PROVIDER REIMBURSEMENT REVIEW BOARD DECISION

2010-D44

PROVIDER -
Southcrest Hospital
Tulsa, Oklahoma

Provider No.: 37-0202

vs.

INTERMEDIARY -
Wisconsin Physicians Service
(Formerly Mutual of Omaha)

DATE OF HEARING -
April 1, 2010

Cost Reporting Periods Ended -
December 31, 2003; December 31, 2004 and December 31, 2005

CASE NOs.: 04-2270; 07-0278; 07-1351 and 08-0169

INDEX

ISSUE:

Whether the hospital as a new provider is entitled to capital hold-harmless methodology under the prospective payment system beyond the 10-year transition period.

MEDICARE STATUTORY AND REGULATORY BACKGROUND:

This is a dispute over the amount of Medicare reimbursement due a provider of Medicare services.

The Medicare program was established to provide health insurance to the aged and disabled. 42 U.S.C. §§1395-1395cc. The Centers for Medicare and Medicaid Services (CMS), formerly the Health Care Financing Administration (HCFA), is the operating component of the Department of Health and Human Services (DHHS) charged with administering the Medicare program. CMS' payment and audit functions under the Medicare program are contracted to organizations known as fiscal intermediaries and Medicare Administrative Contractors (MACs). Fiscal intermediaries determine payment amounts due the providers under Medicare law and under interpretive guidelines published by CMS. See, 42 U.S.C. §1395h, 42 C.F.R. §§413.20 and 413.24.

At the close of its fiscal year, a provider must submit a cost report to the fiscal intermediary showing the costs it incurred during the fiscal year and the portion of those costs to be allocated to Medicare. 42 C.F.R. §413.20. The fiscal intermediary reviews the cost report, determines the total amount of Medicare reimbursement due the provider, and issues the provider a Notice of Program Reimbursement (NPR). 42 C.F.R. §405.1803. A provider dissatisfied with the intermediary's final determination of total reimbursement may file an appeal with the Provider Reimbursement Review Board (Board) within 180 days of the issuance of the NPR. 42 U.S.C. §1395oo(a); 42 C.F.R. §405.1835.

In 1991, in accordance with 42 U.S.C. §1395ww(g), CMS finalized a prospective payment system (PPS) for hospital inpatient capital-related costs which had previously been subject to cost-based reimbursement. The Secretary promulgated regulations that established a phase-in period intended to ease the transition of hospitals from cost reimbursement to the inclusion of capital payments under the PPS (Fed. Reg. Vol. 52, No. 96, May 19, 1987). 42 C.F.R. §412.340 established a ten-year transition to a fully prospective capital payment system with cost reporting periods beginning on or after October 1, 1991. During that period, hospitals were paid based on a varying blend of their own capital costs and the federal prospective rate. At the end of the period, hospitals would be paid solely on the federal prospective rate. 42 C.F.R. §412.324 sets out the general rule that during the ten-year transition period hospitals with a hospital-specific capital rate below the federal rate would be paid based on the fully prospective payment methodology under 42 C.F.R. §412.340, while hospitals with a hospital-specific capital rate above the federal rate would be paid under the hold-harmless methodology under 42 C.F.R. §412.344. The regulation also provides for an exception in the case of a new hospital. Under §412.324(b), a new hospital, as defined under §412.300(b), is paid 85% of its allowable Medicare inpatient hospital capital-related costs through its cost reporting periods ending at least

2 years after the hospital accepts its first patient. For the third year through the remainder of the transition period, the hospital is paid based on the fully prospective payment methodology or the hold-harmless payment methodology. 42 C.F.R. §412.324(b)(3) states:

> "if the hospital is paid under the hold-harmless methodology described in section 412.344, the hold-harmless payment for old capital costs . . . is payable for up to and including eight years and may continue beyond the first cost reporting period beginning on or after October 1, 2000."

This case involves the application of the hold-harmless capital payment methodology to a new provider.

STATEMENT OF THE CASE AND PROCEDURAL HISTORY:

Southcrest Hospital (Provider) is a 180-bed, short-term acute care hospital located in Tulsa, Oklahoma. It was certified for Medicare participation in June of 1999. The Provider qualified as a new hospital pursuant to 42 C.F.R. §412.300(b) and was paid 85% of its capital costs for its cost reporting periods ended December 31, 1999, December 31, 2000 and December 31, 2001. From January 1, 2002 through June 18, 2003 the Provider was paid based upon the "hold-harmless" reimbursement for capital related costs. As of June 19, 2003, the Intermediary began paying the Provider based on 100% of the federal rate for capital costs under PPS, rather than the hold-harmless methodology. There is no dispute that the Provider qualified as a new provider or that the hold-harmless provisions at 42 C.F.R. §412.324 are controlling. At issue is the application of 42 C.F.R. §412.324 to the Provider's operating circumstances.

The Provider appealed the Intermediary's determination to the Board and met the jurisdictional requirements of 42 C.F.R. §§405.1835 - 405.1841. The Provider was represented by Gregory N. Etzel, Esq., of Baker & Hostetler, LLP and Jonathan L. Rue, Esq. of Parker, Hudson, Rainer & Dobbs, LLP. The Intermediary was represented by Byron Lamprecht of Wisconsin Physicians Service.

PARTIES' CONTENTIONS:

The Provider contends the plain language of 42 C.F.R. §412.324(b) mandates hold-harmless payment. It argues the Intermediary's position ignores the intent of the regulation and cites numerous Federal Register discussions from 1991 to 2001[1] to support its argument. It protests that the informal clarification issued by CMS to the Intermediary is a substantive change in policy without merit and contrary to the Administrative Procedure Act (APA). 5 U.S.C. §553. The Provider cites to the HealthEast Woodwinds decision in which both the Federal District Court for the District of Minnesota and the Board found for a provider under similar circumstances.[2]

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[1] The 10-year transition period for capital PPS.

[2] HealthEast Woodwinds Hosp. v. Leavitt, Civ. Action No. 08-4526 at 35 (D. Minn. May 15, 2009) (Provider Appendix K at 31-39); HealthEast Woodwinds Hospital v. BlueCross BlueShield Association/Noridian

The Provider points out CMS acknowledged the Intermediary's hold-harmless capital payments "were correct based on [the Intermediary's] understanding of the rules at the time claims were paid."[3] CMS specifically found that the claims paid prior to June 19, 2003 need not be reprocessed as part of the Intermediary's change to the 100% federal rate payment method.[4] Therefore, the Provider believes even under the Intermediary's incorrect interpretation of the regulation it still qualifies for hold-harmless capital payments as it received hold-harmless payments under 42 C.F.R. §412.324(b)(3).

The Intermediary contends that the Provider is not eligible for a hold-harmless payment on allowable Medicare inpatient hospital capital-related costs because it was not entitled to the hold-harmless payment methodology during the ten-year transition period, identified in 42 C.F.R §412.304(b) as cost reporting periods beginning on or after October 1, 1991 and before October 1, 2001. In support of this position, the Intermediary cites testimony that confirms the Provider did not receive hold-harmless payment until calendar year 2002,[5] after the close of the ten-year transition period, and contends that 42 C.F.R. §412.324(b)(3) requires that a provider must have been paid during the transition period under hold-harmless to continue to receive hold-harmless payments beyond the transition period. The Intermediary concludes that since the Provider was never paid under the hold-harmless methodology during the transition period it does not qualify for hold-harmless payments for cost reporting periods beginning on or after October 1, 2000.

STIPULATIONS:

The parties entered into a stipulation that sets forth the following factual findings:[6]

1. Southcrest Hospital (Provider No. 37-0202)("Provider") is a 180-bed short-term acute care hospital located in Tulsa, Oklahoma.
2. The Intermediary is Wisconsin Physicians Service ("WPS"). At the time of the cost reporting period under appeal, WPS operated as intermediary under the name Mutual of Omaha. WPS and Mutual of Omaha are referenced collectively as "Intermediary" throughout this Stipulation Agreement.
3. The Provider accepted its first patient in May of 1999, and obtained Medicare certification in June of 1999. The Provider's first partial fiscal year ended December 31, 1999, its first full fiscal year began January 1, 2000 and ended December 31, 2000, and its second full fiscal year began January 1, 2001 and ended December 31, 2001.
4. During its fiscal years ending December 31, 1999, December 31, 2000, and December 31, 2001, the Provider was a "new hospital," as defined under 42 C.F.R. §412.300(b). Accordingly, the Provider was paid as a "new provider" pursuant to 42 C.F.R. §412.324(b) and was paid 85 percent of its allowable Medicare inpatient hospital capital-

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Administrative Services, PRRB Hearing Decision No. 2008-D20, March 4, 2008, reversed by the Administrator, May 5, 2008.

[3] Provider Exhibit No. 9.

[4] Id.

[5] Tr. at 130-131.

[6] See Provider's Supplemental Position Paper Exhibit No. 35

related costs for each of its fiscal years 1999, 2000, and 2001 pursuant to 42 C.F.R. §412.324.

5. Regulation 42 C.F.R. §412.304(c)(2) is not applicable to the Provider, because the Provider was not a "new hospital" for cost reporting periods beginning on or after October 1, 2002.
6. On May 6, 2002, the Intermediary issued a Notice of Interim Hospital Specific Rate (HSR) for Capital-Related Costs for Southcrest Hospital (hereinafter "Notice of Interim HSR"). A true and correct copy of the Notice of Interim HSR is set forth in the appeal record at Provider's Supplemental Exhibit 3 (Case No. 04-2270), Provider's Supplemental Exhibit 7 (Case No. 07-0278), Provider's Supplemental Exhibit 6 (Case No. 07-1351), and Provider's Supplemental Exhibit 8 (Case No. 08-0169).
7. In the Notice of Interim HSR, the Intermediary designated the fiscal year ending December 31, 2001 as the Provider's capital base period. The Intermediary determined that the Provider's interim HSR was higher than the adjusted Federal rate, and concluded based on regulatory instructions at 42 C.F.R. §412.324(b)(2) that the Hold-Harmless methodology would be applicable.
8. At the time it issued the Provider's Notice of Interim HSR, the Intermediary's conclusion that the Provider was entitled to payment under the Hold-Harmless methodology was based on the Intermediary's understanding of the regulations, Federal Register publications, manuals, and other guidance.
9. In preparing its FY 2002 cost report and claiming Hold-Harmless payment for its capital costs, the Provider relied on regulations, Federal Register publications, manuals, and specific instruction from the Intermediary.
10. Prior to 2003, the Intermediary believed, based on regulations, Federal Register publications, manuals, and other guidance, that providers (including the Provider) meeting the definition of "new" under 42 C.F.R. §412.300(b) prior to the end of the capital PPS transition period for existing hospitals described at 42 C.F.R. §412.336(a) would be eligible for Hold-Harmless reimbursement for capital-related costs according to 42 C.F.R. §§412.324(b)(2) and (3) for up to and including 8 years (even if such payments continued beyond the first cost reporting period beginning on or after October 1, 2000).
11. In accordance with the Intermediary's understanding of 42 C.F.R. §§412.324(b)(2) and (3), the Provider's capital costs were paid under the Hold-Harmless methodology for its fiscal year ending December 31, 2002 and a portion of its fiscal year ending December 31, 2003.
12. On March 26, 2004, the Intermediary informed the Provider that for time periods after June 19, 2003, the Provider's Hold-Harmless payments would cease, and the Provider would thereafter (beginning June 19, 2003) receive capital-related reimbursement based on the 100% Federal methodology. A true and correct copy of the March 26, 2004 letter is set forth at Provider's Supplemental Exhibit 1 (Case No. 04-2270), Provider's Supplemental Exhibit 8 (Case No. 07-0278), Provider's Supplemental Exhibit 7 (Case No. 07-1351), and Provider's Supplemental Exhibit 9 (Case No. 08-0169).
13. The Intermediary's change in applicable reimbursement methodology for the Provider was directed by CMS. On March 5, 2004, CMS notified the Intermediary that the capital PPS Hold-Harmless payments made to the Provider "were correct based on Mutual's

understanding of the rules at the time the claims were paid," and that no claims for the Provider processed prior to June 19, 2003 should be reprocessed. CMS's instruction did not cite any statutory, regulatory, or other guidance as a basis for CMS's decision to revoke the Provider's Hold-Harmless treatment. A true and correct copy of CMS's instruction is set forth in the record at Provider's Supplemental Exhibit 4 (Case No. 04-2270), Provider's Supplemental Exhibit 9 (Case No. 07-0278), Provider's Supplemental Exhibit 8 (Case No. 07-1351), and Provider's Supplemental Exhibit 10 (Case No. 08-0169).

14. The Provider was not given any opportunity to comment upon the CMS directive to the Intermediary set forth in the March 5, 2004 letter.
15. CMS did not amend the regulation at 42 C.F.R. §412.324. The Rule has not been changed since it was effective on October 1, [1991].[7]
16. In accordance with CMS's directive, the Intermediary did not recoup any Hold-Harmless payments made to the Provider prior to June 19, 2003. As of June 19, 2003, the Intermediary began paying the Provider based on the 100% Federal methodology.
17. The Provider timely appealed the capital hold-harmless issue by appealing both the March 26, 2004 final determination letter revoking its Hold-Harmless payments and its fiscal year 2003, 2004, and 2005 Notices of Program Reimbursement.
18. Based on its understanding of the regulations, Federal Register issuances, and other CMS guidance, the Intermediary paid Hold-Harmless reimbursement to at least four other providers that, like the Provider, met the definition of a "new hospital" under 42 C.F.R. §412.300(b) within the final few years of the capital PPS transition period for existing hospitals described at 42 C.F.R. §412.336(a) (hereinafter the "Other Hold-Harmless Providers"). The following table identifies the first patient admission date, Medicare certification date, and reimbursement methodology applied to the Other Hold-Harmless Providers for fiscal years 1999 through 2003:

	Date 1st Patient Admitted	Date of Medicare Certification	Reimb. Method. FY 1999	Reimb. Method. FY 2000	Reimb. Method. FY 2001	Reimb. Method. FY 2002	Reimb. Method. FY 2003
New Mexico Provider	10/18/99	10/26/99	NH (85%)	NH (85%)	NH (85%)	HH	HH (partial year)
**Ohio Provider		9/16/99	NH (85%)	NH (85%)	NH (85%)	HH	HH (partial year)
California Provider	9/13/99	10/6/99	N/A	NH (85%)	NH (85%)	HH	HH (partial year)
Texas Provider	12/8/98	1/7/99	NH (85%)	NH (85%)	NH (85%)	HH	HH (partial year)

7 See Transcript (tr.) at pg 12 for parties' request to correct stipulation ¶15 from October 1, 2001 to October 1, 1991.

NH="New Hospital" reimbursement at 85% of reasonable costs

HH="Hold-Harmless" reimbursement under the capital PPS

** - The Ohio Provider was not serviced by WPS until October 1, 2002. The new hospital reimbursement at 85% of reasonable costs for FY1999 through FY2001, and hold harmless payments for FY2002, were made by its previous fiscal intermediary.

19. Like the Provider, none of the Other Hold-Harmless Providers referenced in the above chart received Hold-Harmless payments prior to the end of the capital PPS transition period for existing hospitals described at 42 C.F.R. §412.336(a).
20. Similar to its treatment of the Provider, the Intermediary revoked the Other Hold-Harmless Providers' Hold-Harmless status (effective August 19, 2003) based on instructions from CMS, and the Intermediary permitted the Other Hold-Harmless Providers to keep all Hold-Harmless payments made prior to that effective revocation date.
21. The parties agree that Provider's Supplemental Exhibits 1-25 (Case No. 04-2270), Provider's Supplemental Exhibits 1-33 (Case No. 07-0278), Provider's Supplemental Exhibits 1-32 (Case No. 07-1351), Provider's Supplemental Exhibits 1-34 (Case No. 08-0169) and Exhibit 1 to the Intermediary's Supplemental Position Paper are true and correct copies, and that there is no dispute as to the authenticity of these exhibits.

FINDINGS OF FACT, CONCLUSIONS OF LAW AND DISCUSSION:

After consideration of the Medicare law and guidelines, the evidence and the parties' arguments, the Board finds and concludes as follows:

The Board finds that pursuant to the plain language of 42 C.F.R. §412.324(b), combined with indications of the Secretary's intent at the time the regulation was promulgated, the Provider is entitled to hold-harmless payment for capital-related costs for up to eight fiscal years following the two initial years for which the hospital received 85% of reasonable cost reimbursement. 42 C.F.R. §412.324(b) states:

> (b) *New Hospitals.* (1) A new hospital, as defined under §412.300(b), is paid 85 percent of its allowable Medicare inpatient hospital capital-related costs through its cost reporting period ending at least 2 years after the hospital accepts its first patient.
>
> (2) For the third year through the remainder of the transition period, the hospital is paid based on the fully prospective payment methodology or the hold-harmless payment methodology using the base period determined under §412.328(a)(2).
>
> (3) If the hospital is paid under the hold-harmless methodology described in

> §412.344, the hold-harmless payment for old capital costs described in §412.344(a)(1) is payable for up to and including 8 years and may continue beyond the first cost reporting period beginning on or after October 1, 2000.

The Board finds the parties stipulations of fact supported by the record. Based on these stipulations it is undisputed that the Provider was a "new hospital" during the ten-year transition period spanning 1991-2001. CMS intended that "[h]ospitals that are defined as 'new' for purposes of capital payments during the transition period . . . will continue to be paid according to the applicable payment methodology outlined in §412.324."[8] The Provider received payments under the "methodology outlined in §412.324" for its fiscal year 1999, 2000, and 2001 (i.e., 85% of its reasonable costs for capital pursuant to section 412.324(b)(1). Therefore, due to its new provider status during the normal transition period (1991-2001), the Provider is entitled to payment under the hold-harmless payment methodology outlined at 42 C.F.R. §412.324(b) if its hospital-specific rate exceeds the federal rate for the applicable cost reporting year. As the Provider's hospital-specific rate is undisputedly higher than the federal rate, the Provider must be paid under the hold-harmless methodology for up to and including 8 years beyond its fiscal year 2001 in accordance with section 412.324(b)(3).

The Board further finds that the Provider was actually paid under the hold-harmless methodology described in section 412.344 and that these payments were determined by CMS to be proper payments. Thus, the Board concludes that there is an additional basis for "the hold-harmless payment for old capital costs described in §412.344(a)(1)" and that such payments must continue to be paid "up to and including 8 years and may continue beyond the first cost reporting period beginning on or after October 1, 2000" as required by the plain language of section 412.324(b)(3).

This plain reading of the regulation is further supported by CMS's statements of intent at the time of the rulemaking. The following explanation, which appeared in the Federal Register in substantially similar form at least 18 times between 1991 and 2001, was published at the time of the regulation's promulgation and is particularly helpful for purposes of understanding the treatment of new hospitals beginning operations during the normal transition period:

> We agree with the concerns expressed by the commenters and provide in the final rule to exempt new hospitals from the capital prospective payment system for the first 2 years of operation and pay them 85 percent of their reasonable costs during that period. The base year costs would qualify as old capital. Effective with the third year of operation, we will pay the hospital under either the fully prospective methodology, using the appropriate transition blend in that Federal fiscal year, or the hold-harmless methodology. If the hold-harmless methodology is applicable, the hold-harmless payment for assets in use during the base period would extend for 8 years, even though the hold-harmless payments may extend beyond the normal transition period.[9]

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[8] 66 Fed. Reg. at 39,911 (Aug. 1, 2001).
[9] 56 Fed. Reg. at 43,418 (August 30, 1991) (Provider's Appendix G)

Therefore, the Board finds that the Intermediary's contention that a provider must have received hold-harmless treatment during the normal transition period (1991-2001) in order to continue receiving such treatment after the end of the normal transition period is unsupported by the plain language of the regulation as well as by indications of the Secretary's intent at the time of the regulation's promulgation. Finally, the Board finds this appeal to be substantially the same as the appeal in HealthEast Woodwinds, supra. The Board conclusion is the same as in that decision which was supported by the Federal District Court for the District of Minnesota which found:

* * * * *

> The Plaintiff argues that §412.324(b)(2) and (3)'s plain language compels the Secretary to reimburse Woodwinds' capital under the hold-harmless payments. This Court agrees.[10]
>
> * * * * *
>
> It is the Secretary's contention that the transition period ends October 1, 2001. Thus, where Woodwinds' third year began September 1, 2002, the Secretary claims the Plaintiff was ineligible for the hold-harmless payments because the transition period had ended.
>
> Paragraph (b)(3), however, is explicit. Hold-harmless payments are "payable for up to and including eight years and may continue beyond the first cost-reporting period beginning on or after October 1, 2000." Where this paragraph specifically extends the transition period for new hospitals, the Secretary's interpretation contradicts its plain language.[11]

The Board also agrees with the HealthEast Woodwinds court that having concluded "that the language of the Secretary's interpretation is inconsistent and not a reasonable interpretation of the regulatory language,"[12] the Board need not reach the question of the Provider's APA argument.

In summary, based upon its status as a new provider during the transition period, the Board finds that the Provider is entitled to payment under the hold-harmless methodology outlined at 42 C.F.R. §412.324(b). Since its hospital-specific rate for fiscal years 2003, 2004 and 2005 exceeded the federal rate, the Board finds that the Provider was entitled to be paid under the hold-harmless methodology pursuant to 42 C.F.R. §412.324(b)(2). The Board also finds that, pursuant to 42 C.F.R. §412.324(b)(3), the Provider is to be paid under the hold-harmless methodology for up to eight years even though the hold-harmless payments may extend beyond the end of the transition period.

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[10] HealthEast Woodwinds, Provider Appendix K, pg 35.
[11] Id. Provider Appendix K, pg 35-36.
[12] Id. Provider Appendix K, pg 38.

DECISION AND ORDER:

The Intermediary's refusal to reimburse the Provider for capital-related costs under the hold-harmless methodology was improper. The Provider is eligible for hold-harmless payment for its capital costs under 42 C.F.R. §412.324.

The Intermediary is instructed to modify, as necessary, the Provider's FYs 2003, 2004, and 2005 cost reports to make payment under the hold-harmless methodology for capital-related costs.

BOARD MEMBERS PARTICIPATING:

Suzanne Cochran, Esquire
Yvette C. Hayes
Keith E. Braganza, C.P.A.
John Gary Bowers, C.P.A.

FOR THE BOARD:

Suzanne Cochran, Esquire
Chairperson

DATE: September 15, 2010