

DEPARTMENTAL GRANT APPEALS BOARD

Department of Health, Education, and Welfare

Subject: Zavala County Health Association
Docket No. 77-21
Decision No. 57

Date: JUN. 15, 1979

DECISION

Zavala County Health Association ("Grantee") appeals from a determination by the Public Health Service Regional Grant Appeals Board ("PHS") affirming a disallowance by Region VI of an expenditure in the amount of \$16,107.00 1/

On June 27, 1972, the Office of Economic Opportunity ("OEO") awarded grantee a Comprehensive Health Services grant for the period 6/1/72 to 10/3/1973. The grant contained an award of \$251,000 for the construction of an ambulatory health facility. It provided that grantee obtain OEO approval for release of final payment to the construction contractor.

On May 3, 1973, a contract approved by OEO for the construction of the health facility was entered into by grantee with Cristal Contractors, Inc. The obtaining by the contractor of a Performance and Payment bond was a condition of the contract. Contrary to expectations it appeared after work on the contract had commenced that the contractor could not qualify for such bond unless it could show a bank account balance of \$20,000. Unable to show such balance, grantee sought and obtained a loan of \$20,000 from a private lender for the benefit of the contractor. To obtain this loan, grantee had to guarantee its repayment. This it did by resolution of its Board of Directors on September 27, 1973.

On December 2, 1975, PHS issued Notice of Grant Award No. 06-H-000214-02 to grantee. That grant included \$295,000 for continuation of construction left unfinished under the 1972 OEO grant. It contained a condition "that

1/ Grantee in its brief raises the question whether PHS has standing to disallow an expenditure made out of funds awarded under an OEO grant. We answer this question in the affirmative and, for purposes of this case, we need refer to no other authority than that conferred by the Delegation of Authority and Memorandum of Understanding from and between OEO and the Secretary of DHEW, effective July 6, 1973, copies of which are included in the Appeal file.

In one of the earlier documents filed by grantee with this Board, it requested a hearing which would afford it with an opportunity for the taking of testimony of individuals familiar with the facts. The Board finds that in the matter of the instant appeal there is no dispute as to a material fact, the resolution of which would be materially aided by oral testimony. Pursuant to 45 CFR 16.8, this request of the appellant is hereby denied.

grantee submit all obligating documents associated with commitments under the construction award to Weldon R. Wisian and obtain his approval prior to actual obligation of the Funds."

Sometime in 1975-6 the contractor defaulted on the greater part of the loan, and in March 1976, the lender obtained a judgment for \$14,267.93 with interest and costs against the contractor. Upon the latter's continued default, grantee, uncertain of the equities between the parties, paid the amount of \$16,107.09 by check payable to the contractor and the lender in satisfaction of the judgment, pursuant to its resolution of guarantee.

PHS defends the disallowance of the entire sum of \$16,107 on the basis of the special condition in the 1975 grant, and upon the more general contention that the expenditure under review was occasioned through imprudent management of grant funds by the grantee. We believe that a consideration of the issues can be materially aided by considering those relating to the funds of grant No. 60096/OEO, 1972, separately from those concerning money drawn from the PHS, 1975 grant.

I

The record supports the conclusion that of the total sum disallowed, \$14,225 represented money retained by the grantee from funds of OEO grant No. 60096, obligated to the Cristal Contractors under the construction contract approved by OEO on June 29, 1973. The remaining \$1,882.00 derived from funds provided under the 1975 PHS construction budget.

We do not think that the prior approval condition in the 1975 grant can be given retroactive effect in respect of invalidating a transaction otherwise sustainable as within the authority of grantee. It should be observed that the 1975 condition is itself prefaced by a statement that it was to serve as a replacement for a condition "on award dated 5/9/75," thus limiting its applicability. We note, further, a provision in the 1972 award to the effect that funds received in connection with the operation of the program "must be recorded in a separate account in the accounting records." A recognition of the distinctiveness of each of the grants herein considered--quite apart from their separate Agency aspects--is also found in the Audits filed for the relevant periods. Likewise, in the letter of October 31, 1973, in which PHS advised grantee of the delegation of Authority from OEO, that agency informed grantee of authority to extend the current budget period of the OEO grant for three months, with the understanding that "the project plan, including any imposed conditions, remain in effect." In the content of that letter it seems clear that the conditions referred to are those of the 1972 OEO grant. If intended to refer to PHS conditions they could hardly be mandated to "remain" in effect.

PHS agrees that both at the time of the adoption of the guarantee resolution (September 27, 1973) as well as at the time when grantee made payment pursuant to that resolution (July 20, 1976) the portion of the payment which

represented retainage from the contract, (\$14,225) had been fully obligated. In view of this understanding, there is not much substance to the claim that a condition embodied in a subsequent grant should be controlling upon action taken under an earlier, distinct grant by virtue of a Delegation of Authority effective July 6, 1973, from OEO to The Secretary of Health, Education, and Welfare over the earlier, 1972 grant.

The Memorandum of Understanding pursuant to the Delegation of Authority, supra, not atypically, recites that DHEW "shall succeed to all authorities, rights, powers... acquired by OEO by virtue of the grants... including... the rights and interests established under any conditions... incorporated into any grant...." It is not unusual for a successor agency to declare applicable, prospectively, its general policy to a grant over which it has assumed authority by transfer from another agency, or even to modify expressly an existing condition in such grant for future purposes. But we find nothing in the documents relating to the devolution of authority over OEO grant No. 60096 which would empower PHS to declare a special condition in a grant it has awarded to be automatically applicable, by some undefined implication, to a consummated transaction under an earlier grant from another Agency, upon its succession to administration responsibility. Especially does this appear to be true as applied to a case like the present where the guarantee was given by grantee prior to its being notified of the delegation of authority to PHS.

A second ground relied upon in support of the disallowance in the full amount is that by guaranteeing the loan, grantee manifested imprudent management. Disavowing any purpose to question grantee's good intentions, PHS nonetheless contends that the effect of a guarantee of the kind involved here might be that of depriving grantee and its service population of intended benefits.

The record does not support such a conclusion. Whatever the uncertainties in the appeal file, there is no doubt that the loan guarantee was directly related to the progress of the construction project and in furtherance thereof. When PHS characterizes that guarantee and payment thereunder as imprudent management it is employing the term as a euphemism for unreasonableness. But the weight of the evidence is in refutation of such inference. An OEO official had been especially designated to superintend the construction project as officer in charge, and OEO had retained a private architectural consultant to assist in the project. Grantee asserts and the record discloses no denial of this assertion--that these persons were specifically consulted when it became clear that the OEO-approved contractor could not qualify for a Performance and Payment bond for lack of an adequate cash balance in its bank account; that they were informed of the plan and decision to borrow from a private lender, and that they did not object to the guarantee.

Even if this latter allegation not be deemed to have been directly proven, much appears in the surrounding circumstances as corroboration to estop OEO and its successor Agency from arguing that grantee did not follow a course of prudent management. OEO not only reserved to itself the right to approve the construction contract with Cristal Contractors but it did so with

full knowledge that this contracting firm had been but recently organized, and that it had no established history or credit, because of OEO's strong commitment to affirmative action in furtherance of minority business and employment. It is also shown that through its designation of the two persons referred to above, to supervise and assist the project, OEO acquired an on-going presence. Furthermore, OEO had approved the construction of the health facility as a "Fast Track" project in that it permitted the contract to be entered into, and construction to begin, before completion of the final drawings, due to the then-existing energy crisis, steel shortage, and escalating inflation. At the request of the grantee which called attention to the foregoing conditions and to the urgent need for the health facility in the community, OEO agreed to waive its normal competitive bidding requirements, and the record contains the statement of a former OEO officer in charge of 200 health projects, concerning general policy of OEO at the relevant period to assist OEO minority contractors in meeting bonding requirements by interceding with sureties and other agencies with the object of reducing those requirements.

It is clear that when the contractor herein was denied bond, the choice for the grantee and OEO was between cancellation of the contract with Cristal Contractors Inc., with all the delay and substantially higher cost that it would entail, and proceeding with the approved contract pursuant to which work had already begun by agreeing to a guarantee for the repayment of the loan. In light of the existing circumstances, the choice of the latter course appears as eminently reasonable.

It remains to be added that the condition in the 1972 grant does not suggest a different conclusion. It is significant that while that grant requires prior as well as written OEO approval for a number of enumerated actions, it merely directs that grantee "obtain OEO approval for release of final payment to the construction contractor."

The audit report (dated, January 29, 1976) for OEO grant No. 60096, grant period May 1, 1974-April 30, 1975, refers to the guarantee of the loan by the grantee and to the contingent liability to which it gave rise. It states at page 10:

"In accordance with the demands of generally accepted accounting principles, full disclosure of this transaction is being made and adequate provision is included for their contingent liability in the encumbrance enumerated in note 2 above. Exercising the right of set-off, the 10% retainage on the Cristal Contractors Contract that is being held in escrow by Zavala County Health Association, Inc., amounting to \$14,225.40 will be used to partly pay the outstanding balance arising out of this transaction, in the event Ms. Lopez (The Lender) does not secure full payment of this indebtedness through the current litigation." (Emphasis added).

A copy of this audit report was forwarded to PHS and received by it in February 1976, a full five months before grantee paid to the lender the amount of the judgment plus interest and costs. But PHS does not even claim that it has challenged grantee for incurring this liability or that it has directed grantee not to pay it in the manner it did. The file contains evidence which might reasonably have led grantee to believe, under all of the shown circumstances, that PHS had impliedly approved the release of final payment.

II

As suggested previously, the correctness of the determination of disallowance in respect of that part which did not derive from OEO grant 60096 must be weighed on its own merits. Unlike the major component (\$14,225), the sum of \$1,882.00 used by the grantee to satisfy the judgment against the contractor had its source in a separate PHS grant account never under the control of OEO officials. In fact, that grant was for a budget year subsequent to the date of the contract with Cristal Contractors, and its funds were never obligated to the 1972 contract. Grantee admits that it never had any contacts with PHS relative to that contract.

It is true that a single check was drawn by grantee for the entire sum of \$16,107 against an account in which funds from both grants were commingled, in discharge of a unitary obligation. It may even be conjectured that had the approval of PHS been sought in advance of payment, in accordance with the limiting condition in the 1975 grant, its approval might have been given in view of the grantee's good faith and of the fact that the obligation under the guarantee resolution was incurred for the purpose of serving a proper grant objective. But the 1975 condition was imposed long prior to the date when the actual expenditure of the \$1,882 was made from the PHS grant as well as prior to the obligating of that sum, and what it exacted was not merely prior approval, but approval by a particularly designated official. We cannot say that this condition was an invalid exercise of administrative authority, or that grantee was free to disregard it.

For the reasons stated we sustain the appeal as to the sum of \$14,225, and affirm the determination of disallowance to the extent of \$1,882.

/s/ Thomas Malone

/s/ Malcolm S. Mason

/s/ Irving Wilner, Panel Chairman