ 692,965
Less Disallowances/(Allowances):											
1. UTILITIES EXPENSE DISALLOWANCES Providers receiving payments on the basis of reimbursable costs are required to provide adequate cost data based on financial and statistical records that can be verified on audit. Cost data must be current, accurate, and in sufficient detail. The Facility did not provide adequate documentation to substantiate reported utilities expense. Consequently, the unsubstantiated expenses were disallowed. **Regulations: 10 NYCRR Section 86-2.17(a), PRM-1 Sections 2300 & 2304**	Utilities	006	$3,720	85.95%	10.48%					3,197	390
2. UTILITIES EXPENSE DISALLOWANCES Based on information and documentation provided by the Facility, this adjustment has been eliminated.											
3. RECLASSIFICATION OF UTILIZATION REVIEW EXPENSE Utilization review expense included salaries and employee benefit expenses. The Facility could not provide job descriptions for the positions associated with these expenses. As a result, an adjustment was necessary to reclassify the expenses to the Nursing Facility cost center. **Regulations: 10 NYCRR Section 455.20, Public Health Law, Article 49, Title I**	Utilization	020	110,962	86.78%	13.22%					96,293	14,669
	Nurs. Fac.	051	(110,962)	100.00%	0.00%	(110,962)					
Total Disallowances/(Allowances)						$ (110,962)	$ -	$ -	$ -	$ 99,490	$ 15,059
AUDITED OPERATING EXPENSE BY COMPONENT						$ 13,475,690	$ 2,742,826	$ 5,974,503	$ 614,241	$ 1,200,207	$ 677,906

ST. JOHNLAND NURSING CENTER- AUDIT #09-4255
RATE PERIODS JANUARY 1, 2005 THROUGH DECEMBER 31, 2008
PROPERTY EXPENSE DISALLOWANCES/(ALLOWANCES) FOR NURSING FACILITY

	DESCRIPTION	COST CTR.	DISALLOWED (ALLOWED)	TRACE-BACK %	RATE PERIODS 01/01/05 12/31/05	01/01/06 03/31/06	04/01/06 12/31/06	01/01/07 12/31/07	01/01/08 12/31/08
Property Expense Allowed per HE-12B					$ 1,968,690	$ 2,377,339	$ 2,377,339	$ 2,268,885	$ 2,066,379
Less Disallowances/(Allowances):									
1. MORTGAGE INTEREST EXPENSE ADJUSTMENTS									
a) The Bureau of Long Term Care Reimbursment (BLTCR) included an adjustment in the rate computation to include the interest for Loan #1 on line 36 "Other" and Loan #2 on line 38 "Other". BLTCR also included interest for these two loans on line 2 "Interest." The duplicated amounts were disallowed. **Regulation: 10 NYCRR Section 86-2.20(a)**	Mort. Int.	003	243,414	85.55%		208,241	208,241		
b) The OMIG audit included a review of actual mortgage payments, accruals and reversals, and final year-end trial balance account expense. The OMIG identified variances between the amounts allowed by the BLTCR and the actual rate year mortgage interest expense determined on audit. Adjustments were necessary to reflect the Facility's actual rate year mortgage interest expense in the audited rates. **Regulations: 10 NYCRR Sections 86-2.17(a) & 2.20(a), PRM-1 Sections 2300 & 2304**	Mort. Int.	003	66,454	85.50%	56,818				
	Mort. Int.	003	924	85.94%				794	
	Mort. Int.	003	(2,300)	85.92%					(1,976)
2. EQUIPMENT RENTAL EXPENSE DISALLOWANCES									
Providers who receive payments on the basis of reimbursable cost must provide adequate cost data based on financial and statistical records that can be verified on audit. The Facility did not provide adequate documentation to substantiate reported equipment rental expense. Consequently, disallowances were necessary. **Regulations: 10 NYCRR Section 86-2.17(a), PRM-1 Sections 2102.2, 2300, & 2304**	Rent E	043	438	80.70%	353				
	Rent F	051	600	100.00%	600				
	Rent J	051	4,995	100.00%	4,995				
	Rent E	043	4,771	80.65%		3,848	3,848		
	Rent F	043	23,595	80.65%				19,029	
	Rent B	005	3,430	76.01%					2,607
	Rent F	014	2,401	71.38%					1,714
	Rent G	051	15,193	100.00%					15,193
3. MORTGAGE INSURANCE EXPENSE DISALLOWANCES									
The Bureau of Long Term Care Reimbursement reimbursed the Facility mortgage insurance expense on a rate year basis. Audited rate year insurance expense varied from the insurance allowed in the promulgated rates, resulting in disallowances. **Regulations: 10 NYCRR Section 86-2.17(a), PRM-1 Sections 2102.3, 2300, & 2304**	Mort. Ins.	005	2,638	72.83%	1,921				
	Mort. Ins.	005	5,853	73.88%		4,324	4,324		
	Mort. Ins.	006	1,944	86.12%					1,674
4. MORTGAGE EXPENSE AMORTIZATION									
a) Mortgage expense amortization was determined to be included within the building component of Approved Project Cost (APC) #900209. Reported mortgage expense amortization was disallowed since it is being already reimbursed through the APC building and fixed equipment depreciation. **Regulations: 10 NYCRR Sections 86-2.17(a) & 86-2.17(d)**	Mort. Amort.	005	43,740	72.83%	31,856				
	Mort. Amort.	005	46,703	73.88%		34,504	34,504		

ST. JOHNLAND NURSING CENTER- AUDIT #09-4255
RATE PERIODS JANUARY 1, 2005 THROUGH DECEMBER 31, 2008
PROPERTY EXPENSE DISALLOWANCES/(ALLOWANCES) FOR NURSING FACILITY

	DESCRIPTION	COST CTR.	DISALLOWED (ALLOWED)	TRACE-BACK %	RATE PERIODS 01/01/05 12/31/05	01/01/06 03/31/06	04/01/06 12/31/06	01/01/07 12/31/07	01/01/08 12/31/08
4. MORTGAGE EXPENSE AMORTIZATION (CONT.) b) Providers who receive payments on the basis of reimbursable cost must provide adequate cost data based on financial and statistical records that can be verified on audit. The Facility did not provide adequate documentation to substantiate reported mortgage expense amortization, resulting in a disallowance. **Regulations: 10 NYCRR Sections 86-2.17(a) & (d), PRM-1 Sections 2102.3, 2300, & 2304**	Mort. Amort.	005	3,456	76.01%					2,627
5. WORKING CAPITAL INTEREST EXPENSE DISALLOWANCES a) Late fees paid to vendors were included in reported working capital interest expense. According to reimbursement regulations, the prudent and cost conscious buyer not only refuses to pay more than the going price for an item or service, he/she also seeks to economize by minimizing cost. Since the late fees could have been avoided with timely payment, incurring such expense is in conflict with the above concept. In addition, these disallowances were consistent with methodology used by the Bureau of Long Term Care Reimbursement when establishing the rates. **Regulations: 10 NYCRR Sections 86-2.17(a) & (d), PRM-1 Section 2103**	WCI	005	24,894	72.83%	18,130				
	WCI	005	28,733	73.88%		19,750	19,750		
	WCI	005	31,225	75.81%				23,672	
b) Effective April 1, 2006 and thereafter, rates shall not contain a payment factor for working capital interest if the RHCF report utilized to determine such payment factor also shows a positive net income. The Facility had a positive net income for cost year 2004. Consequently, working capital interest expense was disallowed. **Regulation: Public Health Law, Section 2808, Paragraph 22-a**	WCI	005	7,017	73.88%			5,184		
6. MOVABLE EQUIPMENT DEPRECIATION DISALLOWANCES a) The Bureau of Long Term Care Reimbursement has determined the nature of telephone expense to be an operating expense. Since the expense is included in the formula to determine the base, mean, and ceiling prices used to establish the indirect expense corridor, the reimbursement of telephone depreciation expense in the property component amounts to duplicate reimbursement. Consequently, disallowances were necessary. **Regulation: 10 NYCRR Section 86-2.17(d)**	ME Depr.	002	16,458	85.51%	14,073				
	ME Depr.	002	12,207	100.00%		12,207	12,207		
	ME Depr.	002	1,965	0.00%					
	ME Depr.	002	11,795	85.94%				10,137	
	ME Depr.	002	12,996	85.92%					11,166
b) 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 properly chargeable to necessary patient care are allowable. Depreciation on vehicles that were used exclusively by Administrators was disallowed since this expense is not directly related to patient care. **Regulations: 10 NYCRR Section 86-2.17(a) & PRM-1 Sections 2102.3 & 2105.9**	ME Depr.	002	3,191	100.00%		3,191	3,191		
	ME Depr.	002	7,375	85.94%				6,338	
	ME Depr.	002	7,375	85.92%					6,337

ST. JOHNLAND NURSING CENTER- AUDIT #09-4255
RATE PERIODS JANUARY 1, 2005 THROUGH DECEMBER 31, 2008
PROPERTY EXPENSE DISALLOWANCES/(ALLOWANCES) FOR NURSING FACILITY

	DESCRIPTION	COST CTR.	DISALLOWED (ALLOWED)	TRACE-BACK %	RATE PERIODS 01/01/05 12/31/05	01/01/06 03/31/06	04/01/06 12/31/06	01/01/07 12/31/07	01/01/08 12/31/08
7. INVESTMENT INCOME RECOVERY a) The Facility refinanced its mortgage and realized a net gain on the mortgage refinancing of debt. 10 NYCRR Section 86-2.20(c)(1) states that interest expense is to be reduced by investment income. Investment income shall be defined as the aggregate net amount realized from dividends, interest, rental income, interest earned on temporary investment of withholding taxes, as well as all gains and losses. Consequently, the gain on refinancing was offset against interest expense. **Regulation: 10 NYCRR Section 86-2.20(c)** b) Based on information and documentation provided by the facility, this adjustment has been eliminated.	Inc. Offset	003	705,236	85.55%		603,329	603,329		
Total Disallowances/(Allowances)					$ 128,746	$ 889,394	$ 894,578	$ 59,970	$ 39,342
TOTAL AUDITED PROPERTY EXPENSE					$ 1,839,944	$ 1,487,945	$ 1,482,761	$ 2,208,915	$ 2,027,037

ST. JOHNLAND NURSING CENTER- AUDIT #09-4255
RATE PERIODS JANUARY 1, 2005 THROUGH DECEMBER 31, 2008
PROPERTY EXPENSE DISALLOWANCES/(ALLOWANCES) FOR TBI UNIT

	DESCRIPTION	COST CTR.	DISALLOWED (ALLOWED)	TRACE-BACK %	RATE PERIODS 01/01/05 12/31/05	01/01/06 03/31/06	04/01/06 12/31/06	01/01/07 12/31/07	01/01/08 12/31/08
Property Expense Allowed per HE-12B					$ 266,148	$ 301,347	$ 301,347	$ 242,334	$ 256,100
Less Disallowances/(Allowances):									
1. MORTGAGE INTEREST EXPENSE ADJUSTMENTS									
a) The Bureau of Long Term Care Reimbursment (BLTCR) included an adjustment in the rate computation to include the interest for Loan #1 on line 36 "Other" and Loan #2 on line 38 "Other". BLTCR also included interest for these two loans on line 2 "Interest." The duplicated amounts were disallowed. **Regulation: 10 NYCRR Section 86-2.20(a)**	Mort. Int.	003	243,414	10.67%		25,972	25,972		
b) The OMIG audit included a review of actual mortgage payments, accruals and reversals, and final year-end trial balance account expense. The OMIG identified variances between the amounts allowed by the BLTCR and the actual rate year mortgage interest expense determined on audit. Adjustments were made to reflect the Facility's actual rate year mortgage interest expense in the audited rates. **Regulations: 10 NYCRR Sections 86-2.17(a) & 2.20(a), PRM-1 Sections 2300 & 2304**	Mort. Int.	003	66,454	10.78%	7,164				
	Mort. Int.	003	924	10.31%				95	
	Mort. Int.	003	(2,300)	10.37%					(239)
2. EQUIPMENT RENTAL EXPENSE DISALLOWANCES Providers who receive payments on the basis of reimbursable cost must provide adequate cost data based on financial and statistical records that can be verified on audit. The Facility did not provide adequate documentation to substantiate reported equipment rental expense. Consequently, disallowances were necessary. **Regulations: 10 NYCRR Section 86-2.17, PRM-1 Sections 2102.2, 2300, & 2304**	Rent E	043	438	17.90%	78				
	Rent E	043	4,771	17.90%		854	854		
	Rent F	043	23,595	17.90%				4,224	
	Rent B	005	3,430	14.16%					486
	Rent F	014	2,401	4.85%					116
3. MORTGAGE INSURANCE EXPENSE DISALLOWANCES The Bureau of Long Term Care Reimbursement reimbursed the Facility mortgage insurance expense on a rate year basis. Audited rate year insurance expense varied from the insurance allowed in the promulgated rates resulting in disallowances. **Regulations: 10 NYCRR Section 86-2.17(a), PRM-1 Sections 2102.3, 2300, & 2304**	Mort. Ins.	005	2,638	17.20%	454				
	Mort. Ins.	005	5,853	15.41%		902	902		
	Mort. Ins.	006	1,944	10.29%					200
4. MORTGAGE EXPENSE AMORTIZATION a) Mortgage expense amortization was determined to be included within the building component of Approved Project Cost (APC) #900209. Reported mortgage expense amortization was disallowed since it is being already reimbursed through the APC building and fixed equipment depreciation. **Regulations: 10 NYCRR Sections 86-2.17(a) & 86-2.17(d)**	Mort. Amort.	005	43,740	17.20%	7,523				
	Mort. Amort.	005	46,703	15.41%		7,197	7,197		

ST. JOHNLAND NURSING CENTER- AUDIT #09-4255
RATE PERIODS JANUARY 1, 2005 THROUGH DECEMBER 31, 2008
PROPERTY EXPENSE DISALLOWANCES/(ALLOWANCES) FOR TBI UNIT

	DESCRIPTION	COST CTR.	DISALLOWED (ALLOWED)	TRACE-BACK %	RATE PERIODS 01/01/05 12/31/05	01/01/06 03/31/06	04/01/06 12/31/06	01/01/07 12/31/07	01/01/08 12/31/08
4. MORTGAGE EXPENSE AMORTIZATION (CONT.)									
b) Providers who receive payments on the basis of reimbursable cost must provide adequate cost data based on financial and statistical records that can be verified on audit. The Facility did not provide adequate documentation to substantiate reported mortgage expense amortization resulting in a disallowance. **Regulations: 10 NYCRR Sections 86-2.17(a) & (d), PRM-1 Sections 2102.3, 2300, & 2304**	Mort. Amort.	005	3,456	14.16%					489
5. WORKING CAPITAL INTEREST EXPENSE DISALLOWANCES									
a) Late fees paid to vendors were included in reported working capital interest expense. According to reimbursement regulations, the prudent and cost conscious buyer not only refuses to pay more than the going price for an item or service, he/she also seeks to economize by minimizing cost. Since the late fees could have been avoided with timely payment, incurring such expense is in conflict with the above concept. In addition, this disllaowance was consistent with methodology used by the Bureau of Long Term Care Reimbursement when establishing the rates. **Regulations: 10 NYCRR Sections 86-2.17(a) & (d), PRM-1 Section 2103**	WC Int.	005	24,894	17.20%	4,282				
	WC Int.	005	26,733	15.41%		4,120	4,120		
	WC Int.	005	31,225	13.65%				4,262	
b) Effective April 1, 2006 and thereafter, rates shall not contain a payment factor for working capital interest if the RHCF report utilized to determine such payment factor also shows a positive net income. The Facility had a positive net income for cost year 2004. Consequently, working capital interest expense was disallowed. **Regulation: Public Health Law, Section 2808, Paragraph 22-a**	WC Int.	005	7,017	15.41%			1,081		
6. MOVABLE EQUIPMENT DEPRECIATION DISALLOWANCES									
a) The Bureau of Long Term Care Reimbursement has determined the nature of telephone expense to be an operating expense. Since the expense is included in the formula to determine the base, mean and ceiling prices used to establish the indirect expense corridor, the reimbursement of telephone depreciation expense in the property component amounts to duplicate reimbursement. Consequently, disallowances were necessary. **Regulation: 10 NYCRR Section 86-2.17(d)**	ME Depr.	002	16,458	10.76%	1,771				
	ME Depr.	002	1,965	100.00%		1,965	1,965		
	ME Depr.	002	11,795	10.31%				1,216	
	ME Depr.	002	12,996	10.37%					1,348
	ME Depr.	002	727	0.00%					
b) 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 properly chargeable to necessary patient care are allowable. Depreciation on vehicles that were used exclusively by Administrators was disallowed since this expense is not directly related to patient care. **Regulations: 10 NYCRR Section 86-2.17(a) & PRM-1 Sections 2102.3 & 2105.9**	ME Depr.	002	514	100.00%		514	514		
	ME Depr.	002	7,375	10.31%				760	
	ME Depr.	002	7,375	10.37%					765

ST. JOHNLAND NURSING CENTER- AUDIT #09-4255
RATE PERIODS JANUARY 1, 2005 THROUGH DECEMBER 31, 2008
PROPERTY EXPENSE DISALLOWANCES/(ALLOWANCES) FOR TBI UNIT

	DESCRIPTION	COST CTR.	DISALLOWED (ALLOWED)	TRACE-BACK %	RATE PERIODS 01/01/05 12/31/05	01/01/06 03/31/06	04/01/06 12/31/06	01/01/07 12/31/07	01/01/08 12/31/08
7. INVESTMENT INCOME RECOVERY The Facility refinanced its mortgage and realized a net gain on the mortgage refinancing of debt. 10 NYCRR Section 86-2.20(c)(1) states that interest expense is to be reduced by investment income. Investment income shall be defined as the aggregate net amount realized from dividends, interest, rental income, interest earned on temporary investment of withholding taxes, as well as all gains and losses. Consequently, the gain on refinancing was offset against interest expense. **Regulation: 10 NYCRR Section 86-2.20(c)** b) Based on information and documentation provided by the facility, this adjustment has been eliminated.	Inc. Offset	003	705,236	10.67%		75,249	75,249		
Total Disallowances/(Allowances)					$ 21,272	$ 116,773	$ 117,854	$ 10,557	$ 3,165
TOTAL AUDITED PROPERTY EXPENSE					$ 244,876	$ 184,574	$ 183,493	$ 231,777	$ 252,935