

NATIONAL ASSOCIATION OF URBAN HOSPITALS

Private Safety-Net Hospitals Caring for Needy Communities

July 9, 2004

Mark B. McClellan, M.D., Ph.D.
Administrator
Centers for Medicare & Medicaid Services
200 Independence Avenue S.W., Room 443-G
Washington, D.C. 20201

**Subject: CMS-1428-P
Medicare Outliers**

Dear Dr. McClellan:

I am writing on behalf of the National Association of Urban Hospitals (NAUH) to express our opposition to the increase in the outlier threshold that the Center for Medicare & Medicaid Services (CMS) has proposed for the Medicare inpatient PPS system for fiscal year 2005. We believe this increase will result in Medicare failing to pay out its statutorily required proportion of PPS funds as outlier payments for fiscal year 2005 and will cause serious financial harm to hospitals that incur significant costs because of legitimate outlier cases.

Medicare Outliers: The Situation Today

Medicare recognizes that some hospital admissions fall so far outside the norms captured by its prospective payment system that they must be paid in an entirely different manner. Consequently, it employs a system of what it calls outliers. Under this system, hospital cases involving selected medical services, identified in regulations, that exceed a specified Medicare cost threshold are reimbursed by Medicare on a cost basis, through additional payments, in addition to through the Medicare PPS system. These cases are known as outliers. While reimbursement is said to be on a cost basis, outlier payments do not actually reimburse providers for the full costs of the care they provide in cases designated as outliers.

In the current fiscal year, the threshold for a qualified case to become a Medicare outlier is \$31,000.

Medicare Outliers: The Proposed Change in Regulations

In the proposed fiscal year 2005 Medicare inpatient PPS regulation published in the *Federal Register* on May 18, 2004, CMS proposes raising the outlier threshold for the coming year from the current \$31,000 to \$35,085.

Medicare Outliers: NAUH's Objections to the Proposed Policy Changes

NAUH believes that the proposed outlier threshold is too high and will result in Medicare failing to meet its statutory requirement of paying out between five and six percent of its PPS payments as outliers. During the current year, with the threshold at \$31,000, Medicare is on a pace to pay out just about 4.4 percent of its PPS payments in outlier payments – a significant shortfall from the 5.1 percent that was projected for this year and a significant shortfall from the statutory requirement. It stands to reason, we believe, that if Medicare cannot fulfill its statutory minimum of five percent with a threshold of \$31,000 this year, it is likely to fall even further from its statutory minimum, not draw closer to it, if that threshold is raised to \$35,085 – even allowing for a generous increase in the overall cost of health care services. NAUH believes the outlier threshold should be decreased, not increased.

Medicare's failure to pay an appropriate level of outliers has serious implications for hospitals. Even when it does pay out to an appropriate level, outlier payments themselves do not adequately compensate hospitals for the extraordinary costs they incur providing care to patients with extraordinary medical problems; they only help cushion the blow of such costs. Compounding this problem is that in today's environment, hospital margins are shrinking like never before, with more and more hospitals suffering negative margins. In some situations, just a few outlier cases can mean the difference between a hospital breaking even or losing money. This is especially true for large, private, non-profit urban safety-net hospitals such as those represented by NAUH because they care for higher proportions of low-income elderly and uninsured patients than other hospitals. Medicare's failure to live up to its statutory requirements has implications for hospitals nation-wide, and NAUH believes that Medicare should live up to its legal obligation to pay out at least the legally required minimum amount of payments as outliers. The threshold proposed for 2005 will not enable Medicare to achieve this goal.

Medicare Outliers: NAUH's Proposed Solution

NAUH recognizes that developing an outlier threshold for FY 2005 is especially difficult in light of the many developments that have taken place involving Medicare outliers in the past year. CMS recognizes that it has overpaid some hospitals in the past and is now faced with the prospect of using data skewed by the inappropriate reporting of some hospitals to calculate a new threshold for FY 2005. This data is so bad, we believe, that CMS should take a different approach to determining future outlier thresholds. Anything less threatens to put Medicare in jeopardy of violating its statutory requirement for a second consecutive year and to penalize hospitals – including the vast majority of hospitals that did not abuse the outlier process in the past – by depriving them of the appropriate reimbursement they deserve for the legitimate outlier expenses they incur caring for especially sick Medicare beneficiaries. The vast majority of hospitals should not be penalized for the misdeeds of a few.

NAUH recommends that CMS change its methodology for calculating the outlier threshold. The agency proposes looking at charge increases for 2001 and 2002, projecting them forward, and then reducing that figure by the cost-to-charge ratio for 2003. By not using charge and cost figures from the same year, however, this methodology overestimates outlier payments for FY 2005. To address this problem, NAUH suggests that CMS use data – both cost (rather than charge) and cost-to-charge rates – from the same time period (and we believe using data from tentatively settled cost reports rather than audited reports would be acceptable, thereby enabling this process to use more recent data). This approach would enable CMS to estimate increases in costs more accurately, leading to a more appropriate threshold.

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Alternatively, NAUH believes CMS could use a ratio, based on the current threshold and its likely percentage of overall PPS payouts, to revise the threshold and ensure that outliers constitute at least 5.1 percent of overall PPS payments. This would enable CMS to use projections instead of data that is clearly inappropriate and would lead to a significant decrease, instead of an increase, in the FY 2005 threshold.

NAUH would be pleased to work with CMS to refine these methodologies or develop other approaches to this complex problem.

About the National Association of Urban Hospitals

The National Association of Urban Hospitals (NAUH) advocates for adequate recognition and financing of private, non-profit, urban safety-net hospitals that serve America's needy urban communities. These private, urban safety-net hospitals differ from other hospitals in a number of key ways: they serve communities whose residents are much older and poorer; they are far more reliant on Medicare and Medicaid for revenue; they provide far more uncompensated care; and unlike public safety-net hospitals, they have no statutory entitlement to local or state funds to underwrite their costs. NAUH's role is to ensure that when federal officials make policy decisions, they understand the implications of those decisions for these distinctive private, urban safety-net hospitals. NAUH pursues its mission through a combination of vigorous, informed advocacy, data-driven positions, and an energetic membership with a clear stake in the outcome of public policy debates.

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We appreciate your attention to the concerns we have expressed about the proposed increase in the Medicare outlier threshold for fiscal year 2005 and welcome any questions you have about our organization, this issue, or our rationale for the positions we have stated in this letter.

Sincerely,

Ellen J. Kugler, Esq.
Executive Director