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MEDICARE WAGE INDEX— ARE YOU GETTING YOUR FAIR SHARE OF THE REIMBURSEMENT PIE?

The wage index has been a part of Medicare's hospital reimbursement ever since the inpatient prospective payment system was introduced in 1983. The purpose of the wage index is to adjust Medicare payments to hospitals to account for area differences in wage costs. The wage index reflects the relative hospital wage level for each geographic area compared to the national average. Currently the same wage index calculated as part of IPPS is also applied to most other Medicare payment systems including outpatient PPS, IP rehab and psych, skilled nursing facilities, and home health.

Wage index levels vary significantly between areas. For example, the FY 2009 IPPS Proposed Rule reflects levels ranging from .7336 for rural North Dakota to 1.5766 for Santa Cruz-Watsonville, California. The proposed wage index for rural Georgia is .7840 while for Atlanta it is .9760. Such a difference could result in a significant disparity in reimbursement for a hospital based solely on being located just outside the Atlanta area.

To understand the impact from differences in wage index, consider a hypothetical example of two hospitals. For FY 2008 both have 3,000 Medicare discharges, a case mix index of 1.25 and an operating DSH payment percentage of 15 percent. One of the hospitals has a wage index of .9000 and the other has a wage index of .8500, a difference that on paper might not appear significant. However, the difference in Medicare inpatient reimbursement between these two hospitals for just one year is over \$725,000. And this doesn't even take into account the differences in Medicare payments beyond IPPS.

Another factor directly related to wage index is geographic reclassifications. Medicare regulations allow providers meeting specific requirements to reclass to another geographic area for purposes of receiving a higher wage index. The same data used to calculate wage index is a key component of determining eligibility for reclassification.

Needless to say, wage index is a critical component of Medicare reimbursement. But many hospitals are not proactive in ensuring that their wage index fully reflects their actual wage costs. There are a couple factors that often prevent hospital management from giving their wage index the attention it deserves.

First, the ironic nature of the wage index calculation is that it is dependent on data from hospitals that are often competing for both patient volume and qualified labor. Cost report wage survey data from every acute hospital in a specific geographic area is combined to calculate the

wage index for that area. In a perfect world every hospital in a geographic area would work together to make sure their wage index is optimized. Unfortunately, it can be difficult in the real world to get competing hospitals to work together even if the result would be to their mutual benefit.

Second, the wage index is based on the average of three years of data, with a significant lag between when that data is reported in the cost report wage survey and when it is actually applied to the wage index. As a result it is nearly impossible to get a quick-fix result from correcting wage index issues. It can be difficult to have the foresight to address an issue today that might not make a significant difference for several years.

Despite these hindrances, there are providers who have been successful in increasing their area's wage index over time. There are examples of competing hospitals in the same area joining together to assess their area's wage index, often involving a third party to work with the details to prevent individual hospitals from accessing sensitive information. Other hospitals have been successful in working independently to address their wage index issues. The key is to be proactive in identifying and addressing opportunities, both in data that has been submitted but not finalized and in reporting information going forward.

A successful wage index review involves analysis of the detail previously included in the wage survey along with the review of other areas of the cost report to potentially identify additional wage survey costs. A thorough assessment includes not only the appropriate costs but also the related hours, and addresses costs for both employed and contracted personnel. Examples of specific areas to assess that can often be an issue include the following:

- Bonuses
- Severance Payments
- Overtime Hours
- On-call Hours
- Shift Differential
- Baylor Plans
- Legal and Professional Fees
- Physician Benefits
- Home Office Personnel
- Pension Costs
- Employee Physicals
- PTO Buyback

As with most regulations related to the cost report, wage survey rules have many nuances that must be understood when assessing data. A good example is the treatment of pension cost. A thorough grasp of the proper treatment under GAAP will not be enough to understand how to

appropriately reflect the cost in the wage survey. It's possible that proper presentation under GAAP and under wage survey regulations result in two significantly different figures.

Gaining a sufficient understanding of the applicable regulations is just one step in the process. An equally important step is digging into the details. Often it is not enough to depend on a description provided by a payroll report or GL account. A comprehensive assessment includes developing an understanding of the data through analyzing the numbers and discussing with the appropriate personnel. The right interview questions can assist in uncovering important information that may have been previously overlooked.

The key to getting the most benefit from a systematic review of wage data is to include all years not finalized, and establish processes to properly capture data going forward. For example, a hospital with a September 30 year-end will have the opportunity this fall to correct wage survey data included in its FY 2006 cost report. Providers considering implementing a wage index review should begin by looking at their FY 2006 data this summer in order to meet the fall deadline. Any opportunities identified during this process can then be applied to FY 2007 data which should be eligible for correction in the fall of 2009. Opportunities for improvement should then be applied as part of the FY 2008 cost report preparation process.

Because the wage index plays a significant role in Medicare reimbursement, it's a good idea for every hospital to make the effort to perform a wage index review either internally or with outside assistance. Some hospitals will find that the processes they have in place and the resulting amounts that have been reported are on target, and the end result will be peace of mind if nothing else. However, some providers may be surprised by new opportunities that are uncovered that will lead to increased reimbursement down the road.

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