

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**BCFS HEALTH AND HUMAN
SERVICES DID NOT ALWAYS
COMPLY WITH FEDERAL
REQUIREMENTS RELATED TO
LESS-THAN-ARM'S-LENGTH LEASES**

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Office of Inspector General

<https://oig.hhs.gov>

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OFFICE OF AUDIT SERVICES FINDINGS AND OPINIONS

The designation of financial or management practices as questionable, a recommendation for the disallowance of costs incurred or claimed, and any other conclusions and recommendations in this report represent the findings and opinions of OAS. Authorized officials of the HHS operating divisions will make final determination on these matters.



Why OIG Did This Review

The Department of Health and Human Services (HHS), Office of Refugee Resettlement (ORR), manages the Unaccompanied Alien Children (UAC) program. The UAC program served between 7,000 and 8,000 children annually from fiscal year (FY) 2005 through FY 2011. In FY 2012, however, the number of children entering the program began to increase, and in FY 2015, ORR served more than 33,000 children. As the number of children increased, so did the funding for the program. Because of the rapid increase of vulnerable children entering ORR care, and the significant increases in program funding, we are conducting a series of reviews of ORR care providers across the Nation.

The objective of this review was to determine whether BCFS Health and Human Services (BCFS HHS) claimed only allowable expenditures in accordance with applicable laws, regulations, and departmental guidance.

How OIG Did This Review

To verify that BCFS HHS claimed only allowable expenditures, we (1) reviewed a statistical sample of financial transactions and (2) reviewed BCFS HHS accounting policies, procedures, and organizational structure for the period October 1, 2014, through September 30, 2015.

BCFS Health and Human Services Did Not Always Comply With Federal Requirements Related to Less-Than-Arm's-Length Leases

What OIG Found

While BCFS HHS generally claimed only allowable expenditures, it did not comply with Federal regulations related to less-than-arm's-length leases. Of the 140 randomly selected transactions we reviewed, we determined that 138 were allowable, but 2 rental cost transactions for 1 less-than-arm's-length lease were unallowable. We also identified additional rental costs on two less-than-arm's-length leases that exceeded the amount allowable for such leases. These unallowable rental costs on three less-than-arm's-length leases totaled \$658,248. According to BCFS HHS officials, they were unaware of the limitations on rental costs related to less-than-arm's-length lease agreements.

What OIG Recommends

We recommend that BCFS HHS refund \$658,248 to ORR for unallowable rental costs incurred under the less-than-arm's-length lease agreements and limit future rental costs to the amount that would be allowed under 45 CFR part 75.465(c).

In written comments on our draft report, BCFS HHS did not concur with our recommendation. BCFS HHS stated that it did not concur because (1) we failed to apply the correct Federal regulations, (2) we did not understand the intent of the cooperative agreement's purpose, (3) we based our analysis on a narrow reading of Federal regulations, (4) we did not consider prior agreements and approvals of rental costs, (5) we incorrectly calculated depreciation, and (6) our finding threatens the purpose of the UAC program as it relates to the cooperative agreement.

After reviewing BCFS HHS's comments, we maintain that our recommendation is valid. We applied the correct Federal regulation regarding less-than-arm's-length leases. We did not take issue with the need for facilities or the allowability of the rental costs per se. We took issue with how the rental costs were calculated, and we calculated the allowable rental costs to comply with Federal regulations, which the cooperative agreement clearly states are to be followed. From the documentation submitted by BCFS HHS, we cannot determine which, if any, of the costs on the asset listing should be factored into the computation of depreciation for the relevant building costs. We thus decline to make any changes to our calculation and defer to ACF to determine any necessary adjustments.

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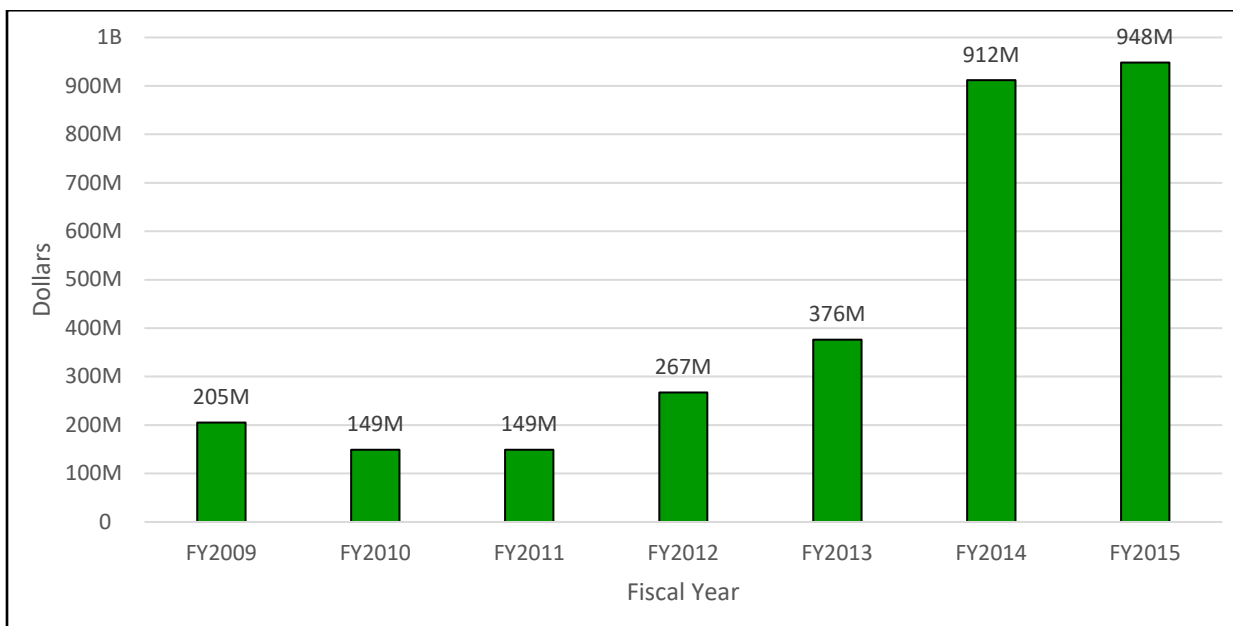
INTRODUCTION

WHY WE DID THIS REVIEW

The Department of Health and Human Services (HHS), Office of Refugee Resettlement (ORR), manages the Unaccompanied Alien Children (UAC) program. The UAC program served between 7,000 and 8,000 children annually from fiscal year (FY) 2005 through FY 2011. In FY 2012, however, the number of children entering the program began to increase, and by the end of FY 2012, the UAC program served approximately 13,625 children. In FY 2013, the program served 24,668 children; in FY 2014, the program served 57,496 children; and in FY 2015, ORR served 33,726 children.

As the number of children increased, so did the funding for the program. From FY 2009 through FY 2014, ORR's funding for its UAC program totaled more than \$2 billion, with about \$912 million (45 percent) of the funding occurring during FY 2014 alone (Figure 1). During FY 2015, funding levels increased to \$948 million.

Figure 1: UAC Program Funding FY 2009–FY 2015



Because of the rapid increase of vulnerable children entering ORR care, the significant increases in program funding, and the changes ORR made to its policies related to the UAC program during FY 2014, we are conducting a series of reviews of ORR care providers across the Nation. We selected BCFS Health and Human Services (BCFS HHS), a nonprofit shelter and foster care provider in San Antonio, Texas, for review because it received the most funding from ORR for the UAC program during FY 2015.

OBJECTIVE

The objective of this review was to determine whether BCFS HHS claimed only allowable expenditures in accordance with applicable laws, regulations, and departmental guidance.

BACKGROUND

The UAC program funds temporary shelter care,¹ transitional² and long-term³ foster care, and other related services for unaccompanied alien children in ORR custody. For project periods⁴ with services beginning in FYs 2014 and 2015, ORR awarded grants totaling \$2.1 billion to providers for the care and placement of children. The UAC program is separate from the State-administered child welfare and traditional foster care systems.

Application of Federal Regulations

For grant awards made prior to December 26, 2014, 45 CFR part 74 establishes uniform administrative requirements governing HHS grants and agreements awarded to nonprofit entities. The allowability of costs incurred by nonprofit organizations is determined in accordance with the provisions of 2 CFR part 230 (formerly OMB Circular A-122) (made applicable by 45 CFR § 74.27(a)). For grant awards made on or after December 26, 2014, 45 CFR part 75 establishes uniform administrative requirements, cost principles, and audit requirements for Federal awards to non-Federal entities. Our audit period encompasses three awards for incremental funding for cooperative agreement 90ZU0102-02: one made on December 23, 2014, to which 45 CFR part 74 applies; and two made on March 27 and August 6, 2015, to which 45 CFR part 75 applies. For the purposes of this report, there were only minor, non-substantive differences in the language between the relevant provisions of the rules that applied to a finding; thus, for simplicity's sake, we cite to the provisions of

¹ Shelter care is a residential care provider facility in which all of the programmatic components (such as the shelter, food, education, and medical services provided as part of the UAC program) are administered onsite in the least restrictive environment. When making placement determinations, ORR's goal is to provide the least restrictive setting that is in the best interests of the child, taking into consideration certain factors such as potential flight risk and danger to the child and others.

² Transitional foster care is an ORR-funded placement option for UAC under 13 years of age, sibling groups with one sibling under 13 years of age, pregnant or parenting teens, or UAC with special needs. UAC are placed with foster families in the ORR network of care, attend school, and receive services from the ORR care provider.

³ Long-term foster care is ORR-funded community based foster care placements and services to which eligible UAC are transferred after a determination is made that the child will be in ORR custody for an extended period. UAC in ORR long-term foster care typically reside in licensed foster homes, attend public school, and receive community-based services.

⁴ A project period for the UAC program is a 36-month project with three 12-month budget periods.

45 CFR part 74 as it applied during the beginning of our audit period. We have included the relevant cites to 45 CFR part 75 in footnotes.

BCFS Health and Human Services

BCFS HHS is a nonprofit shelter and foster care provider in San Antonio, Texas. In FY 2015, BCFS HHS spent approximately \$250 million in Federal funds for the care and placement of approximately 4,340 UAC. BCFS HHS is affiliated with BCFS, a global network of nonprofit organizations operating health and human services programs throughout the United States, Eastern Europe, Latin America, Southeast Asia, and Africa.

HOW WE CONDUCTED THIS REVIEW

To verify that BCFS HHS claimed only allowable expenditures, we reviewed (1) a statistical sample of financial transactions and (2) BCFS HHS accounting policies, procedures, and organizational structure.

Our review covered \$71 million in general ledger financial transactions from October 1, 2014, through September 30, 2015 (audit period). We selected a stratified random sample of 140 financial transactions totaling \$6,681,894 for review. We also reviewed the lease agreements for all facilities.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix A contains the details of our audit scope and methodology; Appendix B contains the details of our sampling methodology and estimate.

FINDINGS

While BCFS HHS generally claimed only allowable expenditures, it did not comply with Federal regulations related to less-than-arm's-length leases.⁵ Of the 140 randomly selected transactions we reviewed, we determined that 138 were allowable, but 2 rental cost transactions for 1 less-than-arm's-length lease were unallowable. We also identified additional rental costs on two less-than-arm's-length leases that exceeded the amount allowable for such leases. These unallowable rental costs on three less-than-arm's-length leases totaled \$658,248.

⁵ As defined in 2 CFR part 230, App. B, section 43.c, "a less-than-arms-length lease is one under which one party to the lease agreement is able to control or substantially influence the actions of the other." See also 45 CFR section 75.465(c).

According to BCFS HHS officials, they were unaware of the limitations on rental costs related to less-than-arm's-length lease agreements.

BCFS HHS Claimed Unallowable Rental Costs Related to Less-Than-Arm's-Length Leases With Three Facilities

Rental costs under "less-than-arms-length" leases are allowable only up to the amount (as explained in subparagraph 43.b regarding rental costs under "sale and lease back" arrangements) that would be allowed had the title to the property vested in the nonprofit organization (2 CFR part 230, App. B, § 43.c).⁶

Rental costs under "sale and lease back" arrangements are allowable only up to the amount that would be allowed had the nonprofit organization continued to own the property. This amount would include expenses such as depreciation or use allowance, maintenance, taxes, and insurance (2 CFR part 230, App. B, § 43.b).⁷ The computation of use allowances or depreciation must be based on the acquisition cost of the assets involved and must exclude the cost of land (2 CFR part 230, App. B, §§ 11.b and 11.c(1)).⁸ When the depreciation method is used, no depreciation is allowed on an asset that would be viewed as fully depreciated (2 CFR part 230, App. B, § 11.f).⁹

We identified less-than-arm's-length leases for three facilities (Baytown, Raymondville, and San Antonio) and determined that BCFS HHS charged \$658,248 in unallowable rental costs related to these leases. BCFS HHS leases these facilities from BCFS. Based upon the totality of their relationship, BCFS has the ability to control or substantially influence the actions of BCFS HHS. Therefore, the leases between BCFS and BCFS HHS are less-than-arm's-length leases subject to the limits on rental costs specified in 2 CFR part 230, App. B, section 43.c.

For the Baytown and Raymondville facilities, we reviewed documentation that BCFS HHS provided to support the acquisition costs of the buildings and were able to determine the allowable rental costs on the basis of the criteria. For these two facilities, we are questioning the difference between the amount claimed by BCFS HHS and the allowable amount using the aforementioned criteria. For the San Antonio facility, BCFS HHS officials stated that the buildings were fully depreciated, and the officials were not able to provide supporting documentation for their acquisition costs. For this facility, we are questioning the entire amount of rental costs claimed by BCFS HHS.

⁶ 45 CFR section 75.465(c).

⁷ 45 CFR section 75.465(b).

⁸ 45 CFR section 75.436(c).

⁹ 45 CFR section 75.436(d)(4).

Table 1: Difference Between BCFS HHS Claims and Allowable Amount

Facility	Claimed Amount	Allowable Amount¹⁰	Finding (Difference)
Baytown	\$228,000	\$34,978	\$193,022
Raymondville	78,000	20,663	57,337
San Antonio	407,889	0	407,889
Total	\$713,889	\$55,641	\$658,248

RECOMMENDATION

We recommend that BCFS HHS refund \$658,248 to ORR for unallowable rental costs incurred under the less-than-arm’s-length lease agreements and limit future rental costs under less-than-arm’s-length lease agreements to the amount that would be allowed under 45 CFR part 75.465(c).

**BCFS HHS COMMENTS AND
OFFICE OF INSPECTOR GENERAL RESPONSE**

BCFS HHS COMMENTS

In its written comments on our draft report, BCFS HHS did not concur with our recommendation. BCFS HHS stated that it did not concur because (1) we failed to apply the correct Federal regulations, (2) we did not understand the intent of the cooperative agreement’s purpose, (3) we based our analysis on a narrow reading of Federal regulations, (4) we did not consider prior agreements and approvals of rental costs, (5) we incorrectly calculated depreciation, and (6) our finding threatens the purpose of the UAC program as it relates to the cooperative agreement.

BCFS HHS’s comments are included in their entirety as Appendix C. We excluded 32 pages of attachments because they contained proprietary information.

OFFICE OF INSPECTOR GENERAL RESPONSE

After reviewing BCFS HHS’s comments, we maintain that our recommendation is valid. We *applied* the correct version of the Federal regulation regarding less-than-arm’s-length leases based upon the award date. However, for the sake of simplicity, we chose to *cite* to 45 CFR part 74 and the incorporated cost principles at 2 CFR part 230 in the body of the report and to *cite* to 45 CFR part 75 in footnotes. We revised the report to clarify this point. Prior to calculating the allowable rental costs, we compared the cost principles at 2 CFR part 230 (as incorporated by 45 CFR part 74) and the cost principles laid out in 45 CFR part 75 as they

¹⁰ The allowable rental cost was calculated on the basis of depreciation of the acquisition cost of the facility, excluding the cost of land.

pertain to less-than-arm's-length leases. We found minor language differences between the two provisions, which we determined were not substantive in nature.¹¹ We note that 45 CFR part 74 allowed less-than-arm's-length rental costs to include either use allowance or depreciation but did not allow a combination of the two methods to be used in connection with a single class of fixed assets; whereas, 45 CFR part 75 only allowed for a calculation of depreciation and provided guidance for situations where depreciation was being introduced to replace the use allowance method. Specifically, 45 CFR 75.436(d)(5) requires that where "the depreciation method is introduced to replace the use allowance method, depreciation must be computed as if the asset had been depreciated over its entire life" In addition, the "total amount of use allowance and depreciation for an asset (including imputed depreciation applicable to periods prior to the conversion from the use allowance method as well as depreciation after the conversion) may not exceed the total acquisition cost of the asset."

BCFS HHS could have selected the use allowance method for all three less-than-arm's-length leases only for the one award that was subject to 45 CFR part 74. For the other two awards that were subject to 45 CFR part 75, BCFS HHS was required to use the depreciation method for all three leases and to ensure that the total amount of use allowance and depreciation for each building did not exceed its total acquisition cost. Because depreciation was permitted for all three awards and because depreciation resulted in a higher allowable amount for the Baytown and Raymondville facilities than would have been permitted under the use allowance method, we used the depreciation method when calculating the allowable rental costs.

We understand the intent of the cooperative agreement is to provide residential services, and we do not take issue with the need for facilities or the allowability of the rental costs per se. We also did not conclude that the rental costs were unallowable because they were for less-than-arm's-length leases. Instead, we took issue with how the rental costs were calculated, and we calculated the allowable rental costs to comply with Federal regulations, which the cooperative agreement clearly states are to be followed.

We also understand the responsibilities of ORR and its approval of BCFS HHS's budget. However, budgets do not always contain sufficient detail to show how costs are actually calculated. Additionally, the terms and conditions of the Notices of Award incorporate the relevant grants administration regulation and HHS Grants Policy Statement (GPS), with which

¹¹ For example, 45 CFR 75.465(c) states that "[r]ental costs under 'less-than-arm's-length' leases are allowable only up to the amount (as explained in paragraph (b) of this section.)" Paragraph (b) (45 CFR 75.465(b)) states that "[r]ental costs under 'sale and lease back' arrangements are allowable only up to the amount that would be allowed had the non-Federal entity continued to own the property." 2 CFR 230, App. B, 43.c states that "[r]ental costs under 'less-than-arms-length' leases are allowable only up to the amount (as explained in subparagraph 43.b. of this appendix) that would be allowed had title to the property vested in the non-profit organization." Subparagraph 43.b states that "[r]ental costs under 'sale and lease back' arrangements are allowable only up to the amount that would be allowed had the non-profit organization continued to own the property." We also note that 45 CFR 75.436(d)(4) states that "[n]o depreciation may be allowed on any assets that have outlived their depreciable lives," while 2 CFR 230, App. B., 11.f, states that "no depreciation may be allowed on any such assets that, under subparagraph 11.d of this appendix, would be viewed as fully depreciated."

the grantee must comply. The GPS provides that “[a]ny waivers of or deviations from these terms and conditions must be requested and approved in writing by the GMO [i.e., the grants management officer].” However, BCFS HHS did not provide written documentation showing that the GMO approved a deviation from the Federal regulations requirements applicable to less-than-arm’s-length leases.

BCFS HHS stated that our depreciation calculations were incorrect but provided no argument in support of its position. Instead, BCFS HHS provided asset listings and associated depreciation costs for BCFS. The assets listed include a broad range of items, such as signage, landscaping, roof repairs, statue and statue delivery, and street lighting, dating as far back as 1994. BCFS HHS provides no explanation of how it calculated depreciation based on these listings, instead simply providing an amount that it claims is accurate.

To summarize our finding, we determined that BCFS HHS claimed unallowable rental costs. BCFS HHS and BCFS were in a less-than-arm’s-length lease arrangement. Rental costs in less-than-arm’s-length leases are allowed up to the amount that would be allowed if the tenant owned the building. This includes expenses such as depreciation or use allowance, maintenance, taxes, and insurance (2 CFR part 230, App. B, § 43.c).¹²

The computation of depreciation is based on the acquisition cost of the asset involved and excludes the cost of land. No depreciation is allowed for any asset that is fully depreciated. Additionally, any portion of the cost of buildings and equipment borne by or donated by the Federal Government shall be excluded from a depreciation calculation (2 CFR part 230, App. B, §§ 11.b, c, and f).¹³

From the documentation of depreciation provided by BCFS HHS, we are unable to determine the nature of the expense and whether or not it should be included in the depreciation calculation. Moreover, some of the items listed are fully depreciated (have a book value of zero) and thus would not be part of a depreciation calculation for a building. We also note at least one listing for land, which is specifically excluded from the calculation of depreciation. Lastly, we cannot tell from the documentation whether any of the costs associated with the asset listings were borne by or donated by the Federal Government.

In addition, we acknowledge that some of the costs on the asset listing may include capital expenditures, including equipment, for which the grantee may calculate depreciation (2 CFR part 230, App. B, § 15.b(5)).¹⁴ We are unable to determine from the documentation which, if any, costs qualify as allowable capital expenditures. Moreover, we would need to ensure that the depreciation of any capital expenditure had not been calculated and claimed separately and thus should not be calculated into building depreciation.

¹² 45 CFR section 75.465(b)

¹³ 45 CFR section 75.436(c) and (d)(4)

¹⁴ 45 CFR section 75.439(b)

In summary, based on the documentation submitted by BCFS HHS, we cannot determine which, if any, of the costs on the asset listing should be factored into the computation of depreciation for the relevant building costs. We thus decline to make any changes to our calculation and defer to ACF to determine any necessary adjustments.

APPENDIX A: AUDIT SCOPE AND METHODOLOGY

SCOPE

We reviewed BCFS HHS's documentation related to grant expenditures claimed for reimbursement and BCFS HHS accounting policies, procedures, and organizational structure to ensure BCFS HHS met applicable Federal and State grant requirements in administering its UAC grant. Our audit covered \$71 million in general ledger financial transactions from October 1, 2014, through September 30, 2015 (audit period). We selected a stratified random sample of 140 financial transactions totaling \$6,681,894 for review.

We performed our fieldwork at BCFS HHS in San Antonio, Texas, from June 2016 through March 2017.

Our objective did not require an understanding of all of BCFS HHS's internal controls. We limited our assessment to BCFS HHS controls related to its financial management system.

METHODOLOGY

To accomplish our objective, we:

- reviewed applicable Federal laws, regulations, and guidance;
- reviewed grant documents and policies and procedures maintained at BCFS HHS;
- interviewed BCFS HHS and BCFS officials;
- reconciled the Federal Financial Reports (FFRs) with BCFS HHS general ledgers;
- reconciled the drawdown amounts with the FFRs;
- selected a stratified random sample of financial transactions that BCFS HHS charged to the grant during FY 2015 (Appendix B);
- reviewed supporting documentation for each sampled transaction (including payments to subcontractors, if applicable);
- reviewed lease agreements for all facilities;
- reviewed BCFS HHS's Federal grant reports—financial and programmatic—for the audit period; and
- discussed our findings with BCFS HHS officials.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

APPENDIX B: STATISTICAL SAMPLING METHODOLOGIES

TARGET POPULATION

The population consisted of all expenditure transactions on BCFS HHS's general ledgers for its residential and foster care¹⁵ grants during FY 2015.

SAMPLING FRAME

We received an Excel file from BCFS HHS for each of its facilities. There were 97,923 transactions totaling \$249,574,824 that BCFS HHS had recorded as expenditures during FY 2015 for both its residential and foster care grants. We manually matched expenditure transactions in the general ledger by verifying accounting system identifiers to remove all transactions that netted to zero. We also removed all prior-period transactions, transactions not charged to the grant, and transactions valued between (\$100) and \$100 (both debits and credits). As a result, our sample frame contained 15,591 transactions totaling \$71,499,380.

SAMPLE UNIT

The sample unit was a general ledger expenditure transaction.

SAMPLE DESIGN

We used a stratified random sample. The sampling frame was divided into five strata. Strata 1 through 4 are based on monetary thresholds, and stratum 5 consists of salary and wage transactions.

Table 2: Sample Strata

Stratum #	Frame Count	Frame Total	Strata Values From	Strata Values To
1	12,924	\$5,458,312.30	(\$15,850.56)	\$1,839.43
2	1,893	7,838,879.69	1,840.12	11,451.56
3	391	9,045,152.27	11,537.98	55,560.98
4	107	10,465,310.78	56,103.86	223,923.51
5	276	38,691,725.06	120.00	510,065.66
Totals	15,591	\$71,499,380.10		

¹⁵ ORR provides temporary shelter care and other related services to UAC in its custody through residential and foster care grants.

SAMPLE SIZE

We selected 140 transactions.

SOURCE OF RANDOM NUMBERS

We used the Office of Inspector General, Office of Audit Services, statistical software to generate the random numbers.

METHOD OF SELECTING SAMPLE ITEMS

We consecutively numbered the transactions in the sample frame. After generating the random numbers, we selected the corresponding frame items.

ESTIMATION METHODOLOGY

We identified two unallowable lease transactions during our review of the statistical sample items. However, we did not estimate the total amount of expenditures that were unallowable.

APPENDIX C: BCFS HHS COMMENTS



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November 13, 2017

Report Number: A-06-16-07007

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Regional Inspector General for Audit Services
Office of Audit Services, Region VI
1100 Commerce Street, Room 632
Dallas, TX 75242

Re: BCFS Health and Human Services (BCFS HHS) Response to Office of Inspector General's Draft Report of October 10, 2017 from Patricia Wheeler, Regional Inspector General for Audit Services

Dear Ms. Wheeler,

As stated in your original OIG draft of October 10, 2017, a response from BCFS Health and Human Services (BCFS HHS) was originally due on November 10, 2017, which is Veterans Day, a Federal holiday, via email to Ms. Thompson which allowed BCFS HHS to submit their response the next business day on Monday, November 13, 2017.

This is BCFS HHS' official response to the Department of Health and Human Services Officer of Inspector General's Draft report titled "BCFS Health and Human Services did not always comply with Federal requirements related to less-than-arm's-length leases" submitted to BCFS HHS on October 10, 2017 by Ms. Patricia Wheeler, Regional Inspector General for Audit Services.

With all due respect to the OIG office efforts, BCFS HHS, does **not concur** with any of the OIG's findings, BCFS HHS is not required to refund the \$658,248 for unallowable rental costs incurred for the following reasons:

1. OIG failed to apply the correct Federal regulations to the OIG's analysis.
2. The failure of the OIG to understand the intent of the cooperative agreement's purpose and the meeting of the minds between The Department of Health and Human Services - Administration for Children Families, Office of Refugee Resettlement (ORR) and BCFS HHS as is stated in the terms and conditions of the cooperative agreement.
3. OIG's overall analysis is based on a narrow reading of cited Federal regulations, but OIG is required to apply the regulations by reading all the documents as a whole.

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4. OIG did not consider the prior agreements and approvals regarding rental costs that have been negotiated yearly between DHHS and BCFS HHS since 2013.
5. OIG's calculations of depreciation are not correct.
6. OIG's findings, if not reconsidered and overturned, threaten the purpose of the unaccompanied alien children program as it relates to cooperative agreement 90ZU0102-02.

BCFS HHS requests that the OIG reconsider their analysis regarding the audit of BCFS HHS' rental costs for the reasons that this response will discuss in detail below.

Throughout BCFS' below discussions in this response BCFS considers some of the factual information discussed is proprietary to BCFS HHS. BCFS HHS requests that OIG give BCFS HHS an opportunity to exclude their proprietary information prior to OIG's public release of this report.

Facilities Brief History

BCFS, parent entity of BCFS HHS, owns the properties known as the San Antonio Campus, Baytown and Raymondville facilities.

The San Antonio shelter property was purchased in 1944. The purchase included an old farmhouse and other farm structures not used as a part of the residential program. BCFS (Not BCFS HHS) made structural building renovations and improvements to the property that have not been fully depreciated. BCFS HHS and BCFS entered into a lease for the property on September 15, 2013 for the purpose of providing residential services and other programs to unaccompanied children at the monthly rate of \$33,990.75, \$407,889 annually. The leased property includes 105.205 acres and all structures which include 11 buildings.

A comparable facility would be [REDACTED], San Antonio, Texas [REDACTED], with an annual rent at \$226,800 and 20,386 rentable square feet.

The Baytown facility was purchased on June 20, 2014, for the land, buildings and facilities. BCFS and BCFS HHS entered into a lease for Baytown on June 1, 2014, for the 18.49 acres and nine buildings of approximately 57,399 rentable square feet and includes all fixtures and furniture on the premises for the rent of \$19,000 per month, \$228,000 annually.

A comparable facility would be [REDACTED], Harlingen TX [REDACTED], with an annual rent of \$1,248,000 and 109,133 rentable square feet.

The Raymondville facility was purchased on April 2, 2013, which included the land and five buildings. BCFS and BCFS HHS entered into a lease for this property on June 1, 2013, for the building and improvements. The rent on this property is \$6,500 per month, \$78,000 annually.

A comparable facility would be [REDACTED], Harlingen TX [REDACTED], with an annual rent of \$1,248,000 and 109,133 rentable square feet.

All related party lease rates are set at below market rates comparable to the surrounding area. All rental lease amounts are described in the budget narrative which is reviewed and approved by the Project Officer, Division of Unaccompanied Children's Operations, Office of Refugee Resettlement. Copies of all lease schedules have been reviewed in detail by the Project Officer before a project funding is approved.

The following is a review of comparable independent third party leases with BCFS HHS that are not related parties. [REDACTED] is 2.9 acres and approximately 20,386 square feet of rentable space which is leased at \$18,900 per month or \$226,800 annually and increased to \$19,845 per month in 2017, \$20,837.00 per month in 2018 and \$21,878 per month in 2019.

The [REDACTED] lease is also with an independent third party for the lease of land, area and includes approximately 19 buildings and approximately 109,133 square feet of rentable space. The lease is from October 2016 through September of 2019 at a monthly rent of \$104,000 per month, \$1,248,000 annually.

OIG failed to apply the correct Federal regulations to the OIG's analysis.

OIG audit report stated the following:

"Our audit period encompasses three awards for incremental funding for cooperative agreement 90ZU0102-02: one made on December 23, 2014 to which 45 CFR part 74 applies; and two made on March 27, 2015 and August 6, 2015, to which 45 CFR part 75 applies. For the purposes of this report, there were only minor, non-substantive differences between the provisions of the rules that applied to a finding; thus, for simplicity's sake, we applied the provisions of 45 CFR part 74, as it applied during the beginning of our audit period. We have included the relevant cites to 45 CFR part 75 in footnotes."

In accordance with the Federal regulations the OIG should have applied 45 CFR part 74 to funding issued on December 23, 2014 analysis and 45 CFR part 75 to the March 27, 2015 and August 6, 2015 funding as stated on the bottom of the funding instrument(s) which state the following:

STANDARD TERMS

1. Paid by DHHS Payment Management System (PMS), see attached for payment information. This award is subject to the requirements of the HHS Grants Policy Statement (HHS GPS) that are applicable to you based on your receipt type and the purpose of this award. This includes requirements in Parts I and II (available at <http://www.hhs.gov/grants/grants/policies-regulations/index.html> of the HHS GPS. Although consistent with the HHS GPS, any applicable statutory or regulatory requirements,

including 45 CFR Part 75, directly apply to this award apart from any coverage in the HHS GPS.

This grant is subject to the requirements as set forth in 45 CFR Part 75.

DGCM-

The wording of 45 CFR part 74 and 45 CFR 75 are different as read in accordance with the Department of Health and Human Services Grants Policy Statement (DHHS GPS), the OIG must redo their analysis based on the correct regulations as they relate to each funding period.

It is BCFS HHS' position that based on the reading of both 45 CFR part 74 and the additional and different wording 45 CFR part 75, BCFS HHS is not required to refund the \$658,248 to ORR for unallowable rental costs incurred, because rental costs are allowable in an accordance with the Federal regulations and the terms of the cooperative agreement between BCFS HHS and the Department of Health and Human Services (DHHS).

OIG Analysis Failed to Review the Intent and Terms of the Cooperative Agreement.

OIG's analysis did not review the intent or terms of the Cooperative agreement, a material element of the agreement is for "residential services" for unaccompanied alien children which cannot be completed without the Baytown, Raymondville and San Antonio Campus, facilities. The lease rental prices are reviewed by the government's project officer for each budget period and are approved and finalized by DHHS.

The DHHS GPS, which is incorporated by reference to the cooperative agreement, allows for the costs of "Services Provided by Affiliated Organizations" which BCFS is an affiliated organization to BCFS HHS. BCFS' lease agreement allows BCFS HHS to incur reduced rental costs at below market rate to BCFS HHS which passes on the lower costs to the DHHS.

The material part of the cooperative agreement is to provide facilities. The facilities are a basic assumption of the cooperative agreement, the cooperative agreement states the following;

Section I

"The program's main purpose is to provide a safe and appropriate environment for UAC during the interim period between the child's transfer into a UAC program and the child's release from custody by ORR or removal from the United States by the Department of Homeland Security (DHS)."

In addition, the cooperative agreement goes on to state:

"Pursuant to Section 462 of the Homeland Security Act of 2002, the Director of the ORR, hereinafter called the Director, approved awards for residential services to Unaccompanied Children. In accordance with this announcement

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and pursuant to the aforementioned laws, BCFS Health and Human Services hereinafter called BCFS has been approved for funding to provide residential services for unaccompanied alien children, which meets the requirements in the previous paragraph”

“This Cooperative Agreement and the attached Terms and Conditions establish the concepts and responsibilities for implementing BCFS’s residential services for UAC. Continued funding is contingent upon satisfactory performance, availability of funds, and determination that continuation is in the best interests of the United States Government”

All of the above sections of the cooperative agreement refer to “residential services”. BCFS Health and Human Services provides sheltering operations for which Baytown provides █ beds, San Antonio provides █ beds, and Raymondville provides █ beds along with other shelter services. All of these direct costs are approved by the project officer prior to a budget being approved. The OIG draft report is written as if the “rental costs” are costs that have not been addressed by the project officer (Department of Health and Human Services).

The terms of the contract allow BCFS HHS, to be paid for their services, the DHHS GPS states,

Services Provided by Affiliated Organizations

A number of universities and other organizations have established closely affiliated, but separately incorporated, organizations to facilitate the administration of research and other programs supported by Federal funds. Such legally independent entities are often referred to as “foundations,” although this term does not necessarily appear in the name of the organization. Typically, the parent organization provides considerable support services, in the form of administration, facilities, equipment, accounting, and other services, to its foundation, and the latter, acting in its own right as a recipient, includes the cost of these services in its indirect cost proposal.

Costs incurred by an affiliated, but separate, legal entity in support of a recipient foundation (foundation) are allowable for reimbursement under HHS grants only if at least one of the following conditions is met:

- *The foundation is charged for, and is legally obligated to pay for, the services provided by the parent organization.*
- *The affiliated organization is subject to State or local law that prescribes how Federal reimbursement for the costs of the parent organization’s services will be expended and requires that a State or local official*

acting in his or her official capacity approves such expenditures.

- *There is a valid written agreement between the affiliated organizations whereby the parent organization agrees that the foundation may retain Federal reimbursement of parent organization costs. The parent organization may either direct how the funds will be used or permit the foundation that discretion.*

If none of the above conditions is met, the costs of the services provided by the parent organization to the foundation are not allowable for reimbursement under an HHS grant. However, the services may be acceptable for cost-sharing (matching) purposes.

Under this term, BCFS is considered the “foundation” thus costs incurred by an affiliated, but separate, legal entity in support of a recipient foundation (foundation) are allowable for reimbursement under DHHS grants. The rental costs for the services of the lease between BCFS and BCFS HHS are allowable based on BCFS providing these services to the affiliated organization BCFS HHS.

BCFS’ “Article II Purpose” states, “The Corporation is organized and shall be operated exclusively for charitable, religious and educational purposes within the meaning of Section 501(c)(3) of the Internal Revenue Code. Within the scope of the foregoing purposes, and not by way of limitation thereof, the Corporation shall provide general administrative support and services to organizations which are exempt from federal income taxation and described in Internal Revenue Code Section 501(c)(3) and/or governmental entities described in Internal Revenue Code Section 0170(c)(1) and instrumentalities thereof (hereafter “exempt entities”), including, but not limited to, its controlled entities, BCFS Property Management Company, Baptist Care Facilities for Persons with Mental Disabilities, Inc. d/b/a Breckenridge Village of Tyler, Children’s Emergency Relief International, Baptist Child & Family Services Foundation, and BCFS Health and Human Services.

The lease agreement allows BCFS HHS to charge less for their services to the Federal Government. The Department of Health and Human Services had complete knowledge of the leases and they approved them in each budget. If BCFS was not providing these leases at below market value prices both BCFS HHS and thus the government would be paying much more for these facilities. The reduced costs can be seen when you compare the rental costs of the [REDACTED] facility which is \$1,248,000 per year which is two hundred percent (200%) higher than the San Antonio facility which has less rentable square feet.

The intent of the agreement and the terms of cooperative agreement supports BCFS HHS position that the rental costs as presented in the budgets and

charged are allowable costs that do not violate Federal regulations and comply with the terms and conditions of the cooperative agreement.

OIG's Analysis is based on a Narrow Reading of Cited Federal Regulations

OIG's analysis is based on a narrow reading of cited Federal regulations that does apply to BCFS HHS when reading the regulations together with the intent of the cooperative agreement and its terms and conditions. In reading the analysis of the OIG in their report, OIG failed to fully read and apply the terms and conditions of the cooperative agreement. The OIG draft report stated that they reviewed the following:

“To accomplish our objective, we:

- reviewed applicable Federal laws, regulations, and guidance;*
- reviewed grant documents and policies and procedures maintained at BCFS HHS;*
- interviewed BCFS HHS and BCFS officials;*
- reconciled the Federal Financial Reports (FFRs) with BCFS HHS general ledgers;*
- reconciled the drawdown amounts with the FFRs;*
- selected a stratified random sample of financial transactions that BCFS HHS charged to the grant during FY 2015 (Appendix B);*
- reviewed supporting documentation for each sampled transaction (including payments to subcontractors, if applicable);*
- reviewed lease agreements for all facilities;*
- reviewed BCFS HHS's Federal grant reports-financial and programmatic-for the audit period; and*
- discussed our findings with BCFS HHS officials.*

OIG states that they “reviewed applicable Federal laws, regulations, and guidance” and “reviewed grant documents and policies and procedures maintained at BCFS HHS” along with the other items listed above. The OIG's entire analysis is based on simply the control issue regarding what is an “arms-length-transaction” and that BCFS has “control” over BCFS HHS.

If OIG did their analysis based on the intent of the cooperative agreement, the approved budgets, the regulations and cooperative agreements terms, the OIG's analysis must conclude that the rental costs are allowable.

The following regulations and the terms and conditions must be considered in the OIG's analysis. The cooperative agreement term "Services Provided by Affiliated Organizations" allows the cost of the affiliated organization's costs to be allowable.

Other federal Regulations that must be considered in making this analysis of cost allowability of the rental costs, such as 45 CFR Part 75.308 states "(a) *The approved budget for the Federal award summarizes the financial aspects of the project or program as approved during the Federal award process.*" Part 75.420 "*In case of a discrepancy between the provisions of a specific Federal award and the provisions below, the Federal award governs.*" The Federal award is the award of this cooperative agreement number 90ZU0102-02.

OIG analysis is too narrow. It simply focused on arms-length transactions and the issue of control then concludes that the rental costs are not allowable. Reading the cooperative agreement as a whole along with the regulations and the intent of both parties established that the rental costs are allowable and have been preapproved by the Department of Health and Human Services.

Department of Health and Human Services had complete knowledge of the leases and rental costs and had pre-approved these costs.

The project budgets have been submitted and approved by the Department of Health and Human Services. The project budgets have been negotiated yearly between DHHS and BCFS HHS since 2013. Federal regulation 45 CFR Section 75.308 states (a) *the approved budget for the Federal award summarizes the financial aspects of the project or program as approved during the Federal award process.*

The following sections from the cooperative agreement was signed on September 30, 2013, stating the requirements for the prior approvals of the project budgets and the responsibilities of the parties regarding the budgets:

Under Section I Background

This Cooperative Agreement and the attached Terms and Conditions establish the concepts and responsibilities for implementing BCFS's residential services for UAC. (Under section I)

Under section IV, Description of Activities, Responsibilities of BCFS,

To submit and/or review the program budget with ORR Project Officer to be sure it accurately reflects proposed activities as described in the project plan;

To amend the approved project plan as needed to comply with standards, goals and priorities established by the ORR Director;

The Responsibilities of ORR;

To confirm project plan (which includes approach, activities, timelines, and results expected) and budget, and discuss minor modifications BCFS;

To submit and/or review project expenditures with BCFS to be sure it accurately reflects proposed activities;

To promptly review written requests for prior approval of deviations from the project plan or approved budget. Any changes that affect the terms and conditions of the grant award or revisions/amendments to the cooperative agreement or to the approved scope of activities will require prior approval by the ORR Project Officer and the Grants Management Specialist in the Office of Grants Management (OGM).

Under SECTION V: Budget and Financial Arrangement

The approved budget is attached to this agreement and reflected in the Notice of Award (NOA).

The Government shall not be obligated to reimburse the recipient for costs incurred in excess of the total amount allotted to this project, and the recipient shall not be obligated to continue performance under the Agreement (including actions under the termination clause) or otherwise to incur costs in excess of the amount allotted to this Agreement unless and until the ORR Project Officer and the Grants Management Specialist have notified the recipient in writing that additional funds have been awarded. No notice, communication, or representation from any person other than the Grants Management Specialist shall authorize the expenditure of additional funds. The United States Government will not be obligated for any excess costs in the absence of a written notice of authorization from the Grants Management Specialist. Changes issued pursuant to this Agreement shall not be considered an authorization to the recipient to exceed the allotted amount of this Agreement unless specifically stated by the Grants Management Specialist.

The award will be based on the budget that is approved by ORR.

Under SECTION VII: Continuation Applications

BCFS must submit a continuation application by June 1. For continuation applications, BCFS will provide the following information: 1) Standard Forms: SF 424 Application for Federal Assistance, SF 424A Budget Information - Non-Construction Program; and SF 424B Assurances-Non-Construction Program, and required compliance, and certifications; 2.) Budget worksheets and narrative; 3) Program Description and Work plan; 4) Current State residential care license; 5) Proof of Insurance; 6) Facility lease or bank mortgage note on property (as applicable); 7) Indirect Cost Rate approval; 8) Current Program Organizational Chart; 9) Staffing and Volunteer Roster; 10) Copy of all Child Protective Services reports,

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allegations and CPS investigations; 11) Property/Inventory List; 12) Current program progress report; and, 13) Standard Financial Reporting Form: SF 425.

Under SECTION VII: Continuation Applications, BCFS HHS was required and did submit the following for the first and all prior budgets, “budget worksheets and narratives” and “facility lease or bank mortgage note on property”. BCFS HHS submitted all budget and narratives and the facility leases, as can be seen in the email exchange of September 24th and 25th 2015 (Attachment #1) between BCFS and DHHS showing the submission of the leases between BCFS HHS and BCFS. DHHS later approved the budget as reasonable rental costs for the budget period, which are below fair market value for similar properties.

OIG’s calculations of depreciation are not correct.

While reviewing the depreciation tables of the OIG draft report, OIG’s depreciation calculations are not correct based on the tables below. BCFS is attaching depreciation tables in support of the corrected calculations (Attachment #2, #3, and #4).

OIG REPORT: CALCULATIONS				
Facility	Claimed Amount	Allowable Amount	Finding Difference	
Baytown	\$ 228,000.00	\$ 34,978.00	\$	193,022.00
Raymondville	\$ 78,000.00	\$ 20,663.00	\$	57,337.00
San Antonio	\$ 407,889.00	\$ -	\$	407,889.00
Total	\$ 713,889.00	\$ 55,641.00	\$	658,248.00

BASED ON ACTUAL DEPRECIATION SCHEDULES

Facility	Claimed Amount	Allowable Amount	Finding Difference	
Baytown	\$ 228,000.00	\$ 53,036.71	\$	174,963.29
Raymondville	\$ 78,000.00	\$ 20,663.00	\$	57,337.00
San Antonio	\$ 407,889.00	\$ 145,775.95	\$	262,113.05
Total	\$ 713,889.00	\$ 219,475.66	\$	494,413.34

In Summary

The rental costs are allowable as approved in the budgets, as they are below market value and have been determined to be reasonable, direct project costs to support the programs goals, and have been preapproved in writing by the project manager. The costs comply with the DHHS terms and conditions of the cooperative agreement that allows support costs of “Services Provided by Affiliated Organizations” and comply with Federal regulations.

OIG’s findings if not reconsidered and overturned potentially threatens the on-going operations of unaccompanied alien children programs as it relates to cooperative agreement 90ZU0102-02.

BCFS HHS is open and willing to have any additional discussions regarding the issues discussed in BCFS HHS’ response or submit any additional documentation to further support BCFS HHS position that the rental costs are allowable.

Sincerely,

/Sonya Thompson/

Sonya Thompson
Executive Director