

(2) For purposes of this section, the term "direct seller's representative" means a person who buys consumer products on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment, or who sells, or solicits the sale of, consumer products in the home or otherwise than in a permanent retail establishment; and

(a) Substantially all of the remuneration paid to such person, whether or not paid in cash, for the performance of services described in this subsection is directly related to sales or other output, including the performance of services, rather than the number of hours worked; and

(b) The services performed by the person are performed pursuant to a written contract between such person and the person for whom the services are performed and such contract provides that the person will not be treated as an employee with respect to such purposes for federal tax purposes.

(3) Nothing in this section shall be construed to imply that a person exempt from tax under this section was engaged in a business activity taxable under this chapter prior to the enactment of this section.

Passed the Senate May 22, 1983.

Passed the House May 17, 1983.

Approved by the Governor June 13, 1983.

Filed in Office of Secretary of State June 13, 1983.

## CHAPTER 67

[Reengrossed Substitute Senate Bill No. 3780]

### NURSING HOMES—AUDITING AND COST REIMBURSEMENT

AN ACT Relating to nursing homes; amending section 4, chapter 177, Laws of 1980 and RCW 74.46.040; amending section 6, chapter 177, Laws of 1980 and RCW 74.46.060; amending section 8, chapter 177, Laws of 1980 and RCW 74.46.080; amending section 10, chapter 177, Laws of 1980 and RCW 74.46.100; amending section 13, chapter 177, Laws of 1980 and RCW 74.46.130; amending section 15, chapter 177, Laws of 1980 and RCW 74.46.150; amending section 16, chapter 177, Laws of 1980 and RCW 74.46.160; amending section 17, chapter 177, Laws of 1980 and RCW 74.46.170; amending section 18, chapter 177, Laws of 1980 and RCW 74.46.180; amending section 19, chapter 177, Laws of 1980 and RCW 74.46.190; amending section 27, chapter 177, Laws of 1980 and RCW 74.46.270; amending section 31, chapter 177, Laws of 1980 and RCW 74.46.310; amending section 41, chapter 177, Laws of 1980 and RCW 74.46.410; amending section 42, chapter 177, Laws of 1980 and RCW 74.46.420; amending section 43, chapter 177, Laws of 1980 and RCW 74.46.430; amending section 45, chapter 177, Laws of 1980 and RCW 74.46.450; amending section 46, chapter 177, Laws of 1980 as amended by section 5, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.460; amending section 47, chapter 177, Laws of 1980 and RCW 74.46.470; amending section 49, chapter 177, Laws of 1980 as amended by section 6, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.490; amending section 53, chapter 177, Laws of 1980 as amended by section 7, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.530; amending section 55, chapter 177, Laws of 1980 and RCW 74.46.550; amending section 56, chapter 177, Laws of 1980 and RCW 74.46.560; amending section 57, chapter 177, Laws of 1980 and RCW 74.46.570; amending section 58, chapter 177, Laws of 1980 and RCW 74.46.580; amending section 61, chapter 177, Laws of 1980 and RCW 74.46.610; amending section 64, chapter 177, Laws of 1980 and RCW 74.46.640; amending section 67, chapter 177, Laws of 1980 and RCW

74.46.670; amending section 69, chapter 177, Laws of 1980 and RCW 74.46.690; amending section 71, chapter 177, Laws of 1980 and RCW 74.46.710; amending section 72, chapter 177, Laws of 1980 and RCW 74.46.720; amending section 77, chapter 177, Laws of 1980 and RCW 74.46.770; amending section 78, chapter 177, Laws of 1980 and RCW 74.46.780; amending section 82, chapter 177, Laws of 1980 and RCW 74.46.820; amending section 92, chapter 177, Laws of 1980 and RCW 74.46.840; amending section 74.09.120, chapter 26, Laws of 1959 as last amended by section 6, chapter 11, Laws of 1981 2nd ex. sess. and RCW 74.09.120; amending section 16, chapter 2, Laws of 1981 1st ex. sess. and RCW 18.51.145; amending section 94, chapter 177, Laws of 1980 as amended by section 10, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.901; creating new sections; adding new sections to chapter 74.46 RCW; repealing section 1, chapter 260, Laws of 1977 ex. sess. and RCW 74.09.550; repealing section 2, chapter 260, Laws of 1977 ex. sess. and RCW 74.09.560; repealing section 3, chapter 260, Laws of 1977 ex. sess. and RCW 74.09.570; repealing section 4, chapter 260, Laws of 1977 ex. sess., section 2, chapter 2, Laws of 1981 1st ex. sess., section 7, chapter 11, Laws of 1981 2nd ex. sess. and RCW 74.09.580; repealing section 1, chapter 2, Laws of 1981 1st ex. sess., section 8, chapter 11, Laws of 1981 2nd ex. sess., section 2, chapter 19, Laws of 1982 1st ex. sess., section 1, chapter 1, Laws of 1982 2nd ex. sess. and RCW 74.09.610; repealing section 5, chapter 19, Laws of 1982 1st ex. sess. and RCW 74.09.620; repealing section 7, chapter 177, Laws of 1980, section 3, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.070; repealing section 11, chapter 177, Laws of 1980 and RCW 74.46.110; repealing section 12, chapter 177, Laws of 1980, section 4, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.120; repealing section 14, chapter 177, Laws of 1980 and RCW 74.46.140; repealing section 40, chapter 177, Laws of 1980 and RCW 74.46.400; repealing section 48, chapter 177, Laws of 1980 and RCW 74.46.480; repealing section 81, chapter 177, Laws of 1980, section 8, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.810; repealing section 13, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.850; repealing section 84, chapter 177, Laws of 1980; making appropriations; providing an effective date; providing expiration dates; and declaring an emergency.

Be it enacted by the Legislature of the State of Washington:

Sec. 1. Section 4, chapter 177, Laws of 1980 and RCW 74.46.040 are each amended to read as follows:

(1) Not later than March 31, 1982, and each year thereafter, each contractor shall submit to the department an annual cost report, and such financial statements as are required by this chapter, for the period from January 1st through December 31st of the preceding year.

(2) Not later than one hundred twenty days following the termination of a contract, the contractor shall submit to the department a cost report, and financial statements as are required by this chapter, for the period from January 1st through the date the contract terminated.

(3) Two extensions of not more than thirty days each (~~(after March 31st)~~) may be granted by the department upon receipt of a written request setting forth the circumstances which prohibit the contractor from compliance with (~~(such)~~) a report due date; except, that the secretary shall establish the grounds for extension in rule and regulation. Such request must be received by the department at least ten days prior to the due date.

~~((3) Not later than one hundred and twenty days following the termination of a contract, the contractor shall submit to the department a cost report, and such financial statements as are required by this chapter, for the period from January 1st through the date the contract terminated.))~~

Sec. 2. Section 6, chapter 177, Laws of 1980 and RCW 74.46.060 are each amended to read as follows:

(1) Cost reports shall be prepared in a standard manner and form, as determined (~~((pursuant to RCW 74.46.070))~~) by the department, which shall provide for financial statements, an itemized list of allowable costs, and a preliminary settlement report. Costs reported shall be determined in accordance with generally accepted accounting principles, the provisions of this chapter, and such additional rules and regulations as are established by the secretary.

(2) All financial statements of a contractor must be prepared in accordance with generally accepted accounting principles, (~~((such additional regulatory requirements developed pursuant to RCW 74.46.070))~~) the provisions of this chapter, and such additional rules and regulations as are established by the secretary.

(3) The records shall be maintained on the accrual method of accounting and agree with or be reconcilable to the cost report and the financial statements.

Sec. 3. Section 8, chapter 177, Laws of 1980 and RCW 74.46.080 are each amended to read as follows:

(1) All records supporting the required cost reports and financial statements, as well as trust funds established by RCW 74.46.700, shall be retained by the contractor for a period of four years following the filing of such reports at a location in the state of Washington specified by the contractor. The department may direct such records to be retained for a longer period if there remain unresolved questions on the cost reports and financial statements. All such records shall be made available upon demand to authorized representatives of the department, the office of the state auditor, and the United States department of health(~~((education))~~) and (~~((welfare))~~) human services.

(2) When a contract is terminated, all payments due will be withheld until accessibility and preservation of the records within the state of Washington are assured.

Sec. 4. Section 10, chapter 177, Laws of 1980 and RCW 74.46.100 are each amended to read as follows:

The principles inherent within (~~((RCW 74.46.110 through 74.46.140))~~) section 5 of this 1983 act and RCW 74.46.130 are:

(1) To ascertain, through (~~((certified))~~) department audit, that the costs for each year are accurately reported, thereby providing a valid basis for future rate determination;

(2) To ascertain, through (~~((certified))~~) department audits of the cost reports, that cost reports properly reflect the financial statements of the contractor, particularly as they pertain to related organizations and beneficial ownership, thereby providing a valid basis for the determination of return as specified by this chapter;

(3) To ascertain, through (~~the certified~~) department audit (~~and the oversight of the office of the state auditor;~~) that compliance with the accounting and auditing provisions of this chapter and the rules and regulations of the department as they pertain to these accounting and auditing provisions is proper and consistent; and

(4) To ascertain, through (~~certified~~) department audits, that the responsibility of the contractor has been met in the maintenance of patient trust funds.

NEW SECTION. Sec. 5. There is added to chapter 74.46 RCW a new section to read as follows:

Cost reports, financial and statistical records, and patient trust accounts of contractors shall be field audited by the department, either by department staff or by auditors under contract to the department, in accordance with the provisions of this chapter. The department shall have the authority to accept or reject audits which fail to satisfy the requirements of this section or which are performed by auditors who violate any of the rules of this section. Department audits of the cost reports and patient trust accounts shall be conducted as follows:

(1) Each year the department will provide for field audit of the cost report, financial and statistical reports, and patient trust funds, as established by RCW 74.46.700, of all or a sample of reporting facilities selected by profiles of costs, exceptions, contract terminations, upon special requests or other factors determined by the department.

(2) Beginning with audits for calendar year 1983, up to one hundred percent of contractors cost reports and patient care trust fund accounts shall be audited: PROVIDED, That each contractor shall be audited at least once in every three-year period.

(3) Facilities shall be selected for sample audits within one hundred twenty days of submission of a correct and complete cost report, and shall be so informed of the department's intent to audit. Audits so scheduled shall be completed within one year of selection.

(4) Where an audit for a recent reporting or trust fund period discloses material discrepancies, undocumented costs or mishandling of patient trust funds, auditors may examine prior unaudited periods, for indication of similar material discrepancies, undocumented costs or mishandling of patient trust funds for not more than two reporting periods preceding the facility reporting period selected in the sample.

(5) The audit will result in a schedule summarizing appropriate adjustments to the contractor's cost report. These adjustments will include an explanation for the adjustment, the general ledger account or account group, and the dollar amount. Patient trust fund audits shall be reported separately and in accordance with RCW 74.46.700.

(6) Audits shall meet generally accepted auditing standards as promulgated by the American institute of certified public accountants and the

standards for audit of governmental organizations, programs, activities and functions as published by the comptroller general of the United States. Audits shall be supervised or reviewed by a certified public accountant.

(7) No auditor under contract with or employed by the department to perform audits in accordance with the provisions of this chapter shall:

(a) Have had direct or indirect financial interest in the ownership, financing or operation of a nursing home in this state during the period covered by the audits;

(b) Acquire or commit to acquire any direct or indirect financial interest in the ownership, financing or operation of a nursing home in this state during said auditor's employment or contract with the department;

(c) Accept as a client any nursing home in this state during or within two years of termination of said auditor's contract or employment with the department.

(8) Audits shall be conducted by auditors who are otherwise independent as determined by the standards of independence established by the American institute of certified public accountants.

(9) All audit rules adopted after March 31, 1984, shall be published before the beginning of the cost report year to which they apply.

NEW SECTION. Sec. 6. There is added to chapter 74.46 RCW a new section to read as follows:

The office of the state auditor shall annually review the performance of the department to ensure that departmental audits are conducted in accordance with generally accepted accounting principles and auditing standards.

Sec. 7. Section 13, chapter 177, Laws of 1980 and RCW 74.46.130 are each amended to read as follows:

(1) For the requirements of (~~RCW 74.46.120(1)~~) section 5 of this 1983 act, the contractor shall be notified by the (~~accountant~~) department at least ten working days in advance of the engagement. Upon such notification, the contractor shall:

(a) Provide access to the facility, all records, and all working papers which are in support of the cost report, financial statements, and patient trust funds; and

(b) Prepare reconciliation of the cost report and financial statements with (i) applicable federal income and federal and state payroll tax returns and (ii) the records for the period covered by the cost report and financial statements.

(2) (~~For the requirements of RCW 74.46.120(2), the contractor shall provide access to the facility and supply all records as required in subsection (1) of this section.~~) To facilitate department audit, the owner or administrator of a facility shall designate and make available an individual or individuals to respond to questions and requests for information from auditors.

The designated individual or individuals shall have sufficient knowledge of the issue or function to provide accurate information.

Sec. 8. Section 15, chapter 177, Laws of 1980 and RCW 74.46.150 are each amended to read as follows:

(1) For each cost center, payments to contractors shall not exceed the lower of prospective reimbursement rates or audited allowable costs, except as otherwise provided in this chapter.

(2) The settlement process shall consist of:

(a) The evaluation of the proposed preliminary settlement ((report)) by cost center contained within the cost report and preparation of the preliminary settlement report;

(b) The evaluation of the audit results, if an audit is conducted, including disallowed costs and preparation of the final settlement report; and

(c) The process of scheduling payment ((as to such)) of underpayments or overpayments determined by preliminary or final settlement.

~~((2) In:~~

~~(a) Rulings on questioned costs; or~~

~~(b) Interpretations resulting in payment of the whole or a portion of a disallowed cost;~~

~~the department shall prepare and maintain such rulings and interpretations with full justification and explanation for the respective contractor and the appropriate standing committees of the legislature.)~~

Sec. 9. Section 16, chapter 177, Laws of 1980 and RCW 74.46.160 are each amended to read as follows:

(1) ~~((Upon))~~ Within one hundred twenty days after receipt of the proposed preliminary settlement ((report)), the department shall verify the accuracy of ((such report)) the proposal and shall issue a preliminary settlement report by cost center to the contractor which fully substantiates disallowed costs, refunds, underpayments, or adjustments to the proposed preliminary settlement.

(2) ~~((Within thirty days))~~ After ((receipt)) completion of the ((audited reports by the secretary)) audit process, including exhaustion or mutual termination of reviews and appeals of audit findings or determinations, the department will submit a ((proposed)) final settlement report by cost center to the contractor which ((rules on questioned costs, and)) fully substantiates disallowed costs, refunds, underpayments, ((and/or)) or adjustments to the ((preliminary settlement)) contractor's financial statements and cost report. Where the contractor is pursuing judicial or administrative review or appeal in good faith regarding audit findings or determinations, the department may issue a partial final settlement to recover overpayments based on audit adjustments not in dispute.

Sec. 10. Section 17, chapter 177, Laws of 1980 and RCW 74.46.170 are each amended to read as follows:

(1) ~~((The settlement will become final))~~ A contractor shall have thirty days after the date the ((proposed)) preliminary or final settlement report is submitted to the contractor((, unless the contractor)) to contest((s the)) a settlement determination under RCW 74.46.780. ((In the event of such action, the contractor has thirty days after the date the proposed final settlement report has been submitted to notify the department of such contesting pursuant to the provisions of RCW 74.46.780:)) After the thirty-day period has expired, a preliminary or final settlement will not be subject to review.

(2) A preliminary settlement report as issued by the department will become the final settlement report if no audit has been scheduled within twelve calendar months following the department's issuance of a preliminary settlement report to the contractor.

(3) A settlement will be reopened if necessary to make adjustments for findings resulting from an audit performed pursuant to ((this chapter)) section 5(4) of this 1983 act.

Sec. 11. Section 18, chapter 177, Laws of 1980 and RCW 74.46.180 are each amended to read as follows:

(1) The state shall make payment of any underpayments within ((fifteen)) thirty days ((of)) after the date the preliminary or final settlement ((becomes final)) report is submitted to the contractor.

(2) ~~((The))~~ A contractor found to have received either overpayments ((and/or)) or erroneous payments under a preliminary or final settlement shall refund such payments to the state within thirty days ((of)) after the date the preliminary or final settlement ((becomes final)) report is submitted to the contractor, subject to the provisions of subsections (3), (4)((, and (5))), and (7) of this section.

(3) Within the cost centers of nursing services and food, all savings resulting from the respective ((audited)) allowable costs being lower than the respective reimbursement rate paid to the contractor during the report period shall be refunded. In computing a preliminary or final settlement, savings in a cost center may be shifted to cover a deficit in another cost center up to the amount of any savings: PROVIDED, That not more than twenty percent of the rate in a cost center may be shifted into that cost center and no shifting may be made into the property cost center.

(4) Within the cost centers of administration and operations and property, the contractor shall retain at least fifty percent, but not more than seventy-five percent, of any savings resulting from the respective, audited, allowable costs being lower than the respective reimbursement rates paid to the contractor during the report period multiplied by the number of authorized medical care client days in which said rates were in effect. The secretary, by rule and regulation, shall establish the basis for the specific percentages of savings to the contractors. Such rules and regulations may provide for differences in the percentages allowed for each cost center to

individual facilities based on performance measures related to administrative efficiency.

(5) All allowances provided by section 27(2) of this 1983 act and RCW 74.46.530 shall be retained by the contractor. Any industrial insurance dividend or premium discount under RCW 51.16.035 shall be retained by the contractor to the extent that such dividend or premium discount is attributable to the contractor's private patients.

(6) In the event the contractor fails to make repayment in the time provided in subsection (2) of this section, the department shall either:

(a) Deduct the amount of refund due plus assessment of interest, as determined by the secretary, from payment amounts due the contractor; or

(b) In the instance the contract has been terminated, (i) deduct the amount of refund due plus an assessment of interest, determined by the secretary, from any payments due; or (ii) assess the amount due plus interest, as determined by the secretary, on the amount due.

(7) Where the facility is pursuing timely-filed judicial or administrative remedies in good faith regarding settlement issues, the contractor need not refund nor shall the department (~~shall not~~) withhold from the facility current payment amounts the department claims to be due from the facility but which are specifically disputed by the contractor. If the judicial or administrative remedy sought by the facility is not granted after all appeals are exhausted or mutually terminated, the facility shall make payment of such amounts due plus interest accrued from the date of filing of the appeal, as payable on judgments, within sixty days of the date such decision is made.

Sec. 12. Section 19, chapter 177, Laws of 1980 and RCW 74.46.190 are each amended to read as follows:

(1) The substance of a transaction will prevail over its form.

(2) All documented costs which are ordinary, necessary, related to care of medical care recipients, and not expressly (~~nonallowable~~) unallowable, are to be allowable.

(3) Costs applicable to services, facilities, and supplies furnished to the provider by related organizations are allowable but at the cost to the related organization, provided they do not exceed the price of comparable services, facilities, or supplies that could be purchased elsewhere.

(4) Beginning January 1, 1985, the payment for property usage is to be independent of ownership structure and financing arrangements.

Sec. 13. Section 27, chapter 177, Laws of 1980 and RCW 74.46.270 are each amended to read as follows:

(1) The contractor shall disclose to the department:

(a) The nature and purpose of all costs which represent allocations of joint facility costs; and

(b) The methodology of the allocation utilized.

(2) Such disclosure shall demonstrate that:



(a) The services involved are necessary and nonduplicative; and

(b) Costs are allocated in accordance with benefits received from the resources represented by those costs.

(3) Such disclosure shall be made not later than September 30, 1980, for the following year and not later than September 30th for each year thereafter; except that a new contractor shall submit the first year's disclosure together with the submissions required by RCW 74.46.670. Where a contractor will make neither a change in the joint costs to be incurred nor in the allocation methodology, the contractor may certify that no change will be made in lieu of the disclosure required in subsection (1) of this section.

~~((3)) (4) The department shall approve such methodology not later than December 31, 1980, and not later than December 31st for each year thereafter. ((Such approval shall include, but not be limited to, the assurance that:~~

~~(a) The services involved are necessary and nonduplicative; and~~

~~(b) Costs are allocated in accordance with benefits received from the resources represented by those costs.~~

~~(4)) (5) An approved methodology may be revised or amended subject to approval as provided in ((subsection (3) of this section and)) rules and regulations adopted by the department.~~

NEW SECTION. Sec. 14. There is added to chapter 74.46 RCW a new section to read as follows:

(1) This section shall cease to be effective on the effective date of RCW 74.46.530.

(2) The contractor's necessary and ordinary interest for working capital and capital indebtedness will be allowable.

(a) To be necessary, interest must be incurred in connection with a loan which satisfies a financial need of the contractor and be for a purpose related to patient care. Interest expense relating to business opportunity or goodwill will not be allowed.

(b) To be ordinary, interest must be at a rate which is not in excess of what a prudent borrower would have to pay at the time of the loan in an arm's-length transaction in the money market.

(c) Interest expense shall include amortization of bond discounts and expenses related to the bond issue. Amortization shall be over the period from the date of sale to the date of maturity or, if earlier, the date of extinguishment of the bonds.

(3) Interest paid to or for the benefit of a related organization will be allowed only to the extent the interest does not exceed the actual cost to the related organization of obtaining the use of funds in an arm's-length transaction.

(4) In computing allowable costs, interest income from the investment or lending of nonrestricted funds shall be deducted from allowable expense.

(5) Interest income from the investment or lending of restricted funds shall not be deducted from allowable interest expense.

NEW SECTION. Sec. 15. There is added to chapter 74.46 RCW a new section to read as follows:

(1) This section shall cease to be effective on the effective date of RCW 74.46.510 and 74.46.530.

(2) Rental or lease costs of land, building or equipment under arm's-length operating leases or depreciation and interest costs of land, building or equipment under arm's-length leases to be capitalized according to generally accepted accounting principles shall be allowable, to the extent the cost is necessary, ordinary, and related to patient care.

Sec. 16. Section 31, chapter 177, Laws of 1980 and RCW 74.46.310 are each amended to read as follows:

The following costs shall be capitalized:

(1) Expenses for facilities or equipment with historical cost in excess of ~~((five))~~ seven hundred fifty dollars per unit and a useful life of more than one year from the date of purchase; and

(2) Expenses for equipment with historical cost of ~~((five))~~ seven hundred fifty dollars or less per unit if either:

(a) The item was acquired in a group purchase where the total cost exceeded ~~((five))~~ seven hundred fifty dollars; or

(b) The item was part of the initial stock of the facility.

(3) Dollar limits in this section may be adjusted for economic trends and conditions by the department as established by rule and regulation.

Sec. 17. Section 41, chapter 177, Laws of 1980 and RCW 74.46.410 are each amended to read as follows:

(1) Costs will be unallowable if they are not documented, necessary, ordinary, and related to the provision of care services to authorized patients.

(2) Unallowable costs include, but are not limited to, the following:

(a) Costs of items or services not covered by the medical care program. Costs of such items or services will be unallowable even if they are indirectly reimbursed by the department as the result of an authorized reduction in patient contribution;

(b) Costs of services and items provided to recipients which are covered by the department's medical care program but not included in care services established by the department under this ~~((act))~~ chapter;

(c) Costs associated with a capital expenditure subject to section 1122 approval (part 100, Title 42 C.F.R.) if the department found it was not consistent with applicable standards, criteria, or plans. If the department was not given timely notice of a proposed capital expenditure, all associated costs will be unallowable up to the date they are determined to be reimbursable under applicable federal regulations;

(d) Costs associated with a construction or acquisition project requiring certificate of need approval pursuant to chapter 70.38 RCW if such approval was not obtained;

(e) Interest costs other than those provided by RCW 74.46.290 on and after the effective date of RCW 74.46.530;

(f) Salaries or other compensation of owners, officers, directors, stockholders, and others associated with the contractor or home office, except compensation paid for service related to patient care;

(g) Costs in excess of limits or (~~violating~~) in violation of principles set forth in this chapter;

(h) Costs resulting from transactions or the application of accounting methods which circumvent the principles of the cost-related reimbursement system set forth in this chapter;

(i) Costs applicable to services, facilities, and supplies furnished by a related organization in excess of the lower of the cost to the related organization or the price of comparable services, facilities, or supplies purchased elsewhere;

(j) Bad debts of non-Title XIX recipients. Bad debts of Title XIX recipients are allowable if the debt is related to covered services, it arises from the recipient's required contribution toward the cost of care, the provider can establish that reasonable collection efforts were made, the debt was actually uncollectible when claimed as worthless, and sound business judgment established that there was no likelihood of recovery at any time in the future;

(k) Charity and courtesy allowances;

(l) Cash, assessments, or other contributions, excluding dues, to charitable organizations, professional organizations, trade associations, or political parties, and costs incurred to improve community or public relations;

(m) Vending machine expenses;

(n) Expenses for barber or beautician services not included in routine care;

(o) Funeral and burial expenses;

(p) Costs of gift shop operations and inventory;

(q) Personal items such as cosmetics, smoking materials, newspapers and magazines, and clothing, except those used in patient activity programs;

(r) Fund-raising expenses, except those directly related to the patient activity program;

(s) Penalties and fines;

(t) Expenses related to telephones, televisions, radios, and similar appliances in patients' private accommodations;

(u) Federal, state, and other income taxes;

(v) Costs of special care services except where authorized by the department;

(w) Expenses of key-man insurance and other insurance or retirement plans not made available to all employees;

(x) Expenses of profit-sharing plans;

(y) Expenses related to the purchase and/or use of private or commercial airplanes which are in excess of what a prudent contractor would expend for the ordinary and economic provision of such a transportation need related to patient care;

(z) Personal expenses and allowances of owners or relatives;

(aa) All expenses of maintaining professional licenses or membership in professional organizations and association dues or that portion of association dues attributable to membership in national organizations;

(bb) Costs related to agreements not to compete;

(cc) Amortization of goodwill;

(dd) Expenses related to vehicles which are in excess of what a prudent contractor would expend for the ordinary and economic provision of transportation needs related to patient care;

(ee) Legal and consultant fees in connection with a fair hearing against the department where a decision is rendered in favor of the department or where otherwise the determination of the department stands;

(ff) Legal and consultant fees of a contractor or contractors in connection with a lawsuit against the department;

(gg) Lease acquisition costs and other intangibles not related to patient care;

(hh) All rental or lease costs other than those provided in RCW 74.46.300(~~;~~and

~~(ii) All audit costs incurred pursuant to RCW 74.46.120(1))~~ on and after the effective date of RCW 74.46.510 and 74.46.530.

Sec. 18. Section 42, chapter 177, Laws of 1980 and RCW 74.46.420 are each amended to read as follows:

The following principles are inherent in RCW 74.46.430 through 74.46.590:

(1) Reimbursement rates will be set prospectively on a per patient day basis;

(2) Rates (~~(will be)~~) established (~~((not lower than the level which is reasonably expected to be))~~) in accordance with this chapter shall be reasonable and adequate to ((reimburse in full the actual, allowable)) meet the costs ((of a facility which is)) that must be incurred by economically and efficiently operated ((and)) facilities to provide ((care)) services which meet((s)) the needs of a medical care recipient in compliance with applicable standards; and

(3) The rates so established will (~~(take into account))~~ be adjusted for economic conditions and trends ((during)) in accordance with appropriations made by the legislature as consistent with federal requirements for the period to be covered by such rates.

Sec. 19. Section 43, chapter 177, Laws of 1980 and RCW 74.46.430 are each amended to read as follows:

(1) The department, as provided by this chapter, will determine prospective cost-related reimbursement rates for services provided to medical care recipients. Each rate so determined shall represent the contractor's maximum compensation within each cost center for each patient day for such medical care recipient.

(2) As required, the department may modify such maximum per patient day rates pursuant to the administrative review provisions of RCW 74.46.780.

(3) Until the effective date of RCW 74.46.510 and 74.46.530, the maximum prospective reimbursement rates for the administration and operations and the property cost centers shall be established based upon a minimum facility occupancy level of eighty-five percent.

(4) On and after the effective date of RCW 74.46.510 and 74.46.530, the maximum prospective reimbursement rates for the administration and operations and the property cost centers and the return on investment allowance shall be established based upon a minimum facility occupancy level of eighty-five percent.

Sec. 20. Section 45, chapter 177, Laws of 1980 and RCW 74.46.450 are each amended to read as follows:

(1) Prospective reimbursement rates for a new contractor will be established within sixty days following receipt by the department of the properly completed projected budget required by RCW 74.46.670. Such reimbursement rates will become effective as of the effective date of the contract and shall remain in effect until rates can be established under RCW 74.46.460 based on a contractor's cost report including at least six months of cost data.

(2) Such reimbursement rates will be based on the contractor's projected cost of operations (~~((through December 31st of the year the contract becomes effective,))~~) and on costs and payment rates of the prior contractor, if any, ~~((and/or))~~ or of other contractors in comparable circumstances.

(3) If a properly completed budget is not received at least sixty days prior to the effective date of the contract, the department will establish preliminary rates based on the other factors specified in subsection (2) of this section. These preliminary rates will remain in effect until a determination is made pursuant to RCW 74.46.460.

Sec. 21. Section 46, chapter 177, Laws of 1980 as amended by section 5, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.460 are each amended to read as follows:

(1) Each contractor's reimbursement rates will be determined prospectively at least once each calendar year, to be effective July 1st.

(2) Rates may be adjusted as determined by the department to take into account variations of more than ten percent in the distribution of patient

classifications or changes in patient characteristics from the prior reporting year, program changes, changes in staffing levels at a facility required by the department, economic trends and conditions, and/or administrative review provided by RCW 74.46.780 and shall be adjusted for any capitalized additions or replacements made as a condition for licensure or certification.

(3) Where the contractor participated in the provisions of prospective cost-related reimbursement in effect prior to July 1, ((+1984)) 1983, such contractor's prospective rate effective July 1, ((+1984)) 1983, will be determined utilizing ((his reported)) the contractor's desk-reviewed allowable costs for calendar year ((+1983)) 1982.

(4) All prospective reimbursement rates for ((+1985)) 1984 and thereafter shall be determined utilizing the prior year's ((audited)) desk-reviewed cost reports.

Sec. 22. Section 47, chapter 177, Laws of 1980 and RCW 74.46.470 are each amended to read as follows:

A contractor's reimbursement rates for medical care recipients will be determined utilizing ((audited)) desk-reviewed cost report data within the following cost centers:

- (1) Nursing services;
- (2) Food;
- (3) Administration and operations; and
- (4) Property.

NEW SECTION. Sec. 23. There is added to chapter 74.46 RCW a new section to read as follows:

(1) The department shall analyze the submitted cost report and financial statements of each contractor to determine if the information is correct, complete, and reported in conformance with generally accepted accounting principles, the requirements of this chapter and such rules and regulations as the secretary may adopt. If the analysis finds that the cost report or financial statements are incorrect or incomplete, the department may make adjustments to the reported information for purposes of establishing reimbursement rates. A schedule of such adjustments shall be provided to contractors and shall include an explanation for the adjustment and the dollar amount of the adjustment. Adjustments shall be subject to review and appeal as provided in this chapter.

(2) The department shall accumulate data from properly completed cost reports and financial statements for use in:

- (a) Exception profiling; and
- (b) Establishing rates.

(3) The department may further utilize such accumulated data for analytical, statistical, or informational purposes as necessary.

NEW SECTION. Sec. 24. There is added to chapter 74.46 RCW a new section to read as follows:

(1) The nursing services cost center shall include all costs related to the direct provision of nursing and related care, including fringe benefits and payroll taxes for the nursing and related care personnel. For rates effective for state fiscal year 1984, the department shall adopt by administrative rule a definition of "related care" which shall incorporate, but not exceed services reimbursable as of June 30, 1983. For rates effective for state fiscal year 1985, the definition of related care shall include ancillary care.

(2) The department shall adopt by administrative rules a method for establishing a nursing services cost center rate consistent with the principles stated in this section.

(3) Utilizing regression or other statistical technique, the department shall determine a reasonable limit on facility nursing staff taking into account facility patient characteristics. For purposes of this section, facility nursing staff refers to registered nurses, licensed practical nurses and nursing assistants employed by the facility or obtained through temporary labor contract arrangements. In selecting a measure of patient characteristics, the department shall take into account:

(a) The correlation between alternative measures and facility nursing staff; and

(b) The cost of collecting information for and computation of a measure.

If regression is used, the limit shall be set at predicted nursing staff plus 1.75 regression standard errors. If another statistical method is utilized, the limit shall be set at a level corresponding to 1.75 standard errors above predicted staffing computed according to a regression procedure.

(4) No facility shall receive reimbursement for nursing staff levels in excess of the limit, except that, if a facility was reimbursed for a nursing staff level in excess of the limit as of June 30, 1983, the facility may choose to continue to receive its June, 1983 nursing services rate plus any adjustments in rates, such as adjustments for economic trends, made available to all facilities. The reasonableness limit established pursuant to this subsection shall remain in effect for the period July 1, 1983 through June 30, 1985. At that time the department may revise the measure of patient characteristics or method used to establish the limit.

(5) The department shall select an index of cost increase relevant to the nursing and related services cost area. In the absence of a more representative index, the department shall use the medical care component index as maintained by the United States bureau of labor statistics.

(6) If a facility's nursing staff level is below the limit specified in subsection (3) of this section, the department shall determine the percentage increase for all items included in the nursing services cost center between the facility's most recent cost reporting period and the next prior cost reporting period.

(a) If the percentage cost increase for a facility is below the increase in the selected index for the same time period, the facility's reimbursement rate in the nursing services cost center shall equal the facility's cost from the most recent cost reporting period plus any allowance for inflation provided by legislative appropriation.

(b) If the percentage cost increase for a facility exceeds the increase in the selected index, the department shall limit the cost used for setting the facility's rate in the nursing services cost area to a level reflecting the increase in the selected index.

(7) If the facility's nursing staff level exceeds the reasonableness limit established in subsection (3) of this section, the department shall determine the increase for all items included in the nursing services cost center between the facility's most recent cost reporting period and the next prior cost reporting period.

(a) If the percentage cost increase for a facility is below the increase in the index selected pursuant to subsection (5) of this section, the facility's reimbursement rate in the nursing cost center shall equal the facility's cost from the most recent cost reporting period adjusted downward to reflect the limit on nursing staff, plus any allowance for inflation provided by legislative appropriation subject to the provisions of subsection (4) of this section.

(b) If the percentage cost increase for a facility exceeds the increase in the selected index, the department shall limit the cost used for setting the facility's rate in the nursing services cost center to a level reflecting the nursing staff limit and the cost increase limit, subject to the provisions of subsection (4) of this section, plus any allowance for inflation provided by legislative appropriation.

(8) The department is authorized to determine on a systematic basis facilities with unmet patient care service needs. The department may increase the nursing services cost center prospective rate for a facility beyond the level determined in accordance with subsection (6) of this section if the facility's actual and reported nursing staffing is one standard error or more below predicted staffing as determined according to the method selected pursuant to subsection (3) of this section and the facility has unmet patient care service needs: PROVIDED, That prospective rate increases authorized by this subsection shall be funded only from legislative appropriations made for this purpose and the increases shall be conditioned on specified improvements in patient care at such facilities.

(9) The department shall establish a method for identifying patients with exceptional care requirements and a method for establishing or negotiating on a consistent basis rates for such patients.

Sec. 25. Section 49, chapter 177, Laws of 1980 as amended by section 6, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.490 are each amended to read as follows:



(1) The food cost center shall include all costs for bulk and raw food and beverages purchased for the dietary needs of medical care recipients.

~~(2) ((The food cost reimbursement rate for each facility shall be computed as follows:~~

~~FR = (TFC/TPD) 1.15, where~~

~~FR = the facility food cost center reimbursement rate;~~

~~TFC = the total of all reporting facilities' food cost center costs; and~~

~~TPD = the total patient days for the prior year of all reporting facilities.~~

~~(3) Unless extended by law for an additional period of time, on and after July 1, 1986, the food cost reimbursement rate for each facility shall be computed as follows:~~

~~FR = (TFC/TPD), where~~

~~FR = the facility food cost center reimbursement rate;~~

~~TFC = the total of all reporting facilities' food cost center costs; and~~

~~TPD = the total patient days for the prior year of all reporting facilities.))~~

Reimbursement for the food cost center shall be at the January 1, 1983, reimbursement rate, adjusted annually for inflation.

NEW SECTION. Sec. 26. There is added to chapter 74.46 RCW a new section to read as follows:

(1) References in RCW 74.46.490 and section 24 of this act to adjustments for inflation mean percentages determined by the legislature in the biennial budget act.

(2) Inflation adjustments shall be applied as follows:

(a) Where a prior period rate forms the basis for the next period rate, the adjustment in subsection (1) of this section shall be applied to that prior period rate.

(b) In the nursing services cost center rates beginning July 1, 1984, and the administration and operations cost center rate, the adjustments in subsection (1) of this section shall be applied to prior period annual costs in establishing July rates. Where a July rate is based upon a cost report covering less than twelve months, the department shall reduce the inflation adjustment factor in subsection (1) of this section proportionately.

NEW SECTION. Sec. 27. There is added to chapter 74.46 RCW a new section to read as follows:

(1) This section shall apply for rate setting beginning July 1, 1983, and shall cease to be effective on December 31, 1984.

(2) The department shall pay a return on net equity, as defined in federal medicare rules and regulations, at the annual rate of twelve percent, except that this return shall not exceed two dollars per patient day.

(3) Property cost center reimbursement for both leased and owner-operated facilities shall not exceed the predicted cost plus 1.75 standard deviation of the necessary and ordinary prior period allowable annual cost report costs of depreciation, and interest, of owner-operated facilities utilizing a multiple regression formula developed by the department of social and

health services, recognizing factors which may be significant, including location, age, and type of facility. Rental costs of leased facilities and depreciation and interest costs of owner-operated facilities, for leases or mortgages entered into prior to July 1, 1979, shall be reimbursed to the extent they do not exceed the reimbursement rate payable for the property cost center as of June 30, 1979, adjusted to meet any discrepancies as determined by the federal government between the reimbursements made and the approved state medicaid plan, the reimbursement rate payable July 1, 1979 or the regression formula rate, whichever is higher, and adjusted for any approved capitalized additions or replacements.

Sec. 28. Section 53, chapter 177, Laws of 1980 as amended by section 7, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.530 are each amended to read as follows:

(1) ~~((The department shall first establish a total state-wide return on investment pool for use in determining individual facility return on investment allowances:~~

(a) ~~In establishing the total state-wide return on investment pool the department shall determine the sum of net invested funds as of the end of the most recent reporting period of all facilities participating in the medical care program:~~

(b) ~~In computing the portion of net invested funds representing the net book value of tangible fixed assets, the same assets, depreciation bases, lives, and methods referred to in RCW 74.46.330, 74.46.350, 74.46.360, and 74.46.370, including owned and leased assets, shall be utilized, except that the capitalized cost of land upon which the facility is located and such other contiguous land which is reasonable and necessary for use in the regular course of providing patient care shall also be included. In the case of leased facilities where the net invested funds are unknown or the contractor is unable to provide necessary information to determine net invested funds, the secretary shall have the authority to determine an amount for net invested funds based on an appraisal conducted according to RCW 74.46.360(1):~~

(c) ~~The sum of net invested funds shall then be multiplied by 1.4 times the average of the rates of interest on special issues of public debt obligations issued to the federal hospital insurance trust fund for the last completed calendar quarter prior to rate-setting to establish the total state-wide return on investment pool:~~

(2)) The department shall establish for individual facilities return on investment allowances composed of two parts: A financing allowance and a variable return allowance.

(a) The financing allowance shall be determined by multiplying the net invested funds of each facility by ~~((1.07 times the average of the rates of interest on special issues of public debt obligations issued to the federal hospital insurance trust fund for the last completed quarter prior to rate=~~

setting)) .11, and dividing by the contractor's total patient days. If a capitalized addition or retirement of an asset will result in a different licensed bed capacity during the ensuing period, the prior period total patient days used in computing the financing and variable return allowances shall be adjusted to the anticipated patient day level.

(b) In computing the portion of net invested funds representing the net book value of tangible fixed assets, the same assets, depreciation bases, lives, and methods referred to in RCW 74.46.330, 74.46.350, 74.46.360, and 74.46.370, including owned and leased assets, shall be utilized, except that the capitalized cost of land upon which the facility is located and such other contiguous land which is reasonable and necessary for use in the regular course of providing patient care shall also be included. In the case of leased facilities where the net invested funds are unknown or the contractor is unable to provide necessary information to determine net invested funds, the secretary shall have the authority to determine an amount for net invested funds based on an appraisal conducted according to RCW 74.46.360(1).

(c) In determining the variable return allowance:

(i) The department will first rank all facilities in numerical order from highest to lowest according to their average per diem allowable costs for the sum of the administration and operations and property cost centers for the previous ~~((reimbursement))~~ cost report period.

(ii) The department shall then compute the variable return allowance by multiplying the appropriate percentage amounts, which shall not be less than one percent and not greater than ~~((five))~~ four percent, by the total prospective rate for each facility, as determined in RCW 74.46.450 through 74.46.510. The percentage amounts will be based on groupings of facilities according to the rankings as established in subparagraph (2)(b)(i) of this section. Those groups of facilities with lower per diem costs shall receive higher percentage amounts than those with higher per diem costs.

~~((iii)) Such percentage amounts shall be calculated so that the variable return allowance plus the financing allowance times the total patient days for each facility, when summed for all facilities, shall be as close in amount to the total state-wide return on investment pool as is practical, except that, such percentage amounts for equivalent groups of facilities as determined in subparagraph (2)(b)(ii) of this section shall be no less than the percentage amounts as calculated pursuant to this subsection on July 1, 1984.~~

~~((c))~~ (d) The sum of the financing allowance and the variable return allowance shall be the return on investment for each facility, and shall be added to the prospective rates of each contractor as determined in RCW 74.46.450 through 74.46.510.

~~((d))~~ (e) In the case of a facility which was leased by the contractor as of January 1, 1980, in an arm's-length agreement, which continues to be leased under the same lease agreement, and for which the annualized lease

payment, plus any interest and depreciation expenses associated with contractor-owned assets, for the period covered by the prospective rates, divided by the contractor's total patient days, minus the property cost center determined according to RCW 74.46.510, is more than the return on investment allowance determined according to ~~((RCW 74.46.530(2)(c)))~~ subsection (1)(d) of this section, the following shall apply:

(i) The financing allowance shall be recomputed substituting the fair market value of the assets as of January 1, 1982, as determined by the department of general administration through an appraisal procedure, for the net book value of the assets in determining net invested funds for the facility. A determination by the department of general administration of fair market value shall be final unless the procedure used to make such determination is shown to be arbitrary and capricious.

(ii) The sum of the financing allowance computed under ~~((subparagraph (2)(d)(i)))~~ subsection (1)(c)(i) of this section and the variable allowance shall be compared to the annualized lease payment, plus any interest and depreciation expenses associated with contractor-owned assets, for the period covered by the prospective rates, divided by the contractor's total patient days, minus the property cost center rate determined according to RCW 74.46.510. The lesser of the two amounts shall be called the alternate return on investment allowance.

(iii) The return on investment allowance determined according to ~~((RCW 74.46.530(2)(c)))~~ subsection (1)(d) of this section or the alternate return on investment allowance, whichever is greater, shall be the return on investment allowance for the facility and shall be added to the prospective rates of the contractor as determined in RCW 74.46.450 through 74.46.510.

~~((3))~~ (2) In the event that the department of health ~~((education))~~ and ~~((welfare))~~ human services disallows the application of the return on investment allowances to nonprofit facilities, the department shall modify the measurements of net invested funds used for computing ~~((both total state-wide return on investment pool and))~~ individual facility return on investment allowances as follows: Net invested funds for each nonprofit facility shall be multiplied by one minus the ratio of equity funds to the net invested funds of all nonprofit facilities.

~~((4))~~ (3) Each biennium, beginning in ~~((1984))~~ 1985, the secretary shall review the adequacy of return on investment allowances in relation to anticipated requirements for maintaining, reducing, or expanding nursing care capacity. The secretary shall report the results of such review to the legislature and make recommendations for adjustments in the return on investment rates utilized in this section, if appropriate.

Sec. 29. Section 55, chapter 177, Laws of 1980 and RCW 74.46.550 are each amended to read as follows:

~~((1))~~ The reimbursement rates shall not exceed the contractor's customary charges to the general public for comparable services.

~~((2) Rates shall not exceed the limits set forth in 42 CFR 450.30(b)(6).))~~

Sec. 30. Section 56, chapter 177, Laws of 1980 and RCW 74.46.560 are each amended to read as follows:

The department will notify each contractor in writing of its prospective reimbursement rates ~~((at least thirty days in advance of))~~ by the effective date of the rates. Unless otherwise specified at the time it is issued, the rate will be effective from the first day of the month in which it is issued until a new rate becomes effective. If a rate is changed as the result of an appeal in accordance with RCW 74.46.780, it will be effective as of the date the appealed rate became effective.

Sec. 31. Section 57, chapter 177, Laws of 1980 and RCW 74.46.570 are each amended to read as follows:

(1) Prospective rates are subject to adjustment by the department as a result of errors or omissions by the department or by the contractor. The department will notify the contractor in writing of each adjustment and of ~~((its))~~ the effective date of the adjustment, and of any amount due to the department or to the contractor as a result of the rate adjustment.

(2) If a contractor claims an error or omission based upon incorrect cost reporting, amended cost report pages shall be prepared and submitted by the contractor. Amended pages shall be accompanied by a certification signed by the licensed administrator of the nursing facility and a written justification explaining why the amendment is necessary. The certification and justification shall meet such criteria as are adopted by the department. Such amendments may be used to revise a prospective rate but shall not be used to revise a settlement if submitted after commencement of the field audit. All changes determined to be material by the department shall be subject to field audit. If changes are found to be incorrect or otherwise unacceptable, any rate adjustment based thereon shall be null and void and resulting payments or payment increases shall be subject to refund.

(3) The contractor shall pay an amount ~~((it owes))~~ owed the department resulting from an error or omission, or commence repayment in accordance with a schedule determined by the department, within sixty days after receipt of notification of the rate adjustment, unless the contractor contests the department's determination in accordance with the procedures set forth in RCW 74.46.780. If the determination is contested, the contractor shall pay or commence repayment within sixty days after completion of these proceedings. If a refund is not paid when due, the amount thereof may be deducted from current payments by the department.

~~((3))~~ (4) The department shall pay any amount ~~((it owes))~~ owed the contractor as a result of a rate adjustment within thirty days after ~~((it notifies))~~ the contractor is notified of the rate adjustment.

~~((4))~~ (5) No adjustments will be made to a rate more than one hundred twenty days after the final ~~((settlement))~~ audit narrative and summary

for the period the rate was effective is sent to the contractor or, if no audit is held, more than one hundred twenty days after the preliminary settlement becomes the final settlement, except when a settlement is reopened as provided in RCW 74.46.170((2))(3).

Sec. 32. Section 58, chapter 177, Laws of 1980 and RCW 74.46.580 are each amended to read as follows:

The department shall provide all interested members of the public with an opportunity to review and comment on the proposed rate-setting factors, indices, measures, and guidelines ~~((not later than May 15th of each year prior to their being used to set rates))~~, consistent with federal requirements.

Sec. 33. Section 61, chapter 177, Laws of 1980 and RCW 74.46.610 are each amended to read as follows:

(1) A contractor shall bill the department each month by completing and returning a facility billing statement as provided by the department which shall include, but not be limited to:

- (a) Billing by cost center;
- (b) Total patient days; and
- (c) Patient days for medical care recipients.

The statement shall be completed and filed in accordance with rules and regulations established by the secretary.

(2) A ~~((contractor))~~ facility shall not bill the department for service provided to a recipient until an award letter of eligibility of such recipient ~~((pursuant to))~~ under rules ~~((and regulations))~~ established ~~((according to the provisions of))~~ under chapter 74.09 RCW has been received by the ~~((contractor except that, a contractor))~~ facility. However a facility may bill and shall be reimbursed for all medical care recipients referred to the ((contractor's)) facility by the department prior to the receipt of the award letter of eligibility or the denial of such eligibility. ((At that time it may bill for service provided back through the date the recipient was admitted or became eligible:))

- (3) Billing shall cover the patient days of care.

Sec. 34. Section 64, chapter 177, Laws of 1980 and RCW 74.46.640 are each amended to read as follows:

(1) Payments to a contractor may be withheld by the department in each of the following circumstances:

(a) A required report is not properly completed and filed by the contractor within the appropriate time period, including any approved extension. Payments will be released as soon as a properly completed report is received;

(b) State auditors, department auditors, or authorized personnel in the course of their duties are refused access to a nursing home or are not provided with existing appropriate records. Payments will be released as soon as such access or records are provided;

(c) A refund in connection with ~~((an annual))~~ a settlement or rate adjustment is not paid by the contractor when due. The amount withheld will be limited to the unpaid amount of the refund; and

(d) Payment for the final thirty days of service under a contract will be held pending final settlement when the contract is terminated.

(2) No payment will be withheld until written notification of the suspension is provided to the contractor, stating the reason therefor.

Sec. 35. Section 67, chapter 177, Laws of 1980 and RCW 74.46.670 are each amended to read as follows:

(1) Each new contractor shall submit a projected budget to the department at least sixty days before its contract will become effective.

(2) The projected budget shall cover the ~~((period to December 31st))~~ contractor's first twelve months of operation from the date the contractor will enter the program. It shall be prepared on forms and in accordance with rules and regulations established by the secretary.

Sec. 36. Section 69, chapter 177, Laws of 1980 and RCW 74.46.690 are each amended to read as follows:

(1) When a facility contract is terminated for any reason, the old contractor shall submit final reports as required by RCW 74.46.040. Payment for care provided during the final thirty days of service under a contract will be held until the contractor has filed a properly completed final ~~((audited))~~ cost report, an audit has been completed by the department, and final settlement has been determined, such settlement not to exceed ((sixty)) ninety days following ~~((submittal of the final audited cost report))~~ completion of the audit process.

(2) Following final settlement, a payment withheld pursuant to subsection (1) of this section will be sent to the contractor after any overpayment determined in connection with final settlement has been deducted. If the contractor contests the settlement determination in accordance with RCW 74.46.170, the department will hold the amount in dispute pending completion of the appeal process, but will release the balance of such payment to the contractor.

(3) The department will release a payment which would be withheld pursuant to subsection (1) of this section, provided a bond issued by a bonding company acceptable to the department is filed by the contractor. The bond shall:

(a) Be in an amount equal to the released payment;

(b) Be for a term sufficient to ensure effectiveness after final settlement and the exhaustion of administrative and judicial remedies;

(c) Provide that the full amount of the bond shall be paid to the department if a properly completed final audited cost report is not filed in accordance with this chapter, or if financial records supporting this record are not preserved and made available to the auditor; and

(d) Provide that an amount equal to any recovery the department determines is due from the contractor at settlement, but not exceeding the amount of the bond, shall be paid to the department in the event the contractor does not pay the refund within sixty days following receipt of written demand or the conclusion of administrative or judicial proceedings to contest settlement issues.

(4) If a contract is terminated solely in order for the same owner to contract with the department to deliver services to another classification of medical care recipients at the same facility, the contractor is not required to submit final cost reports, and payment for the final thirty days will not be withheld.

Sec. 37. Section 71, chapter 177, Laws of 1980 and RCW 74.46.710 are each amended to read as follows:

(1) The contractor shall maintain a subsidiary ledger with an account for each recipient for whom the contractor has money in trust.

(2) Each account and related supporting records shall:

(a) Be kept current;

(b) Be balanced each month; and

(c) Show in detail, with supporting verification, all moneys received on behalf of the recipient and the disposition of all moneys so received.

(3) Records of each account shall be available for audit pursuant to (~~RCW 74.46.140~~) section 5 of this 1983 act and shall be retained for a minimum of four years. When an account has attained the maximum limit established by rules and regulations promulgated by the secretary, the contractor will notify the department within five days.

(4) Any charge for medical services otherwise properly made to a recipient's trust account must be supported by a written denial of such services from the department.

Sec. 38. Section 72, chapter 177, Laws of 1980 and RCW 74.46.720 are each amended to read as follows:

(1) The contractor may maintain a petty cash fund originating from trust moneys of an amount determined by the department which shall be reasonable and necessary for the size of a facility and the needs of the recipients.

(2) Such petty cash fund shall be maintained as an imprest fund. All moneys over and above the trust fund petty cash amount shall be deposited intact, within twenty-four hours, in a trust fund checking account, separate and apart from any other bank account or accounts of the facility or other facilities.

(3) Cash deposits of recipient allowances from any source must be made intact to the trust account within one week from the time that payment of such allowances are received.



(4) Any related bankbooks, bank statements, checkbook, check register, and all voided and canceled checks, shall be made available for audit pursuant to ~~((RCW 74.46.140))~~ section 5 of this 1983 act and shall be retained by the facility for not less than four years.

(5) No service charges for such checking account shall be paid from recipient trust moneys.

(6) The trust account per bank shall be reconciled monthly to the trust account per patient ledgers.

Sec. 39. Section 77, chapter 177, Laws of 1980 and RCW 74.46.770 are each amended to read as follows:

~~((f(1)))~~ (1) If a contractor wishes to contest the way in which a rule or contract provision relating to the prospective cost-related reimbursement system was applied to the contractor by the department, it shall first pursue the administrative review process set forth in RCW 74.46.780.

(2) The administrative review and fair hearing process in RCW 74.46.780 need not be exhausted if a contractor wishes to challenge the legal validity of a statute, rule, or contract provision.

Sec. 40. Section 78, chapter 177, Laws of 1980 and RCW 74.46.780 are each amended to read as follows:

(1) Within thirty days after a contractor is notified of an action or determination it wishes to challenge, the contractor shall request in writing that the secretary review such determination. The request shall be signed by the contractor or the licensed administrator of the facility, shall identify the challenged determination and the date thereof, and shall state as specifically as practicable the grounds for its contention that the determination was erroneous. Copies of any documentation on which the contractor intends to rely to support its position shall be included with the request.

(2) After receiving a request meeting the above criteria, the secretary or his designee will contact the contractor to schedule a conference for the earliest mutually convenient time. The conference shall be scheduled for no later than ~~((thirty))~~ ninety days after a properly completed request is received unless both parties agree in writing to a specified later date.

(3) The contractor and appropriate representatives of the department shall attend the conference. In addition, representatives selected by the contractor may attend and participate. The contractor shall ~~((bring to the conference, or))~~ provide to the department in advance of the conference ~~((;))~~ any documentation on which it intends to rely to support its contentions. The parties shall clarify and attempt to resolve the issues at the conference. If additional documentation is needed to resolve the issues, a second session of the conference shall be scheduled for not later than thirty days after the initial session unless both parties agree in writing to a specific later date.

(4) A written decision by the secretary will be furnished to the contractor within ~~((thirty))~~ sixty days after the conclusion of the conference. ~~((The~~

~~secretary shall prepare such decision for the fiscal and other appropriate standing committees of the legislature.))~~

(5) If the contractor desires review of an adverse decision of the secretary, it shall within thirty days following receipt of such decision request a fair hearing in writing in accordance with the provisions of chapter 34.04 RCW. A request for fair hearing shall satisfy the criteria for a review request as set forth in subsection (1) of this section.

Sec. 41. Section 82, chapter 177, Laws of 1980 and RCW 74.46.820 are each amended to read as follows:

(1) Cost reports and their final audit reports (~~(with any accompanying schedule of questioned costs submitted to the secretary))~~) shall be subject to public disclosure pursuant to the requirements of chapter 42.17 RCW. Notwithstanding any other provision of law, financial statements and any accompanying schedules summarizing the adjustments to a contractor's financial records, reports on review of internal control and accounting procedures, and letters of comments or recommendations relating to suggested improvements in internal control or accounting procedures which are prepared pursuant to the requirements of this chapter shall be exempt from public disclosure.

(2) Regardless of whether any document or report submitted to the secretary pursuant to this chapter is subject to public disclosure, copies of such documents or reports shall be provided by the secretary, upon written request, to the legislature and to state agencies or state or local law enforcement officials who have an official interest in the contents thereof.

Sec. 42. Section 92, chapter 177, Laws of 1980 and RCW 74.46.840 are each amended to read as follows:

If any part of this ~~((act))~~ chapter and RCW 18.51.145 and 74.09.120 is found by an agency of the federal government to be in conflict with federal requirements which are a prescribed condition to the receipts of federal funds to the state, the conflicting part of this ~~((act))~~ chapter and RCW 18.51.145 and 74.09.120 is hereby declared inoperative solely to the extent of the conflict and with respect to the agencies directly affected, and such finding or determination shall not affect the operation of the remainder of this ~~((act))~~ chapter and RCW 18.51.145 and 74.09.120 in its application to the agencies concerned. In the event that any portion of this ~~((act))~~ chapter and RCW 18.51.145 and 74.09.120 is found to be in conflict with federal requirements which are a prescribed condition to the receipt of federal funds, the secretary, to the extent that the secretary finds it to be consistent with the general policies and intent of ~~((this))~~ chapters 18.51, 74.09, and 74.46 RCW, may adopt such rules as to resolve a specific conflict and which do meet minimum federal requirements. In addition, the secretary shall submit to the next regular session of the legislature a summary of the specific rule changes made and recommendations for statutory resolution of the conflict.

NEW SECTION. Sec. 43. There is added to chapter 74.46 RCW a new section to read as follows:

If any provision of this act or its application to any person or circumstance is held invalid, the remainder of the act or the application of the provision to other persons or circumstances is not affected.

Sec. 44. Section 74.09.120, chapter 26, Laws of 1959 as last amended by section 6, chapter 11, Laws of 1981 2nd ex. sess. and RCW 74.09.120 are each amended to read as follows:

The department shall purchase necessary physician and dentist services by contract or "fee for service." The department shall purchase hospital care by contract or by all inclusive day rate, or at a reasonable cost based on a ratio of charges to cost. Any hospital when requested by the department shall supply such information as necessary to justify its rate, charges or costs. All additional services provided by the hospital shall be purchased at rates established by the department after consultation with the hospital. The department shall purchase nursing home care by contract. The department shall establish regulations for reasonable nursing home accounting and reimbursement systems which ~~((comply with RCW 74.09.610. The regulations))~~ shall provide that no payment shall be made to a nursing home which does not permit inspection by the department of social and health services of every part of its premises and an examination of all records, including financial records, methods of administration, general and special dietary programs, the disbursement of drugs and methods of supply, and any other records the department deems relevant to the establishment of such a system.

All other services and supplies provided under the program shall be secured by contract.

The department may purchase care in institutions for the mentally retarded, also known as intermediate care facilities for the mentally retarded. The department shall ~~((develop))~~ establish rules for reasonable accounting and reimbursement systems for such care ~~((and report such rules to the next regular session of the legislature for review prior to implementation))~~. Institutions for the mentally retarded include licensed nursing homes, public institutions, licensed boarding homes with fifteen beds or less, and hospital facilities certified as intermediate care facilities for the mentally retarded under the federal medicaid program to provide health, habilitative, or rehabilitative services and twenty-four hour supervision for mentally retarded individuals or persons with related conditions and includes in the program "active treatment" as federally defined.

Sec. 45. Section 16, chapter 2, Laws of 1981 1st ex. sess. and RCW 18-51.145 are each amended to read as follows:

Inspections of nursing homes by local authorities shall be consistent with the requirements of chapter 19.27 RCW, the state building code. Findings of a serious nature shall be coordinated with the department and the state

fire marshal for determination of appropriate actions to ensure a safe environment for nursing home residents. The state fire marshal shall have exclusive authority to determine appropriate corrective action under this section.

**NEW SECTION.** Sec. 46. (1) In administrating the nursing home payment system under chapter 74.09 RCW, the department of social and health services shall calculate preliminary settlements for the 1978 and 1979 cost reporting periods. The preliminary settlements shall be computed by comparing the rates paid to a contractor with that contractor's reported or audited allowable costs, as available. For 1978 reporting periods, the department shall on preliminary settlements permit providers the option of: (a) Retaining cost savings in the administration and operations and property cost centers as computed according to department regulations in effect for 1978; or (b) receiving a return on owner's net invested equity as computed according to procedures established by the department. For 1979 reporting periods, pending final disposition of litigation concerning retention of cost savings in the administration and operations and property cost centers for June 1979, the department shall not recover such cost savings for the calendar year.

(2) Contractors shall make repayment of overpayments identified through this process within thirty days of receipt of written notice from the department of the amount of overpayments.

(3) Where deemed appropriate by the department, repayment of overpayments may be made according to a schedule determined by the department.

(4) Failure on the part of a nursing home contractor to tender payment due in full within thirty days after notice is received from the department shall render the contractor liable for the payment of interest to the department at the rate of one percent per month for any unpaid balance from thirty days after the date of notification until payment in full is received by the department. Liability for interest payments under this subsection shall remain in effect whether a contractor is in default of repayment or is making repayment according to a schedule determined by the department in lieu of payment in full upon notification of payment due.

(5) Unless payment due from a nursing home contractor is received in full within thirty days after notification from the department or unless principal and interest payments are received according to a schedule determined by the department, recoupment from current reimbursement payments due a contractor in default will commence according to a schedule determined by the department.

(6) Interest expense incurred by a contractor in making repayment of overpayments for 1978 and 1979 reporting periods shall not be reimbursable by the state as an allowable cost.

(7) Nothing in this section prejudices the rights of contractors or the department regarding audit adjustments or revised settlements which may be promulgated by the department from time to time in individual contractor cases.

NEW SECTION. Sec. 47. There is appropriated from the general fund to the department of social and health services for the biennium ending June 30, 1985, the sum of \$3,300,000, of which \$1,650,000 is from federal funds, to carry out the purposes of section 24 of this act. Expenditures under this appropriation shall not exceed amounts recovered under section 46 of this act.

NEW SECTION. Sec. 48. The following acts or parts of acts are each repealed:

- (1) Section 1, chapter 260, Laws of 1977 ex. sess. and RCW 74.09.550;
- (2) Section 2, chapter 260, Laws of 1977 ex. sess. and RCW 74.09.560;
- (3) Section 3, chapter 260, Laws of 1977 ex. sess. and RCW 74.09.570;
- (4) Section 4, chapter 260, Laws of 1977 ex. sess., section 2, chapter 2, Laws of 1981 1st ex. sess., section 7, chapter 11, Laws of 1981 2nd ex. sess. and RCW 74.09.580;
- (5) Section 1, chapter 2, Laws of 1981 1st ex. sess., section 8, chapter 11, Laws of 1981 2nd ex. sess., section 2, chapter 19, Laws of 1982 1st ex. sess., section 1, chapter 1, Laws of 1982 2nd ex. sess. and RCW 74.09.610;
- (6) Section 5, chapter 19, Laws of 1982 1st ex. sess. and RCW 74.09.620;
- (7) Section 7, chapter 177, Laws of 1980, section 3, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.070;
- (8) Section 11, chapter 177, Laws of 1980 and RCW 74.46.110;
- (9) Section 12, chapter 177, Laws of 1980, section 4, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.120;
- (10) Section 14, chapter 177, Laws of 1980 and RCW 74.46.140;
- (11) Section 40, chapter 177, Laws of 1980 and RCW 74.46.400;
- (12) Section 48, chapter 177, Laws of 1980 and RCW 74.46.480;
- (13) Section 81, chapter 177, Laws of 1980, section 8, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.810;
- (14) Section 13, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46-.850; and
- (15) Section 84, chapter 177, Laws of 1980.

Sec. 49. Section 94, chapter 177, Laws of 1980 as amended by section 10, chapter 2, Laws of 1981 1st ex. sess. and RCW 74.46.901 are each amended to read as follows:

- (1) Sections 2, 7, 83, 85, 86, and 91 of chapter 177, Laws of 1980 are necessary for the immediate preservation of the public peace, health, and safety, the support of the state government and its existing public institutions, and shall take effect on April 4, 1980.

(2) Section 27 of chapter 177, Laws of 1980 shall take effect on July 1, 1980.

(3) ~~((Sections 3, 4, 5, 6, 8, 9, 11, and 12 of chapter 177, Laws of 1980 shall take effect on July 1, 1983.~~

~~(4) All other sections of chapter 177, Laws of 1980 shall take effect on July 1, 1984)) RCW 74.46.300, 74.46.360, 74.46.510, and 74.46.530 shall take effect on January 1, 1985.~~

(4) All other sections of chapter 74.46 RCW, except those which took effect before July 1, 1983, shall take effect on July 1, 1983, which shall be "the effective date of this act" where that term is used in chapter 177, Laws of 1980.

NEW SECTION. Sec. 50. There is appropriated for the biennium ending June 30, 1985, from the general fund to the office of the state auditor, the sum of sixty thousand dollars, or so much thereof as may be necessary, for the purposes of section 6 of this act.

NEW SECTION. Sec. 51. This act is necessary for the immediate preservation of the public peace, health, and safety, the support of the state government and its existing public institutions and shall take effect on July 1, 1983, with the exception of section 28 of this act, which shall take effect on January 1, 1985.

Passed the Senate May 24, 1983.

Passed the House May 24, 1983.

Approved by the Governor June 13, 1983.

Filed in Office of Secretary of State June 13, 1983.

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## CHAPTER 68

[Engrossed Senate Bill No. 3858]

### ANNEXATION OF UNINCORPORATED AREAS—WRITTEN CONSENT OF REAL PROPERTY OWNERS

AN ACT Relating to the annexation of unincorporated areas by cities and towns; and amending section 35.13.180, chapter 7, Laws of 1965 as amended by section 4, chapter 332, Laws of 1981 and RCW 35.13.180.

Be it enacted by the Legislature of the State of Washington:

Sec. 1. Section 35.13.180, chapter 7, Laws of 1965 as amended by section 4, chapter 332, Laws of 1981 and RCW 35.13.180 are each amended to read as follows:

City and town councils of second and third class cities and towns may by a majority vote annex new territory outside the city or town limits, whether contiguous or noncontiguous for park, cemetery, or other municipal purposes when such territory is owned by the city or town or all of the