Reforming Medicare's wage index systems

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March 2, 2023

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Roadmap

- Current Medicare wage indexes
- Concerns
- Alternative wage index approach and illustrative method
- Examples of how alternative wage indexes address concerns
  - IPPS hospitals
  - Skilled nursing facilities
- Chair's draft recommendation

Note: IPPS (inpatient prospective payment systems).

Construction of the current Medicare wage indexes

- Medicare's wage indexes adjust base payment rates for geographic differences in labor costs

	Current wage indexes
Data	IPPS hospitals' aggregate labor costs (per cost reports)
Labor market areas	Metropolitan statistical areas and statewide rural areas
Exceptions	Numerous and often non-empirical exceptions for IPPS hospitals (and none for most other types of providers)

Note: IPPS (inpatient prospective payment systems). The IPPS wage index also uses data from an occupational-mix survey of IPPS-eligible hospitals. The physician and other Medicare fee schedules have different geographic adjustments, which are beyond the scope of this presentation.

Concerns with current Medicare wage indexes

- Current wage indexes fail to accurately reflect differences in labor costs across geographic areas and create inequities across providers

	Concern
Data	IPPS hospital data is circular and can deviate from market-wide labor costs
Labor market areas	Broad areas mask differences in labor costs within areas and creates large differences across some adjacent areas
Exceptions	Can exacerbate inaccuracies and inequities, be manipulated, and add administrative burden

Note: IPPS (inpatient prospective payment systems).

Approach for improving Medicare's wage indexes and illustrative alternative method

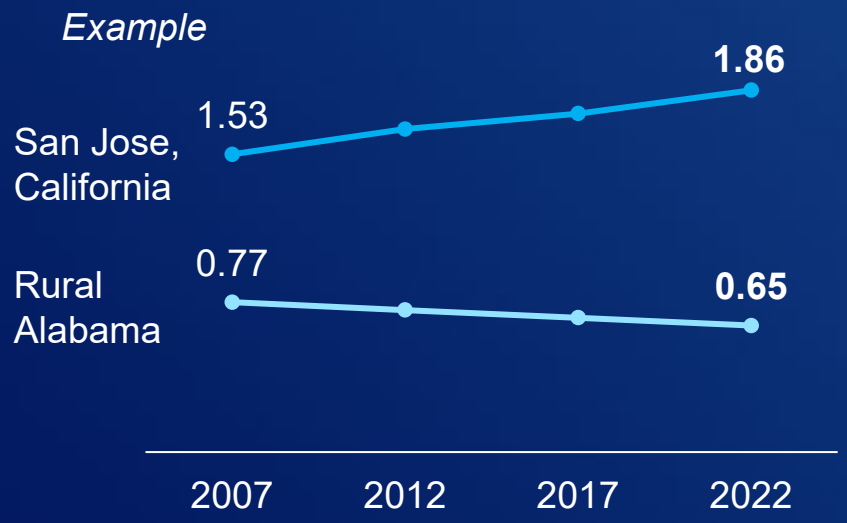
	Approach	Illustrative alternative
Data	Use all-employer, occupation-level wage data with different occupation weights for the wage index of each type of provider	Data from BLS and US Census Bureau
Labor market areas	Reflect local area differences in wages between *and within* MSAs / statewide rural areas	Blend of MSA / statewide rural and counties (up to +/- 5%);
	Smooth wage index differences across adjacent local areas	Cap wage index cliffs between adjacent counties (at 10%)

MEDPAC Note: BLS (Bureau of Labor Statistics); MSA (metropolitan statistical area).

Alternative IPPS wage index decreases circularity and more accurately reflects labor market costs

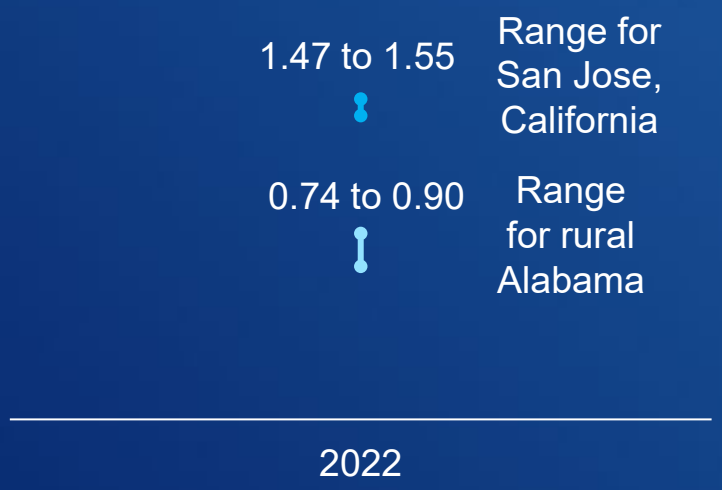
Current IPPS wage index (prior to exceptions)

- Highest wage index values have been growing and lowest have been decreasing



Alternative IPPS wage index

- Using all-employer data more accurately reflects market-wide labor market costs



Impacts on IPPS payments (aggregate)

$ Hospitals in areas with very *high* current wage index values

$ Hospitals in areas with very *low* current wage index values

Note: IPPS (inpatient prospective payment systems).
Source: MedPAC analysis of CMS final rules for fiscal year 2022 and alternative MedPAC wage index data.

Alternative IPPS wage index varies at the county level and mitigates wage index cliffs

Current IPPS wage index (prior to exceptions)

- Masks variation in labor costs within MSAs/statewide rural areas
- Large differences across adjacent areas

Alternative IPPS wage index

- Reflects variation within broader labor market areas
- Mitigates differences across adjacent areas

Impacts on IPPS payments (aggregate)

$ Hospitals in counties where labor costs are *lower* than their broader labor market area

$ Hospitals in counties where labor costs are *higher* than their broader labor market area

Example (2022)

Note: IPPS (inpatient prospective payment systems); MSA (metropolitan statistical area).
Source: MedPAC analysis of CMS final rules for fiscal year 2022 and alternative MedPAC wage index data.

Alternative IPPS wage index increases accuracy and removes opportunities for wage index manipulation

Current IPPS wage index *with* exceptions

- 67% of IPPS hospitals' wage index values were affected by at least one wage index exception
- Some can be manipulated

Example (2022)

Massachusetts rural floor based on single high-wage hospital that converted from a CAH when it joined a larger system

Floor increased wage index value for almost all Massachusetts hospitals (up to 35%)

Alternative IPPS wage index

- No exceptions

Impacts on IPPS payments (aggregate)

Hospitals receiving wage index exceptions, especially when large

Hospitals currently receiving no exceptions

Note: IPPS (inpatient prospective payment systems); CAH (critical access hospital).
Source: MedPAC analysis of CMS final rules for fiscal year 2022 and alternative MedPAC wage index data.

Hospitals also use current IPPS wage index exceptions to gain non-wage-index benefits

- In response to a court ruling, since 2018, hospitals can have dual-reclassifications that can be used to gain non-wage-index benefits for "rural" hospitals while maintaining (or increasing) their wage index value

Example (2022)

Over 350 urban hospitals, including large hospitals in major metropolitan areas:

- First reclassified to a rural area, and thereby gained
  - a Rural Referral Center designation, which has lower eligibility for 340B drug program; and
  - for the over 250 that were teaching hospitals, increases to Medicare's IME residency cap for "rural" hospitals
- Then reclassified back to their home area (or a different, higher wage area) for wage index purposes

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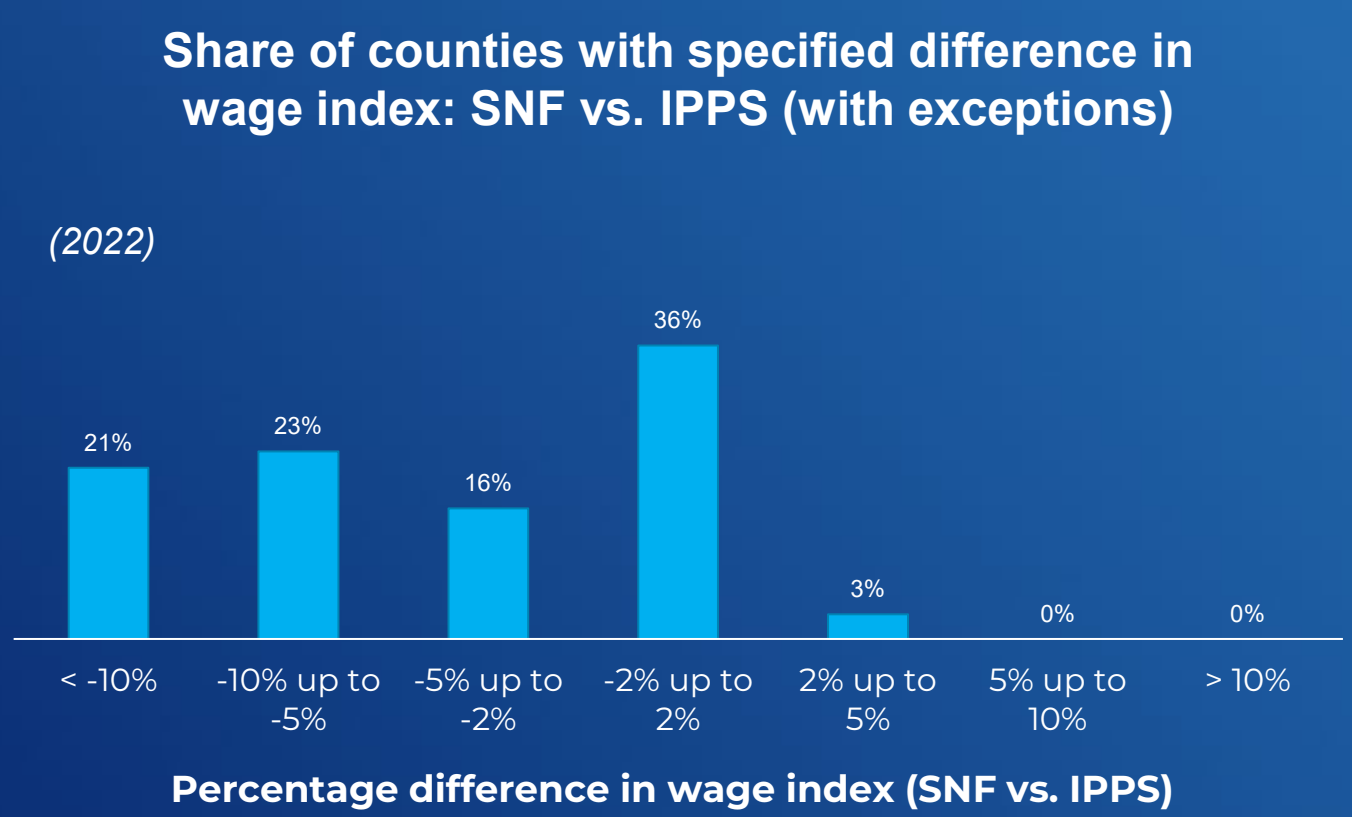
Note: IPPS (inpatient prospective payment systems); IME (indirect medical education).
Source: MedPAC analysis of CMS final rules for fiscal year 2022.

Removing wage index exceptions would also remove inequities between IPPS hospitals and other providers

- Current wage index values for SNFs are generally lower than for IPPS hospitals within the same markets, because only IPPS hospitals are eligible for wage index exceptions



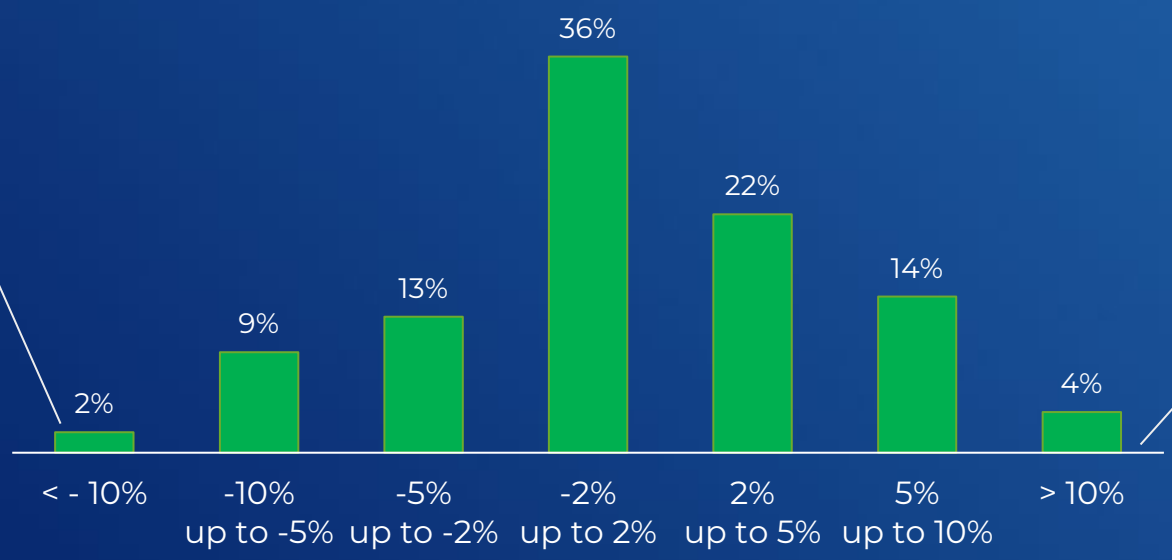
Note: IPPS (inpatient prospective payment systems); SNF (skilled nursing facilities).
Source: MedPAC analysis of 2022 SNF and IPPS final rule wage index files.

Redistributional effects of alternative IPPS wage index on many hospitals would be material

For example

- Hospitals in areas with very *high* current wage index values (> 1.5)
- Hospitals with very large current wage index exceptions

Share of hospitals with specified impact on IPPS payments



Percentage change in IPPS payments (budget neutral)

For example

- Hospitals in areas with very *low* current wage index values (<0.7)
- Hospitals in areas where hospital-reported labor costs are much *lower* than those of all-employers

Note: IPPS (inpatient prospective payment systems). IPPS payments exclude uncompensated care, were estimated under a budget-neutral policy, and assumed no changes in eligibility for enhanced IPPS payments. Impacts are when comparing to current wage index values excluding temporary low-wage exception.
Source: MedPAC analysis of 2021 MedPAR data, 2022 IPPS final rule wage index files, and alternative MedPAC wage index.

Alternative skilled nursing facility (SNF) wage index

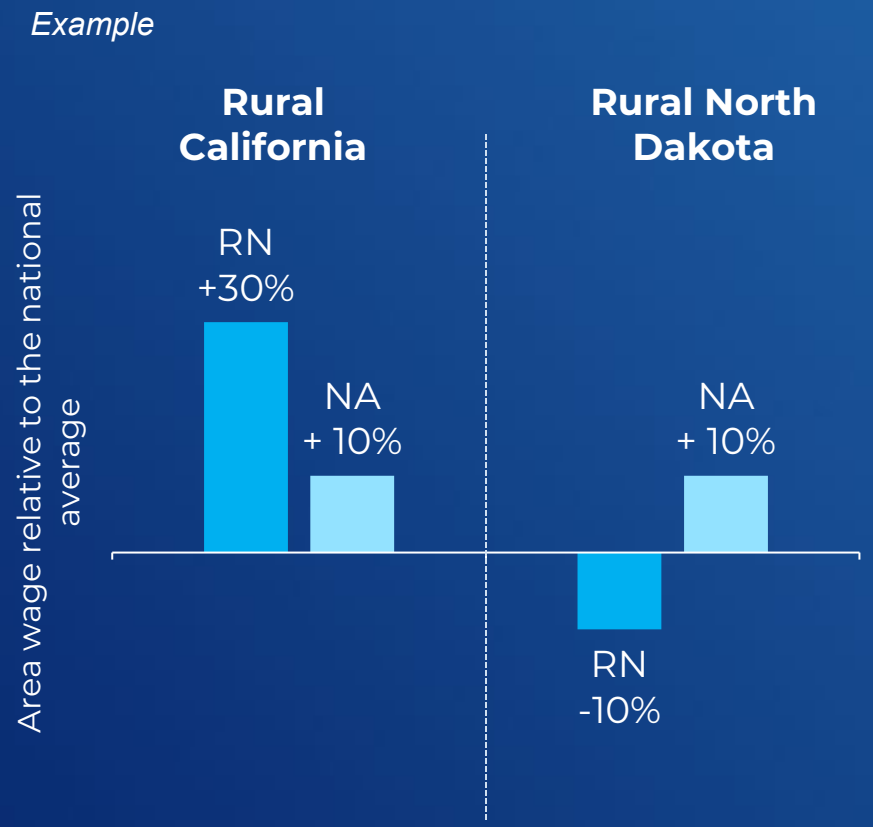
	Current SNF	Alternative IPPS	Alternative SNF
Data	IPPS hospitals (cost reports)	All-employer, occupation-level data (BLS, Census)	Same as alternative IPPS
Occupation weights	None (IPPS hospitals' aggregate labor costs)	Each occupation weighted by national share of *hospitals'* institutional wages: RN: 47% NA: 4%	Each occupation weighted by national share of *SNFs'* institutional wages: RN: 17% NA: 28%

Note: IPPS (inpatient prospective payment systems); SNF (skilled nursing facility); BLS (Bureau of Labor Statistics); RN (registered nurse); NA (nursing assistant).
Source: MedPAC analysis of 2019 BLS data.

Relative labor costs for an area can vary across occupations

Using SNF-specific occupation weights increases the accuracy of the SNF wage index because:

- Relative labor costs in an area can vary across occupations; and
- SNFs employ a different mix of occupations than IPPS hospitals (e.g. more nursing assistants)



Therefore, the IPPS wage index value should be far higher in rural California than in rural North Dakota. However, the SNF wage index values for the two states should not differ as much, as the relative wages for nursing assistants are similar

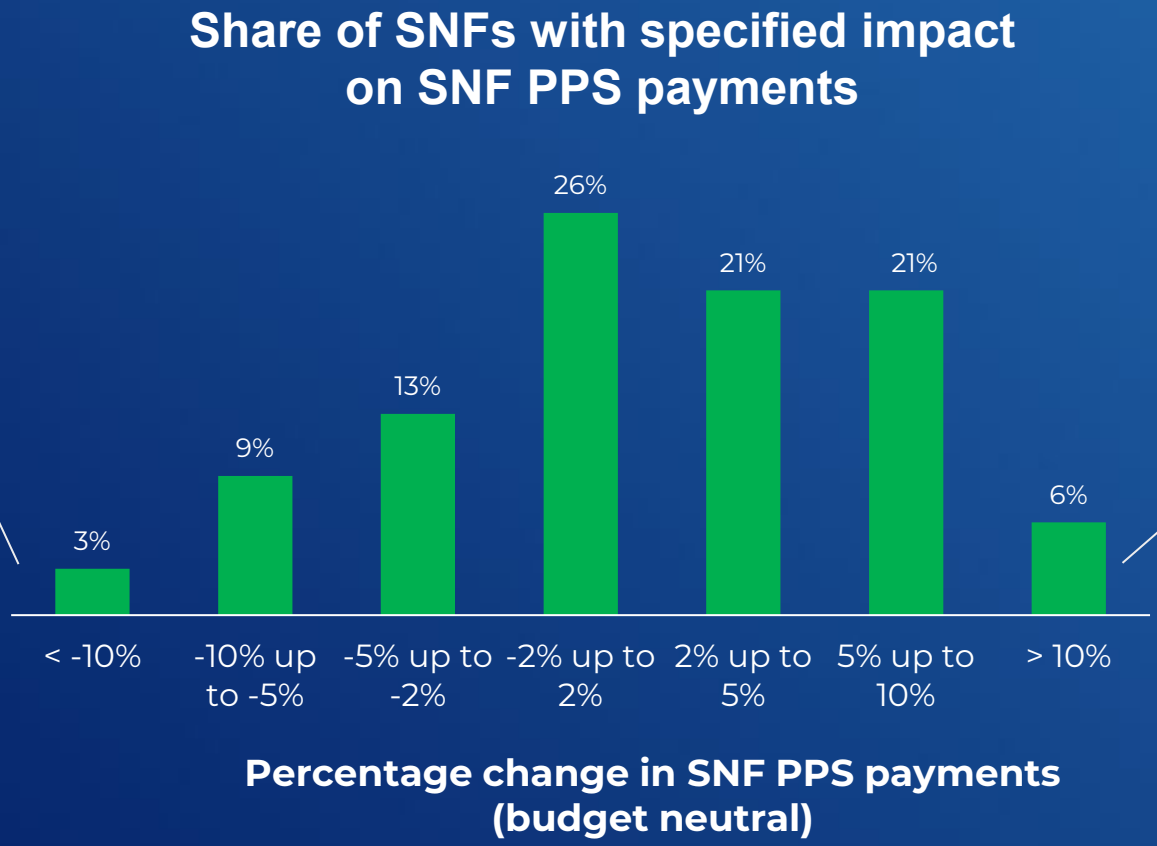
Note: IPPS (inpatient prospective payment systems). SNF (skilled nursing facility). NA (nursing assistant). RN (registered nurse).
Source: MedPAC analysis of 2019 BLS data.

Results are preliminary and subject to change

Redistributional effects of alternative wage index on many SNFs would be material

For example

- SNFs in areas with very *high* current wage index values
- SNFs in areas where SNFs face materially *lower* relative labor costs than IPPS hospitals



For example

- SNFs in areas with *low* current wage index values
- SNFs in areas where SNFs face materially *higher* relative labor costs than IPPS hospitals

Note: IPPS (inpatient prospective payment systems). PPS (prospective payment system). SNF (skilled nursing facility).
Source: MedPAC analysis of 2021 MedPAR data, CMS's 2022 SNF final rule wage index files, and alternative MedPAC wage index data.

Conclusion

- Current Medicare wage index systems are broken
- There are no perfect sources of labor cost data, or definition of labor market areas
- However, alternative wage indexes consistent with proposed approaches would be a substantial improvement:
  - More accurately measure relative labor costs
  - More equitable across providers
  - Less gameable and less administratively burdensome

Conclusion (cont.)

- Because many IPPS hospitals and SNFs would be materially affected by the move to alternative wage indexes, there would need to be a transitionary period
  - Phased in over a fixed period of time; or
  - Managed through a stop-loss policy so that no provider experiences changes in Medicare payments of more than a specified percent in any one year due to the transition

Note: IPPS (inpatient prospective payment systems). SNF (skilled nursing facility).