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# United States Senate

COMMITTEE ON FINANCE

WASHINGTON, DC 20510-6200

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February 9, 2006

## Via Electronic Transmission

The Honorable Mark McClellan, M.D., Ph.D.  
Administrator  
Centers for Medicare & Medicaid Services  
Department of Health and Human Services  
200 Independence Avenue, SW  
Washington, DC 20201

Dear Administrator McClellan:

As Chairman and Ranking Member of the Senate Committee on Finance, we are writing to ensure that the Centers for Medicare and Medicaid Services (CMS) is moving forward with significant refinements to the hospital inpatient prospective payment system (PPS) for fiscal year 2007. These refinements are needed to improve the accuracy of Medicare payments to hospitals.

On March 8, 2005, the Medicare Payment Advisory Commission (MedPAC) released its report and recommendations on physician-owned specialty hospitals and testified on its findings before the Senate Committee on Finance. MedPAC found that there were large differences in relative profitability across and within the diagnosis related groups (DRGs) that comprise the inpatient PPS. MedPAC indicated that these significant differences inappropriately encouraged hospitals to specialize in treating patients in profitable DRGs, as well as to select low-cost patients within a DRG.

To correct these inaccuracies, MedPAC recommended (1) refining the current DRGs to more fully capture differences in the severity of illness among patients, (2) basing the DRG relative weights on the estimated cost of providing care rather than on charges, (3) basing the DRG relative weights on the national average of hospitals' relative values in each DRG, and (4) adjusting the DRG relative weights to account for differences in the prevalence of high-cost outlier cases.

On May 12, 2005, you testified before the House Committee on Energy and Commerce hearing on specialty hospitals that CMS would be taking steps to improve the accuracy of Medicare inpatient payments. Specifically, in your testimony you stated:

First, to help reduce the possibility that specialty hospitals may take advantage of imprecise payment rates in the inpatient hospital prospective payment system, CMS is analyzing MedPAC's recommendations to improve the accuracy of payment rates for inpatient hospital services and expects to adopt significant revisions in FY07. CMS will fully examine and simulate the changes and proceed with those that actually lead to significant improvements in the accuracy of our payment system.

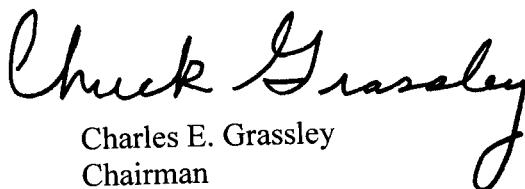
We appreciate the initial steps you took in the 2006 hospital inpatient PPS final rule to revise the cardiovascular surgery DRGs to better recognize patient severity of illness. These changes included differentiating cardiac surgery patients based on whether they had a "major cardiovascular condition" that would lead to a more complicated patient stay requiring greater resource use. This move was a good first step in improving the accuracy of payment among cardiac DRGs. For 2007, we encourage CMS to undertake such refinements to all appropriate DRGs.

Medicare payments should reflect what it actually costs hospitals to provide care to beneficiaries. Specialty hospitals have been able to cherry pick the most profitable patients, leaving community hospitals to treat the less profitable, the poor and the uninsured. This patient selection is inappropriate. Any incentives in the payment system to systematically choose one patient over another must be removed.

Consistent with the work you began with last year's hospital inpatient PPS final rule, and the Department's commitment to move forward with additional refinements of the DRG payment system in this year's inpatient PPS rule, we want to again lend our support for a detailed discussion, and adoption, if appropriate, of MedPAC's March 2005 recommendations.

If you have any questions, please contact Ashley Thompson of Senator Grassley's staff at 202-224-7616 or Pat Bousliman of Senator Baucus' staff at (202) 224-4515.

Sincerely,

  
Charles E. Grassley  
Chairman

  
Max Baucus  
Ranking Member