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## MEMORANDUM

March 13, 2018

TO: Contract Support Cost Clients

FROM: Hobbs, Straus, Dean & Walker, LLP /s/

RE: ***IHS CSC Workgroup Meets, Reaches Compromise Recommendation on 97/3 Option***

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The Indian Health Service (IHS) Contract Support Cost (CSC) Workgroup met March 6-7, 2018, in Albuquerque to address IHS's recent and abrupt departure from the CSC policy it negotiated and agreed to with tribes. As we have reported, in December IHS unilaterally rescinded the so-called 97/3 method for determining a duplication offset for indirect costs included in Service Unit funding assumed by tribes. Like the longstanding 80/20 rule for Area Office and Headquarters tribal shares, the 97/3 option allows tribes to accept a default duplication offset—3% of Service Unit shares—and spare themselves and IHS the ordeal of scrutinizing Service Unit funding line-by-line in search of duplicated costs.

The tribal response to IHS's unilateral action ranged from disappointment to outrage, and the meeting provided an opportunity to clear the air and reset the relationship. It only partially succeeded in doing so, though it did result in a compromise recommendation.

### *Acting Director's Opening Remarks*

Tribal representatives had requested that Rear Admiral Michael Weahkee, the Acting Director of IHS, attend the Workgroup meeting. For his opening remarks, RADM Weahkee read from a prepared statement that essentially followed the script of his February 16, 2018 letter to Tribal Co-Chair Andy Joseph.<sup>1</sup> He said that the group was "not here to negotiate a policy," by which he apparently meant that the Workgroup's role is merely to provide recommendations to IHS, which makes the decisions. He pointed to two agency imperatives that seem to be in tension if not contradiction. On the one hand, IHS seeks to simplify its bureaucratic processes, including those for the calculation and payment of CSC, in accordance with the Administration's initiative to reduce red tape.

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<sup>1</sup> See our report of February 21, 2018 for a description of the letter and the correspondence leading up to it.

(The 97/3 option, along with its much older sister the 80/20 rule for tribal shares, presents the preeminent example of such simplification in the CSC policy.) On the other hand, IHS must comply with all applicable laws, and IHS and its lawyers have concluded that the 97/3 method, in some instances, results in violations of the Indian Self-Determination and Education Assistance Act (ISDEAA). The charge of the Workgroup was to resolve, if possible, this tension.

Co-Chairman Joseph framed a simple response: We had an agreement, and it should be honored. IHS's unilateral revocation of the 97/3 option damaged tribes' trust in IHS and the government-to-government relationship. Other tribal representatives echoed the sense of frustration and sadness that a hard-fought compromise could be so easily cast aside. Tribes recognize that they have a fundamental legal difference with IHS over the meaning of the ISDEAA's mandate to avoid duplication of costs, but as litigation of that issue proceeds, the 97/3 option provides an efficient and practical method for both sides to arrive at a reasonable agreement while avoiding contentious line-by-line negotiations. IHS came under particular criticism for the way in which its decision was imposed with no notice, let alone consultation, violating several of the guiding principles included in the policy as well as the general principle of respect on which the government-to-government relationship is based.

This procedural point seemed to hit home with Acting Director Weahkee and the other IHS officials, who acknowledged that the rollout process could have been handled much better. Still, they stressed that, as much as they personally would like tribes to be better funded, IHS bears a "federal fiduciary responsibility" to taxpayers to avoid CSC overpayments. Elizabeth Fowler, IHS Deputy Director for Management Operations, said that the legality of the CSC policy is under scrutiny by the Department, as the Department's former General Counsel Alex Azar now serves as the Secretary. RADM Weahkee noted that, in any event, the 97/3 option has been revoked temporarily, not permanently, pending consultation.

#### *IHS Data on 97/3 vs. "Known" Amounts of Duplication*

Tribal representatives had requested, in Chairman Joseph's January 3 letter, that IHS provide the Workgroup the data on which the agency relied in making its decision to abruptly rescind the 97/3 option. IHS belatedly complied with that request by transmitting the attached letter dated March 5, 2018, on the eve of the Workgroup meeting. The letter contains a table with data on instances where "application of the 97/3 method does not conform with the ISDEAA." A quick review of the table—which is all tribal representatives had time for—confirmed that implementation of the 97/3 option is hardly causing a federal fiduciary crisis. First, the table contains only 13 "cases," reflecting the fact that the 97/3 option applies sparingly and the vast majority of tribal contracts and compacts are grandfathered under the policy. Second, at least some of these cases, including Case 1, IHS's primary example of an alleged ISDEAA violation, are purely hypothetical, as the tribal organization has accepted the "known" offset and not even asked for the 97/3 option. Third of the 13 cases, perhaps 6 show significant differences

unfavorable to IHS between the 3% and "known" amounts; the rest are either in IHS's favor or a virtual wash. Fourth, it is not clear how IHS has calculated the "known" amounts of indirect cost funding associated with service unit shares in column 4; IHS presented no methodology or calculations for these figures.

Roselyn Tso, CSC lead for IHS, acknowledged that the table demonstrates that for the most part the 97/3 option works, as in several instances the 97/3 and "known" amounts differed by around 3% or less. But in a few cases the 97/3 offset came in significantly lower than the "known" amount, causing the agency consternation.

IHS clarified that in all 13 instances, IHS and the tribe or tribal organization had already negotiated and agreed on a duplication offset number, but in some cases the tribe or tribal organization had come back and proposed the 97/3 option instead of the negotiated ("known") amount. As Ms. Fowler clarified, "known" means negotiated, calculated, and agreed on. So the IHS focus is on past negotiations that have been completed but that a tribe subsequently seeks to reopen.

Given the limited applicability of 97/3, and the even rarer cases in which the use of 97/3 results in a significantly different offset than a close analysis, tribal representatives called on IHS to reinstate the 97/3 option and deal with outliers on a case-by-case basis. The policy states that the ISDEAA prevails in the case of a conflict, so this "ISDEAA supremacy clause" provides IHS ample authority to deal with these few exceptions to the general rule that the 97/3 method works. Tribal representatives conveyed a consensus position that the policy need not, and should not, be changed at all.

IHS rejected these positions and insisted that the policy must be changed. The current language, according to Ms. Fowler, is "a direct contradiction to a legal position that the agency holds" on duplication of costs, and if the Workgroup couldn't come up with a recommendation to resolve this conflict, IHS would implement a solution itself.

#### *Proposals, Counterproposals, and Recommendation on 97/3*

Tribal representatives gamely crafted language narrowly addressing the IHS concern, which involves the third "trigger" requiring a duplication analysis: when a tribe seeks to renegotiate the duplicative Service Unit amount. (The other two triggers are (i) assumption of new or expanded programs, and (ii) new costs in the indirect cost pool resulting in a change in the value of the pool of 5% or more. Neither of these scenarios are at issue.) Tribes proposed that, in the case of a tribal renegotiation request—but only in that case—tribes would no longer be able to compel a 3% offset but that the parties would negotiate the offset using a line-by-line analysis, 97/3, "or any other mutually acceptable approach." IHS countered with language that would have made duplication under *all three* trigger scenarios subject to negotiation through line-by-line analysis, 97/3, or "any other

mutually acceptable approach." In other words, tribes would lose the ability to elect the approach they wished to take, effectively nullifying the 97/3 option in all scenarios.<sup>2</sup>

Tribal representatives responded to the IHS proposal with dismay, but took a last shot at compromise language, proposing a limited carve-out similar to their first proposal. The policy's section on alternatives for calculating duplication of Service Unit shares would read as follows (new language highlighted):

Limited to the above circumstances, the awardee shall elect the method for determining the amount of IDC associated with the Service Unit shares and the remaining IDC that may be eligible for CSC funding, to identify duplication, if any, pursuant to 25 U.S.C. § 5325(a)(3), using one of two options listed below or any other mutually acceptable approach. In connection with 3.iii, above, if an earlier funding agreement reflects a prior identification of duplicated Service Unit costs, then the parties shall negotiate a new duplicate amount considering the alternatives available under Alternative A [line-by-line], Alternative B [97/3], or any other mutually acceptable approach.

The general rule would stay the same: in "the above circumstances"—i.e., all three trigger scenarios—the tribe gets to elect whether to go line-by-line, take the 97/3 split, or use some other method. But in scenario 3.iii—when a tribe seeks to renegotiate the duplication—the tribe does not get to choose the method *if an earlier funding agreement already identifies a duplication amount*. In other words, if the parties have already negotiated and agreed on a duplication amount, the tribe would not be able to elect the 97/3 method to reduce that amount.

The federal representatives agreed with this approach, and the Workgroup voted unanimously to recommend that this change to the policy be put forward for tribal consultation. IHS will issue a "Dear Tribal Leader" letter announcing the proposed change and setting a 30-day period for consultation.

Thus tribes succeeded in limiting the proposed change to the rare circumstance in which the parties have already negotiated and agreed on a duplication offset and the tribe seeks to re-open those negotiations. If IHS eventually agrees to reinstate the 97/3 option in all other circumstances, the damage will have been minimized.

#### *Indirect-Type Costs and Duplication*

As you know, under the IHS CSC policy tribes may negotiate a lump sum for indirect-type costs—or may have to do so if the tribe's indirect cost rate is expired. During

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<sup>2</sup> The IHS language would also have changed the applicability of the duplication options from "the negotiation of indirect CSC funding in or after FY 2016" to "ISDEAA agreements entered into in or after FY 2017." Tribal representatives objected to this change, IHS did not push it, and it was not included in the proposed policy revision described below.

the discussions of duplication, it came to light that IHS believes the 97/3 option is never available to establish the duplication offset for indirect-type costs. That is because, according to IHS, the agency must conduct a line-by-line analysis simply to establish the allowable costs, which necessarily entails weeding out duplication.

Tribal representatives felt this position unfairly deprives some tribes of the 97/3 option merely because they negotiate indirect-type costs. The IHS approach could also result in a double-duplication offset, as IHS applies a line-by-line analysis up front and then lops off another 3% on the back end. To address this problem, tribal Workgroup members proposed an amendment that would add the following sentence to section 6-3.E(2) of the policy:

The identification of indirect-type costs shall not reflect any deduction for duplicated costs, and shall be limited to an assessment of the appropriateness of costs as described above. Duplicated costs shall be identified as provided in Section 6-3.2E(3).

So if a tribe negotiating indirect-type costs tells IHS it elects the 97/3 method, the process should then proceed in two steps: (1) negotiate the full amount of costs, regardless of duplication; (2) apply the 3% duplication offset.

IHS refused to endorse the tribal amendment. Instead, the agency agreed to establish a small tribal-federal subgroup to review data IHS has on this issue, with the full Workgroup to reconvene in 45-60 days to revisit and resolve this issue.

### *Conclusion*

The 97/3 option remains out of play pending the upcoming tribal consultation, but it appears that if the Workgroup amendment is ultimately approved, the 97/3 option will be reinstated except in the narrow circumstances described above. In the meantime, a subgroup will analyze data from indirect-type cost negotiations and develop some recommendations for the Workgroup's next meeting.

We will continue to follow CSC developments in both IHS and the Bureau of Indian Affairs on your behalf. If you have any questions about this memorandum, please do not hesitate to contact Joe Webster ([jwebster@hobbsstrauss.com](mailto:jwebster@hobbsstrauss.com) or 202-822-8282), Geoff Strommer ([gstrommer@hobbsstrauss.com](mailto:gstrommer@hobbsstrauss.com) or 503-242-1745), or Steve Osborne ([sosborne@hobbsstrauss.com](mailto:sosborne@hobbsstrauss.com) or 503-242-1745).