Department of Health and Human Services

DEPARTMENTAL APPEALS BOARD

Appellate Division

SUBJECT: Babyland Family Services, Inc. DATE: August 28, 2007
Docket No. A-07-19
Decision No. 2109

DECISION

By letter dated November 7, 2006, Babyland Family Services, Inc. (Babyland) appealed the decision of the Administration for Children and Families (ACF) to terminate Babyland's Early Head Start Program (EHSP) grant. ACF relied on Babyland's "failure to correct all deficiencies within the time period specified in prior written notice." ACF letter to Babyland at 1 (Oct. 5, 2006)(ACF termination notice). Babyland argued that it submitted a corrective action plan, which ACF did not reject, and that all the cited deficiencies were corrected before Babyland received the termination notice. Babyland also alleged that all of the deficiencies cited in the termination letter were included in the corrective action plan and corrected before the date of the termination letter. Babyland therefore asked that the termination be dismissed as premature and, in the alternative, for a hearing. ACF denied that Babyland was given (or was required to be given) an opportunity to file a corrective action plan instead of correcting all the deficiencies within 30 days Of receipt of ACF's initial review report. ACF moved for summary disposition on the grounds that Babyland did not dispute the facts of the deficiency findings or allege that they were corrected within 30 days as required.

For the reasons explained below, we conclude that Babyland was required to correct the deficiencies within 30 days of receipt of the initial review report, regardless of whether Babyland prepared a corrective action plan. Babyland has not challenged the factual bases for the deficiency findings and has offered no evidence that the deficiencies were corrected within the 30 days allowed. Whether some or all were corrected after that date is not relevant. We conclude that Babyland's legal arguments are unavailing and termination is justified as a matter of law. We have also considered all of Babyland's other arguments for reversing the termination but find them without merit. Given the

undisputed facts we find here, we find no material issue about which to conduct an in-person hearing. Therefore, we deny Babyland's requests for dismissal or, in the alternative, for a hearing, grant ACF's motion for summary affirmance, and uphold the termination action.

Applicable law

Head Start is a national program providing comprehensive developmental services, including health, nutritional, educational, social and other services, to economically disadvantaged preschool children and their families. 42 U.S.C. §§ 9831 et seq. The EHSP specifically provides "low-income pregnant women and families with children from birth to age 3 with family-centered services that facilitate child development, support parental roles, and promote self-sufficiency." 45 C.F.R. § 1304.3(a)(8). The Secretary of the Department of Health and Human Services (HHS), is empowered to establish by regulation performance standards for Head Start services, including administrative and financial management standards. 42 U.S.C. § 9836a.

HHS, through ACF, provides funds to grantees to serve as Head Start agencies within designated communities and periodically reviews their performance in meeting program, administrative, and fiscal requirements. See generally 42 U.S.C. § 9836. Full reviews are conducted at least once during each three-year period, in addition to "followup reviews including prompt return visits to agencies and programs that fail to meet the standards." 42 U.S.C. § 9836a(c)(1)(A) and (C).

If as a result of a review, ACF finds that a grantee has one or more "deficiencies," the Head Start Act provides that ACF shall –

> (A) inform the agency of the deficiencies that shall be corrected;
> (B) with respect to each identified deficiency, require the agency--
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> > (i) to correct the deficiency immediately, if the Secretary finds that the deficiency threatens the health or safety of staff or program participants or poses a threat to the integrity of Federal funds;
> > (ii) to correct the deficiency not later than 90 days after the identification of the deficiency if the Secretary finds, in the discretion of the Secretary, that such a 90-day period is reasonable, in light of the nature and magnitude of the deficiency; or

> (iii) in the discretion of the Secretary (taking into consideration the seriousness of the deficiency and the time reasonably required to correct the deficiency), to comply with the requirements of paragraph (2) concerning a quality improvement plan [(QIP)]; and
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> (C) initiate proceedings to terminate the designation of the agency unless the agency corrects the deficiency.

42 U.S.C. 9836a(d)(1).

The implementing regulations provide that the "responsible HHS official" must "notify the grantee promptly, in writing, of the finding, identifying the deficiencies to be corrected and, with respect to each identified deficiency, . . . inform the grantee that it must correct the deficiency either immediately or pursuant to a [QIP]." 45 C.F.R. § 1304.60(b).

The QIP must be approved by the responsible HHS official and must meet certain requirements. See 42 U.S.C. § 9836a(2)(A); 45 C.F.R. § 1304.60(d). The statute prescribes a 30-day period in which to either approve a QIP or specify why it is not approvable. 42 U.S.C. § 9836a(2)(B). The period for correcting deficiencies under an approved QIP may, in any case, not exceed one year from the date the grantee is notified about them. 42 U.S.C. § 9836A(d)(2)(A); 45 C.F.R. § 1304.60(c).

The term "deficiency" is defined, in relevant part, as an -

> area or areas of performance in which an Early Head Start . . . grantee agency is not in compliance with State or Federal requirements, including but not limited to, the Head Start Act or one or more of the regulations under parts 1301, 1304, 1305, 1306, or 1308 of this title and which involves:
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> (C) A failure to perform substantially the requirements related to . . . Program Design and Management; or
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> (D) The misuse of Head Start grant funds.

45 C.F.R. § 1304.3(a)(6)(i). Failure to perform "substantially" does not "necessarily mean that a majority of the requirements are not being met but, rather, that a knowledgeable person reviewing the findings would determine that the grantee agency is

not operating a quality program." 61 Fed. Reg. 57,185, 57,207 (Nov. 5, 1996).

Section 1304.3(a)(6)(iii) provides that "any other violation" of the Head Start Act or regulations which "the grantee has shown an unwillingness or inability to correct within the period specified by the responsible HHS official, of which the responsible HHS official has given the grantee written notice of [sic] pursuant to section 1304.61" is also to be considered a "deficiency." Under this provision, a violation of the Head Start Act or regulations that does not constitute a deficiency under sections 1304.3(a)(6)(i) or (ii) is deemed to be a deficiency only after the grantee has demonstrated an inability or unwillingness to correct it within the time frame specified by the responsible HHS official.

The federal requirements with which ACF alleged that Babyland was not in compliance included program requirements in 45 C.F.R. Part 1304 and grant administration requirements in 45 C.F.R. Part 74, Office of Management and Budget (OMB) Circular A-133 (Audits of States, Local Governments, and Non-Profit Organizations), and Cost Principles for Non-Profit Organizations (OMB Circular A-122) codified at 2 C.F.R. Part 230.

Termination of a grantee is justified in the following situations, as relevant here:

> (3) The grantee has failed to comply with the required fiscal or program reporting requirements applicable to grantees in the Head Start program;
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> (4) The grantee has failed to timely correct one or more deficiencies as defined in 45 C.F.R. Part 1304;
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> * * *
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> (7) The grantee has failed to comply with the requirements of the Head Start Act; [or]
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> (9) The grantee fails to abide by any other terms and conditions of its award of financial assistance, or any other applicable laws,

> regulations, or other applicable Federal or State requirements or policies.

45 C.F.R. § 1303.14(b). Section 1304.60(f) states that any deficiency that is not timely corrected shall also be considered a material failure of a grantee to comply with the terms and conditions of an award within the meaning of 45 C.F.R. § 74.61(a)(1).[1]

Factual background

This section sets out factual and historical matters that are not in dispute as a context for our discussion of the issues raised in this appeal. Babyland is a not-for-profit childcare services agency operating since 1970 and providing EHSP services since June 1998. During the program year from June 1, 2005 through May 31, 2006, Babyland received $1,294,496 in funding for EHSP.

Babyland's independent audit report for the period ending June 30, 2004 was not received by ACF until June of 2005 and concluded that since "Babyland does not maintain certain accounting records and supporting documents or have adequate internal

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[1]Section 74.61(a)(1) is part of the Department's uniform administrative requirements for certain types of grant awards, including awards to nonprofit organizations such as Babyland. It provides in relevant part that grants may be unilaterally terminated by the HHS awarding agency only "if a recipient materially fails to comply with the terms and conditions of an award." The preamble to the Head Start regulations explains that section 1304.60(f) was promulgated as --

> part of the implementation of the requirement at Section 641A(d)(1)(C) of the Head Start Act, as amended, that the Secretary must initiate proceedings to terminate the designation of an agency as a Head Start grantee unless the grantee corrects the deficiency; it also is consistent with past agency interpretation that the failure to comply with any of the Program Performance Standards and other requirements constitutes a material breach of the terms of the grant. The language also further establishes that, since a deficiency, by its nature, materially impairs the accomplishment of program goals, the failure to correct a deficiency in a timely manner will constitute grounds for termination.

61 Fed. Reg. 57,185, 57,207.

control . . . the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements." ACF Ex. 3, at 1. The auditors determined that Babyland had suffered a decline in net assets of $1,911,123 in the past year and recurring net losses over the preceding couple of years, and was in an uncertain financial position due to an "increase of $117,000 in the cash overdraft, non-compliance with certain financial and reporting covenants regarding its bank line of credit, the unknown status of various legal matters with Babyland's attorneys, and the possibility of recoupment of costs found to be ineligible." Id. at 9. As a consequence, the auditors noted that "Babyland's ability to continue as a going concern" was in doubt. Id. The auditors reported four material weaknesses in internal control relating to failure to perform timely monthly bank reconciliations (Finding 2004-1), failure to file timely reports with grantor agencies (Finding 2004-2), recording of many journal entries without supporting documentation (Finding 2004-3), and lack of information to support allocation of expenses among program, administrative and fundraising costs (Finding 2004-4). Id. at 16-20. The auditors described the reportable conditions they observed as "significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect [Babyland's] ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements." Id. at 21.

ACF also reports, and Babyland does not dispute, that additional problems were identified during an on-site Program Review Instrument for Systems Monitoring (PRISM) review in August 2004. ACF gave Babyland 90 days from November 9, 2004 to correct the areas of noncompliance and submit a certificate of full compliance. ACF Ex. 7. In February 2005, Babyland requested additional time to correct noncompliance in the area of fiscal management, noting that its Finance Department was "currently in transition" and asserting that full compliance would be achieved by May 31, 2005. ACF Ex. 8, at 1, 3. ACF submitted an affidavit from its Region II Regional Manager, Matthew Schottenfeld, in which he recounts that no certificate of compliance was ever submitted (and none appears in the record). ACF Ex. 6, at 2. A meeting was held on January 17, 2006 between ACF and Babyland staff to discuss the continuing fiscal issues from the 2004 PRISM report. Id.

ACF then proceeded to place Babyland in high-risk status by letter dated March 23, 2006. ACF Ex. 1. In doing so, ACF pointed to the findings in the 2004 audit (the audit for the period ending June 30, 2005 had not yet been provided but was due

on March 31, 2006). Specifically triggering the high-risk designation were Babyland's failure to "perform monthly bank reconciliations in a timely manner," to "file required financial reports in a timely basis," and to post "accounting transactions . . . in a timely manner." ACF Ex. 1, at 1. In addition, ACF noted that Babyland was found not to be "in compliance with financial reporting requirements" and not to be maintaining its general ledger "in such a way that costs could be properly allocated to different categories and funding streams." Id. At that point, Babyland was found to have accumulated "a recurring net loss for the last two years." Id.

ACF then performed an on-site review of Babyland's management of its EHSP grant on April 2, 2006 and found a number of deficiencies which were identified in an April 26, 2006 report to Babyland. ACF Ex. 2 (April report). ACF determined that "[o]ne or more of the deficiencies constituted a threat to the integrity of Federal funds," and instructed Babyland that Babyland was therefore "required to correct this immediate threat within 30 calendar days of receipt of this report." Id. at 1. The April report indicated that deficiency findings under two standards amounted to misuse of federal funds as defined under 45 C.F.R. § 1304.3(a)(6)(i)(D). The findings of misuse were cited under 45 C.F.R. § 74.21 and 2 C.F.R. Part 230 (Apps. A(A)(2)(g) and B(8)(m)(1)). The April report reiterated that, "[a]s these deficiencies pose a threat to the integrity of Federal funds, the areas of noncompliance constituting these deficiencies must be corrected within 30 days (per Sec. 641A(d)(1)(B)(i) of the Head Start Act, 42 U.S.C. 9836a)." Id. In addition, the April report found that Babyland had failed to perform substantially in ten areas relating to Program Design and Management under 45 C.F.R. § 1304.3(a)(6)(i)(C) and required that these deficiencies also be corrected within 30 days. The report concluded that, if Babyland continued "to have uncorrected deficiencies beyond the specified timeframe(s)," ACF would issue "a letter stating our intent to terminate your Head Start grant." Id. at 10.

The deficiency findings are set out in detail in the April report and are summarized here:

- The distribution of salaries to awards was not supported by personnel activity reports. Review of spreadsheets and interviews with grantee staff revealed that, contrary to written procedures, allocation of personnel costs was simply done by historical percentage with no comparison with actual time sheets. ACF Ex. 2, at 3, citing 2 C.F.R. Part 230 (Apps. A(A)(2)(g) and B(8)(m)(1)).

- Babyland had not paid its employee payroll taxes for May and June 2005, and its board chair explained that the omission was due to "poor decisionmaking." Id. at 2.[2] Babyland could not account for what happened to the money included in the grant for payment of payroll taxes. Additional amounts were in dispute with the Internal Revenue Service as of April 6, 2006. Id. at 2-3, citing 45 C.F.R. § 74.21.

- The 2004 audit showed a lack of internal controls including maintaining "accounting records and supporting documents" adequate to "provide safeguards over Babyland assets and to assure the proper recording of transactions." The Board of Trustees had experienced two-thirds turnover since the 2004 audit, and new members had not yet been able to "address all the internal control problems." ACF Ex. 2, at 4, citing 45 C.F.R. § 1304.50(g)(2).

- "[I]nternal financial reports were prepared only twice in 2005, in May and November." Id. at 5, citing 45 C.F.R. § 74.21(b)(4).

- "The grantee's financial management system did not provide for comparison of outlays with budgeted amounts for each award." Babyland's Chief Grants and Budget Officer (CGBO) stated that Babyland knew it had not overspent "as long as there were funds to be drawn down from the PMS system." Budget reports were not provided to the EHSP Director or the Policy Council even after requests. Id., citing 45 C.F.R. § 74.21.

- Salaries were charged to one grant year that were for work accrued in other years because first and last pay periods were not properly charged. Id. at 5-6, citing 45 C.F.R. § 74.28.

- Babyland had no policy governing the performance of employees engaged in the award and administration of contracts, contrary to the specific requirements for a code of conduct at 45 C.F.R. § 74.42. Id. at 6.

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[2] When belatedly submitted, the 2005 audit report confirmed that Babyland had unpaid federal and state payroll taxes of $1,074.011 and a net operating deficit of $2,084,686. ACF Ex. 5, at 4, 12.

- Of the financial reports due between December 30, 2003 and December 30, 2005, Babyland filed four late and three not at all. Babyland's CGBO explained that Babyland did not have enough staff or systems in place to complete the reports, and that "timely reporting was not a priority for the Fiscal Department because it had ongoing work that was to be completed by a few staff." Id. at 6-7, citing 45 C.F.R. § 74.52(a)(i)(iv).

- Babyland failed to identify and properly allocate administrative and developmental costs relating to its EHSP. The CGBO reported that there had been "no calculation of administrative costs completed for any period;" the accountant reported that no system was in place to monitor administrative costs. Financial status reports for grant periods ending in 2003, 2004 and 2005 did not list any administrative costs. Id. at 7-8, citing 45 C.F.R. § 1301.32(b)(2).

- Babyland failed "to establish or maintain an efficient and effective reporting system and did not disseminate timely and accurate fiscal information to management staff, the Governing Board, or the Policy Council." The EHSP Director reported that Babyland "did not have the ability to produce efficient and effective reports," and that his "repeated requests for timely budget reports" went unanswered. Policy Council minutes showed repeated requests for monthly reports which had not been provided as of April 4, 2006. The CGBO reported that "only two reports were produced for the year ending May 31, 2005, and that only one report was produced covering 6 months (June 1, 2005, to November 30, 2005)," and that those reports were prepared in order to submit Financial Status Reports (SF-269s) to ACF and not in order to "control program quality, maintain program accountability, or advise the policy groups or staff of program progress." Id. at 8, citing 45 C.F.R. § 1304.51(h)(1).

- Babyland did not implement ongoing monitoring procedures for its fiscal operations, despite establishing a procedure to use the PRISM as the evaluation tool for fiscal management compliance. No time frames were established to perform monitoring, and no duties for fiscal monitoring were assigned to specific staff members. Babyland's Chief Financial Officer (CFO) reported that the plan was to use the PRISM review but

provided no evidence that this procedure was actually carried out, and the lead accountant reported that no system was in place to monitor administrative costs. Id. at 9, citing 45 C.F.R. § 1304.51(i)(2).

- Babyland was required to prepare and implement a corrective action plan for the June 30, 2004 audit findings. The CFO reported at the beginning of the April 2006 on-site visit that "these issues were still uncorrected," and Babyland's senior accountant reported that "bank reconciliations were still not completed and that all entries have not been documented or corrected." Records showed no documentation of administrative costs or of actual time usage to support allocation of personnel costs. Id. at 9-10, citing OMB Circular A-133, ¶315(a).

- Babyland audits were submitted late for three consecutive years. Id. at 10, citing OMB Circular A-133, ¶320(a).

ACF conducted a follow-up monitoring review on site at Babyland from May 31, 2006 to June 2, 2006. The findings were issued in a report to Babyland dated October 6, 2006 and sent along with the ACF determination. ACF Ex. 7, Letter Report from ACF to Babyland (Oct. 6, 2006) (June Report). The report concluded that four deficiencies had been corrected but that eight deficiencies remained uncorrected. June Report at (unnumbered pages) 2 and 6. The deficiencies that were found to have been corrected were those cited under 45 C.F.R. §§ 74.21(b)(4), 74.42, 74.52(e)(1)(iv), and 1304.51(h)(1).

The uncorrected deficiency findings are set out in detail in the June report and are summarized here:

- As of June 2, 2006, the Governing Board had still not ensured timely audit submission, appropriate allocation of administrative expenses, or final reconciliation of major assets and liabilities. The CFO and Board President acknowledged that Babyland had "not submitted a Corrective Action Plan for the audit findings to the awarding official as required" and did not yet have a current audit. June Report, at 7-8, citing 45 C.F.R. § 1304.50(g)(2).

- Babyland had engaged a payroll service as of January 27, 2006, and opened a separate account for EHSP. ACF found, however, that Babyland did not demonstrate that a

  financial management system had been implemented that "could reasonably provide effective control over and accountability for all grant funds, property and other assets." Babyland remained in negotiation with the IRS on payment of back payroll taxes, including $21,948.28 for Babyland's EHSP for the period ending May 31, 2006. Id. at 8-9, citing 45 C.F.R. § 74.21(b)(3).

- Babyland did not take corrective action "to address salaries previously charged to the incorrect award periods." A Babyland administrator stated that the final SF-269s for years ending May 31, 2005 and May 31, 2006 would be amended or adjusted to correct accrued salaries for initial pay periods, but those tasks were not completed by the end of the June review. Id. at 9-10, citing 45 C.F.R. § 74.28.

- Babyland developed but then failed to fully implement "a system for allocating the salaries of employees working for more than one program." Employees were provided time allocation sheets with a memorandum dated May 18, 2006. However, ACF found that Babyland "failed to demonstrate a process for using and monitoring employee time sheets to properly allocate salary costs to the correct funding sources." Id. at 10-11, citing 2 C.F.R. Part 230 (Apps. A(A)(2)(g) and B(8)(m)(1)).

- Babyland took no corrective action to properly identify and allocate administrative costs to EHSP. Babyland did not present any plan "to properly charge development and administrative costs" or "to monitor organization-wide management costs." Id. at 11, citing 45 C.F.R. § 1301.32(b)(2).

- A plan for revising the Finance Policy Manual to provide for monitoring fiscal operations, including regular reports on financial specifics to the Board of Trustees and the Policy Council not less than quarterly and review by the CFO of a Fiscal Checklist for internal controls, had been written. The plan had no time frame for completion or indication of how often the Fiscal Checklist would be performed. The draft written policies contained in the plan had not been implemented

as of the June review. Id. at 11-12, citing 45 C.F.R. § 1304.51(i)(2).

- Babyland did not have a current audit showing correction of significant audit findings from the 2004 audit, and the 2005 audit was overdue as of the June review. Id. at 12-13, citing OMB Circular A-133, ¶315(a).

- As noted, the audit report for the period ending June 30, 2005 was already overdue as of the June 2006 review. A letter from the audit firm indicated Babyland would begin negotiations on June 5, 2006 for preparation of "two audits for the years ending June 30, 2005 and June 30, 2006. Id. at 13-14, citing OMB Circular A-133, ¶320(a).

ACF's termination notice accompanied the June report. This appeal followed.

Standard of review

The Board has held that once presented with a prima facie case that would support a termination, a grantee must present evidence sufficient to challenge ACF's case or risk disposition of its appeal without an evidentiary hearing. See, e.g., Springfield Action Commission, DAB No. 1547, at 5 (1995). A grantee always bears the burden to demonstrate that it has operated its federally funded program in compliance with the terms and conditions of its grant and the applicable regulations. See, e.g., Lake County Economic Opportunity Council, Inc., DAB No. 1580, at 5 (1996); Meriden Community Action Agency, Inc., DAB No. 1501, at 41 (1994), aff'd Meriden Community Action Agency, Inc. v. Shalala, 80 F.3d 524 (D.C. Cir. 1996); Rural Day Care Association of Northeastern North Carolina, DAB No. 1489, at 8, 16 (1994), aff'd Rural Day Care Ass'n of Northeastern N.C. v. Shalala, No. 2:94-CV-40-BO (E.D. N.C. Dec. 20, 1995); see also 45 C.F.R. § 74.21(b)(2). Moreover, a grantee is clearly in a better position to establish that it did comply with applicable requirements than ACF is to establish that it did not. Therefore, the Board has held that the ultimate burden of persuasion is on the grantee to show that it was in compliance with program standards.

In moving for summary affirmance, ACF triggers the standard for granting summary judgment. Summary judgment is appropriate when there is no genuine dispute as to any material fact, and the moving party is entitled to judgment as a matter of law. Union Township Community Action Organization, DAB No. 1976, at 6. The

party moving for summary judgment bears the initial burden of showing the basis for its motion and identifying the portions of the record that it believes demonstrate the absence of a genuine factual dispute. See Celotex Corp. v. Catrett, 477 U.S. 317, 323 (1986). If a moving party carries its initial burden, the non-moving party must "come forward with 'specific facts showing that there is a genuine issue for trial.'" Matsushita Elec. Industrial Co. v. Zenith Radio, 475 U.S. 574, 587 (1986) (quoting Fed. R. Civ. P. 56(e)). To defeat an adequately supported summary judgment motion, the non-moving party may not rely on general denials in its pleadings or briefs, but must furnish evidence of a genuine dispute concerning a material fact - a fact that, if proven, would affect the outcome of the case under governing law. Id. at 586, n.11; Celotex, 477 U.S. at 322. In deciding a summary judgment motion, a tribunal must view the entire record in the light most favorable to the non-moving party, drawing all reasonable inferences from the evidence in that party's favor. Union Township.

Issues

The issues before the Board are as follows:

1) Is summary judgment appropriate?
   a) Was Babyland entitled to another opportunity to correct the violations at issue based on its claim that they were mere technicalities?
   b) Was ACF authorized to require correction within 30 days?
   c) Was ACF required to permit Babyland to make corrections according to a QIP?
   d) Did Babyland timely correct all deficiencies?
   e) Are material facts in dispute that require a hearing?
2) Do Babyland's procedural arguments have merit?
   a) Is Babyland entitled to further discovery?
   b) Is Babyland entitled to summary disposition in its favor because ACF's brief was two days late?

Analysis

1. **Summary judgment is appropriate here.**

A. ACF did not act prematurely in seeking to terminate Babyland.

The gravamen of Babyland's case is the contention that it was entitled to more time in which to correct the deficiencies than

the 30-day period permitted by ACF. The main reasons which Babyland offers for this proposition are:

> (1) that the areas of noncompliance cited as deficiencies for failure to perform substantially the requirements relating to program design and management (45 C.F.R. § 1304.3(a)(6)(i)(c)) should have been considered "other violations" which constitute deficiencies only after a "grantee has demonstrated an inability or unwillingness to correct" in a required time frame pursuant to 45 C.F.R. § 1304.3(a)(6(iii);[3]
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> (2) that the cited noncompliances were not substantial enough to constitute material deficiencies but rather amounted to "mere technicalities;[4] and
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> (3) that Babyland should have been given at least 90 days to correct or have been permitted to correct any deficiencies within one year pursuant to a QIP.

We discuss and reject each of these reasons below. We then address the remaining issues which Babyland identified as requiring a hearing and conclude that no material facts are in dispute.

i. Babyland was not entitled to another opportunity to correct the deficiencies here.

As explained earlier, a violation may be considered a deficiency, among other reasons, if it involves either a failure to "perform substantially" requirements relating to certain areas (including program design and management) or involves a misuse of grant funds. 45 C.F.R. § 1304.3(a)(6)(i)(C) and (D). Other violations

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[3] Since such violations become deficiencies only after the failure to correct, Babyland argues, the grantee is then entitled to the opportunity to correct them immediately or pursuant to a QIP, as with other deficiencies. Babyland Br. at 8-9.

[4] Babyland relied on a statement in a Head Start termination case before the Board that "ACF should not seek to end a grantee's Head Start participation on a mere technicality. Babyland Br. at 9-10, quoting Community Action Agency of Franklin County, Inc., DAB No. 1609, at 3 (1997).

may become deficiencies if the grantee demonstrates an inability or unwillingness to correct them. 45 C.F.R. § 1304.3(a)(6)(iii). Babyland argues that the violations cited as deficiencies under section 1304.3(a)(6)(i)(C) did not rise to the level of substantial performance failures in program design and management

and did not involve a misuse of grant funds. Babyland Br. at 9. According to Babyland, therefore, only when the re-review found that these noncompliances were not corrected could they have become deficiencies, which Babyland would then have to be given an opportunity to correct. Id.

For purposes of this discussion, the issue we must address is whether the allegations were significant enough to constitute substantial performance failures or misuse of grant funds. If they were, then ACF properly characterized them as deficiencies ab initio and has already provided Babyland with an opportunity to correct them before the re-review.

The undisputed facts set out above establish widespread and longstanding failures in financial management and program governance that go to the heart of a grantee's obligation to account for the use of federal funds in program operation. Babyland argues that ACF did not contend that "any of the recipients of the services offered by Babyland are at risk as a result of the alleged deficiencies." Babyland Reply at 3. In reaching this conclusion, Babyland seems oblivious to the potential consequences of failing to pay taxes, account for funds or respond to audit findings on the continued viability of the program on which those recipients depend.[5] When, for example, payroll taxes are unpaid and the funds allocated to make those payments cannot be traced, ACF may reasonably conclude that Babyland has lost "effective control over and accountability for all funds, property and other assets" and has failed to "adequately safeguard all such assets and assure that they are used solely for authorized purposes." ACF Br. at 9-10, quoting 45 C.F.R. § 74.21(b)(3). The vulnerability of the program to misdirection of funds to unauthorized purposes was further increased by the findings of late or absent financial reports and audits and the absence of any ongoing monitoring procedures. These violations of federal requirements were identified to Babyland at least as of the 2004 Prism report and yet remained uncorrected throughout. The fact that audit reports were filed long after the due dates for four years in a row is a symptom of the overall inadequacy of management control. Furthermore, the audit reports when completed simply documented the seriousness of the internal control vacuum. See, e.g., ACF Ex. 3, at 24-25.

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[5] As noted earlier, this concern is far from speculative with the auditors questioning whether Babyland can continue as a going concern with its growing deficits and liabilities. See, e.g., ACF Ex. 5, at 4, 12.

On top of these fundamental concerns, the undisputed facts establish serious grant management violations. Babyland was repeatedly found to lack any system to calculate or monitor its administrative costs, to fail to follow its procedures to allocate salaries to grants according to actual work done for different grant programs, and so on.

Even if Babyland could have successfully argued that some individual findings were not sufficient standing alone to establish material failures to comply with federal requirements, to substantially perform its responsibilities in the area of Program Design and Management, and to properly handle and account for grant funds, no reasonable reviewer could conclude other than that collectively these findings amply support the bases for ACF's determination to terminate Babyland. These are not "mere technicalities" but major abdications of the core responsibilities of those who receive federal funds to serve recipients in need. We conclude that findings and violations discussed above meet the standards for termination under 45 C.F.R. § 1303.14(b).

Given that conclusion, it follows that Babyland was not entitled to yet another opportunity to correct these issues before they could be considered deficiencies. We therefore need not consider ACF's argument that many of the findings had been cited previously and gone uncorrected by the time of the April report, so that they should be considered repeat findings and deficiencies.

ii. Babyland was not entitled to a minimum of 90 days to make corrections.

Turning to various procedural attacks that Babyland makes on the validity of the termination action, we first address its claim that the statute guarantees a grantee at least 90 days in which to correct deficiencies. Babyland cites 42 U.S.C. § 9836a(d)(1)(B)(ii) as requiring "at least" a 90-day "opportunity for corrective action on deficiencies in meeting performance standards." Babyland Br. at 16.

On its face, the statute does not oblige ACF to allow 90 days for correcting deficiencies. Instead, ACF may require a grantee "to correct the deficiency immediately, if the Secretary finds that the deficiency threatens the health or safety of staff or program participants or poses a threat to the integrity of Federal funds." 42 U.S.C. § 9836a(d)(1)(B)(ii). ACF made a finding here that the nature of the deficiencies did threaten federal funds. Contrary to Babyland's contentions, we see nothing arbitrary or

capricious in ACF's decision to require Babyland to correct its deficiencies within 30 days, especially in light of the history of financial mismanagement, basic reporting failures, and precarious financial situation of the grantee. Babyland emphasizes that ACF knew that "Babyland had completely new management and financial staff" which was addressing "many of the governance and financial issues." Babyland Br. at 16. We do not agree, however, that a complete turnover in leadership and financial personnel necessarily should have reassured ACF that no further threat existed to federal funds. Babyland also points the June 2004 audit as another source of assurance to ACF that any threat had already passed by the time of the April review. Not only did the June 2004 audit report itself paint an alarming picture of a program deeply in debt and lacking many structural systems needed to account for funds, the fact that the June 2004 audit report was undisputedly again submitted late simply reinforces the lack of corrections. Babyland's high-risk designation also evidences the urgency and seriousness of ACF's concerns. We thus find no error in ACF's requirement that Babyland make immediate corrections or in setting the time for completion of those corrections to remove the threat to federal funds as 30 days.

Furthermore, the statute permits a grantee to be given up to 90 days to correct deficiencies, only "if the Secretary finds, in the discretion of the Secretary, that such a 90-day period is reasonable, in light of the nature and magnitude of the deficiency." Plainly, the Secretary did not find that a 90-day period would be reasonable here given the "nature and magnitude" of the deficiencies found.

Babyland also argues that the 30-day time frame was unreasonable and prejudicial because Babyland's high-risk designation meant that the "probability that program funds would be misused became an impossibility." Babyland Br. at 16. This argument has no merit. Babyland had been designated high risk by letter dated March 23, 2006 based on its 2004 audit report and was required by the same letter to meet four specific requirements. Babyland Ex. 9. On May 25, 2006, Babyland wrote to ACF to request a 30-day extension of the 60-day deadline to meet two of these requirements, relating to fully identifying its deficit and detailing a plan to eliminate it. ACF Ex. 9. ACF responded by letter the next day denying the extension request but allowing Babyland until May 30, 2006 to submit the information. The information Babyland submitted on March 30, 2006 was hardly reassuring. It identified a current indebtedness of $5,337,177 including almost a million dollars of federal payroll tax liability for which Babyland was still negotiating a repayment

plan with the Internal Revenue Service and numerous other liabilities still to be renegotiated. ACF Ex. 11.

iii. Babyland was not required to produce a QIP and did not have an approved QIP, and hence was not entitled to delay correcting the cited deficiencies to dates in its own corrective plan.

Babyland also suggests that it was entitled to correct the deficiencies by the terms of a corrective action plan which, according to Babyland, "comported to be a quality improvement plan," and which was submitted to ACF near the end of the 30-day correction period (on May 26, 2006).[6] Babyland Br. at 3. Babyland relies here on the third statutory alternative for ACF to use in requiring correction of deficiencies, i.e., allowing a grantee, "in the discretion of the Secretary (taking into consideration the seriousness of the deficiency and the time reasonably required to correct the deficiency), to comply with the requirements" for a QIP.

The deficiency findings were issued on April 26, 2006 and were required to be corrected within 30 days of receipt of the findings. Babyland Ex. 1, at 1. The corrective action plan claimed only scattered steps as having been taken up to that point. See, e.g., Babyland Ex. 3, at 3-4. The plan did not assert that the deficiency findings that led ACF to conclude that an immediate threat existed had been corrected or even that they would be corrected by the required date. Babyland Ex. 3, passim. Instead, the plan set out a series of "due dates" for numerous corrective actions, some of them not planned for completion before the end of 2006. Id.

Babyland does not point to any direct evidence to support its assertions that ACF requested that Babyland produce a QIP or informed Babyland that any QIP would result in extending the very explicit requirement that the deficiencies in the April report be corrected within 30 days of receipt. Instead, Babyland relies on its account of a meeting which occurred during that 30-day period between a consultant hired by Babyland and an ACF consultant "to discuss correcting the deficiencies," and claims that all present agreed that Babyland could not correct in the required time frame. Babyland Reply Br. at 4. Even assuming this account to

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[6] Although Babyland asserts this date in its brief, Babyland's declarant, Early Head Start Director James B. Tilghman, states that the plan was not submitted until June 2, 2006. Tilghman Decl. at 2.

be true and construing the description in the light most favorable to Babyland, a recognition by an ACF contractor that Babyland cannot fix its deficiencies in time does not constitute permission from ACF to continue to operate with the serious program and management issues and the immediate threats to federal funds uncorrected. Anticipating failure does not amount to excusing failure.

Babyland also proffers an unexecuted and unsigned certificate with an attached one-page declaration from Mr. Tilghman to the effect that ACF's consultant also joined in Babyland's consultant's recommendation that Babyland should draft a plan "to project who, what and when each outstanding deficiency would be fully reconciled" and that the ACF consultant visited Babyland "once during the thirty day time period and made two follow up telephone calls to check on the progress of the plan." Tilghman Decl. at 2. Again, we find nothing in these events, even accepted as true and read most favorably, to justify Babyland in assuming that its inability to complete correction in 30 days would be excused if only it prepared a corrective action plan within the 30 days. Mr. Tilghman's further assertion that Adia Brown of the "ACF review team" gave input before the plan was put in final form does nothing to alter this conclusion.

Babyland argues that ACF should nevertheless be equitably estopped from terminating Babyland for failing to make timely corrections, on the grounds that ACF staff or consultants were aware of and even discussed with Babyland the corrective action plan before it was finalized. Babyland Reply at 4. We see no reason that assisting Babyland in its efforts to plan how to get its financial house fully in order was inherently inconsistent with expecting Babyland to comply with the 30-day deadline to correct the deficiencies threatening its handling of federal funds. The April report made clear that correction in the 30 days was required and that a QIP was not necessary, but certainly did not prohibit Babyland from developing a corrective action plan.

In any case, the Board, like many federal courts, has questioned whether equitable estoppel can ever lie against the government. See, e.g., Northstar Youth Services, Inc., DAB No. 1883 (2003), and cases cited therein, including Office of Personnel Management v. Richmond, 496 U.S. 414 (1990) and Heckler v. Community Health Services of Crawford County, Inc., 467 U.S. 51 (1984). At a minimum, some intentional misrepresentation on the part of the government would be necessary to consider such a step. Babyland's claims here do not come close to establishing that Babyland detrimentally relied on any intentional

misrepresentation. At best, Babyland might have been confused by or have misunderstood the input from ACF representatives. Mr. Schottenfield points out in his declaration, however, that any such confusion is belied by the fact that not only the April report itself, but an e-mail dated May 22, 2006 from ACF to Mr. Tilghman made explicit that the "deficiencies were subject to immediate correction, i.e., within 30 days, and that a [QIP] was not required." Schottenfield Decl. at 1, referencing ACF Ex. 14. Babyland points to no response by it to this e-mail that might evidence a reaction consistent with having believed until then that ACF or its consultants had approved preparation of a QIP in lieu of immediate correction. Certainly, Babyland was not ignorant of the true facts (one of the elements of traditional estoppel) and could not reasonably rely to its detriment on any contrary understanding (also required for estoppel) after receiving two written instructions from ACF requiring immediate correction within 30 days.

Finally, Babyland's development of a QIP, even were we to treat the corrective action plan as such, would not mean that the timeframes for correction in the QIP would apply automatically. A QIP must first be approved by ACF and ACF may require corrective actions to be taken within timeframes different from those specified in the QIP as proposed. Babyland points to no communication from ACF following Babyland's submission of its corrective action plan that could be conceivably construed as approving it as a QIP. Babyland's implication that the passage of time in itself constituted sub silencio approval simply cannot form the basis for estoppel against the government.

iv. Babyland did not timely correct the deficiencies.

Babyland argues that ACF could not properly terminate its program because all the violations were actually addressed by Babyland "months before receiving the notice of termination." Babyland Br. at 11. It is important to note that Babyland does not contend that the deficiencies were timely corrected, i.e., during the 30-day correction period which (as extended) ended May 30, 2006. Instead, Babyland claims to have made necessary corrections before the final termination notice issued on October 5, 2006, substantially after the on-site follow-up review begun on May 31, 2006 found the uncorrected deficiencies at issue here. As a matter of law, later steps to correct deficiencies still outstanding after a grantee has been given an opportunity to correct cannot remove authority from ACF to terminate based on the failure to timely correct. See Philadelphia Housing Authority, DAB No. 1977, at 14-15 (2005) ("the regulations are clear that all deficiencies must be corrected by the end of the

period for correction . . . . 45 C.F.R. § 1304.60(c)"). As discussed above, we see no support for Babyland's apparent assumption that the length of time that elapsed between the follow-up review and the issuance of the termination letter somehow implied that the correction period was extended, despite the express denial of Babyland's extension request in May 2006.

Moreover, Babyland proffered no documentation tending to support its assertions that the deficiencies were all corrected before the termination notice was issued. In fact, the evidence submitted by Babyland on its face would serve mainly to further undercut any possibility that many of the deficiencies found in the April report were corrected even by October 2006, much less within the required 30 days. The corrective action plan developed by Babyland, discussed elsewhere in this decision, makes clear that many steps were not even expected to be completed until November or December of 2006. The late submission of the 2005 audit report, by nine months, shows a continuing lack of fiscal responsibility and solvency. In a number of areas where correction could have been shown by documentation (such as establishing payments to or settlement with the IRS for tax liabilities, producing copies of amended financial status reports, or showing necessary revisions to policies), Babyland made no attempt to document actual corrections.

We conclude that Babyland has proffered no evidence to support its claim of having corrected its deficiencies in the time before the termination letter issued. In any case, even if taken as true, this claim would not legally change the outcome here, since, as we have found, Babyland was required to correct its deficiencies with 30 days of its receipt of the April report.

v. ACF is not time-barred from terminating Babyland's grant.

Babyland asserts that, because ACF did not notify it of the termination until October, Babyland was "blindsided" and prejudiced because it "began its planning for the following fiscal year with the belief that it would be receiving the grant dollars." Babyland Br. at 14-15. Babyland asserts that it reasonably assumed that it would have been notified within 30 days of the follow-up visit if ACF were not satisfied that the deficiencies were eliminated, since ACF notified Babyland within 30 days after the initial site review. Id. Babyland describes the "delay" as violating the "spirit and intent" of 45 C.F.R. § 1303.15(b). Id. at 14. According to Babyland, this "failure

to comply with notice requirements is grounds for dismissal of a termination action" under 45 C.F.R. § 1303.14(c)(6). Id.

We do not agree that Babyland had a "right to rely on the ACF's inertia." Babyland Reply at 3.[7] Of course, prompt action is always desirable, but no legal requirement justified Babyland in assuming that the outcome of the follow-up review would be favorable merely because ACF took longer to process it than the initial site visit. ACF has discretion in allocating its resources among its competing priorities and, furthermore, it is not unreasonable that review results that would require termination might be subjected to greater consideration and take longer to finalize. Babyland could not, moreover, rely on the continuation of ordinary grant management steps in the interim as proof that ACF would not act on the follow-up review findings.

In any case, we see no authority for the proposition that a termination action is barred by mere passage of time between a final review finding failure to correct deficiencies and the issuance of the resulting termination letter. See Southern Delaware Center for Children and Families, DAB No. 2073 (2007) (regulations provide no consequence for failure to promptly notify grantee of results of follow-up review).

B. No hearing is required because no issues of material fact are in dispute.

Finally, having disposed of the legal issues, we turn to Babyland's position, pressed in its reply brief, that an in-person hearing is required because "issues of material fact" remain in dispute. Babyland Reply at 2. Babyland listed the six issues which it sought to address at a hearing, as follows:

> 1. Did the ACF require Babyland to prepare a corrective action plan and did Babyland rely on ACF's conduct in that regard to its detriment?
>
> 2. Given the lateness of the filing of the notice of termination, was [sic] the findings set forth in the report "cured" prior to the thirty day period?

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[7] Nor do we accept Babyland's assertion, made at the same page of its brief, that ACF allowed other "offending agencies" to submit QIPs while denying that opportunity to Babyland in similar circumstances. Babyland provided no basis in fact for its implication of selective enforcement.

> 3. In making its decision to terminate the grant, did the ACF consider the impact of its termination on the community?
>
> 4. Were the deficiencies set forth in the initial notice of deficiencies merely technical violations which did not arise to the level of a regulatory or statutory deficiency? In other words, were the deficiencies material?
>
> 5. Should the ACF, due to its delay in terminating the grant, be barred from terminating the head start grant because of laches?
>
> 6. Should ACF be estopped from relying on the Notice of Deficiencies and its thirty-day cure period as a basis for grant termination after working with Babyland to prepare a corrective action plan?

Letter from Babyland counsel to the Board, at 1-2, dated March 15, 2007. The bulk of these "issues" are legal questions which we have addressed already.

The only factual questions specifically identified here are whether ACF did "require" Babyland to prepare a QIP and whether ACF considered the impact of termination on the community. As to the first, as we discussed above, the evidence which Babyland proposes to present about ACF's awareness of or even involvement in Babyland's development of its corrective action plan, even if accepted, does not come close to placing at issue whether ACF effectively extended the time frame for correction. Indeed, given the nature of the deficiencies, the short time frame for correction, and the multiple unresolved audit issues and special conditions, making a plan for accomplishing corrections would certainly seem to be nothing more than common sense on the part of Babyland management. It does not follow that information about such a plan being developed put ACF on notice that Babyland thought it could delay correcting the deficiencies in the April report beyond the specified date.

As to the second, Babyland argues in its brief that ACF claims to have a substitute grantee ready to serve the community but Babyland asserts that ACF's plan presupposes "the good will of Babyland" in permitting use of its facility and transfer of its staff. Babyland Reply Br. at 5. Babyland argues that ACF should be required to show at a "full hearing on the merits" that ACF had an alternative plan to continue serving the community. Babyland points to no authority that would require ACF to make a

factual showing as to its selection process for a replacement grantee in order to terminate an existing grantee which has failed to correct serious deficiencies. The regulations which Babyland cites contain no such requirement but rather add to the normal grantee selection process additional considerations that ACF will take into account in order to minimize disruption from the changeover when replacing a grantee. 45 C.F.R. §§ 1302.10-11. Further, ACF states that it will use the services of an experienced corporation as an interim grantee to ensure continuity of services while selecting a permanent replacement if Babyland is terminated. ACF Br. at 30-31. We thus discern no material facts relating to either of these issues which require resolution at a hearing.

Finally, it is not quite clear what Babyland means by the issue listed as number two. To the extent Babyland means to reiterate the claim that deficiencies were eventually corrected before the termination notice was issued in October, we have already explained why such late correction would not be material. If the issue is to be read as a contention that Babyland should be deemed to have made corrections within 30 days because the termination letter did not issue until several months later, we find no more justification for this version of equitable estoppel than we have found for other such formulations by Babyland. In neither case has Babyland proffered evidence which, if believed, would show actual timely correction of the deficiencies.

2. Babyland's procedural arguments are without merit.

A. Babyland has not established a need for further discovery.

ACF objects to Babyland's request for interrogatories and depositions. Letter from ACF counsel, dated March 21, 2007. ACF argues that the regulations provide no "general right to discovery nor for the taking of depositions in particular." Id. at 2. ACF further points to Board procedures as discouraging formal discovery methods unless they appear to be the only way to resolve an appeal. Id. ACF contends there is no such necessity here.

These proceedings are intended to be relatively informal and speedy means of resolving disputes. The regulations governing them do not provide any right to discovery but empower the Board to order the production of relevant information and to take such steps as are required to develop the record and support and sound decision. 42 C.F.R. § 16.9. To that end, the Board has developed a practice manual for parties appearing before it and

has explained its approach to discovery requests there as follows:

> **Can a party use interrogatories or depositions in appeals before the DAB Appellate Division?**
>
> The DAB discourages interrogatories and depositions unless these are the only means to adequately develop the record on an issue that the DAB must decide to resolve the appeal. The DAB will take whatever steps are appropriate to ensure the fairness of its decision-making process, but discourages use of discovery devices which tend to delay DAB proceedings without contributing in any meaningful way to developing specific and substantive issues which the DAB must address to produce a sound decision.
>
> Whenever a party seeks to use a discovery device such as interrogatories or depositions, the first step is to seek a voluntary agreement with the other side. If the party cannot obtain such an agreement, it may request an order, but must be able to show relevance and necessity. The DAB grants such requests infrequently. In denying requests for depositions previously, we have noted that depositions are not generally required in administrative proceedings and that a deposition request would be granted only if the presiding Board member involved in the case determined it was the only way a record could be adequately developed (for example, if a material witness could not appear at a hearing).

Departmental Appeals Board, Appellate Division -- Practice Manual FAQ, at http://www.hhs.gov/dab/appellate/manual.html#22 (bold in original).

In accordance with this approach, we consider whether Babyland has shown that the requested interrogatories and depositions are relevant and necessary to develop a sound record. We note, first, that both parties have already submitted relevant documentation as part of their appeal files. Babyland offers no explanation of what information it needs that is not available in the appeal files. Indeed, Babyland does not identify any of the witnesses it would like to depose or explain why deposing them (or posing written interrogatories) would be essential to adequately develop the record. We would therefore not be inclined to grant the extraordinary level of discovery sought by Babyland.

Given our ultimate conclusion, explained above, that Babyland failed to place any material fact in genuine dispute, we see no basis to believe that Babyland's request amounts to more than a fishing expedition looking for support for equitable relief which is, in any case, not available in this forum.

B. The brief delay in submission of ACF's brief resulted from good cause and did not prejudice Babyland.

Babyland objects that it received ACF's brief responding to the appeal only on March 1, 2007, when the due date was February 26, 2007, and that the ACF's brief was accompanied by its motion for summary disposition without prior disclosure by ACF of its intent to file such a motion with its brief. Babyland Reply at 1-2. As a consequence, Babyland asks that we suppress ACF's brief and treat Babyland's appeal as unopposed, granting summary disposition in favor of Babyland. Id. Counsel for ACF candidly admits that ACF's brief was not placed in the mail until February 28th, but explains that she was unexpectedly called out of the office on both February 26 and 27th due to family medical emergencies. ACF counsel's letter to the Board, dated March 21, 2007, at 1. ACF further argues that the resulting two-day delay caused no prejudice to Babyland. Babyland did not dispute any of these representations by ACF.

As explained in the Board's e-mail to the parties dated March 21, 2007, the family emergencies of ACF counsel had already been found to constitute good cause for an extension and, in the absence of any showing of prejudice to Babyland, the additional two-day delay is excusable for the same reasons. Furthermore, Babyland has identified no basis to expect advance notice before the filing a summary disposition motion along with a brief. We therefore deny Babyland's motion for suppression of the brief and summary disposition in its favor.

Conclusion

For the reasons discussed above, we grant ACF's motion for summary affirmance and uphold ACF's termination of Babyland's Early Head Start grant.

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Judith A. Ballard

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Constance B. Tobias

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Leslie A. Sussan
Presiding Board Member