[COMMITTEE PRINT]

EXPLANATION OF THE ADMINISTRATION'S MEDICARE HOSPITAL PROSPECTIVE PAYMENT PROPOSAL AS COMPARED TO CURRENT LAW

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MEDICARE HOSPITAL INSURANCE

Issue	Current Law
Summary	Basic medicare reasonable cost reimbursement was modified last year in P.L. 97-248 (TEFRA) to provide: (1) expanded "section 223" reimbursement limits applying to total (not only on routine) inpatient operating costs; and (2) temporary growth rate targets (expiring after fiscal year 1985) rising annually by one percentage point plus the increase in the "marketbasket" of goods and services purchased by hospitals. TEFRA also directed the Secretary of HHS to develop and report on a system of prospective payment for hospitals.
1. Prospective payment amount	a. Medicare payment amounts are retrospectively determined based upon a hospital's reasonable costs, subject to the limits established by TEFRA. Certain reimbursement limits are applied to (1) hospital inpatient operating costs ("section 223" limits) and (2) the rate of increase in inpatient operating costs (this limit expires after FY 1985).

Administration Proposal	Recommendations
Medicare payment for inpatient operating costs of hospitals would be determined in advance and made on a per case basis. A fixed amount would be paid for each type of case, identified by the "diagnosis related group" (DRG) into which the case is classified.	
a. The Secretary would be required to determine prospectively a payment amount for each hospital discharge.	
Hospital cases (discharges) would be classified into "diagnosis related groups" (DRG's). There would be a separate payment amount for each of 467 DRG's.	

MEDICARE HOSPITAL INSURANCE—Continued

Issue	Current Law
2. DRG national standard rates	a. Not applicable.
3. Regional wage adjustment	a. The Bureau of Labor Statistics adjustor for hospital wages is used under current Section 223 limits to adjust for area differences in hospital wage levels.

Administration Proposal	Recommendations
a. The Secretary would be required to determine a national standard rate per discharge for each DRG. The rate would be the product of: (1) an "appropriate standard cost level per discharge," as determined by the Secretary; and (2) an "appropriate weighting factor" for each DRG as determined by the Secretary.	
a. The national average rate per discharge would be adjusted for area differences in hospital wage levels using the same Bureau of Labor Statistics adjustor as current law.	

MEDICARE HOSPITAL INSURANCE—Continued

Issue	Current Law
4. Initial payment level	Medicare payments to hospitals are made according to the lower of actual reasonable costs, the section 223 limits as expanded by TEFRA, or the rate of increase limit added by TEFRA. a. The TEFRA rate-of-increase limits are based on each hospital's historical cost. b. The cost is updated to establish the cost limit for the first of the 3 years the TEFRA limits are in effect by the hospital market basket plus 1 percentage point.
5. Annual updates	a. Under TEFRA the rate of increase limits are updated by the increase in a market basket of goods and services purchased by hospitals plus one percentage point

Administration Proposal	Recommendations
a. The national standard rate for each DRG would be derived from historical medicare cost data. b. The rate would be updated to FY 1983 by the estimated industry-wide actual increase in hospital costs.The rate would be further updated to FY 1984 by the increase in the marketbasket of goods and services purchased by hospitals.	
a. The Secretary would be required to update annually the payment amounts to a level which he or she determined would be adequate compensation for efficiently and economically operated hospitals, taking into account changes in the hospital marketbasket of goods and services, productivity, technological and scientific advances. Hospitals that are not included in the prospective payment proposal would be subject to the rate of increase provision similar to TEFRA, including the incentive payments, except that for hospital cost reporting periods ending before October 1, 1984, the rate of increase will be limited to marketbasket only. For hospital cost reporting periods beginning after September 30, 1984, the rate of increases would be marketbasket plus one percentage point.	

MEDICARE HOSPITAL INSURANCE—Continued

Issue	Current Law
6. Recalibration	a. Not applicable.
7. Atypical cases/Outliers	a. Note item number 10(d).
	b. Not applicable.
	c. Not applicable.

Administration Proposal	Recommendations
a. The Secretary would be permitted to adjust payment amounts, from time to time, to take into account changes in DRG's, the proportion of costs attributable to wages, the types of costs subject to the system, regional differences in non-wage goods and services. Also, the Secretary would be authorized to establish payment amounts for new DRG's.	
a. The Secretary would be authorized to provide for additional payment amounts for cases which are extraordinarily costly to treat relative to other cases within the DRG. The proposal would allow the Secretary to provide additional payment amounts for any discharge whose length of stay exceeds by 30 or more days the mean length of stay of the discharges in the DRG to which the discharge belongs. b. It is the intention of the Administration to pay for days in excess of the 30 days at a per diem rate. A per diem rate would be calculated for each DRG by dividing the DRG payment amount by the mean length of stay for the DRG. The Administration proposes to reimburse 60% of that daily rate for each "outlier" day. c. The provision is intended, to be budget neutral. Additional amounts reimbursed for the outlier days would reduce the DRG payment level across the board.	

MEDICARE HOSPITAL INSURANCE—Continued

Issue	Current Law
8. Capital Expenses	a. Medicare reimburses hospitals for the reasonable costs of capital (including depreciation, interest and rent). In addition, proprietary hospitals receive a return on net equity. The Secretary is authorized to exclude from reimbursement to providers certain costs related to capital expenditures that have been disapproved through the health planning process. b. Not applicable.
9. Medical Education Expenses	
a. Direct Costs	a. Medicare reimburses direct medical education expenses, such as the salaries of interns and residents in approved education programs on the basis of reasonable cost.
b. Indirect Costs	b. The Section 223 limits provide an adjustment to recognize individual hospital differences in indirect costs due to approved teaching activities.

Administration Proposal	Recommendations
a. Capital would continue to be reimbursed on a reasonable cost basis. In addition, the return on equity would continue to be paid as under the current system.	
b. The Secretary would be permitted to include in the prospective payment system, by regulation, at such time as he or she deemed appropriate, capital or other costs.	
The bill does not expressly exclude direct or indirect medical education costs from the prospective payment amount.	
a. However, it is the intention of the Administration to reimburse direct medical education expenses, as under current law. Under the bill, the Secretary would be authorized to include costs such as direct medical education costs under the prospective payment system when he or she deemed appropriate.	
b. It is the intention of the Administration that the prospective payment amount would be increased to take into account indirect education costs. As under current Section 223 limits, a "teaching adjustment" would be provided based upon the hospital's ratio of interns and residents to beds.	

MEDICARE HOSPITAL INSURANCE—Continued

Issue	Current Law
10. Exemptions, exceptions, and adjustments	
a. Psychiatric, long-term care, and children's hospitals	a. Under TEFRA, Section 223 limits do not apply to children's hospitals, long-term care hospitals or to rural hospitals with less than 50 beds. In addition the Secretary is required to provide exemptions exceptions, and adjustments to the Section 223 limits as he deems appropriate to take into account the special needs of psychiatric hospitals serving a disproportionate number of low income or medicare beneficiaries.
b. Sole community providers	b. Under TEFRA the Secretary is required to privide exemptions, exceptions, and adjustments to the Section 223 limits as he deems appropriate to take into account the special needs of sole community providers.
c. Public and other hospitals	c. Under TEFRA the Secretary is required to provide exemptions, exceptions, and adjustments to the Section 223 limits as he deems appropriate to take into account the special needs of public and other hospitals that serve a disproportionate number of low income or medicare beneficiaries.
d. Other providers	d. Under TEFRA the Secretary is required to provide exemptions, exceptions, and adjustments to the Section 223 and the rate of increase limits as he deems appropriate to take into account the special needs of new hospitals, risk-based health maintenance organizations, and hospitals providing atypical or essential services; extraordinary circumstances beyond a hospital's control; and for other purposes.
e. Study provision	e. Not applicable.

Administration Proposal	Recommendations
a. The proposal would not apply to psychiatric, long-term care and children's hospitals, however, the Secretary would be authorized to provide for prospective payment for such hospitals at some time in the future, by regulation.	
b. The Secretary would be authorized to provide for exceptions and adjustments to take into account the special needs of sole community providers.	
c. No provision.	
d. No provision.	
e. No provision.	

MEDICARE HOSPITAL INSURANCE—Continued

Issue	Current Law
11. Peer Review	a. Current law requires the Secretary to enter into contracts for utilization and quality control peer review with professional review organizations or other review organizations, including medicare intermediaries (subject to certain conditions and limitations).
12. Payments to HMO's and CMP's	a. Current law provides that HMO's and CMP's may be reimbursed either on the basis of reasonable costs, or under a risk-based contract, a payment equal to 95% of the adjusted average per capita cost (AAPCC) for medicare enrollees in the HMO's area. (The provision in TEFRA authorizing risk-based contracts has not as yet been implemented.)
13. Effective Date/Transition	a. Under TEFRA, the Section 223 limits are authorized indefinitely; the rate of increase limits would not apply to hospital cost reporting periods beginning on or after October 1, 1985.

Administration Proposal	Recommendations
a. No provision.	
a. The proposal would permit, at its election, an HMO or a CMP that receives medicare payments on a risk-basis to choose to have the Secretary directly pay hospitals for inpatient hospital services furnished to medicare enrollees of the HMO or CMP. The payment amount would be at the DRG rate (or on the basis of reasonable cost, as applicable) and would be deducted from medicare payments to the HMO or CMP.	
a. The proposal would be effective with individual hospital accounting years beginning on or after October 1, 1983. No other transitional arrangements are specified. Reimbursement limits provided in TEFRA would be repealed, however, hospitals not included in the prospective payment system would be subject to a new rate on increase limitation similar to that in TEFRA, except that, for hospital cost reporting periods ending before October 1, 1984, the rate of increase would be limted to the marketbasket only. After September 30, 1984, the rate of increase would be the marketbasket plus one percentage point.	

MEDICARE HOSPITAL INSURANCE—Continued

Issue	Current Law
14. Payors covered	a. Medicare reimbursement applies only to the program itself (although some medicaid programs follow medicare).
15. State Cost Control Systems	a. The Secretary of HHS has authority to establish medicare demonstration projects. (There are currently four State-wide medicare demonstrations (MD, NJ, NY and MA) and one area-wide (Rochester, NY demonstration). b. In addition, TEFRA authorizes the Secretary, at the request of a State, to pay for medicare services according to the State's hospital cost control system if such system— (1) applies to substantially all non-Federal hospitals; (2) applies to at least 75% of all inpatient revenues; (3) treats payors, hospital employees and patients equitably; and (4) will not result in greater medicare expenditures over a three-year period than would otherwise have been made. (To date, no State systems have been approved under this authority.)

Administration Proposal	Recommendations
a. Same as present law.	
a. The Secretary would be expressly authorized to continue to develop, carry out, or maintain medicare experiments and demonstration projects.	
b. The authority under TEFRA would be repealed.	

MEDICARE HOSPITAL INSURANCE—Continued

Issue	Current Law
16. Administrative and Judicial review	a. A provider may request administrative review of a final decision of fiscal intermediary by the Provider Reimbursement Review Board (PRRB). b. A provider may appeal the PRRB decision to Federal court or, where it involves a question of law or regulation which the PRRB does not have the authority to review, the provider may appeal directly to Federal court. An individual provider may bring suit in the judicial district in which it located or the District of Columbia. Groups may bring suit only in the District of Columbia.
17. Beneficiary Liability	a. After adequate notice the Secretary may allow hospitals to impose charges on individuals for costs in excess of those detemined to be reasonable and necessary under the 223 limits. (The Secretary has never provided such notice.)

Administration Proposal	Recommendations
a. No provision with respect to administrative review.	
b. Payment amounts, exceptions, adjustments and rules established by Secretary would not be appealable to the court.	
a. Hospitals are prohibited from charging beneficiaries amounts in excess of the statutory deductible and coinsurance. The prospective payment would be considered payment in full.	

MEDICARE HOSPITAL INSURANCE—Continued

Issue	Current Law
18. Studies and reports	a. TEFRA directed the Secretary to develop and report to Congress on proposals to reimburse hospitals, skilled nursing facilities, and, to the extent possible, other providers on a prospective basis.
19. Research on payment methods	a. There is general authority for the Secretary to conduct research on payment methods and other matters relating to medicare.

Administration Proposal	Recommendations
a. No provision.	
a. No provision.	