HOBBS
STRAUS
DEAN &
WALKER

806 SW Broadway, Suite 900
Portland, OR 97205
T 503.242.1745
F 503 242 1072
HOBBSSTRAUS.COM

MEMORANDUM

March 3, 2015

TO: Contract Support Cost Clients

FROM: HOBBS, STRAUS, DEAN & WALKER, LLP Geoff Strommer by SDO

RE: ***IHS CSC Workgroup Meets***

The Indian Health Service (IHS) convened its Contract Support Cost (CSC) Workgroup on February 26-27 in Washington, DC. The Technical Workgroup, a subset of the larger group, met on the first day, and the full Workgroup met on the second. Although no formal decisions or recommendations were made, several hot-button CSC issues were addressed:

- the Administration's proposal to transfer CSC funding from discretionary to mandatory appropriations;
- a proposal to establish fixed lump-sum and fixed rate options for CSC negotiations;
- the IHS reconciliation process, which the agency believes must tie CSC needs back to expenditures and could extend for five years beyond the contract year;
- direct CSC (DCSC) renegotiations, in which IHS has recently contended that the federal fringe rate has jumped from 21% to 32%, dramatically lowering the amount of DCSC owed to tribes;
- CSC language for FY 2016 funding agreements;
- data requests from IHS, including funding balances for FY 2014 and FY 2015 and shortfall reports for FY 2012 and FY 2013; and
- interim guidance from IHS on its current method of administering CSC funding.

The Administration's Mandatory CSC Proposal

As you know, the President's FY 2016 budget included a proposal that CSC be moved to a mandatory appropriation for a three-year period starting in FY 2017, with FY 2016 devoted to consultation and fine-tuning. Specific amounts would be appropriated each year, amounts comfortably large enough to pay the full projected CSC needs. If enacted by Congress, the mandatory CSC appropriation would be separate from the rest of IHS's discretionary budget, eliminating the possibility of program funds needing to be reprogrammed to cover CSC needs. The limited term and amount of the Administration's proposed mandatory appropriation differ from the permanent, indefinite appropriation for which we advocated in our 2014 white paper. But the Administration's proposal represents a tremendous step in the right direction. As indicated in the attached comment letters we prepared for the joint consultation on the proposal, our clients as well as other interested tribes and tribal organizations overwhelmingly support it, with certain modifications such as implementation beginning in FY 2016 rather than FY 2017.[1]

Dr. Yvette Roubideaux, Senior Advisor to Secretary Burwell, addressed the full Workgroup and discussed the Administration's proposal at length. She called on the Workgroup members to support the President's budget, and expressed optimism that Congress would adopt the mandatory CSC proposal. If the Office of Management and Budget (OMB) can be convinced, she said, so can Congress.

Dr. Roubideaux noted that congressional champions will be needed to lead the charge. Bemidji Area representative Aaron Payment pointed out that Sen. Heidi Heitcamp (D-ND), Sen. Jon Tester (D-Montana), and Sen. Al Franken (D-MN) all spoke strongly in favor of the proposal at the NCAI Executive Session earlier in the week. Dr. Roubideaux said the House Appropriations Committee also appeared supportive during her testimony there. Ushering the mandatory appropriation into law would be a "huge legacy" for a congressional champion.

Dr. Roubideaux stressed over and over the importance of working together and presenting a united front to Congress. It was "really hard" to get the Administration behind the proposal, she said, and dissension would provide Congress an excuse to bury it.

A tribal representative asked why the appropriation would be authorized for only three years rather than permanently. Dr. Roubideaux said that a permanent appropriation would have been too big a political lift, and the strategy was to put forward something feasible. Another representative raised a doomsday scenario in which the mandatory appropriation was enacted, then not reauthorized, leaving no CSC in either mandatory or discretionary appropriations. Dr. Roubideaux pointed out that mandatory appropriations are routinely reauthorized, and that the intent is for the three-year period to recur indefinitely. A tribal representative commented that getting in the door for three years would set a monumental precedent that would not likely be reversed.

Another representative commented that the proposed amounts seemed too high, and that an indefinite appropriation might actually be scored lower by the Congressional Budget Office. Dr. Roubideaux indicated that the Administration disagreed. The amounts, like the three-year duration, were purposefully determined by the Administration. They are politically feasible, yet almost certainly large enough—even though large mandatory CSC appropriations might serve as an incentive for tribes to assume new and expanded contracts and compacts.

[1] See the attached comment letter dated February 20, 2015, as well as the supplemental comment letter dated February 27, 2015.

Dr. Roubideaux was asked more generally whether the Administration would support legislative proposals that differed from the Administration's. She did not answer directly, stating that it is up to Congress now, and she could not advise tribes on how to approach Congress. She said the Administration's proposal, developed after nearly a year of tribal consultation and backed by OMB, is on the table, and she suggested that significant changes could, at a minimum, delay implementation. "I can't tell you what to say," she concluded, "except support the President's budget."

The IHS Reconciliation Process

The agency's misreading of the Indian Self-Determination and Education Assistance Act (ISDEAA) and the Supreme Court's decision in the *Ramah* case has spilled over from the claims settlement process into CSC administration moving forward. At both the technical meeting and before the full Workgroup, IHS described its view that CSC payments for every fiscal year must be reconciled back to expenditures in that year. This view, which derives from the agency's belief that the ISDEAA defines CSC as "costs incurred," leads to what one tribal representative described as "a dark, dark place." Events that occur well after the close of the contract year—such as the issuance of a final indirect cost rate, or the completion of an audit—could significantly change IHS's assessment of the amount of CSC incurred, and thus owed, in that year. Tribes that simply carry forward funding from one year to another, as allowed by the ISDEAA, risk having IHS seek to claw back the CSC associated with those funds, only to have IHS pay it back in the year in which the program funds are spent (or a year or two *after* that, once the audit establishes the expenditure).

IHS plans to keep funds from each year's appropriation for five subsequent years—until by law the funds revert to the Treasury—to pay contractors who could establish that they incurred more CSC during the year of the appropriation. Conversely, IHS would seek to recover "overpayments" if it finds—any time within the five-year reconciliation period—that a contractor incurred less CSC than it was paid.

Tribal representatives universally objected to this process. But IHS representatives made clear that the agency's position is that it must pay full CSC, as defined by costs incurred, and no more. The Workgroup will not likely be able to budge IHS from this legal position, although, as discussed below, there may be ways around it.

Fixed Lump-Sum and Fixed-Rate Options

The CSC Technical Workgroup spent a full day discussing issues associated with a proposal to establish options for tribal contractors to negotiate lump sums or apply fixed rates for an agreed-on period of years. The lump-sum proposal was initially presented to the Workgroup at the previous meeting as a white paper by Alaska representative Lee

Olsen.[2] Mr. Olsen refined and expanded the proposal to include a fixed-rate option similar to the old IHS Pilot Project. Both options are designed to reduce the number of variables in the CSC needs calculus, lending greater stability and predictability for both the contractor and IHS. These options are described in detail in the attached draft Fixed CSC Pilot Project Program Implementation Guidelines prepared by Mr. Olsen.

To varying extents, both proposed options streamline and simplify the CSC negotiation and reconciliation process. The lump-sum option would avoid reconciliation altogether. Once IHS paid the agreed-on sum, neither party could come back later and claim the amount was wrong—assuming the contract language is well drafted. The fixed-rate option would eliminate one—but only one—of the variables driving the reconciliation process throughout (and well beyond) the contract year.

Roselyn Tso and Ashley Metcalf of IHS expressed several concerns with the proposal. Most fundamentally, the agency has not determined conclusively whether it has the authority to agree to a locked-in sum or rate, and if it did, whether such an agreement would protect it from liability if the contractor ended up incurring more CSC than IHS paid. IHS will eventually seek the opinion of the Office of General Counsel (OGC) on this issue, but for now the agency is still studying how these proposed options would work.

DCSC Renegotiation

With the advent of the full-funding era in FY 2014, many contractors sought to renegotiate their DCSC requirements. Since the lion's share of DCSC is fringe benefits, the negotiation essentially boils down to determining the contractor's fringe costs and subtracting the agency's (which were included in the program or "Secretarial" amount under section 106(a)(1) of the ISDEAA). The difference—plus certain other, smaller costs—is payable as DCSC.

As we have reported, IHS recently developed a new "profile" that increased the agency's fringe rate from its traditional level of 21.12% to 32.4%, resulting in dramatically lower calculations of DCSC need.[3] It did this by reclassifying certain costs from salaries to benefits—improperly, according to Alaska representative Dave Mather and others. Dr. Mather requested, first, that IHS revert to its former profile with the 21.12% rate; and second, that tribes be given the option to have IHS pay DCSC at a flat 15% of salaries, as the Bureau of Indian Affairs does. Dr. Mather will develop a formal proposal for the Workgroup addressing DCSC negotiation.

---

[2] See our report of February 2, 2015 and attachment.

[3] See our memorandum of November 19, 2014 at 7-8.

FY 2016 Funding Agreement Language

Last year during the Alaska Tribal Health Compact negotiations, tribes and IHS agreed on template CSC language that reflected the new full-funding requirement, and that language was used in some other agreements around the country. This year, the Workgroup believes that tribes may wish to include language designed to cut off the reconciliation process at the end of the contract year or some reasonable time thereafter. Tribal representatives valued finality and certainty over the possibility of receiving an additional reconciliation payment two or more years down the line—especially since the tribe could just as easily receive a bill. Tribal and OGC attorneys will try to develop common language that achieves this purpose and protects both parties from claims. The Workgroup looked at draft language, but IHS was not prepared to comment on it, except to indicate ominously that the agency may lack the authority to agree to a reconciliation cut-off date.

Data Requests from IHS

Tribal representatives renewed their longstanding request that IHS release its shortfall reports for FY 2013 (2012 data) and FY 2014 (FY 2013 data). These reports contain essential information to help the Workgroup make informed recommendations on CSC policy. Tribal representatives also requested funding balances for FY 2014 and FY 2015. The balance for FY 2014 could yield insight into IHS's reconciliation process, and the FY 2015 balance would help the Workgroup evaluate the chances of IHS having to reprogram funds again in FY 2015.

Interim Guidance from IHS

With all of the changes in CSC law, policy, and practice in the last year, Workgroup members recognize that most tribes must find it extremely difficult to keep up. In fact, even Workgroup members themselves are not entirely sure of IHS's current practices, as evidenced by the animated discussion of reconciliation at these meetings. And IHS Area Office staff are not implementing CSC policy consistently.

Although things remain in flux due to the mandatory proposal, and it may thus be too soon to undertake a comprehensive revision of the CSC policy manual, tribal and federal representatives agreed that written interim guidance is needed. The guidance would likely take the form of a series of letters from IHS explaining its current practice with respect to the calculation and payment of CSC needs. The first such letter, to be developed by the tribal-federal technical group and vetted with the full Workgroup, would include explanations of the ACC template and the exclusions matrix, and perhaps a description of the reconciliation process as envisioned by IHS. Future guidance could be issued on DCSC negotiation, once the Workgroup has developed its recommendations on this issue and IHS has decided how it will proceed. Written guidance on all of these subjects would help both tribes and IHS Area Office staff understand IHS's current practice and help them navigate the changes still to come.

Conclusion

The next meeting of the Workgroup is tentatively set for April 7-8 or 8-9 in Palm Springs, in conjunction with the National Indian Health Board meetings. In the meantime, the Technical Workgroup will work on the issues with particular relevance to the upcoming IHS negotiation cycle: the interim guidance letter, the FY 2016 FA language, and DCSC negotiation practice.

If you have any questions about this memorandum, please do not hesitate to contact Joe Webster (jwebster@hobbsstraus.com or 202-822-8282), Geoff Strommer, (gstrommer@hobbsstraus.com or 503-242-1745), or Steve Osborne (sosborne@hobbsstraus.com or 503-242-1745).