

Over the years, the federal government has created a variety of policies and programs that adjust standard Medicare payments to healthcare providers. Some of these adjustments are intended to account for the varying needs of different providers, based on factors such as location and volume of low-income patients. Others are intended to advance objectives such as incentivizing high-quality care, subsidizing medical education, and facilitating adoption of new technologies. This fact sheet summarizes several types of Medicare payment adjustments.

## Safety-Net and Underserved Hospital Support

**DISPROPORTIONATE SHARE HOSPITAL (DSH) PAYMENTS:**<sup>1</sup> Hospitals that treat disproportionate shares of certain low-income patients are eligible for adjusted payments meant to offset losses due to uncompensated care.

Medicare calculates a DSH patient percentage for each Medicare-licensed hospital based on the number of days DSH patients are treated. DSH patients include Medicare patients with Social Security income and Medicaid patients not enrolled in Medicare. A hospital is considered a DSH hospital if its DSH patient percentage exceeds 15%, with some exceptions.

Medicare payments are adjusted by a percentage that is calculated based on a hospital's location, DSH patient percentage, size, and hospital type. Adjustments are capped at 12% for small urban hospitals and large rural hospitals. Twenty-five percent of the adjusted amount is paid upfront, and the rest is withheld and redistributed based on each hospital's relative share of uncompensated care among DSH hospitals.

**340B DRUG PRICING:**<sup>2</sup> Qualifying hospitals that treat disproportionate shares of low-income or uninsured patients are eligible to buy certain drugs at a government-negotiated discount rate.

A facility that falls into one of 16 statutorily designated eligibility categories based on its share of low-income or uninsured patients gets discounts on certain medications, amounting to 20%-50% savings on overall medication costs. Federal law does not restrict use of the savings, but the program is meant to support care for low-income patients.

## Value-Based Care Initiatives

**HOSPITAL VALUE-BASED PURCHASING:**<sup>3</sup> Payments are adjusted based on measures of hospitals' quality of care.

Every hospital receives performance scores for a set of quality measures. For each measure, Medicare calculates two scores, one reflecting current performance and another reflecting improvement from past performance. The higher score for each measure is used to calculate a total performance score. The program withholds 2% from payments under the Inpatient Prospective Payment System (IPPS) — Medicare's reimbursement system for inpatient care — then redistributes those funds according to each hospital's score relative to its peers. A hospital may receive more or less than the 2% initially withheld, creating an incentive for quality improvement.

**HOSPITAL READMISSIONS REDUCTION PROGRAM (H-RRP):**<sup>4</sup> Payments are reduced for hospitals with high rates of unplanned readmissions.

Hospitals report counts of unplanned readmissions within 30 days of discharge for a list of specific conditions and procedures, which Medicare then compares against benchmark values. Hospitals with excess readmissions receive a payment reduction percentage, capped at 3%. Percentages are reported annually to hospitals, which then have 30 days to submit corrections before the adjustment goes into effect.

**HOSPITAL-ACQUIRED CONDITION REDUCTION PROGRAM (HACRP):**<sup>5</sup> Payments are reduced for hospitals with poor performance on patient safety measures.

Medicare calculates a score for each hospital based on the incidence of a list of healthcare-associated infections and other patient safety measures. Hospitals in the worst-performing 25% are subject to a 1% reduction in IPPS payments. Scores are reported annually to hospitals, which then have 30 days to submit corrections before the adjustment goes into effect.

<sup>1-11</sup> For references, see [www.achi.net/publications/medicare-payment-adjustments](http://www.achi.net/publications/medicare-payment-adjustments)

## Educational Subsidies

**DIRECT GRADUATE MEDICAL EDUCATION:**<sup>6</sup> Teaching hospitals receive supplemental payments based on the number of medical residents they host.

Medicare calculates a per resident amount (PRA) for a hospital based on past education costs, adjusted for inflation. The PRA is multiplied by the number of full-time equivalent residents, then adjusted to reflect the proportion of Medicare patients the hospital serves, to determine an interim payment. Interim payments are paid throughout the year and reconciled after submission of the hospital's annual Medicare cost report.

**INDIRECT MEDICAL EDUCATION:**<sup>7</sup> IPPS claims from teaching hospitals are adjusted to account for additional patient care costs.

Each hospital receives payment adjustments based on a formula that accounts for its intern-and-resident-to-bed ratio, the effect of teaching activities on patient care costs, and a multiplier set by Congress, which has not changed since 2003 and translates to a 5.5% increase in IPPS payments for every 10% increase in the intern-and-resident-to-bed ratio.

## Situational Adjustments & Other Subsidies

**OUTLIER PAYMENT ADJUSTMENT:**<sup>8</sup> Medicare increases payment for IPPS claims that exceed a threshold amount.

Each year, Medicare sets a fixed-loss outlier threshold that it uses to calculate payments for exceptionally high-cost claims. The threshold is adjusted for each hospital based on its area wage index. A hospital reports the total charges for a claimed procedure, and Medicare adjusts this amount using the hospital's historical cost-to-charge ratio. If the adjusted charges exceed the adjusted threshold, Medicare pays 80% of the amount above the threshold in addition to the standard payment.

**NEW TECHNOLOGY ADD-ON PAYMENT (NTAP):**<sup>9</sup> Medicare makes supplemental payments to providers offering new technologies that are more costly than standard treatments.

Medicare offers three pathways for technologies to qualify for NTAP payments: a "traditional" pathway and two alternatives. To qualify under the traditional pathway, a treatment must use technology that is new, is so costly that the applicable standard payment is inadequate, and substantially improves diagnosis or treatment. The alternative pathways allow technologies to bypass some of these criteria if they have received special designations from the Food and Drug Administration. Payments are equal to 65% of the reported cost of the technology or 65% of the amount by which the cost of the technology exceeds the standard payment for the claim, whichever is lower.

**ESSENTIAL MEDICINES BUFFER STOCK PAYMENT:**<sup>10</sup> Small, independent hospitals can receive extra IPPS payments to purchase essential medicines.

Independent hospitals with fewer than 100 beds are eligible to receive payments to purchase up to a six-month supply of certain medicines. The payments will not support building a new stock of a medication considered by the Centers for Medicare and Medicaid Services to be in shortage, but a hospital can receive payments to replenish a stock that existed before a shortage began.

**PROSPECTIVE PAYMENT SYSTEM (PPS)-EXEMPT CANCER HOSPITALS:**<sup>11</sup> A handful of hospitals are reimbursed for inpatient hospital care outside of the IPPS.

Because cancer treatments are often complex and require long inpatient stays, they tend to be inadequately reimbursed under the IPPS. Eleven cancer hospitals (none of them in Arkansas) are designated by name in federal legislation as PPS-exempt. Reimbursement for inpatient care at PPS-exempt hospitals is based on the reported costs of treatment, which tends to result in higher per-case reimbursement. While criteria for becoming a PPS-exempt hospital are defined in legislation, no additional hospitals have received the designation since 1997.

<sup>1-11</sup> For references, see [www.achi.net/publications/medicare-payment-adjustments](http://www.achi.net/publications/medicare-payment-adjustments)