

but rather have chosen to continue to address those specifics in the Provider Reimbursement Manual. Therefore, the proposed regulation did not provide a more restrictive liquidation policy than existing policy in the Provider Reimbursement Manual.

However, we intend to revise section 906.4 of the Provider Reimbursement Manual to deny recognition of the liquidation of liabilities by use of a promissory note without the actual transfer of assets within 75 days of the close of the cost reporting period. Revised section 906.4 then will be consistent with instructions in section 2305 of the Provider Reimbursement Manual concerning requirements for liquidating liabilities. Those instructions (albeit with different time limitations) require that a liability actually be liquidated by the end of the appropriate time period, rather than being extended by way of another liability, for example, a promissory note.

F. FICA and Other Payroll Taxes

Comment: One commenter asserted that accrual of employer-related FICA liabilities is clearly appropriate under GAAP as well as under § 413.24(b)(2), and that HCFA should continue to allow recognition of these costs especially as they relate to the accrual of year-end wages.

Response: We believe that employer-related FICA taxes should be accrued and claimed for Medicare payment only in the period in which actual payment to the employee is made. It is not until that point that the liability for the employer-related FICA tax is incurred.

Comments: One commenter pointed out that the preamble language in the proposed rule stated that FICA and other payroll taxes related to vacation pay and nonpaid workers would be paid only in the period in which payment is actually made to the employee. Yet, the language of proposed § 413.24(c)(3)(vi) indicated that all FICA and payroll taxes would be handled in the same way. The commenter suggested that we clarify the discrepancy in the final rule.

Response: Even though the preamble language for the proposed rule specifically addressed only payroll taxes related to vacation pay and nonpaid workers, our intent was to prohibit the accrual and claim for Medicare payment of such taxes for all types of payments until the period in which payment (on which the tax is based) is actually made to the employee. Thus, as the commenter suggests, and as the regulations text has always specified, this policy applies to all FICA and payroll taxes.

Comment: Some commenters stated that the applicable FICA and other payroll taxes should be accrued during the same period that the employee benefits are earned and accrued. One commenter stated that FICA and other payroll accruals apply equally to accrued vacation, holiday, and sick pay benefits. Another commenter suggested that if such payments are not made to employees in subsequent years, Medicare may recover the excess cost in subsequent years.

Response: We continue to believe that such taxes should not be accrued and claimed for Medicare payment until the period in which actual payment to the employees is made. It is at that point that the liability for the related payroll taxes is incurred.

G. Sick Pay

Comment: Regarding the sick leave example in the proposed rule (56 FR 50835), one commenter believes that providers would not typically accrue for forfeitable sick leave. Even if providers do so, the commenter believes that Medicare could avoid payment by requiring forfeitures to be offset against subsequent sick pay costs.

Response: We agree with the commenter that providers should not accrue forfeitable sick leave. However, we disagree that where forfeitable sick leave is accrued and claimed for Medicare payment, Medicare would avoid payment by requiring forfeitures to be offset against sick pay costs incurred during the period in which the forfeitures occur. Handling forfeitable sick leave in this manner would result in Medicare recognizing and paying for excessive sick leave costs up until the point of forfeiture.

As a result of this comment, we have made two revisions to this final rule. First, we have clarified under § 413.100(c)(2)(iii)(A) that if sick leave is funded in a deferred compensation plan, the contributions to the fund must take into account forfeitures. Second, if an employee has the right to demand cash payment at the end of the year, we believe that forfeitures are not an issue because the employee has earned a nonforfeitable right. Accordingly, we also have specified under § 413.100(c)(2)(iii)(B) that if a provider's sick leave plan grants employees the nonforfeitable right to demand cash payment for unused sick leave at the end of each year, sick pay is includable in allowable costs, without funding, in the cost reporting period in which it is earned.

Comment: One commenter asserted that providers should not be financially disadvantaged by disallowance of

accrued benefits that are vested but subject to forfeiture clauses. The commenter stated that such clauses are financially prudent and result in lower Medicare program costs.

Response: We believe the commenter is concerned that if forfeitures are possible, Medicare would not recognize any accrual of sick leave. On the contrary, as discussed in the response to the preceding comment, if sick leave is funded in a deferred compensation plan, the contributions to the fund must take into account forfeitures. That is, the accrual of the contributions to the deferred compensation fund reflects anticipated forfeitures. However, the issue of forfeitable sick leave occurs only in the context of contributions to a deferred compensation fund. In a situation in which an employee has the right to demand cash at the end of the year for unused sick leave, the employee has earned a nonforfeitable right. In all other situations, sick pay can be claimed for Medicare payment only on a cash basis for the year in which the benefits are paid; therefore, the issue of accrual of forfeitable sick leave does not arise.

In proposing to incorporate Medicare's policy on sick leave costs (contained in section 2144.8 of the Provider Reimbursement Manual) into the regulations, we believe it was understood that sick pay costs can be claimed for payment only in the cost reporting period in which paid, unless the sick leave is funded in a deferred compensation plan or unless an employee has the nonforfeitable right to demand cash at the end of the year for unused sick leave. This policy has been included in section 2144.8 for many years. Nevertheless, we have revised the regulations by specifying under § 413.100(c)(2)(iii)(C) that sick pay costs can be claimed only on a cash basis if paid on any bases other than those in § 413.100(c)(2)(iii)(A) or (B) (that is, through a funded deferred compensation plan, or in situations in which the sick leave plan grants employees the nonforfeitable right to demand cash payment for unused sick leave at the end of each year).

Comment: One commenter stated that although timing differences will occur in any accrual method of accounting, in total, the program is not overpaying since any overestimate of expenses in one year is offset by reduction in accrued expenses in a subsequent period when the sick leave, vacation, and other types of leave are determined to be overaccrued.

Response: The purpose of the longstanding policy on liquidation of liabilities, which we proposed to incorporate in the regulations, is to