CMS FINALIZES CHANGES FOR LOW WAGE HOSPITALS AND RURAL FLOOR

On August 16, 2019, the Federal Fiscal Year ("FFY") 2020 Medicare Inpatient Prospective Payment System ("IPPS") final rule ("IPPS Final Rule") was published in the Federal Register. In the IPPS Final Rule, the Centers for Medicare & Medicaid Services ("CMS") finalized several changes announced in the proposed rule, including several changes to address disparities between high and low wage index areas and fixing the so-called "rural floor." We estimate that these changes would shift more than $200 million/year of Medicare IPPS payments to hospitals in the lowest quartile of wage areas, all on a budget neutral basis. Below is a brief overview of the Medicare wage index system as well as a summary of the final changes to the wage index and rural floor that will take effect on October 1, 2019.

In a previous article, we described the changes as set forth in the FFY 2020 IPPS Proposed Rule.

BACKGROUND OF WAGE INDEX SYSTEM

The 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 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.

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. In another article, we discussed the history of previous wage index reform, including a recent OIG report on the vulnerabilities of the wage index system.

SUMMARY OF CHANGES

Many of the commenters to the proposed rule expressed a common concern that the current wage index system creates and perpetuates the disparities between high and low wage index hospitals. In essence, because of their higher Medicare payments, hospitals in high wage index areas can afford to pay higher wages to employees, which allows them to continue as higher wage index areas. However, hospitals in lower wage index areas are forced to cut costs (including wages), which lowers their future wage index. CMS refers to this situation as the "downward spiral."

To help address these disparities in the Medicare wage index system, under the IPPS Final Rule CMS: (1) increased the wage index values for certain hospitals with low wage index values by applying a uniform budget neutral adjustment to the standardized amount; (2) changed the calculation of the rural floor; and (3) provided for a transition for hospitals that will experience comparatively significant decreases in their wage index values in a budget neutral manner.

BUDGET NEUTRAL LOW WAGE INDEX ADJUSTMENT

Under the IPPS Final Rule, CMS finalized the increase in wage index for hospitals with a wage index value in the lowest quartile (i.e., those below the 25th percentile wage index), which is 0.8457. For any hospitals in this group, CMS increased their wage indices by 50 percent of the difference between the otherwise applicable wage index value for that hospital and the 25th percentile wage index value (0.8457). To illustrate how this adjustment will work, refer to the following example from the proposed rule:

> [A]ssume the otherwise applicable final FY 2020 wage index value for a geographically rural hospital in Alabama is 0.6663, and the

25th percentile wage index value for FY 2020 is 0.8457. Half the difference between the otherwise applicable wage index value and the 25th percentile wage index value is 0.0910 (that is, (0.8457 – 0.6663)/2). Under the IPPS Final Rule, the FY 2020 wage index value for such a hospital would be 0.7573 (that is, 0.6663 + 0.0910).

It is important to note that CMS considered other methodologies for addressing low wage index disparities, such as establishing a national wage index floor but believed it was important to preserve the rank order of wage index values.

To make this adjustment budget neutral, CMS originally proposed to target a budget neutrality adjustment on high wage hospitals by decreasing the wage index for hospitals with a wage index in the top quartile (i.e., those above the 75th percentile wage index). CMS ultimately decided not to finalize this proposal. Instead, CMS adopted an alternative budget neutrality adjustment of 0.997987, which will be applied to the national standardized amount reducing payments for all hospitals (not just those in the top quartile). This policy will be effective for at least four years, beginning in FFY 2020, to allow wage increases implemented by low wage hospitals sufficient time to be reflected in the wage index calculation.

CHANGES TO RURAL FLOOR

As stated above, the rural floor policy states that the wage index applied to urban hospitals in a state cannot be lower than the rural area wage index for that state. One of the concerns that commenters and CMS expressed is that an urban hospital could reclassify as rural under 42 C.F.R. § 412.103 to raise the rural floor, which could also raise the wage index of urban areas in the state for hospitals that did not reclassify as rural. Further, because the rural floor policy is budget neutral, this can create the situation where urban hospitals in states with a high rural floor get an increase in their wage index, which is paid for by all hospitals throughout the country.

While urban hospitals would still be able to reclassify as rural, to fix this issue, CMS will exclude wage data of urban to rural hospital reclassifications from the calculation of the rural floor wage index value beginning in FY 2020. CMS will not raise the wage index for urban hospitals that have not reclassified as rural, including hospitals with no reclassification as well as those with an MGCRB reclassification, based on an increased wage index due to one or more urban hospitals reclassifying as rural under 42 C.F.R. § 412.103. Based on data in the IPPS Final Rule, this policy change will impact the calculation to the rural floor in several states, including Arizona, California, Connecticut, Florida, Hawaii and Massachusetts.

Notably, the Social Security Act requires that CMS establish the rural floor policy but does not specify how the rural floor is to be calculated. CMS stated that it is adopting these changes based on its concern that its inclusion of rural reclassified hospitals in the rural floor calculation could increase the disparities between low and high wage index areas.

TRANSITION FOR NEGATIVELY IMPACTED HOSPITALS

To smooth payment decreases due to these wage index changes, CMS will apply a 5 percent cap on any decrease in a hospital's wage index from its final wage index for FFY 2019. In other words, a hospital's final wage index for FFY 2020 would not be less than 95 percent of its final wage index for FFY 2019, which allows the effects to be phased in over two years. CMS stated that this 5 percent cap will be applied to all hospital wage index changes regardless of whether they are due to the above policy changes or some other factor. It is important to note that there would be no cap on decreases for FFY 2021. To maintain budget neutrality for the transition policy, CMS will apply a budget neutrality factor of 0.998838 to the FFY 2020 standardized amount.

PRACTICAL TAKEAWAYS

Beginning October 1, 2019 the following policies will be effective under the IPPS Final Rule:

- Hospitals with a wage index value in the lowest quartile (below 0.8457 in the IPPS Final Rule) would receive a wage index adjustment of 50 percent of the difference between the otherwise applicable wage index value for that hospital and the 25th percentile wage index value (0.8457).
- CMS adopted a budget neutrality adjustment to the national standardized amount for the low wage adjustment, which will reduce IPPS payments for all hospitals.
- The low wage adjustments will be in effect for at least 4 years.
- Hospitals with an urban to rural reclassification under 42 C.F.R. § 412.103 will no longer be included in the calculation of their state's rural floor wage index value beginning in FY 2020.

- CMS will apply a transition cap of five percent for any decreases in wage index from these policy changes.

If you have any questions about the wage index and rural floor policies or how they may affect your facility, please contact:

- David Snow at (414) 721-0447 or dsnow@hallrender.com;
- Lori Wink at (414) 721-0456 or lwink@hallrender.com;
- Benjamin Fee at (720) 282-2030 or bfee@hallrender.com;
- Joseph Krause at (414) 721-0906 or jkrause@hallrender.com;
- Lindsey Croasdale at (414) 721-0443 or lcroasdale@hallrender.com; or
- Your regular Hall Render attorney.