

Chapter 7: Fiscal/Employer Agent Services

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Chapter 7

Fiscal/Employer Agent Services¹

Self-direction programs offer participants choice of and control over their long-term services and supports. However, with choice and control come responsibilities, including those associated with being an employer, such as management of payroll and employment-related taxes. (In this chapter and throughout the Handbook, the term “participant” categorically includes their representatives.)

Various models of Financial Management Services (FMS) can reduce the employer-related burden for participants and program staff, but they often are the most complex component of self-direction programs to implement. Thus, in order to successfully implement self-direction programs using FMS, it is essential that states have designated program staff with the necessary knowledge who will make the commitment to stay up-to-date with Medicaid rules and regulations related to these programs; applicable FMS models; and federal/state/local tax, labor, and workers’ compensation insurance requirements as they relate to household employers and domestic service workers.

This chapter describes the key features of five FMS models but focuses on the issues and challenges related to two in particular: the Government and Vendor Fiscal/Employer Agent (F/EA) models. These two FMS models are highlighted because they provide participants with a high degree of choice and control over their services—allowing them to be the common law employer of their workers while providing needed payroll and other fiscal supports.

A. Overview of Financial Management Services

What Are Financial Management Services?

The Centers for Medicare and Medicaid Services (CMS) defines Financial Management Services as: *A service/function that assists the family or participant to: (a) manage and direct the distribution of funds contained in the participant-directed budget; (b) facilitate the employment of staff by the family or participant by performing as the participant’s agent such employer responsibilities as processing payroll, withholding and filing federal, state, and local taxes, and making tax payments to appropriate tax authorities; and (c) performing fiscal accounting and making expenditure reports to the participant and/or family and state authorities.*²

The provision of FMS is essential when implementing self-direction programs for several reasons.

- The Medicaid §1915(c) waiver authority does not permit payments for

services to be made directly to participants, either to reimburse them for expenses incurred or to enable them to directly pay a service provider. Rather, payments on the participant's behalf must be made by an intermediary organization (i.e., either a qualified Medicaid provider or an entity under administrative contract with the state). This restriction also applies to the provision of Medicaid State Plan services.³

- Medicaid funds are permitted to be disbursed directly to participants under §1115 self-direction programs and the decision whether to require participants to use FMS is determined by the state based on its program design.⁴ In addition, under §1915(j) of the Social Security Act, CMS does not require states to mandate the use of FMS for participants who elect the “cash” option. Instead, these participants may choose to retain responsibility for some or all of their fiscal and employer-related responsibilities. Even if participants choose to receive some benefits in cash and distribute workers' payroll checks directly, they may choose to have an FMS organization manage the federal and state tax filings and deposits and generate payroll checks for their workers.
- Some FMS organizations may act as a neutral bank for receiving and disbursing public funds (i.e., Fiscal/Employer Agents).⁵ These entities do not provide direct care services, but rather, make payments to service providers and vendors per the direction of participant. This allows the participant to change service providers and vendors as they see fit, based on their level of satisfaction, helping to ensure the quality of their home and community-based services (HCBS).
- FMS provide fiscal accountability for state and local government agencies and safeguards for individuals enrolled in self-direction programs and their workers by ensuring that payroll,⁶ workers' compensation insurance policy management, and vendor payment tasks are performed accurately and in accordance with federal, state, and local rules and regulations, and in a timely manner.
- Some FMS organizations (i.e., Fiscal/Employer Agents) can perform as a “mini management information system” for programs and participants providing a variety of financial reports related to the receipt of public funds, service use, and payments. These reports inform participants about their service use and related expenditures and also act as a fiscal and/or fraud monitoring tool for them and the program's staff.
- When an FMS organization provides services under a co-employment arrangement⁷ with participants (e.g., an Agency with Choice or Public Authority/Workforce Council model), it can provide services directly for workers, (i.e., recruitment, training and supervision of workers, and provision of emergency backup staff), ideally, only at the request of participants who are acting as their worker's managing employer.⁸

Currently, states use one or more of five FMS models to implement Medicaid and state-funded self-direction programs: (1) Fiscal Conduit, (2) Government F/EA, (3) Vendor F/EA, (4) Agency with Choice, and the (5) Public Authority/Workforce Council model. These models are described briefly in Table 1 below.

Table 1. Financial Management Services Models and Key Characteristics

FMS Model	Operating Entity⁹	Worker's Employer	Responsibilities
Fiscal Conduit	State or County (government agency) or Vendor	Participants, unless agency services are used	Disburses public funds via cash or voucher payments to participants and performs other related duties as defined by the program. Some may also provide training and testing for participants on payroll and funds management before allowing them to manage all employer tasks including payroll.
Government Fiscal/ Employer Agent	State or County government agency (In accordance with §3504 of the IRS Code and IRS Rev. Proc. 80-4, 1980-1 C.B. 581 and as modified by IRS Proposed Notice 2003-70)	Participants, unless agency services are used	<p>Under IRS rules, a state or local government entity acts as an “employer agent” for participants—performing all that is required of an employer for wages paid on the employer’s behalf and all that is required of the payer for requirements of backup withholding, as applicable.¹⁰</p> <p>It receives, disburses, and tracks public funds based on participants’ approved service plans and budgets; assists participants with completing participant enrollment and worker employment forms; conducts criminal background checks of prospective workers; and verifies workers’ information (i.e., social security numbers, citizenship or legal alien verification documentation).</p> <p>It also prepares and distributes payroll including the withholding, filing, and depositing of federal and state income tax withholding and employment taxes and locality taxes;¹¹ processes and pays vendor invoices for approved goods and services, as applicable; generates reports for state program agencies, counselors (also called support brokers, support coordinators, and other names), and participants; and may arrange and process payment for workers’ compensation and health insurance, when appropriate.</p> <p>The Government F/EA may choose to delegate employer agent tasks to a reporting or subagent per <i>IRS Proposed Notice 2003-70</i>.</p>

(continued)

Table 1. Financial Management Services Models and Key Characteristics

FMS Model	Operating Entity⁹	Worker's Employer	Responsibilities
Vendor Fiscal/ Employer Agent	Vendor (§3504 of the IRS Code and IRS Rev. Proc. 70–6, 1970–1 C.B. 420 and as modified by IRS Proposed Notice 2003–70)	Participants, unless agency services are used	Performs similar tasks to Government F/EA described above except as a vendor in accordance with IRS Rev. Proc. 70–6, 1970–1 C.B. 420 as modified by IRS Proposed Notice 2003–70. The Vendor F/EA may delegate agent tasks to a reporting agent per IRS Forms 2678 instructions.
Agency with Choice	Agency (e.g., Center for Independent Living [CIL], Home Health, Area Agency on Aging [AAA] or Social Service)	Co-employer (also referred to as joint-employer) arrangement with participants and an agency or its subcontracting agency (e.g., CIL, Home Health, AAA, or Social Service)	<p>The agency and participants are co-employers of the workers whom participants recruit and refer to the agency for hire and assignment back to them.¹² The agency is the primary employer of the worker, for the purpose of human resources and payroll management and Medicaid provider requirements. Participants are the secondary employer of their workers and perform or actively participate in the recruitment, training, supervision, and discharge of their workers.</p> <p>The agency also may provide a variety of supportive services to assist participants in recruiting workers and being a managing employer (if requested by participants), i.e., establish and maintain a worker registry, provide referrals and emergency backup staff, or provide training and supervision directly to participants' workers.</p>
Public Authority/ Workforce Council¹³	Independent or quasi-governmental entity	Multiple-employer arrangement with participants and independent or quasi-governmental entity, state or local community-based service program, or human service department	<p>Participants serve as the employer of their workers for recruitment, training, supervision, and discharge purposes. State or county program agencies may serve as the employer of participants' workers for the purpose of managing payroll including withholding, filing and depositing federal and state income tax withholding and employment taxes and locality taxes.</p> <p>The Public Authority (PA) or Workforce Council (WC) serves as the employer of participants' workers for collective bargaining purposes with the union that represents the workers and, in some cases, performs the payroll task. The PA/WC also may maintain a worker registry, and offer voluntary training for workers and participants and emergency backup services to participants.¹⁴</p>

In general, the Vendor F/EA and Agency with Choice FMS models appear to be more popular than other models with states implementing self-direction programs.¹⁵ While many participants only want to hire and manage their workers and therefore prefer the agency with choice model, the Vendor F/EA model (as does the Government F/EA model) affords participants a greater degree of choice and control over their services and workers than other FMS models because it allows participants to be the common law employer of their workers. This level of choice and control is the hallmark of self-direction.

Although a smaller percentage of self-direction programs use the Government F/EA model, the number has increased since October 2003 when the Internal Revenue Service (IRS) first allowed state and local Government F/EAs to contract with and delegate employer agent tasks to a subagent or reporting agent.¹⁶ In addition, the number of states using some form of the Public Authority model (currently referred to in some state legislation as Workforce Councils) has grown from one to five over the past five years: California, Massachusetts, Michigan, Oregon, Washington.

Historically, states that use the Fiscal Conduit model have implemented it in conjunction with state-funded or Medicaid §1115 self-direction demonstration programs to provide participants with the option of receiving and managing all or part of their public benefit funds directly in cash or voucher payments. However, with the passage of §6087 of the Deficit Reduction Act of 2005, codified as §1915(j) of the Social Security Act, which permits states to pay cash to Medicaid participants who direct their services, more states may choose to use the Fiscal Conduit model in the future, possibly in conjunction with the Government or Vendor F/EA model.¹⁷

Employment Status of Workers in Self-Direction Programs

Prior to the early 1990s, most publicly funded self-direction programs considered workers hired directly by participants as “self-employed independent contractors,” and—incorrectly—made no provision for the filing and depositing of federal, state, and local income tax withholding and employment taxes. Although this strategy reduced program costs and the employer burden for state program administrators and participants, it presented states and participants with significant potential liability for unpaid taxes because workers often did not pay their self-employment taxes. Over the past 25 years, the IRS and a number of state unemployment insurance agencies have taken enforcement action against states who classified these workers as independent contractors.

The 2001 IRS Tax Payer Advocate Report stated that directly hired home-based service workers are “employees” and typically they do not meet the IRS’ independent contractor criteria. In addition, under IRS common law rules, workers who provide services to individuals (i.e., participants) are their

employees if the individuals control what will be done and how it will be done, even when freedom of action is afforded to workers.¹⁸ Control refers not only to the results to be accomplished by the work but also the means and details by which that result is accomplished.¹⁹ In order to classify workers correctly as employees; address potential federal, state, and local tax liability for states and individuals; and respond to recent IRS guidance, states have implemented various FMS models, in particular, the two Fiscal/Employer Agent models.

B. Fiscal/Employer Agents: Key Characteristics

Two models of Fiscal/Employer Agents (F/EAs) operate under §3504 of the IRS code: Government and Vendor.²⁰ F/EAs are most effective for implementing self-direction programs, particularly those that allow participants to have individual budgets, for several reasons. First, using an F/EA provides participants a high degree of control over their workers as their common law employers, while reducing their employer-related burden by managing the payroll and bill payment tasks. Second, using an F/EA provides safeguards for participants by ensuring that all required taxes are paid and all Department of Labor and workers' compensation insurance requirements are met. Third, using an F/EA can provide fiscal accountability for states.

The following sections will further describe the key characteristics of these two FMS models, highlighting the tasks performed under each model, and the advantages and challenges of using the models from a state's and an F/EA provider's perspective.

Government Fiscal/Employer Agents

Under the Government Fiscal/Employer Agent ("Government F/EA") model, a state or local government entity applies for and receives authorization from the IRS to act as the employer agent for participants enrolled in its self-direction program in accordance with §3504 of the IRS code, Revenue Procedure 80-4, 1980-1 C.B. 581 (and modified by IRS Proposed Notice 2003-70.) This authority allows the Government F/EA to perform all that is required of an employer for wages paid on the employer's behalf and all that is required of the payer for requirements of backup withholding, as applicable.²¹ Government F/EAs act as a "neutral bank" for the receipt, disbursement, and tracking of participants' public benefits funds, and perform payroll, vendor payment, administrative, and reporting tasks described in Table 1. A Government F/EA may perform these tasks without being considered the common law employer of workers directly hired by participants.

A Government F/EA must file for and obtain a separate, "special" Federal Employer Identification Number (FEIN) for the limited purpose of filing and depositing federal income tax withholding and employment tax forms and depositing federal taxes for the participant-employers it represents.²² Then it must

prepare and submit an application to and receive authorization from the IRS to be authorized as the employer agent for all participants-employers enrolled in its self-direction program.²³

The Government F/EA also must obtain authorization from the IRS to communicate with the IRS regarding employer-related federal tax filings and payments.²⁴ Until the Government F/EA receives the employer agent authorization from the IRS, the participant-employer is liable for any unfulfilled federal income tax withholding and employment tax obligations, including penalties and interest. Once employer agent authorization is received, the Government F/EA is equally liable with participant-employers for any unfulfilled federal income tax withholding and employment tax obligations, including penalties and interest.²⁵

Some state revenue and unemployment tax agencies also require participant-employers to execute limited powers-of-attorney granting Government F/EAs the authority to withhold, file, and deposit state income tax withholding and/or unemployment insurance taxes, and to communicate with state tax agencies regarding these filings and deposits. It is important that program staff know their state and local tax and state labor requirements and how they relate to their self-direction program and the F/EA model used prior to implementing F/EA services.

Delegation of Employer Agent Tasks

IRS Proposed Notice 2003–70 allows a Government F/EA to delegate employer agent tasks to a subagent²⁶ or reporting agent²⁷ to ease its administrative burden. The Notice also provides Government F/EAs with a number of paperwork reduction opportunities.²⁸

When a Government F/EA decides to contract with and delegate F/EA tasks to a reporting agent, it must execute an IRS Form 8655, Reporting Agent Authorization, between itself and the reporting agent. The reporting agent is not liable for any unfulfilled federal income tax withholding and/or employment tax obligations, including penalties and interest.²⁹ Rather, the Government F/EA and the participant-employer are equally liable.³⁰ State and local tax agencies may have similar rules regarding reporting agent liability, which can differ by state.

When a Government F/EA uses a subagent, the IRS requires that it obtain a statement from all participant-employers authorizing the Government F/EA to appoint a subagent to assist in meeting its responsibilities as their employer agent. The IRS also requires the Government F/EA to execute a second IRS Form 2678, Agent/Payer Authorization, between itself and its subagent making the subagent the Government F/EA's employer agent.³¹ The subagent is not liable for any unfulfilled federal income tax withholding and employment tax obligations, including penalties and interest, until authorization is received from the IRS. Once authorization is received, the Government F/EA, the subagent, and the participant-employers are all equally liable for any unfulfilled tax obligations,

including penalties and interest.³² State and local tax agencies may have similar rules regarding subagent liability, which can differ by state.

To reduce the likelihood of any unfulfilled federal, state, and local tax obligations, including penalties and interest, due to reporting agent or subagent errors or omissions, it is important that a Government F/EA be able to determine that the reporting agent or subagent has the knowledge and experience necessary to provide the required services. In addition, the Government F/EA should develop and execute a performance-based contract with the reporting agent or subagent that holds these entities accountable for any federal, state, or local taxes not filed and/or paid—including penalties and interest—that may result from errors or omissions made by the entity in the performance of its duties.

Advantages to States in Implementing a Government F/EA

Implementing a Government F/EA provides several advantages for state and local government program staff.

- Current IRS policies and procedures for Government F/EAs are better documented and have fewer ambiguities than those for Vendor F/EAs. In addition, the IRS employer agent authorization process for Government F/EAs need not delay the enrollment of individuals in self-direction programs if the initial implementation date of F/EA services coincides with the receipt of IRS Government F/EA authorization.
- The IRS has afforded Government F/EAs and their reporting agent or subagent paperwork economies as described in Internal Revenue Service Proposed Notice 2003–70.³³ These paperwork economies can reduce costs related to the provision of F/EA services for states and participants.
- States can furnish F/EA services “in-house,” providing a state with full control over the provision of F/EA services while avoiding the need to manage vendor selection and monitor vendor performance with its associated expenses.
- States can target scarce resources for F/EA implementation and quality monitoring activities on two or fewer entities (i.e., itself as Government F/EA and one subagent or reporting agent, if the state program agency chooses to use one) in a cost effective manner. However, states still need to develop and implement a Government F/EA manual that describes the policies, procedures, and internal controls for all F/EA tasks, any tasks delegated to a reporting agent or subagent, and tasks associated with communicating with and monitoring the performance of these entities in order to ensure effective provision of F/EA services. This manual should be updated at least annually and be the basis for any Government F/EA reporting agent/subagent performance review protocol developed and implemented by program staff.

Challenges for States Implementing a Government F/EA

Implementing a Government F/EA may present a number of challenges for state and local government program staff.

- State and local government program staff may lack the knowledge, staff resources and needed infrastructure, and/or the desire to perform as a Government F/EA with or without the assistance of a reporting agent or subagent.
- Some program staff have reported difficulty implementing the IRS' Government F/EA authorization process due to incomplete and/or conflicting information received from IRS regional office staff.
- Using only one reporting agent or subagent could present difficulties for the Government F/EA in ensuring seamless delivery of financial management services to participants should it or its reporting agent or subagent choose to terminate the reporting agent's or subagent's contract for any reason.
- When states implement self-direction programs using a Government F/EA, the costs associated with providing FMS, and any reporting agent or subagent services, must be billed as an administrative expense for the purpose of claiming federal Medicaid matching funds. This is because participants' freedom of choice of provider is limited.³⁴ Thus, when evaluating the feasibility of implementing a Government F/EA, a state's Medicaid agency and program staff should assess the economic impact of using this model on the receipt of federal Medicaid matching funds and the administrative costs to the state associated with monitoring multiple F/EA operations.
- Current state and local income tax withholding and employment tax filing and depositing policies, procedures, and forms are not easily applied to self-direction programs. Moreover, some state and local tax agency staff are unfamiliar with Government F/EAs and are unsure how to apply their policies, procedures, and forms to these entities and what the liabilities may be. It is critical that program staff meet with key state and local tax agency staff early on to receive input and guidance regarding policies, procedures, and issues, and to avoid problems in implementing the self-direction program and Government F/EA services.³⁵

Vendor Fiscal/Employer Agents

Under the Vendor Fiscal/Employer Agent (“Vendor F/EA”) model, a vendor entity must apply for and obtain authorization from the IRS to act as an employer agent for each participant it represents. Vendor F/EAs operate under §3504 of the IRS code and the tasks they perform are similar to the Government F/EA. However, Vendor F/EAs operate under different IRS provisions (Revenue Procedure 70–6, 1970–1 C.B. 420 and as modified by Proposed Notice 2003–70). Vendor F/EAs

also may contract with and delegate tasks to a reporting agent if the program allows this.³⁶

A Vendor F/EA must file for and obtain a separate, “special” Federal Employer Identification Number (FEIN) for the limited purposes of withholding, filing, and depositing federal income tax withholding and employment taxes.³⁷ In contrast with IRS employer agent authorization procedures for Government F/EAs, Vendor F/EAs must submit an IRS Form 2678 to and receive authorization from the IRS for each participant-employer it represents as an employer agent.³⁸ They also must obtain IRS tax information authorization to communicate with IRS staff about participant-employers’ federal tax filings and payments.³⁹

A Vendor F/EA is not liable for any unfulfilled federal income tax and employment tax obligations, including penalties and interest for participant-employers until employer agent authorization is received from the IRS.⁴⁰ Once IRS authorization is received, both participant-employers and the Vendor F/EA are equally liable for any unfulfilled federal income tax and employment tax obligations, including penalties and interest.

Delegation of Employer Agent Tasks

When a Vendor F/EA chooses to use a reporting agent, it must execute an IRS Form 8655, Reporting Agent Authorization, with the reporting agent. The reporting agent is not liable for any unfulfilled federal income tax withholding or employment tax obligations including penalties and interest.⁴¹

Some state and local revenue and unemployment tax agencies also require all participant-employers to execute limited powers-of-attorney granting Vendor F/EAs the authority to file and deposit state income tax withholding and/or unemployment taxes and to communicate with the tax agencies regarding these filings and deposits. As mentioned earlier, it is important that program staff know how the state and local tax and state labor requirements apply to the program and F/EA services prior to implementing F/EA services.

Advantages to States in Implementing a Vendor F/EA

Implementing a Vendor F/EA provides several advantages for state and local government program staff.

- It allows states to engage vendor entities, either under contract or as qualified Medicaid service providers, who have the knowledge, experience, resources, and infrastructure necessary to provide effective financial management services, and to negotiate cost-effective fees for F/EA services rendered, rather than providing these services in-house.
- States have the option to (1) select a discrete number of Vendor F/EAs, using a Request for Proposal or other solicitation process, and bill F/EA costs

as an administrative expense (at a uniform federal matching funds rate of 50 percent), or (2) develop Medicaid F/EA provider standards and provide freedom of choice of provider to participants, and bill F/EA costs as a service expense for the purpose of claiming federal matching funds (at a federal matching funds rate that ranges from 50 to 83 percent).⁴²

- States can further distance themselves from being considered the employer of participants' workers—by workers and state workers' compensation and unemployment insurance agencies—by implementing a contract making the Vendor F/EA equally liable, with the participant-employer, for any unfulfilled federal and state income tax withholding and employment tax obligations, including penalties and interest.⁴³

Challenges for States Implementing Vendor F/EAs

Implementing a Vendor F/EA may present a number of challenges for state and local government program staff.

- In order to select vendor entities and effectively monitor the quality of their performance, designated state program staff must have adequate knowledge of federal, state, and local (as applicable) tax policies, procedures, and forms as they relate to household employers, domestic service workers, and Vendor F/EAs, and understand Vendor F/EA operations.
- Current IRS employment tax policies, procedures, and guidance pertaining to Vendor F/EAs are, in some cases, incomplete and ambiguous.
- IRS staff knowledge of IRS policies and procedures related to Vendor F/EAs varies, sometimes resulting in incomplete and/or inconsistent guidance.
- Current state income tax withholding and employment tax policies, procedures, and forms are not easily applied to self-direction programs. Moreover, some state tax agency staff are unfamiliar with Vendor F/EAs and their operations and unsure of how to apply their policies, procedures, and forms to these entities. State and local tax agency staff also are unsure of what the liability is, if any, for Vendor F/EAs and their reporting agents, relative to any unfulfilled state income tax withholding, employment tax, and locality tax obligations, including penalties and interest. Thus, it is critical that program staff meet with key state tax agency staff early on to present their program and F/EA design and receive input and guidance, preferably in writing, to clarify procedures and issues and avoid problems in implementing its program and Vendor F/EA services.

C. Key Issues For States Using Government and Vendor F/EAs to Provide FMS

State and local government program staff must address several issues when implementing—and monitoring the performance of—Government and Vendor F/EAs.

Need to Obtain F/EA-Agent-Related Knowledge

State and local government program staff must be knowledgeable about (1) federal and state tax, labor, and workers' compensation insurance, locality taxes, and Medicaid rules, policies, and procedures that apply to F/EAs, household employers, and domestic service workers; and (2) federal and state program requirements for F/EA operations for the model it plans to implement. This knowledge is essential for state and local government program staff in order to (a) develop and implement effective Medicaid standards and provider agreements, (b) develop and execute solicitations (i.e., Request for Proposals [RFP] or Intent to Negotiate [ITN]) for F/EA services and administrative contracts with Vendor F/EAs and reporting agents and subagents (as applicable); (c) assess F/EAs', reporting agents', and subagents' readiness to perform the required F/EA tasks; and (d) monitor F/EAs', reporting agents' and subagents' ongoing performance.

Verifying State and Local Tax, Labor, and Workers' Compensation Insurance Requirements

Program staff should meet with applicable state tax, labor, and workers' compensation insurance agencies to present their program and F/EA design and obtain feedback early on. Moreover, it is recommended that feedback be obtained in writing. This is important to determine if any state tax, labor, and workers' compensation rules, policies, or procedures conflict with the state's program and F/EA design (e.g., if the state prohibits participants from being the common law employer of the workers they hire directly).⁴⁴ It also will enable program staff to receive guidance on the best way to implement state employer requirements and complete the required processes and forms. States that have various locality tax requirements should repeat this process with the appropriate local tax authorities.

Need to Assess States' Data and Information Systems Capabilities to Implement F/EA Services

States need to assess their data and information systems capabilities to determine if they are sufficient to implement an effective self-direction program with F/EA services. The assessment should include, but not be limited to: (1) an evaluation of the state's ability to generate and transmit data, including participant service plan, budget, and authorization information to counselors and F/EAs; and (2) its ability to link its Medicaid Management Information System (MMIS) and

Medicaid claims processing system with the Government or Vendor F/EA billing procedures and generate reports, as required. A state should review its capacity not only for the initial submission of budget, service plan, and authorization information to applicable stakeholders, but also its capacity and methodology for submitting edits and updates in an accurate and timely manner.

Determining Whether F/EA Services Will Be an Administrative Function or Program Service

When states implement a self-direction program using a Government F/EA—under either a Medicaid §1915(c) waiver program or the Medicaid State Plan, including under the §1915(j) option—the costs associated with providing FMS and any reporting agent or subagent services must be billed as an administrative expense for the purpose of claiming federal Medicaid matching funds. When states use a Vendor F/EA in conjunction with a Medicaid State Plan self-direction program—either through the personal care option or the new §1915(j) option⁴⁵—the costs for the F/EA and reporting agent services also must be billed as an administrative expense. Given that administrative expenses are matched by the federal government at a uniform 50 percent rate while service expenses are matched from 50 to 83 percent (depending on the state), the decision about which model to use can have major cost implications for a state.

For Vendor F/EA services to be reimbursed as a waiver service, states must meet a number of federal requirements. States must develop a service definition that includes a set of provider qualifications and the tasks that will be performed by the Vendor F/EA and any reporting agent. States must verify a provider’s qualifications before services are initiated and must provide a detailed description of the frequency and methods by which provider qualifications will be re-verified and ongoing performance will be monitored. States must treat Vendor F/EAs as they would any Medicaid service provider. States may not arbitrarily limit the number of Vendor F/EAs available to participants since this would restrict their freedom of choice of provider and disqualify the state from claiming Vendor F/EA expenses for federal matching funds purposes as a waiver service. Finally, states must monitor Vendor F/EAs’ and any reporting agents’ performance on an ongoing basis.

Determining How Many F/EAs to Use

Program staff continue to struggle with determining how many Vendor F/EAs are sufficient to meet participants’ demand for FMS. In determining “how many Vendor F/EAs are enough,” states often must balance several factors with participants’ freedom of choice of F/EA provider and a state’s need to maximize federal matching funds. These factors are: (1) the number of participants; (2) the need to achieve economies of scale and a cost-efficient price for Vendor F/EA services; and (3) the resources needed and associated expenses related to contracting with and assessing

the readiness of and monitoring the performance of Vendor F/EAs, or certifying and re-certifying Vendor F/EAs and their reporting agents and subagents.

A significant number of states limit the number of Vendor F/EA providers and forgo the receipt of federal service matching funds in order to obtain cost efficiencies and effectively manage the monitoring of F/EA service delivery.⁴⁶ The majority use some type of solicitation process (i.e., RFP or ITN) to select one or more Vendor F/EA providers for their program. However, some states report challenges related to this strategy such as (1) the need to write an effective solicitation (i.e., RFP or ITN) document that accurately and completely reflects F/EA requirements; (2) the need to evaluate F/EA knowledge and experience for proposal review and vendor selection purposes; (3) interruptions in the continuity of F/EA providers because a satisfactory F/EA provider must rebid at the end of each contract period and may not be reselected (e.g., if they are not the lowest bidder, which may be a priority for a state's purchase and property department responsible for managing the solicitation process); (4) the resources and time required to complete a solicitation, including addressing any bidder challenges; and (5) developing and executing effective performance-based contracts.

Other states provide freedom of choice of F/EA service providers for participants in order to receive federal service matching funds.⁴⁷ Again, some of these states have experienced challenges such as (1) having sufficient knowledge of federal and state F/EA requirements and operations to prepare Medicaid standards and execute Medicaid provider agreements effectively; (2) preparing effective protocols for certifying F/EA entities as Medicaid providers and monitoring their performance through periodic recertification; and (3) having the staff and financial resources necessary to conduct F/EA certifications and recertification/performance monitoring in a timely and effective manner.

Allowing Sufficient Time to Set Up F/EA Services

Historically, states have underestimated the amount of time it takes to set up F/EA services. (Many states call this process the start-up period.) Poor planning on the part of program staff—or a belief that cost savings can be achieved by minimizing the time allocated to ensure that everything is working as it should—can result in too little time being allocated to set up F/EA services. Without sufficient time, decisions made in haste can lead to mistakes that must be corrected and paid for during the first year of program implementation. Thus, it is important for program staff to allow sufficient time to set up F/EA services to effectively support the implementation of a self-direction program.

Establishing Reimbursement for F/EA Services

Program staff should establish reasonable and adequate reimbursement for Vendor F/EA and reporting agent and subagent services that reflect the costs of

providing these services. CMS has approved a variety of methods for determining reimbursement for FMS.

Basic Transaction-Based Reimbursement Method

The most basic reimbursement method is transaction-based. This approach closely links reimbursement for F/EA services to the actual cost of providing services. Using this method, key F/EA (and subagent or reporting agent) tasks are identified and their associated costs computed by program staff. Then program staff develop a fee schedule for each identified task and pay the F/EA for transactions completed in accordance with the fee schedule.

Some states have found the basic transaction-based F/EA payment system problematic, particularly when program enrollment is low (e.g., during the initial start-up period). This is because the total reimbursement provided for a small number of transactions often does not cover the Vendor F/EA or reporting agent or subagent's initial start-up expenses, costs of base level staffing, and/or other fixed costs.

Modified Transaction-Based (Per Member Per Month) Reimbursement Method

Another CMS-approved reimbursement method is to reimburse a Vendor F/EA (and a subagent or reporting agent, if used) for services rendered, as a function of transaction-based costs and anticipated service volume for a specific period or a modified transaction-based, per member per month (PMPM) rate. Under a modified PMPM rate, a state costs out the F/EA, reporting agent and/or subagent services by tasks and estimates the service volume for the rate period. The state uses this information to compute a total annual reimbursement amount to be paid to the F/EA, reporting agent or subagent, as applicable.⁴⁸ Using that amount, the state then computes a PMPM rate for Vendor F/EA, or reporting agent or subagent services.⁴⁹

Some states have further adapted the modified transaction-based PMPM reimbursement methodology for Vendor F/EAs and reporting agents and subagents by establishing a minimum monthly fee for the initial implementation period (i.e., up to a certain number of active participants), and then implement a PMPM rate after the initial enrollment target is met to address both the costs associated with the initial start-up period and ongoing F/EA operations. This reimbursement strategy provides states with an incentive to efficiently enroll individuals in the program and with the F/EA, while ensuring the Vendor F/EA, reporting agent and/or subagent receives sufficient reimbursement to operate during the initial implementation period and on an ongoing basis.

It should be noted that some participants have questioned the equity of using a flat PMPM rate for F/EA services when the services are paid, in whole or in part,

from their individual budgets. For example, they ask: “Is it equitable to charge a participant who needs two payroll checks and one vendor payment processed in a month the same F/EA fee as a participant who needs six payroll checks and two vendor payments processed in a month?” States need to balance administrative ease and cost effectiveness with equity concerns and participants’ costs when establishing payment methods for F/EA services.⁵⁰

Finally, a number of states have developed discrete payments for the completion of a one-time activity (i.e., development of participant enrollment and worker employment packets, and a state-specific F/EA policies and procedures manual). These payments are in addition to the PMPM rate paid to the F/EA for services delivered on an ongoing basis.

Percent of Budget Reimbursement Method

Finally, some states use an F/EA reimbursement method—the percent of budget method—that is not approved by CMS.⁵¹ Under this method, a Vendor F/EA, or a reporting agent or subagent, is reimbursed on the basis of a percentage of the total dollar volume of services that an FMS entity processes. This is not an optimal approach because the amount paid does not reflect the actual costs of providing the F/EA services.

Transitioning Participants From One F/EA to Another

When states have to transition participants from one F/EA to another for any reason, the process can be complicated and costly for the state and the F/EA.⁵² States need to develop policies and procedures for transitioning participants from one F/EA to another that address all the possible contingencies, reflect these policies and procedures in the Medicaid provider agreement and/or contract it executes with the F/EA, and then price the transition function accordingly.

Coordinating FMS with Counseling Services and Ensuring Effective Communication Between F/EAs and Counselors

Program staff continue to struggle with the decision of whether to provide counseling (also known as support broker or support coordinator) services and Vendor F/EA services separately or under one or more “umbrella” organizations.⁵³ Two advantages of providing F/EA and counseling services together include: (1) the seamless provision of supportive and financial management services to participants, and (2) opportunities for effective communication between the two functions due to their co-location.

One challenge for states using this approach is making sure that an umbrella organization does not put undue pressure on participants and try to steer them toward using the umbrella organization’s services exclusively, particularly when the services provided by the umbrella organization do not meet all of a

participant's needs. Another challenge for states is if both counseling and F/EA services are provided under the same umbrella organization, a state would have to find a new provider for both types of services if the organization stops providing services for any reason. One advantage of providing F/EA and counseling services separately is that participants have more choice and control over who provides these services and can mix and match providers, selecting the most capable provider for each service, thereby helping to ensure the quality of both. However, states face two challenges related to providing counseling and F/EA services separately: (1) the amount of training and monitoring that must be provided by the state, and (2) communication between the two entities can be fragmented, resulting in inconsistent service delivery for participants.

Need to Assess Initial Readiness and Monitor the Ongoing Performance of F/EAs

It is essential that program staff develop protocols, assess initial readiness, and monitor the ongoing performance of F/EAs, and any reporting agents and subagents.⁵⁴ To do this, states must ensure that staff are knowledgeable about (1) federal and state tax, labor, workers' compensation insurance, locality tax, and Medicaid requirements for F/EAs, reporting agents and subagents; (2) F/EAs' operations; and (3) federal and state regulations as they pertain to household employers and their workers. These staff also must be comfortable using and staying up-to-date with this information and with financial audit/review techniques that may be different from those they use when certifying and monitoring the performance of traditional HCBS providers.

D. Key Issues for Government and Vendor F/EAs

Government and vendor entities must address several key issues when operating as an F/EA.

Staying Up-to-Date with Federal, State, and Local Tax, Labor, and Workers' Compensation Insurance and Medicaid Requirements

Government and Vendor F/EAs need to have a system in place and written policies, procedures, and internal controls for staying up-to-date with federal, state, and local requirements related to receiving authorization and providing F/EA services in order to comply with these requirements.⁵⁵

Developing and Maintaining a Government or Vendor F/EA Policies and Procedures Manual

Government and Vendor F/EAs must prepare and maintain a policies and procedures manual that describes the systems, policies, procedures, and internal controls for all F/EA tasks. When a Government F/EA uses a reporting agent or

a subagent, or a Vendor F/EA uses a reporting agent, the manual should include the systems, policies, procedures, and internal controls for the tasks delegated to the reporting agent or subagent and those associated with communicating and coordinating with and monitoring the performance of the reporting agent or subagent. This manual should be updated at least annually and should be the basis of any Government F/EA reporting agent/subagent performance review conducted by state program staff.

Developing and Maintaining Effective Information Systems Capabilities

Government or Vendor F/EAs (and their reporting agents or subagents) need to have information systems capabilities that allow them to effectively perform all required F/EA tasks in an accurate and timely manner; receive from and transmit information to the state program, counselors, and participants; and link to the state Medicaid claims processing system. For example, “off the shelf” payroll systems often can not manage payroll for large numbers of employers in accordance with federal, state, and local tax and Medicaid program rules. Thus, F/EA’s information systems must be customized for self-direction programs.

Key to the success of a Government or Vendor F/EA is how well it manages the paperwork related to providing F/EA services. In the case where self-direction programs authorize individual budgets for participants, F/EAs’ information systems must be able to maintain individual budgets and track activity for each participant. F/EAs’ information systems must be transparent for audit purposes to ensure that all required paperwork is collected and processed prior to making any payments. Finally, F/EAs must be able to implement an automated system for documenting all contacts with participants, counselors, workers, and vendors; recording actions taken to resolve issues raised; and complying with any mandatory reporting requirements.

Developing and Implementing Effective Customer Services, Including Orientation and Training for Participants

It is important that Government and Vendor F/EAs develop and implement an effective customer service system that includes orientation and skills training for participants and their representatives. Key elements of effective customer service systems include, but are not limited to, providing participants with (1) clear and complete information about enrolling with the F/EA, using its services and staff contacts, and their role and responsibilities and those of the F/EA; (2) accessible, user-friendly, web-available information about F/EA services;⁵⁶ (3) user-friendly participant enrollment and worker employment packets and assistance with completing and submitting the required information to the F/EA; (4) orientation and skills training that address using F/EA services and the employer role and responsibilities; and (5) an automated system for receiving, tracking, and responding to participant inquiries and complaints. F/EA staff must be able to

communicate in alternative formats and multiple languages and the self-direction philosophy should be applied to all aspects of the delivery of customer service.

Developing Quality Management Systems

Historically, states have worked with case managers and service providers to develop quality management systems to safeguard the health and welfare of participants in the traditional HCBS delivery system. In self-direction programs, a significant amount of the responsibility for quality management is transferred to participants, their representatives (when applicable), their counselor, and, to a certain extent, their FMS provider.

Government and Vendor F/EAs are responsible for monitoring the receipt and disbursement of participants' budgetary funds and ensuring that only authorized hours, goods, and services are paid for. Thus, they need to implement a system, and document policies, procedures, and internal controls for tracking and comparing expenditures with participants' spending plans and for identifying and reporting any incidences of outlier spending behavior. Outlier spending behavior may be due to under- and over-reporting on workers' time sheets and/or purchases of goods and services not approved in the spending plan. Mandatory reporting of this information to program staff should be based on pre-determined criteria and made through pre-determined channels.

Vendor and Government F/EAs also need to develop and conduct participant satisfaction surveys, analyze the information collected, and prepare periodic reports for internal quality assurance purposes, for program staff, and for participants. Program staff should work with F/EA staff and participants to develop the survey tool and to determine implementation frequency. Experts suggest that participants be surveyed 60 days after enrolling with the F/EA, to evaluate their satisfaction with the enrollment process, and then annually.

E. Promising Practices Related to the Provision of Government and Vendor F/EA Services

States and Government and Vendor F/EAs have developed several promising practices related to F/EA operations.

Advances in F/EA Information Technology

In response to the lack of “off the shelf” software products available to meet the needs of Government and Vendor F/EAs, a number of Vendor F/EAs have made significant progress in customizing database, accounting, and payroll software to enhance their information technology capabilities and F/EA operations. For example, some systems solutions have been developed for the processing and management of workers' timesheets and for paperwork management, using optical character recognition and electronic document management systems

technologies.⁵⁷ However, developing and testing information technology is expensive and some Vendor F/EAs are struggling to recover these costs through their F/EA fees and still stay price competitive.

The Cash & Counseling National Program has developed a technology solution to support the timely, efficient, and user-friendly flow of information among participants, counselors, F/EAs, and state and local government program administrators as they all assist participants to develop their spending plans, manage their individual budgets, choose and manage employees, and direct their own care. This software solution is called the Consumer Direction Module and is discussed in Appendix II.

Timely Participant Budget Reports

Some Vendor F/EAs have developed easy-to-read financial/budget reports that are at or close to real time, increasing their utility for participants, counselors, and program staff.

Timely Payment of Workers

It is essential that workers be paid on time. The majority of Vendor F/EAs generate “off cycle” payroll checks when necessary. In addition, many now offer a direct deposit option for workers while others offer a debit card option. These options make it possible for workers to receive their pay in a timely manner with minimum delay and/or loss.⁵⁸

Maximizing the Availability of Cost Effective Workers’ Compensation Insurance

States are developing effective ways to arrange for and manage the payment of workers’ compensation insurance premiums for participants and their workers. For example, Massachusetts developed a specific code for household participant-employers and their personal care attendants for workers’ compensation insurance rating purposes (MA-specific code 0918, Domestic Service - Inside Physical Assistance). This code allows for more accurate workers’ compensation insurance rating for support service workers.⁵⁹

In addition, Massachusetts found a workers’ compensation insurance agent who recruited a voluntary insurer to underwrite affordable workers’ compensation insurance policies for the 15,000 participants in the Massachusetts Medicaid Personal Care Assistance Program rather than having to purchase policies through the more costly state assigned risk plan.⁶⁰ To reduce paperwork for the insurance carrier and the Vendor F/EA, the voluntary insurer issues three bills, one to each of three Vendor F/EAs for premiums for the total number of policies held by the participants represented by each Vendor F/EA (instead of issuing 15,000 bills). The three Vendor F/EAs facilitate the receipt of participants’ initial

workers' compensation insurance policies, renewals, and premium payments. They also provide wage information to the insurer so it can determine workers' compensation insurance benefits for injured workers in compliance with state law.

Currently, New Mexico has implemented a state-specific version of MA code 0918 for participant-employers and workers enrolled in its self-direction programs. Illinois and Rhode Island are in the process of implementing a state-specific code 0918 and Pennsylvania is examining the feasibility of doing so for its programs.

Using Credit Unions as Vendor F/EAs

The State of Iowa has implemented self-directed services by contracting with a credit union to provide F/EA services.⁶¹ Contracting with a credit union allows participants to not only receive F/EA services; they and their workers also can use other services the credit union offers.

F. Outstanding Issues

State and local government program staff continue to struggle with a number of issues related to the development and implementation of F/EA services.

Clarifying Federal and State Tax Procedures Related to F/EA Operations

Program staff continue to be frustrated with the status of IRS policies and procedures for Government and Vendor F/EAs. Existing guidance, when available, often is not clear and/or complete, is unavailable in locations accessible to the public, or is not used effectively to educate IRS staff so they can provide consistent, reliable information to the public. In addition, some program and F/EA staff continue to struggle with applying state employer registration, income tax withholding and employment and locality tax policies, procedures, and forms to F/EA operations.

Implementing Effective Data and Information Systems Infrastructure

Developing and implementing effective data and information systems infrastructure and capabilities related to the administration of self-direction programs using F/EAs can be very challenging. For example, program staff need to develop and enhance systems for generating and transmitting individual service plans, budgets, and service authorization information to counselors and F/EAs. They also need to link the state Medicaid claims processing system with Government or Vendor F/EA billing procedures.

Determining Effective Reimbursement Rates for F/EA Services

Determining how much to pay for F/EA services can be challenging. Increasingly states want F/EAs to provide additional services and supports for the state as well as participants, but they often cannot afford the associated costs of doing so. In addition, some states are not prepared to administer programs that use F/EA services, and as a result, rely heavily on their F/EAs, thereby increasing F/EA costs.

Recruiting More Workers' Compensation Insurance Agents to Broker and Carriers to Underwrite Policies for Self-Direction Program Participants

Workers' compensation insurance carriers are concerned that total revenues from low premiums will not cover claims incurred and administrative costs. Although recent research and reports from Vendor F/EAs indicate low workers' compensation insurance claims associated with self-direction programs,⁶² it is difficult to convince state insurance commission staff and workers' compensation insurance agents and carriers of this fact. Thus, many participants end up paying high premiums because they only can obtain coverage through states' assigned risk plans (insurers of last resort). Massachusetts successfully addressed many of its insurance agents' and carriers' concerns; however, its self-direction program benefits from a large number of participants—approximately 15,000 in 2007.

Addressing the Disconnects Between IRS Procedures and Medicaid Freedom of Choice of Provider Rules When a Participant Changes F/EAs Mid-Year

Participants switching F/EA providers in the middle of a calendar tax year has been, and continues to be, problematic for Vendor F/EAs and program staff. Often, when a mid-year switch occurs for any reason, it is difficult to reconcile federal taxes filed and paid by two different F/EAs (i.e., causing a bifurcated federal tax year). The answer is to have participants switch at the beginning of a calendar year after an “open” F/EA enrollment period. However, this strategy violates the Medicaid freedom of choice of provider rule and does not address situations when an F/EA switch can not be delayed until the end of the calendar year (e.g., when an F/EA ceases to provide services due to poor performance or when a participant moves to another part of the state and another F/EA must function in the first F/EA's stead).

Obtaining Health Insurance and Other Benefits for Direct Service Workers

Providing health insurance and other benefits (i.e., disability, dental, and vision insurance; vacation and sick leave; access to retirement savings plans) for participants' workers continues to be a challenge for state self-direction programs. Some efforts have been made to provide some type of health insurance coverage for workers but, to date, the benefits available under these plans are limited.⁶³

Resources

Publications

Centers for Medicare & Medicaid Services. (2008). *Application for a §1915(c) Home and Community-Based Waiver [Version 3.5]: Instructions, Technical Guide and Review Criteria.* Baltimore, MD: US Department of Health and Human Services (USDHHS).

This publication contains extensive information concerning federal policies that apply to the operation of an HCBS waiver, including incorporating self-direction into the delivery of waiver services.

Available as “Version 3.5 Instructions Final 2.1.2008”, a part of the 1915(c) Waiver Application and Accompanying Materials under links and downloads at: <https://www.hcbswaivers.net/CMS/faces/portal.jsp>

Doty, P. and Flanagan, S.A. (2002). *HIGHLIGHTS: Inventory of Consumer-Directed Support Programs.* Washington, DC: USDHHS, Assistant Secretary for Planning and Evaluation (ASPE).

This publication describes the results of a 2001 descriptive inventory of publicly funded HCBS programs that use a self-direction approach and various types of financial management services.

Available at: <http://aspe.hhs.gov/daltcp/Reports/highlight.htm>

Flanagan, S.A. (2004). *Accessing Workers’ Compensation Insurance for Consumer-Employed Personal Assistance Service Workers: Issues, Challenges and Promising Practices.* Washington, DC: USDHHS, Assistant Secretary for Planning and Evaluation.

This publication describes the results of a 50-state and seven jurisdictions (District of Columbia, five territories, and one tribal government) study of workers’ compensation laws and systems as they pertain to domestic service workers, and in particular, personal assistance workers.

Available at: <http://aspe.hhs.gov/daltcp/Reports/paswork.htm> and at <http://www.cashandcounseling.org/resources/20060113-121929>

Flanagan, S.A. & Green, P.S. (2000). *Fiscal Intermediaries: Reducing the burden of consumer-directed support.* *Generations.* vol. XXIV (III):94–97.

This publication describes the development of the Fiscal Conduit, Government and Vendor Fiscal Intermediary (Fiscal/Employer Agent) models, and current issues related to the implementation of these financial management service models.

Hughes, S.L., & Sabatino, C.P. (2004). *Addressing Liability Issues in Consumer-Directed Personal Assistance Services (CDPAS): The National Cash*

and Counseling Demonstration and Selected Other Models. Washington, DC: Department of Health and Human Services, Office of the Assistant Secretary for Planning and Evaluation.

This report addresses the liability issues that may arise in government-sponsored self-direction programs, including liability related to the provision of Fiscal Intermediary (Fiscal/Employer Agent) services. The report focuses on programs implemented in Arkansas, Florida, and New Jersey as part of the Cash & Counseling Demonstration and Evaluation and briefly describes an analysis of potential liability for the California In-Home Supportive Services Program and the New York Consumer-Directed Personal Assistance Program.

Available at: <http://www.cashandcounseling.org/resources/20051205-111452>

Web-Accessible Resources

Assistant Secretary for Planning and Evaluation (ASPE)

Web-address: <http://www.aspe.hhs.gov>

This website contains wide-ranging resources that address self-direction, the design and implementation of self-direction programs, labor, tax, workers' compensation insurance, and liability issues related to self-direction programs, and financial management services.

Cash & Counseling National Program Office

Web-address: <http://www.cashandcounseling.org>

This is the official website of the Cash & Counseling National Program Office. It contains extensive information about self-direction programs using the Cash & Counseling model, including the use of Government and Vendor Fiscal/Employer Agents.

Centers for Medicare & Medicaid Services

Web-address: [http://www.cms.hhs.gov/MedicaidStWaivProgDemoPGI/05_HCBSWaivers-Section1915\(c\).asp](http://www.cms.hhs.gov/MedicaidStWaivProgDemoPGI/05_HCBSWaivers-Section1915(c).asp)

This website contains extensive information concerning HCBS waiver programs, including those with self-direction options and financial management services. The website contains technical guidance concerning the design and operation of such programs.

Web-address: <http://www.cms.hhs.gov/PromisingPractices/HCBSPPR/list.asp>

This website contains information about promising practices that states employ to improve the delivery of HCBS to Medicaid participants, including self-directed services.

Clearinghouse for Home and Community Based Services

Web-address: <http://www.hcbs.org/>

This website serves as a portal to extensive information and resources about the delivery of HCBS to a wide range of Medicaid participants, including self-direction programs that offer a variety of financial management service models to participants and their representatives. For example:

Government and Vendor Fiscal/Employer Agent Workshop: Building Sustainable Fiscal Supports For Self-Directed Service Programs, authored by Susan Flanagan, includes presentations by states, vendors, and subject matter experts from the November 2007 F/EA Workshop. Topics include Promising Practices in Workers' Compensation, CMS Policies, the Role of Reporting Agents, Government and Vendor F/EA Operations, and Design and Implementation Issues.

Available at: *Web-address: <http://www.hcbs.org/moreInfo.php/doc/2092>*

Tasks to Be Performed By a Government and Vendor Fiscal/Employer Agent, prepared by Susan Flanagan, includes information to assist state and local program agency staff in understanding the requirements and key elements of Government and Vendor F/EA operations and developing a Government F/EA policies and procedures manual, when applicable.

Available at: *Web-address: <http://www.hcbs.org/moreInfo.php/doc/1880>*

Internal Revenue Service

Web-address: <http://www.irs.gov>

The official website of the Internal Revenue Service contains extensive information and resources regarding IRS policies, revenue procedures, notices, publications, and forms relevant to Government and Vendor Fiscal/Employer Agents, and household employers and their employees.

Citations, Additional Information, and Web Addresses

- 1 Susan Flanagan, MPH, Ph.D. is the author of this chapter.
- 2 Centers for Medicaid & Medicare Services (2008). *Application for a §1915(c) Home and Community-Based Waiver [Version 3.5] Instructions, Technical Guide and Review Criteria: Appendix C: Participant Services, Attachment: Core Services Definitions, Section D, Services in Support of Participant Direction, #2 Financial Management Services*, p.176. See the Resources section in this chapter for a link to this document.
- 3 Ibid. Appendix E: *Participant Direction of Services, Overview: Financial Management Services*, p.201. States may also provide cash to waiver participants by advancing state funds and only claiming federal match after goods and services have been rendered and receipts received.
- 4 CMS will not approve a §1115 waiver solely to offer a self-direction program. States are encouraged to implement self-direction programs either through the §1915(j) option under their Medicaid State Plan and/or the §1915(c) waiver option.
- 5 The term “neutral bank” is used because the F/EA is not providing direct care services to participants so it is “neutral” about which providers they use. Prior to the use of F/EAs, some participants with developmental disabilities found it difficult to move between/among agency service providers because their Medicaid benefit was often allocated to one service organization for the fiscal year, which had a financial interest in who provided services to participants.
- 6 Payroll includes, but is not limited to, the collection and processing of worker timesheets; making sure that workers are paid in accordance with federal and state labor laws; the withholding, filing and payment of federal and state income tax withholding and employment taxes, and locality taxes; processing of the advanced federal earned income credit, when applicable, and any garnishments, liens or levies against workers pay, as required; and generating and distributing payroll checks.
- 7 Also referred to legally as a “joint employer” relationship; the term co-employment is often used to describe the relationship among two or more employers when each has specific actual or potential legal responsibilities to the same worker or group of workers.
- 8 When participants are not able or willing to act solely as their workers’ employer, their representatives can assume this role if they are willing to do so.
- 9 The “Operating Entity” refers to the organization providing the FMS, not the operating entity of a Medicaid §1915(c)waiver.

- 10 June 2002 version of IRS Form 2678, *Employer Appointment of Agent*, Instructions.
- 11 Some local governments are authorized to impose a variety of local taxes from earned income tax to real property taxes to various other taxes. Some of these are imposed on workers and withheld and deposited by their employers. For example, Pennsylvania has both a local Earned Income Tax (EIT) and a Local Services Tax (LST) (formerly know as the Emergency and Municipal Service Tax and before that the Occupational Tax).

All employers with work sites within the taxing jurisdiction are required by law (PA Act 7 of 2007, The Local Tax Enabling Act which amended PA Act 511 of 1965) to register with the appropriate municipal authority. An employer then deducts EIT and LST from their employees' wages and deposits them with the municipal authority if the taxes are listed in the Local Tax Register of the PA Department of Community and Economic Development for the municipality.

- 12 Participants may also interview and select a worker referred by the agency for assignment back to them.
- 13 Based on Scherzer, T., Wong, A., & Newcomber, R. (2007). Financial management services in consumer-directed programs. *Home Health Services Quarterly*, 26(1), 35–36.
- 14 Ibid.
- 15 Doty, P. and Flanagan, S.A. (2002). *HIGHLIGHTS: Inventory of Consumer-Directed Support Programs*. U.S. Department of Health and Human Services, Washington, DC, p.4. Of the 139 self-direction programs reviewed, which reported using some model of financial management services: 45 percent used the Vendor F/EA model, 21 percent used the Agency with Choice model, 12 percent used the Fiscal Conduit model, six percent used the Government F/EA model, and one program (California's In-Home Supportive Services Program) used a Public Authority. Washington State reported using a model of FMS where the state is the statutory employer of participants' workers for the purpose of processing payroll in accordance with §3401(d)(1) of the IRS code.

Staff from the IRS Office of General Counsel for Employment Tax reported that states should implement FMS under §3504 of the IRS code rather than §3401(d)(1) of the IRS code so that the FMS entity may file and deposit federal income tax withholding and FICA in the aggregate, an option not available to statutory employers under §3401(d)(1) of the IRS code.

- 16 IRS Proposed Notice 2003–70, Q&A #18.
- 17 Fiscal Conduit services are provided effectively under the Government

or Vendor F/EA models because of the fiscal nature of their tasks and the fact that participants using the Fiscal Conduit FMS model are the common law employers of the workers they hire directly like participants who use Government or Vendor F/EA services.

- 18 <http://www.irs.gov/businesses/small/article/0,,id=99921,00.html>
- 19 IRS Proposed Notice 2003–70, Q&A #5.
- 20 Flanagan, S. A., & Green, P. S. (2000). Fiscal Intermediaries: Reducing the burden of consumer-directed support. *Generations*, 24(111), 94–95. This publication describes the development of Fiscal/Employer Agents and current issues.
- 21 June 2002 version of IRS Form 2678, Employer Appointment of Agent, Instructions.
- 22 An FEIN is obtained by completing and filing the IRS Form SS-4, *Application for Employer Identification Number* with the IRS. Federal employment taxes include Medicare and Social Security taxes or FICA (Federal Insurance Contribution Act) and FUTA (Federal Unemployment Tax Act).
- 23 Agent approval is obtained by the Government F/EA filing one IRS Form 2678, *Employer/Payer Appointment of Agent*, for the program. Then it must execute (but not submit to the IRS) an IRS Form 2678 with each participant it represents and maintain the form in each participant’s file. When the Government F/EA ceases being the employer agent for a participant permanently, it must revoke the IRS Form 2678 it has with the participant, per IRS instructions, and keep the revoked form in the participant’s file (i.e., not submit it to the IRS).

If the Government F/EA delegates employer agent tasks to a reporting agent, it must execute an IRS Form 8655, *Reporting Agent Authorization*, between itself and the reporting agent. This form should be revoked per IRS instructions if/when the Government F/EA ceases to use the reporting agent.

If the Government F/EA delegates employer agent tasks to a subagent, the subagent must execute and submit to the IRS an IRS Form 2678, *Employer/Payer Appointment of Agent*, with the Government F/EA to obtain authorization to be the employer agent to the Government F/EA. This form should be revoked per IRS instructions if/when the Government F/EA ceases to use the subagent.

- 24 The Government F/EA also obtains federal tax information authorization to communicate with the IRS regarding federal taxes it files and deposits on participants’ behalf by executing an IRS Form 8821, *Tax Information Authorization*, with each participant it represents as employer agent and

submitting it to the IRS.

If the Government F/EA uses a reporting agent or subagent it should list this entity as a second appointee on the Form 8821 it executes with the participant.

If the Government F/EA uses a subagent, it should execute an IRS Form 8821 between itself and the subagent and submit it to the IRS so that the subagent has authorization to communicate with the IRS regarding federal taxes it files and deposits on the Government F/EA's behalf.

Each IRS Form 8821 executed needs to be renewed periodically and should be revoked if the Government F/EA no longer represents the participant permanently, per IRS Form 8821 instructions.

- 25 10/07 IRS Form 2678, *Employer/Payer Appointment of Agent*, Instructions.
- 26 A subagent, is defined by the IRS in Proposed Notice 2003–70, Section II, *Definitions*, as “an individual or entity designated as agent by a state agent in accordance with Rev. Proc. 70–6 and this revenue procedure.”
- 27 A reporting agent, is defined by the IRS in Proposed Notice 2003–70, Section III, as “an accounting service, bank, service bureau or other entity authorized to perform one or more acts on behalf of an employer, including sign and file IRS Forms 940 and 941 and make federal tax deposits for the taxes reported on those forms.”
- 28 Paperwork reductions granted to Government F/EAs and their reporting agent and subagents, when applicable, include: (1) applying for and receiving employer agent approval for all participants enrolled in a self-direction program through one authorization application, rather than filing for and obtaining IRS employer agent authorization for each participant as Vendor F/EAs have to; (2) filing and depositing FUTA in the aggregate using its special FEIN (this also applies when a Government F/EA is using a reporting agent or subagent); and (3) being able to deposit federal income tax withholding, FICA, and FUTA when they are filed using the IRS Forms 941 and 940, respectively. Item 3 applies only when Government F/EAs use reporting agents—but not subagents.
- 29 IRS Proposed Notice 2003–70, Q&A-19. In addition, a Government F/EA can only use one reporting agent or subagent. The Government F/EA or its reporting agent or subagent files and deposits federal income tax withholding, FICA and FUTA in the aggregate using the IRS Forms 941 and 940, respectively, the Government F/EA's contact information and its special FEIN.
- 30 IRS Proposed Notice 2003–70, Q&A-19 and 10/07 IRS Form 2678, *Employer/Payer Appointment of Agent*, Instructions.

- 31 IRS Proposed Notice 2003–70, Q&A 25. The Government F/EA’s separate FEIN should be reported in Part 2 of the form and the subagent’s corporate FEIN reported in Part 3 of the form. A Government F/EA can only use one subagent as discussed in Endnote 28.
- 32 IRS Proposed Notice 2003–70, Q&A-26.
- 33 See Endnote 28.
- 34 Participants’ choice of provider is limited because per IRS regulations, only one entity (a Government F/EA or its reporting agent or subagent if it chooses to use one) can file and deposit the required federal taxes for participants and their workers under the same entity name and FEIN on the required IRS Forms.
- 35 It is important for state program agencies and F/EAs to obtain state and local tax information and guidance in writing so that policies and procedures are consistent even when there is a change in state and local tax agency staff.
- 36 IRS Form 2678, *Agent/Payer Authorization*, (rev. October 2007). Although the IRS has clarified that Vendor F/EAs may use reporting agents, some states may require a Vendor F/EA to perform all employer agent tasks itself.
- 37 This FEIN should be in addition to the entity’s corporate FEIN and only participants’ and their workers’ federal income tax withholding and employment taxes should be reported and deposited using this FEIN.
- 38 A Vendor F/EA must revoke its employer agent authorization with the IRS when it no longer represents a participant-employer permanently.
- 39 This is accomplished by executing an IRS Form 8821, *Tax Information Authorization*, with each participant it represents as an agent and filing it with the IRS. The Vendor F/EA must renew this authorization periodically and revoke it if and when it no longer represents a participant permanently per Form 8821 instructions. If the Vendor F/EA uses a reporting agent, it should list the entity as a second appointee on Form 8821.
- 40 IRC §31.3504–1 as described in the 8/13/07 IRS letter to Ellen Wendt, F/SE Manager at MRCI in Mankato, MN, from Curtis L. Freedman, Chief of the Business Forms and Publications Branch. During the period of operation before Vendor F/EA authorization is received, the taxpayer (the participant or his/her representative) is liable for the payment of any unfulfilled federal income tax withholding, including penalties and interest. However, IRS Office of General Counsel for Employment Tax reported that if these taxes and associated penalties and interest can not be collected from the taxpayer, the IRS will follow the flow of funds to the original source (e.g., the self-direction program agency or Medicaid agency, as applicable).

- 41 IRS Proposed Notice 2003–70. Q&A-19.
- 42 If a state implements a Medicaid State Plan self-direction program in accordance with §1915(j) of the Social Security Act, the costs associated with Vendor F/EA services must be billed as an administrative expense for the purpose of claiming federal matching funds.
- 43 Staff at the IRS Office of General Counsel for Employment Tax reported that if there is any unfulfilled federal income tax withholding or employment tax obligation, including penalties and interest, that can not be addressed by a Vendor F/EA, or for that matter a reporting agent or subagent under contract with a Government or Vendor F/EA, the IRS will follow the flow of funds back to the original source (i.e., the state’s Medicaid program) to recover these obligations.
- 44 Minnesota had and Montana has a state unemployment insurance law that prohibits individuals receiving publicly funded services from being the common law employer of their workers. Minnesota Unemployment Insurance Law §268.035 Definitions subd. was subsequently amended to allow participants in self-direction programs to be the common law employers of their workers. Montana currently is reviewing its law to determine what, if any, amendments can be promulgated to facilitate the implementation of self-directed services using a Vendor F/EA.
- 45 Under §6087 of the Deficit Reduction Act of 2005.
- 46 States that limit the number of Vendor F/EA providers available to participants include, but are not limited to, Alabama, Idaho, Iowa, Illinois, Maryland, Massachusetts, Missouri, New Jersey, New Mexico, Tennessee, Virginia, and Vermont. Alabama has implemented its pilot self-direction program under its Medicaid State Plan by using the §1915(j) authority of the Social Security Act. New Jersey converted its Personal Preference Program from operating under a §1115 Medicaid Demonstration Waiver to the §1915(j) authority effective July 1, 2008. The Missouri Division of Developmental Disabilities has implemented a Government F/EA and performs all tasks internally. West Virginia’s Bureau of Medical Services and Florida’s Department of Elder Affairs and Agency for Persons with Disabilities have implemented a Government F/EA and use a subagent. States that restrict participant choice of F/EA provider, including states that implement Government F/EAs or programs using §1915(j) of the Social Security Act, are reimbursed for F/EA costs at the federal administrative matching rate.
- 47 States include, but are not limited to: Pennsylvania (53 percent Medicaid service match rate), Michigan (58.10 percent Medicaid service match rate), Minnesota (50 percent Medicaid service match rate), and Rhode Island (52.35 percent service match rate).

- 48 Massachusetts implemented an abbreviated Vendor F/EA cost report for a two-year period to determine the costs of providing Vendor F/EA services. During that period, the Vendor F/EAs were paid based on an initial F/EA rate that was retroactively adjusted at the end of the rate year based on the allowable costs reported on their cost report. Once a historic cost base was determined, the State implemented a flat PMPM rate for all Vendor F/EAs. In FY 2006, the State converted its PMPM F/EA rate to a per diem rate (\$1.72/day for an annual cost of \$627.80 per participant per year).
- 49 CMS guidance for acceptable FMS payment methodologies for services provided under a Medicaid §1915(c) waiver is contained in the waiver application instructions with an acknowledgement that these policies are continually evaluated for their efficacy.
- 50 At least one state (Utah) has implemented a two-tiered PMPM rate schedule to reflect the potential variation in F/EA transactions. Effective July 1, 2008 the low usage cluster rate for F/EA services will be \$30.08 PMPM and the rate for the high usage cluster will be \$98.30 PMPM, according to Paul Day, MPA at the Utah Department of Human Services Division of Services for People with Disabilities.
- 51 CMS §1915(c) HCBS Waiver Application Instructions, Appendix E, Item E-1-I Provisions of FMS, version 3.5, p.204. See the Resources section in this chapter for a link to this document.
- 52 Transitioning a participant from one F/EA to another at any time other than at the beginning of a calendar year will result in a bifurcated federal tax year, which creates problems that are difficult for F/EAs to resolve due to the aggregate filing and depositing of federal income tax withholding and employment taxes. In addition, the new F/EA may have to resolve errors and omissions made by the previous F/EA, which can be time consuming and costly. Finally, customer service costs can increase due to increased calls from participants who are transitioning.
- 53 Although both counselors and F/EA entities provide employer orientation and skills training—depending on the program—opinions differ about which entity should provide these supports.
- 54 Some states report that they perform audits of F/EAs. However, a true financial audit is costly as it must meet the requirements of generally accepted accounting principles which are extensive. To address the fiscal issues related to F/EA operations, state program staff often enlist financial audit staff resources to assist in the development of the protocol and participate in the performance of either ongoing performance reviews, often referred to as “agreed-upon procedures reviews,” or F/EA recertifications.

- 55 These include, but are not limited to: (1) obtaining federal agent authorizations; (2) obtaining F/EA's special FEIN and participant-employers' FEINs; (3) withholding, filing, and depositing federal and state income tax withholding, employment taxes and locality taxes for participants and their workers; (4) establishing state/local employer accounts and powers of attorney, as required, for state income tax withholding and employment tax filing and depositing any required locality taxes; (5) ensuring workers are paid in accordance with federal and state department of labor rules; (6) registering workers in accordance with state new hire reporting requirements; (7) performing US Bureau of Citizenship Services requirements for verifying workers' citizenship and legal alien status; (8) verifying workers' social security numbers; and (9) brokering workers' compensation insurance coverage for participants in accordance with applicable laws.
- 56 Materials should be available in alternate formats such as Braille, large print, and audiocassette.
- 57 Optical character recognition, usually abbreviated to OCR, is defined by Wikipedia as "the mechanical or electronic translation of images of handwritten or typewritten text (usually captured by a scanner) into machine-editable text." The OCR term has been broadened to include digital image processing as well. Electronic document management is defined by Wikipedia as "a computer system (or set of computer programs) used to track and store electronic documents and/or images of paper documents. The term has some overlap with the concepts of content management systems and is often viewed as a component of enterprise content management systems and related to digital asset management, document imaging, workflow systems and records management systems."
- 58 Losses can occur if workers are not paid on time and checks they have written bounce, leading to bank charges.
- 59 Prior to the development of this code, Massachusetts used National Council on Compensation Insurance (NCCI) codes 0908, Domestic Service, Inside, Part-time and 0913, Domestic Service Inside (full-time) to rate personal care workers for workers' compensation insurance purposes. These codes did not accurately reflect the tasks performed by workers. NCCI subsequently inappropriately amended these codes by deleting personal assistance workers and including them in NCCI code 8835, *Homemaker Services*, with home health industry providers. This resulted in excessive workers' compensation insurance premiums for personal care/support service workers.
- 60 The insurance agent was C.J. McCarthy Insurance (now Hub International) and the insurer was Atlantic Charter. For the rating period (2/1/07–2/1/08), the cost per household policy for all workers working in the home was approximately \$292.46.

- 61 Veridian Credit Union, Waterloo, IA.
- 62 Flanagan, S.A. (2004). *Assessing Workers' Compensation Insurance for Consumer-Employed Personal Assistance Service Workers: Issues, Challenges and Promising Practices*, for US Department Health and Human Services, Washington, DC: June 7th.
- 63 One Vendor F/EA in Pennsylvania—a Center for Independent Living—was able to broker limited health insurance coverage for workers employed by participants the CIL represents as their F/EA. They added the workers to a group policy offered by the PA Council on Independent Living to its members.