



State of New Jersey

DEPARTMENT OF HUMAN SERVICES

DIVISION OF AGING SERVICES

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STATE OF NEW JERSEY  
DEPARTMENT OF HUMAN SERVICES  
DIVISION OF AGING SERVICES

MONMOUTH CONVALESCENT  
CENTER, 229 BATH AVENUE,  
LONG BRANCH, NEW JERSEY 07740,  
MONMOUTH,

Petitioner,

v.

NEW JERSEY DEPARTMENT OF  
HEALTH AND SENIOR SERVICES,  
Respondent.

ADMINISTRATIVE ACTION

FINAL AGENCY DECISION

OAL DKT. NO. HLT 03727-12

The Director of the Division of Aging Services (Division)<sup>1</sup> has reviewed the record in this matter consisting of the Initial Decision of the Honorable Elia A. Pelios, ALJ, and the documents in evidence presented to the Office of Administrative Law. The Director also has reviewed the Exceptions submitted by Brian N. Rath, attorney for Petitioner, and by Deputy Attorney General, T. Nicole Williams-Parks, attorney for Respondent.

**STATEMENT OF CASE AND PROCEDURAL HISTORY**

This matter involves the Medicaid per diem reimbursement rate set for the Petitioner, Monmouth Convalescent Center, by the Respondent, Division of Aging

<sup>1</sup> Effective July 1, 2012, functions related to nursing facility rate setting were reorganized from the former Department of Health and Senior Services into the new Division of Aging Services in the Department of Human Services.

Services, for Fiscal Year 2012.<sup>2</sup> Petitioner contends that Respondent failed to take into account the unique circumstances presented by the promulgation and implementation of a new reimbursement rate methodology during Petitioner's capital improvement project, namely the construction of a new building, and Respondent's strict application of the new methodology led to an inequity in the calculation of Petitioner's Medicaid per diem reimbursement rate for July 1, 2011, through June 30, 2012. The application of the new methodology failed to provide Petitioner with a return on its investment.

Petitioner is a long-term care facility located in Monmouth County, New Jersey. Petitioner began construction of the new building in 2009 and completed construction in 2011. By that time, Respondent had promulgated new regulations pertaining to the method for calculating the rate at which nursing facilities would be reimbursed for Medicaid residents.

Petitioner's Medicaid per diem reimbursement rate on June 30, 2010, was \$196.95 (the last rate under the former methodology). For July 1, 2010, the first calculated rate under the new methodology, Petitioner's Medicaid per diem reimbursement rate was set at \$191.95. On or about August 9, 2011, Petitioner filed a Level I appeal with Respondent and requested an adjustment to the Fair Rental Value component of the rate, effective May 5, 2011, based upon the new building. Respondent denied the appeal for a mid-year adjustment to the Fair Rental Value allowance but recognized the new construction in the rate beginning July 1, 2011, rather than waiting until July 1, 2012. Petitioner's Medicaid per diem reimbursement rate for July 1, 2011, was set at \$188.89. On or about November 14, 2011, Petitioner filed a

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<sup>2</sup> The fiscal year begins July 1st and ends June 30th of the following year. Fiscal Year 2012 began July 1, 2011, and ended June 30, 2012.

Level I appeal of that rate contesting the comparison of the rate for the new building to the rate for the older facility. Respondent denied the appeal.

Petitioner's Medicaid per diem reimbursement rate for July 1, 2012, was set at \$196.16.

Petitioner filed a Level II appeal and the matter was transmitted to the Office of Administrative Law.

On or about May 2, 2013, Petitioner filed a motion for summary decision. On or about August 5, 2013, Respondent filed a letter brief in opposition to the motion and in support of a cross-motion for summary decision. On or about September 4, 2013, Petitioner filed a letter brief in response to Respondent's cross-motion for summary decision. On or about September 27, 2013, Respondent filed a response to Petitioner's opposition to the cross-motion. The Honorable Elia A. Pelios, ALJ, heard oral argument on February 4, 2014. On or about February 7, 2014, Petitioner submitted a supplemental letter brief. On or about February 20, 2014, Respondent submitted a letter brief in response to Petitioner's supplemental letter brief. The record was reopened for a status conference on April 7, 2014. The matter was closed on May 29, 2014. Judge Pelios issued the Initial Decision on October 6, 2017.

On or about October 19, 2017, Petitioner filed Exceptions. On or about October 31, 2017, Respondent filed a letter brief in opposition to Petitioner's Exceptions.

## **STATEMENT OF FACTS**

The Honorable Elia A. Pelios, ALJ, (ALJ) recited the following findings of facts in the Initial Decision:

1. Petitioner is a long-term care nursing facility that receives funding through Respondent under the Medicaid program.
2. In 2006, Petitioner began planning a multi-million dollar project to build a new nursing facility and to completely renovate its older facility.
3. In or around November 2009, Petitioner began construction on the new building.
4. On May 11, 2011, the new building was completed, the older facility was closed for renovations and patients were transferred to the new building.
5. The exact number of beds in Petitioner's facility is uncertain.
6. By the time Petitioner completed its project, Respondent had promulgated new regulations for reimbursing nursing facilities for Medicaid patients.
7. Prior to July 1, 2010, appropriate compensation for capital investments was calculated using an assessment of the nursing facility's value.
8. In 2011, the regulations were revised to utilize a Fair Rental Value (FRV) allowance for calculating reimbursement rates for capital investments. The FRV allowance is calculated and then is combined with other costs and expenses to determine a nursing facility's Medicaid per diem reimbursement rate.
9. The new regulations were based, in part, on the estimated depreciated value of a nursing facility's capital assets. The new regulations did not provide for direct reimbursement for allowable depreciation, amortization, capital related interest, rent expenses and lease expenses as did the previous regulations.

- 10.If funding is not available through the Legislature's appropriations, then the Medicaid per diem reimbursement rate may be reduced in a several ways.
- 11.If such reductions are not sufficient to match the funds appropriated by the Legislature, a Budget Adjustment Factor (BAF) is applied to the Medicaid reimbursement rate. The BAF reduces the overall Medicaid per diem reimbursement rate, on a percentage basis, to match the amount of money appropriated by the Legislature for that particular Fiscal Year (FY).
- 12.Due to the change to FRV for capital investment rates, the new regulations provided a transition mechanism referred to as a rate corridor, which limits the variance of a nursing facility's Medicaid per diem reimbursement rate by a specified dollar amount.
- 13.The Appropriations Act for FY 2012<sup>3</sup>, which was enacted under line-item veto, significantly reduced the funding to nursing facilities.
- 14.On August 5, 2009, Respondent requested from Petitioner information to aid in accurately determining the FRV of Petitioner's facility under the new regulations.
- 15.Petitioner did not respond to the request.
- 16.On September 2, 2009, Respondent sent to Petitioner another request for information regarding FRV of Petitioner's facility.
- 17.Petitioner did not respond to the follow-up request.
- 18.On or about July 20, 2010, Respondent issued to Petitioner an online FRV allowance survey and warned Petitioner that FRV would be set at 40 years, or calculated based on Respondent's current information, until Petitioner submitted

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<sup>3</sup> The ALJ refers to "the 2011 Appropriations Act." Based upon the context and the citation to the article, I determined that the ALJ is referring to the Appropriations Act passed in 2011, which is for FY 2012.

an "FRV Data Report." Petitioner also was advised that, if Petitioner provided updated information, any change to the FRV allowance would be applied the following year.

19. On June 30, 2010, before the new regulations took effect, Petitioner's Medicaid per diem reimbursement rate was \$196.95.
20. On March 11, 2011, Respondent calculated Petitioner's Medicaid per diem reimbursement rate for FY 2011 (July 1, 2010, through June 30, 2011) to be \$181.31; \$83.82 was for care, \$88.04 was for administration and \$9.45 was for capital investments. The FRV allowance was based on the older facility, which was in use at the time.
21. No BAF was applied, but a rate corridor prevented Petitioner's rate from decreasing more than \$5.00 from the previous year so that Petitioner's final rate was set at \$191.95.
22. On August 9, 2011, Petitioner filed a Level I appeal with Respondent and sought a rate adjustment, effective May 5, 2011, due to the construction of the new building.
23. In response to the appeal, Respondent acknowledged that, because the new beds were placed in service May 5, 2011, the regulations normally would recognize the new beds beginning July 1, 2012. Due to the hardship created by the new regulations and the timing of Petitioner's project, Respondent modified the FRV allowance one year earlier, beginning July 1, 2011.

24. On October 14, 2011, Respondent determined Petitioner's rate to be \$204.91, effective July 1, 2011<sup>4</sup>. \$98.48 was for care, \$85.90 was for administration and \$20.53 was for capital investments. The higher FRV allowance reflected the new building.
25. However, due to lower appropriations under the Appropriations Act,<sup>5</sup> a BAF of 0.92180 was applied and Petitioner's rate was reduced from \$204.91 to \$188.89.
26. The rate corridor did not affect the reduced Medicaid per diem reimbursement rate of \$188.89 because this rate was within \$10.00 of the FY 2010 rate of \$196.95.
27. On November 14, 2011, Petitioner filed another Level I appeal contesting the rate determination because the previous rate for the older facility was compared to the new rate for the new building.
28. For July 1, 2012, through June 30, 2013, Respondent determined Petitioner's rate to be \$216.04; \$108.13 was for care, \$87.79 was for administration and \$20.12 was for capital investments. For this time period, a BAF of 0.90800 was applied and Petitioner's Medicaid per diem reimbursement rate was reduced to \$196.16.
29. There was no rate corridor and, since the adjusted rate was higher than the rate for the previous year, no other adjustments were made to Petitioner's rate.

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<sup>4</sup> The ALJ states FY 2011, but refers to Respondent's Exhibit E, which indicates July 1, 2011.

<sup>5</sup> The ALJ refers to "the 2011 Appropriations Act." Based upon the context and the ALJ's previous reference to this Appropriations Act, I determined that the ALJ is referring to the Appropriations Act passed in 2011, which is for FY 2012.

## **SUMMARY OF FILED EXCEPTIONS AND REPLIES**

In its Exceptions, Petitioner makes several arguments. First, Petitioner argues generally that the ALJ erred in deferring to Respondent's erroneous and inequitable rate setting.

Second, Petitioner asserts that the ALJ failed to recognize the true nature of the appeal and give it the proper analysis. Petitioner states that the financial loss suffered by Respondent's strict application of the rate setting regulations is the very basis of the appeal. Petitioner sets forth, at length, the inequity of Respondent's actions and states that that inequity, itself, as evidenced by Petitioner's significant loss, is the sole basis of the appeal. The misapplication of the rate corridor is merely an example of the mechanism used to create the inequity; it is not the subject of the appeal itself. Petitioner's rate is such a situation where strict application of the rate setting mechanism caused an inequitable result for Petitioner and allows for Petitioner to appeal the inequity. Petitioner also contends that the ALJ erred in deferring to Respondent's "apples to oranges comparison" in the application of the rate corridor because Respondent's adjustment of Petitioner's rate to include the new building did not address the inequity. Petitioner asserts that, to fairly and accurately account for the investment, Respondent must compare like things – either the new building under both the previous and current regulations or the older facility under both the previous and current regulations.

Next, Petitioner argues that the ALJ erred in failing to consider the other arguments presented. Petitioner asserts that the Medicaid per diem reimbursement rate set by Respondent is inequitable, caused undue harm and should be recalculated



to recognize the extensive capital investment to the facility based on the following: the rate resulted in an inequality to Petitioner as a result of an unusual situation; the rate is arbitrary, capricious and unreasonable; the rate must be revised as dictated by the doctrine of fundamental fairness; the rate violates the square corners doctrine; the rate violates equal protection principles; and the rate is contrary to public policy.

Finally, Petitioner contends that it was unduly prejudiced by the extensive delay in receiving the Initial Decision. Waiting over three years for any resolution to this matter has incalculably harmed Petitioner.

Respondent filed opposition to Petitioner's Exceptions.

First, Respondent contends that the ALJ considered whether Petitioner suffered an inequity. Respondent cites to specific instances where the ALJ referred to equity or the inequity of the situation.

Next, Respondent asserts that the ALJ is not required to include all of Petitioner's arguments in the Initial Decision; however, although not explicitly stated, the ALJ did address all relevant arguments.

Finally, Respondent contends that the time frame for issuing the Initial Decision did not unduly prejudice Petitioner because a decision in favor of the Petitioner would have resulted in an adjustment to Petitioner's Medicaid per diem reimbursement rate for the year in question and the subsequent years.

## **DECISION AND ANALYSIS**

Petitioner seeks a decision requiring Respondent to recalculate its Medicaid per diem reimbursement rate in such a way as to recognize Petitioner's significant capital investment. Petitioner seeks such relief on the grounds that the timing of its capital improvement project, along with the drastic changes to regulations, presents a rare and unusual circumstance that created an inequity when Respondent strictly applied those regulations; that Respondent's imposition of the rate in light of the inequity is arbitrary, capricious and unreasonable; that the doctrine of fundamental fairness dictates an appropriate rate for Petitioner; that the strict application of the regulations violates the square corners doctrine; that the strict application of the regulations violates equal protection principles; and that Respondent's failure to adjust the rate is contrary to public policy. Petitioner contends that the strict application of the regulations fails to provide a return on its investment.

The foundation for Petitioner's arguments is the regulatory rate setting methodology and the inequity caused by the strict application of the regulations. This, however, ignores the role of the State budget in the calculation of Petitioner's rate and the limitations imposed by the Appropriations Act for FY 2012 on the rates for all nursing facilities. Of utmost relevance and significance here is that the Appropriations Act for FY 2012 did not appropriate sufficient funds to cover the initial Medicaid per diem reimbursement rates of all nursing facilities as calculated by Respondent.

To resolve this matter, it is necessary to address the funding made available through the budget process for the relevant years. The Appropriations Act provided for the appropriation of funds for Medicaid patients in nursing facilities. The Acts also

limited the fluctuation of the Medicaid per diem reimbursement rate for nursing facilities.<sup>6</sup>

The Appropriations Act for FY 2011, effective July 1, 2010, provided that a nursing facility's Medicaid per diem reimbursement rate shall not vary more than \$5.00 from the rate received by that facility during FY 2010.<sup>7</sup> In FY 2010, Petitioner's rate was \$196.95. On March 11, 2011, Respondent calculated Petitioner's initial rate for FY 2011 to be \$181.31. Since the applicable Appropriations Act included a rate corridor that prevented the rate from varying more than \$5.00 from the previous year, Petitioner's rate for FY 2011 could not be less than \$191.95 so Respondent adjusted the rate accordingly. Petitioner's final adjusted rate was \$191.95

The Appropriations Act for FY 2012, effective July 1, 2011, provided that a nursing facility's Medicaid per diem reimbursement rate shall not vary more than \$10.00 from the rate received by that facility during FY 2010.<sup>8</sup> This Appropriations Act also significantly reduced the funding to nursing facilities. On October 14, 2011, Respondent determined Petitioner's initial rate to be \$204.91. Because there was a significant decrease in appropriations, the Medicaid per diem reimbursement rates of all nursing facilities had to be reduced in such a way so as to match the amount of funds available. Respondent applied a BAF to the rate of each nursing facility and, as a consequence of the application of the BAF to the rates, Petitioner's rate was reduced to \$188.89. Although the applicable Appropriations Act included a rate corridor of \$10.00 from the FY 2010 rate, Respondent did not apply the legislative rate corridor to Petitioner's rate.

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<sup>6</sup> This is known as a rate corridor.

<sup>7</sup> See P.L. 2010, c. 35, approved June 29, 2010.

<sup>8</sup> See P.L. 2011, c. 85, approved June 30, 2011.

Since Petitioner's FY 2010 rate was \$196.95, Respondent did not adjust the FY 2012 rate. Petitioner's final adjusted rate was \$188.89.

The Appropriations Act for FY 2013, effective July 1, 2012, provided that the Medicaid per diem reimbursement rate for a nursing facility shall not be less than the rate last received by the facility for FY 2012.<sup>9</sup> For FY 2013, Respondent determined Petitioner's initial rate to be \$216.04. Respondent applied a BAF of 0.90800 to the rate of each nursing facility and, consequently, Petitioner's rate was reduced to \$196.16. Since Petitioner's FY 2012 rate was \$188.89 and the FY 2013 rate was greater than that amount, Respondent did not adjust the FY 2013 rate. Petitioner's final adjusted rate was \$196.16.

Petitioner contends that the changing of the reimbursement rate methodology during its ongoing capital improvement project and the strict application of the regulations caused the inequity in the calculation of its final adjusted rate for July 1, 2011. Petitioner repeatedly refers to the replacement of appraisals by the FRV allowance and the imposition of artificially limiting regulatory rate corridors in support of its arguments. Although the regulations provide for a FRV allowance and rate corridors, Petitioner cannot escape the fact that the reduction to its rate for July 1, 2011, was made as a direct result of the State budget. As found by the ALJ, the Appropriations Act for FY 2012 significantly reduced the amount of funds available to nursing facilities. It was that decrease in funding that necessitated the application of a BAF. Respondent applied a BAF for the purpose of reducing the Medicaid per diem reimbursement rates to match the appropriations. While it is true that the regulations provided for rate corridors, it is also true that a rate corridor was mandated by the Appropriations Act.

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<sup>9</sup> See P.L. 2012, c. 18, approved June 29, 2012.

Furthermore, Petitioner's rate was not decreased due to a rate corridor. Petitioner's rate was decreased, as were the rates of all nursing facilities, due to budgetary constraints.

The Appropriations Act supersedes the regulations. Had sufficient funding been available, there would have been no need to reduce the rates of the nursing facilities. A BAF was necessitated by the limited funding. Respondent determined the percentage by which each nursing facility's initial rate would be reduced. A BAF of 0.92180 was applied to each of the nursing facilities and each nursing facility received a reduction of its rates based upon the BAF.

Petitioner is correct in asserting that N.J.A.C. 8:85-3.1 permits Respondent to review the application of the rules on the grounds of inequity, but the argument misses two important points. First, Respondent did not have discretion with the appropriations. The funding, through the Appropriations Act, dictated Respondent's course of conduct. Second, discretion involves a choice. Just as Respondent can choose to exercise discretion, Respondent also can decide against exercising discretion. For these reasons, Respondent cannot be forced to exercise discretion in this matter.

I agree with the ALJ that the BAF was a source of Petitioner's rate decrease. The State budget necessitated the application of a BAF in order to reduce the rates to match the funding. Petitioner's initial rate was set at \$204.91. It was only after Respondent determined that appropriations were insufficient to match the initial rates of all nursing facilities that the rates for all nursing facilities, including Petitioner, were reduced by a BAF.

I disagree with Petitioner that the ALJ failed to address its other arguments. The ALJ found that the BAF reduced Petitioner's rate and that the "BAF is, in fact, the only source of the rate decreases Monmouth suffered." Petitioner essentially has argued that Respondent acted in an arbitrary, capricious, unreasonable and/or unfair manner in applying the regulations. These assertions, however, are not supported by the record. Funding was limited by the budget and Respondent applied a BAF because the appropriations were insufficient to cover the initial rates of all nursing facilities. In denying Petitioner's motion and granting Respondent's cross-motion, the ALJ in essence found that Respondent's conduct did not cause the inequity and, as a result, Respondent's conduct was not arbitrary, capricious, unreasonable and/or unfair.

Based upon a full review of the record, the Director hereby **ADOPTS** the conclusions of the Administrative Law Judge in upholding Respondent's calculation of Petitioner's Medicaid per diem reimbursement rate and granting Respondent's cross-motion for summary decision.

Petitioner has the right to appeal this Final Order within 45 days to the New Jersey Superior Court, Appellate Division, Richard J. Hughes Justice Complex, PO Box 006, Trenton, New Jersey 08625-0006.

**THEREFORE**, it is on this 17<sup>th</sup> day of November, 2017,

**ORDERED:**

That the Initial Decision of the Administrative Law Judge is hereby **ADOPTED**; and Respondent's cross-motion for summary decision is granted.

**FURTHER ORDERED:**

That any action required by this decision be promptly implemented by the appropriate Division staff.

Date: 11/17/17

  
Laura Otterbourg  
Division Director