



Special Bulletin

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CMS ISSUES FINAL RULE ON MEDICAID DSH CALCULATION

The Centers for Medicare & Medicaid Services (CMS) on March 30 issued a [final rule](#) on how third-party payments are treated when calculating the hospital-specific limitation on Medicaid disproportionate share hospital (DSH) payments. According to CMS, the rule clarifies current policy that uncompensated care costs for Medicaid-eligible individuals include only those that remain after accounting for payments hospitals receive by or on behalf of Medicaid-eligible individuals. This includes Medicare and other third-party payments that compensate hospitals for care furnished to such individuals. The agency originally issued this policy in sub-regulatory guidance, which it now codifies in this rule.

The AHA is [deeply disappointed](#) in CMS's action to finalize its rule regarding how third-party payments are treated when calculating the hospital-specific limitation on Medicaid DSH payments. Of particular concern is the decision by CMS to ignore requests to apply this change in policy in a prospective manner to give states and hospitals sufficient time to make needed adjustments to ensure compliance.

The Medicaid statute limits Medicaid DSH payments to a given hospital to no more than its Medicaid shortfall and uncompensated care costs. The agency, over the years, has issued regulation and guidance through FAQs to define what costs count toward Medicaid shortfall and uncompensated care in establishing the hospital's specific DSH payment limit. While the statute expressly states that uncompensated care costs must be calculated net of Medicaid payment, in these FAQs, CMS stated that not only must uncompensated care cost be net of Medicaid payment but also of third party payments including Medicare and private insurance (e.g. commercial insurance). Various court cases have challenged that CMS violated not only the Medicaid statute but also the Administrative Procedures Act by providing state Medicaid agencies and their contracted Medicaid DSH auditors with only informal guidance through the FAQs. The legal challenges have specifically focused on the fact that the FAQs instruct a state to subtract payments received from private health insurance and Medicare from the costs incurred to provide hospital services to those patients.

The AHA in its comment [letter](#) on the proposed rule argued that the policies set forth in these FAQs are inconsistent with both the statute and CMS's own 2008 Medicaid DSH audit regulation. In that 2008 regulation, CMS instructed states to calculate a hospital's total annual cost for individuals without health insurance and specified only the subtraction of Medicaid payment; it did not call for the subtraction of payment for Medicare or private insurance. The AHA called for CMS to withdraw the proposed rule, which was "substantive and establishes new policy, specifically with the intent of avoiding potentially unfavorable federal district court rulings."

However, the final rule claims it is clarifying existing CMS policy on the treatment of third-party payment from other payers for calculating an individual hospital's DSH payment limit. Specifically, the rule defines uncompensated care costs as:

- net of third-party payments, including but not limited to payments by Medicare and private insurance;
- designed to capture the total burden on the hospital of treating Medicaid-eligible patients prior to payment by Medicaid; and
- calculated in the aggregate, not by estimating the cost of individual patients.

In addition, the AHA had argued that if CMS chose to finalize the rule, it should be done prospectively to give states and hospitals sufficient time to make needed adjustments to ensure compliance. Unfortunately, in response to comments requesting prospective application of the policy, CMS now claims that prospective application is irrelevant since this is longstanding CMS policy.

The final rule comes on the heels of a March 2 [federal court decision](#) that permanently barred CMS from using sub-regulatory guidance to calculate Medicaid DSH payments for New Hampshire hospitals. The AHA supported the plaintiff's arguments in that case. In issuing the final rule, CMS appears to be responding to court challenges.

NEXT STEPS

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