



*Advising the Congress on Medicare issues*

# Assessing payment adequacy: hospital inpatient and outpatient services

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# Use of hospital services

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- Over 4,800 hospitals (including critical access hospitals) participate in the Medicare program
- Hospital spending per FFS beneficiary increased 6 percent from the prior year
  - Inpatient spending grew 4.2 percent
  - Outpatient spending grew 11.7 percent
- Total inpatient FFS —\$114 billion
- Total outpatient FFS —\$34 billion

Source: MedPAC analysis of Medicare cost reports and claims files.

# Review of payment adequacy indicators

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- Access is strong
  - Outpatient volume increased by 4 percent
  - Hospital-based office visits grew by 9 percent
  - Inpatient volume declined by 1 percent
- Quality metrics were mixed. Either they improved or did not change significantly
- Access to capital is adequate
- Medicare overall margins remain low: -5.2 percent in 2009

# Hospitals' overall financial health in 2009 is similar to past years

	2003	2006	2009
Median total (all payer) margins	3%	4%	3%
Share with negative total margins, in most recent three years (e.g. 2000-2002)	16%	11%	17%
EBITDAR / expenses (a cash flow metric)	NA	11%	10%
Share with negative EBITDAR, in two of the most recent three years	NA	5%	5%

EBITDAR: Earnings before interest, taxes, depreciation, amortization, and rent.

The capital expense data is not available for 2003.

Source: MedPAC analysis of Medicare cost reports.

# Hospitals under financial pressure tend to keep their costs down

2009 performance	Financial pressure 2004 to 2008		
	High pressure*	Medium	Low pressure**
Number of hospitals	756	390	1,747
Relative standardized cost	92%	96%	104%
Non-Medicare margin	-3.8%	2.7%	10.7%
Medicare margin	4.7%	-1.1%	-10.2%
Total (all-payer) margin	-0.7%	1.7%	5.4%

\* High pressure hospitals have a non-Medicare margin <1% and stagnant or falling net worth.

\*\*Low pressure hospitals have a non-Medicare margin >5% and growing net worth.

Source: MedPAC analysis of Medicare cost reports and claims files from CMS.

# Comparing 2009 performance of relatively efficient providers to others

2009 measure	Top performers during 2006-2008	Other hospitals
Number of hospitals	219	1,952
30-day mortality (CMS measures) (relative to national median )	3 to 7% below	1 to 2% above
Readmission rates (3M) (relative to national median )	4% below	Average
Standardized costs (relative to national median )	10% below	2% above
Non-Medicare margin	3%	6%
Medicare margin	3%	-6%
Total (all-payer) margin	3%	3%

Note: medians for each group are compared to the national median

Source: MedPAC analysis of Medicare cost reports and claims files from CMS

## Documentation and coding adjustments are required to restore budget neutrality

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- In 2007-2009, CMS phased-in MS-DRGs and cost-based weights to improve payment accuracy
- MS-DRGs created financial incentives to better document and code secondary diagnoses
- Documentation and coding improvements (DCI) increased payments, without any real change in average patient complexity or the cost of care
- By law, changes in DRGs and weights must be budget neutral



# DCI adjustment principles (from March 2010 recommendation)

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- Treat providers and taxpayers fairly by making the transition to MS-DRGs fully budget neutral
  - Adjustments should be made to stop continuing overpayments (a 3.9% adjustment is needed)
  - Adjustments should be made to recover all past overpayments
- Avoid a large financial shock to hospitals that would occur if all the necessary adjustments were made in a single year



# Factors in determining the update recommendation

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	Update computation
Contemplated update in the absence of DCI	2.5%
Initial DCI adjustment to prevent further overpayments (3.9% - 1.5% leaves 2.4% to be taken in future years)	-1.5
Productivity and budget adjustments	0.0
<b>Recommended net increase in payment rates</b>	<b>1.0</b>

# Outpatient Considerations

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- Outpatient volume growth of 4 percent
- Office visits at hospital-based clinics grew by 9% compared to 1% at free-standing clinics
- Payment rates are significantly higher at hospitals than free-standing clinics
- A 1 percent update would be consistent with the update for physicians you discussed earlier