COST TO RELATED ORGANIZATIONS
HOSPITAL AND SKILLED NURSING FACILITY AUDIT PROGRAM (1999)

COST TO RELATED ORGANIZATIONS

Regulation Reference: 42 CFR 413.17

OBJECTIVES:
1. To determine that the costs applicable to services, facilities and supplies furnished to the provider by the related organization are included in the allowable cost of the provider at the cost of the related organization.
2. To determine that costs and supplies furnished by the provider to a related organization are properly accounted for on the cost report.

OTHER REFERENCES:

PRM-I, §§202.2, 1000, 2150, 2151, 2152 and 2153
PRM-II

Cost Report Forms: Hospital:

HCFA-2552, Worksheet A-8-1
HCFA-2552, Worksheet B-1

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INDICATIONS OF RELATED ORGANIZATIONS

1. Where there are indications through discussion with provider personnel, during the review of the provider cost report questionnaire (Form HCFA-339), permanent file, board minutes, Form HCFA-2552, Worksheet A-8-1, lease agreements, management contracts, SEC Form 10K, Form 990, annual reports of both investor-owned and nonprofit corporations or other sources, that the provider has dealings with related organizations, perform the following audit steps:

   A. Obtain a listing of all affiliates and subsidiaries of the provider and the services provided to and from them.

   B. Obtain details of relationships, amount of expense and classifications of expenses with a related organization. Reconcile the data to Worksheet A-8-1, Part B.

   C. Determine the extent of business conducted with other organizations related by common ownership or control. Where applicable, request the following documentation relative to the related organizations.

      1. Lease agreements;

      2. Management contracts; and

      3. Consultant contracts.

   D. Request the related organization's working trial balance, financial statements or other documentation that adequately supports the cost claimed on the provider's cost report.

   E. Request a copy of the provider's home office cost statement, if available.

   F. The related organization analysis should be cross referenced to Exhibit 7, Step 7, Investment Income.

TEST OF COSTS CLAIMED

2. Examine the amounts claimed as cost to related organizations.

   A. Obtain documentation to support that, where material, the costs are reasonable, necessary, proper and related to patient care.

   B. Evaluate the cost incurred by the related organization as to accuracy and reasonableness.

      1. Review documentation supporting the cost claimed to

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ascertain that it includes, in sufficient detail, the nature of the cost by expense account. Reconcile the amount claimed on the cost report to the supporting documentation.

2. Ascertain that the costs claimed are not budgeted amounts, estimated costs or the fair market value of the services, facilities and supplies furnished.

3. Review the cost to ensure that the cost allowed does not exceed the lower of the allowable cost to the related organization or the price of comparable services, facilities or supplies that could be purchased elsewhere. Document this determination.

4. Where the provider included in allowable costs the fees or charges of the related organization, delete those amounts from the cost report and request the provider to obtain the costs and the basis for computation from the related organization.

5. Where rent paid to a related organization was included, delete the amount and ask the provider to supply the detailed costs of ownership.

C. Ascertain the propriety and reasonableness of the bases used in allocating costs from the related organization, where not audited by a designated fiscal intermediary.

Note: An example of an unacceptable basis would be the allocation of utilities based on the ratio of total hospital expenditures to total university expenditures, data processing cost allocated on square feet and business office expense allocated on an arbitrary ratio.

Identify offsetable revenue items that are directly assigned to specific providers.

D. Propose an audit adjustment, where necessary.

GOVERNMENT ENTITY

3. If the provider is operated by a state or local government and has included costs allocated to it from other components of the government entity, evaluate the costs by determining:

A. The nature and appropriateness of the types of services represented by the costs.

B. The bases used to allocate the costs to the provider and other

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governmental activities.

C. That the amount is actual cost and not a budgeted or estimated amount, which would be disallowed.

Note: Do not allow allocations not normally a facility cost (police, fire, tax assessment, etc.).

HOME OFFICE COSTS/EQUITY

4. Review Worksheet A-8-1 to determine the following:

A. If home office costs were claimed by the provider and/or management fees or charges were assessed to the provider for services rendered, ensure that these home office costs were supported by a cost statement showing the calculation of home office costs allocated to the organizations in the chain, including the provider, in accordance with PRM-I, §§2150 through 2153.

B. Determine that the provider's cost report reflects its proper allocable share of home office equity as identified by pooled and direct equity allocations.

C. If a copy of the applicable home office cost statement schedules has not been furnished, propose an audit adjustment to disallow home office costs until the cost statement has been submitted, in accordance with PRM-I, §2153.

D. If the provider and the home office have different fiscal year ends, disallow any of the home office costs relating to the part of the provider's cost reporting period not yet covered by a home office cost statement that exceed the average rate of the previous year's home office cost statements, as determined by that year's home office cost statement, in accordance with PRM-I, §2150.3.

SHARED-SERVICE ORGANIZATION

5. Determine if the provider is part of a shared-service organization. If so, review the documents of the shared-service organization to ascertain if a related party relationship exists. If a related party relationship exists, the cost of services or supplies from the shared-service organization should be reviewed based upon the related organization principle. Propose an audit adjustment, where necessary.

PROVIDER SERVICES TO RELATED ORGANIZATIONS

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6.	Obtain the provider's working papers supporting costs that are allocated to related organizations, joint service operations whose costs are shared, etc. Review the amounts, compositions and bases of the cost allocations for propriety and reasonableness.		
	A. Compare current and prior period costs. Significant cost variances between the two periods should be explained.		
	B. Review the bases for allocating costs to the related party for accuracy and reasonableness.		