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HOSPITAL WAGE INDEX REFORM DEJA VU? OIG RELEASES REPORT ON VULNERABILITIES OF WAGE INDEX SYSTEM, RECOMMENDS OVERHAUL OF SYSTEM

On November 21, 2018, the Department of Health and Human Services Office of Inspector General ("OIG") released a report ("Report") outlining what it believes are multiple deficiencies in the Medicare wage index system. OIG recommended several changes, including revisiting the possibility of comprehensive reform and seeking authority to penalize hospitals that submit inaccurate wage data. In response to the Report, CMS agreed to explore implementing an in-depth wage data audit program and will consider recommending other provisions that require statutory changes as part of the next budget process. The Report, which is available here, is the latest in a series of studies, analyses and reports on potential changes to the Medicare wage index system. It is important to note that, so far, past proposals to reform the wage index system have failed to gain traction.

BACKGROUND OF WAGE INDEX SYSTEM

The Medicare Hospital Inpatient Prospective Payment System ("IPPS") is designed to pay hospitals for services provided to Medicare beneficiaries based on a national standardized amount adjusted for the patient's condition and related treatment. Further, Social Security Act Section 1886(d)(3)(E) requires that the standardized amount be adjusted for differences in hospital wage levels, which CMS implemented through the wage index system. CMS also uses the hospital wage index for the Outpatient Prospective Payment System ("OPPS") and prospective payment systems for inpatient rehabilitation facilities, inpatient psychiatric facilities, long-term-care hospitals, home health agencies, hospices, ESRD facilities, ambulatory surgical centers and skilled nursing facilities.

In computing the wage index, CMS calculates an average hourly wage ("AHW") for each urban and rural area (total wage costs divided by total hours for all hospitals in the geographic area) and a national AHW (total wage costs divided by total hours for all hospitals in the nation). A labor market area's wage index value is the ratio of the area's AHW to the national AHW.

CMS defines hospital labor market areas based on the definitions of Core-Based Statistical Areas ("CBSAs") established by the Office of Management and Budget. A Metropolitan Statistical Area ("MSA") is a CBSA associated with at least one urbanized area that has a population of at least 50,000 that comprises the central county or counties containing the core plus adjacent outlying counties that have a high degree of social and economic integration with the central county measured through commuting. Medicare payment programs classify hospitals into rural and urban status for a variety of purposes. An "urban area" is defined as an area within an MSA. Except for all-urban states (Delaware, Rhode Island and New Jersey), CMS calculates a "rural area" wage index for each state based on the wage data of the state's rural hospitals, regardless of their location with respect to each other. In other words, the "rural area" of a state is not necessarily one contiguous area.

The wage indexes applied to urban hospitals in a state cannot be lower than the rural area wage index for that state. This provision is called the "rural floor." The rural floor was created to correct the "anomaly" of "some urban hospitals being paid less than the average rural hospital in their states." CMS must apply the rural floor in a manner that is budget neutral on a national level, which means that for any increase in wage indexes for hospitals based on getting the rural floor, CMS must lower wage indexes nationally by applying a rural floor budget neutrality factor.

Finally, hospitals can reclassify to a nearby urban or rural area with a higher wage index if they meet certain criteria related to proximity and AHW. Since 2016, CMS regulations have also allowed hospitals to take advantage of so called "2-step" reclassification, "rurban" reclassification or reclassification "stacking," which involves urban to rural reclassification and wage index reclassification. Many hospitals have, through completely legal and transparent (to CMS) means, utilized these options to improve reimbursement and optimize costs (e.g., qualifying for 340B Program enrollment). This has created an even more complex web of wage index consequences under these rules.

HISTORY OF WAGE INDEX REFORM

Because of the inequities that some see in the wage index system, it has been the target of numerous studies, analyses and reports that have focused on disparities between the wage index values for individual hospitals and the wage index values among different geographic areas and ways to improve the Medicare wage index. CMS, OIG and others have had various proposals throughout the years, but, to date,

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there has not been comprehensive changes to the wage index system. Below, we touch on some of the major reports and proposals, but there have also been various legislative proposals to fix specific parts of the wage index system that have failed to be enacted.

The Tax Relief and Health Care Act of 2006 included a requirement for a MedPAC report on revision of the wage index. This resulted in a June 2007 MedPAC Report, which recommended Congress repeal the existing wage index system and allow the Secretary of HHS to establish a new system that would use Bureau of Labor Statistics ("BLS") data from all employers and industry-specific occupational weights. This system would be adjusted for geographic differences in the ratio of benefits to wages at the county level and would smooth large differences between counties. MedPAC also recommended the new system be phased in over a transition period.

Later, CMS engaged Acumen, LLC to review and evaluate MedPAC's recommendations, which resulted in a series of reports between 2009 and 2011. Generally, Acumen concluded that MedPAC's recommended methods for revising the wage index would be an improvement over the existing methods and that the BLS data should be used. However, Acumen found that MedPAC's blending and smoothing method was not well suited to the existing Medicare wage index. Acumen recommended further exploration of labor market definitions using a wage area framework based on hospital-specific characteristics, such as the commuting times from hospitals to population centers, to construct a more accurate hospital wage index. In 2011, Acumen issued an updated report proposing an alternative formulation known as the Commuting-Based Wage Index ("CBWI"), which would use commuting data to create more flexible hospital-specific labor markets at the zip code or census tract level.

The Affordable Care Act also included a requirement that HHS submit to Congress a plan to comprehensively reform the wage index applied to the Medicare hospital IPPS and take into considerations from MedPAC and Acumen reports. In April 2012, HHS submitted a report to Congress recommending using the CBWI discussed in the Acumen report to establish a labor market area and wage index value for each hospital (as opposed to labor market areas). Commuting data would be used to identify areas from which a hospital hires its workers and to determine the proportion of its workers hired from each area to calculate hospitals-specific wage index. The CWBI would also eliminate sharp differences or "cliffs" in a wage index just because the nearby hospital is in a different or adjacent CBSA. HHS also stated that a more up-to-date reporting system for collecting commuting data from hospitals would need to be established.

OIG has also issued various reports over the years on various aspects of the wage index system, mostly in respect to audits of specific hospital wage data. Finally, in the FFY 2019 Proposed Rule, CMS once again asked for comments related to the wage index system. However, so far, Congress and CMS have not made major changes based on the recommendations in the various reports. It is also important to note that any comprehensive reform in the wage index system would necessarily create a both winners and losers in moving to a new system, which can create a high hurdle to any substantive changes.

OBJECTIVE AND METHODOLOGY OF OIG REPORT

OIG's stated objective in the Report was to describe vulnerabilities observed in the wage index system. To accomplish this objective, OIG reviewed policies relevant to the wage index system and analyzed vulnerabilities observed during previous reviews of individual hospitals' wage data. Specifically, OIG:

- Reviewed and analyzed the observations made during prior reviews;
- Reviewed applicable federal laws, regulations, standards and guidance;
- Reviewed CMS controls relating to vulnerabilities identified in prior wage index reports; and
- Discussed observations with CMS.

OIG REPORT FINDINGS

In the Report, OIG noted the following vulnerabilities in the wage index system based on its prior audits:

- CMS lacks the authority to penalize hospitals for inaccurate or incomplete wage or occupational mix data in the absence of misrepresentation or falsification. OIG noted that in recent reports, it estimated 272 hospitals received an increase of $140 million in Medicare payments due to inaccurate data, which led to decreased payments to other hospitals because of budget neutrality.
- Desk reviews by the Medicare Administrative Contractors ("MACs") do not always identify inaccurate wage data; specifically, in recent OIG audits, inaccurate wage data that the OIG found were not detected during the MACs' desk reviews.

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- The rural floor decreases wage index accuracy. Because the rural floor is applied on a national budget neutral basis, it can potentially benefit a small number of states, which then must be funded by the other states, including mostly rural states.
- Hold harmless provisions in federal law and CMS policy pertaining to geographically reclassified hospitals' wage data decrease wage index accuracy.

As a result of these vulnerabilities, wage indexes may not always accurately reflect local labor prices; therefore, Medicare payments to hospitals and other providers may not be appropriately adjusted to reflect local labor prices.

OIG RECOMMENDATIONS

First, based on the issues found in the wage index system, OIG recommended that CMS and the Secretary revisit comprehensively reforming the hospital wage index system. This would include a previously researched option of a commuting-based wage index that was part of a 2012 plan submitted to Congress. In the absence of comprehensive reform, OIG recommended that CMS:

1. Seek legislative authority to penalize hospitals that submit inaccurate or incomplete wage data in the absence of misrepresentation or falsification;
2. Work with the MACs to develop in-depth wage data audit program at a limited number of hospitals each year, focusing on hospitals whose wage data has a high level of influence on the wage index of their area;
3. Seek legislation to repeal the law creating the rural floor wage index;
4. Seek legislation to repeal the hold-harmless provisions in the Act relating to the wage data of reclassifying hospitals, which would allow CMS to calculate each area wage index based on the wage data of hospitals that reclassify into the area and the wage data of hospitals geographically located in the area if they do not reclassify out; and
5. Rescind the hold harmless policy to use the wage data of a reclassified hospital to calculate the wage index of its original geographic area.

CMS RESPONSES TO THE REPORT

In written comments, CMS stated that it continues to evaluate the hospital wage index system on an annual basis. In the FFY 2019 IPPS Proposed Rule, CMS solicited comments for future changes to the wage index system. CMS will also consider whether to recommend a statutory proposal to implement a comprehensive wage index reform.

In addition, CMS concurred with recommendation Number 2 above to work with MACs developing in-depth wage data audit programs. However, CMS did not concur with recommendation Number 5 above to rescind its policy relating to geographically reclassified hospitals' wage data because this policy provides the most accurate and stable measure. Finally, CMS stated that it will consider whether to recommend for inclusion the statutory proposals for the other four recommendations in the next budget.

PRACTICAL TAKEAWAYS

- There have been several proposals to reform the wage index system in the past, but so far those have failed to get wide-spread support.
- There are no changes scheduled at this time based on the Report, but OIG and CMS continue to evaluate the wage index system, including potential comprehensive reforms.
- CMS intends to develop an in-depth wage data audit program with MACs.
- CMS will also consider whether to recommend the other changes in the Report requiring statutory revisions be included in the next budget process.

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