

December 8, 2023

+5.6% Hospital Update for 2025 (MedPAC)

HH -7%, Rehab -5%, SNF -3%, Hospice 0%, Dialysis +2%

Relevant Companies



»» Our Take & Next Up

MedPAC pay proposals for CMS/Congress will be voted upon in January. In recent years the Commission had wielded less influence, but the Commission will vote on payment recommendations to Congress at its January '24 meeting. Post acute was the most beat-up: with the non-partisan Commission recommending -7% for Home Health, -5% for IRF (Rehab Hospitals) and -3% for SNF, that are under new orders by the Biden Administration to increase staffing (see our analysis [here](#)). Physician pay recommendations were unsurprising, as Congress seeks to lessen-the-blow to Physician pay in 1Q24 (which we think will happen, though not a full reversal of the -3.4% fee schedule cut). Dialysis would see an update, as FFS utilization comes down (seniors opting for home dialysis, others accessing care via MA plans).

»» Key Points

HOSPITALS = +5.6% UPDATE IN '25

REC #1: MedPAC recommends that Congress update pay for acute care hospitals (THC, UHS, HCA, CYH, others) by "current law" (+2.8%) + 1.5% in 2025. Hospitals would also likely get an extra +1.3% from the Medicare Safety Net Index (MSNI) that is recommended. This is compared to updates of +2.4% in 2021, +2.5% in 2022, and +2.5% in 2023.

Aggregate Medicare margin for IPPS hospitals in 2022 was -11.6% (including relief funds). For more efficient hospitals, the overall Medicare margin was -2%. "All-payer" margin for 2022 declined to +2.7%, from a high of +8.8% in 2021, due to an 8% growth in operating costs.

Medicare margin for all IPPS hospitals in 2024 is projected to be -8% (with 340B payments). As a reminder, CMS will provide \$9 B in lump sum, one-time payment to hospitals affected by the lower 340B payments in 2018-2021. The one-time 340B remedy payments are expected to positively impact Medicare margins in 2024. 2025 margins are expected to be closer to -13%.

A majority of the Commissioners support the update in light of hospital closures. Slides [here](#). Commissioners support the update largely due to a challenging cost environment. However, there was opposition from Commissioner Brian Miller who wants the Commission to think about increased payment impact

holistically and reluctant support from Scott Sarran who feels Medicare isn't getting enough value for the payment update.

REC #2: MedPAC recommends that Congress should redistribute existing DSH and uncompensated care payments through the Medicare Safety Net Index (MSNI) using the mechanism described in 2023 recommendations and add \$4 B to the MSNI pool. As a reminder, in March 2023, Commissioners made the same [recommendations](#), but only allocated \$2 B to the MSNI pool. The amount for the MSNI pool was double to include funding for Medicare Advantage with \$2 B each for FFS and MA. MSNI would essentially replace existing DSH payments and would boost payouts to Medicare safety-net hospitals.

The Commission also discussed holding hospitals accountable for population health and for poor performance on patient experience measures. Commissioner Larry Casalino noted that only around 50% of patients at discharge understood their care plan. He and others recommended the Commission explore ways of holding hospitals accountable for patient care experience and follow-up.

PHYSICIANS = MB+ 50% MEI AS -3.4% PAYCUT FIX LOOMS

REC #1: MedPAC discussed recommending that Congress update the Medicare base payment rate for physicians by current law plus 50% of the projected increase in the Medicare Economic Index (MEI) for 2025. CMS forecasts a +2.6% MEI increase in 2025.

REC #2: Chair proposed that the Commission reiterate March 2023 recommendations for additional payment to support safety net clinicians. These would be a 15% add-on for primary care clinicians and 5% add-on for non-primary care clinicians. The Commission recommends that add-on payments should not be subject to beneficiary cost sharing and not be budget neutral.

Median physician compensation from all payers grew by +9% per year from 2021 to 2022. Commercial PPO payment rates were 136% of FFS Medicare rates in 2022, up from 134% in 2021. Growth in commercial payments is likely due to increased provider consolidation that creates greater negotiating power with insurance companies. Link to slides is [here](#).

Commissioners are concerned about physician consolidation. Commissioner Larry Casalino did not support the recommendation due to his concerns of impact on access and increased physician burnout, meanwhile Commissioner Scott Sarran opposed the MEI update due to lack of increased value per beneficiary despite increase in physician reimbursement. Hospital acquisition of physician practices was also discussed and the need for smaller practices to have more resources in the current regulatory environment.

Beyond hospital acquisitions, there is an increase in private equity (PE) firms and insurance acquisition of physician practices. In practice, UNH recently announced they have approximately 10% of all physicians in the U.S. employed or affiliated. Commission members also brought up concerns about contract labor & whether it is normalized, and what percentage of those formerly contracted employees are now fully employed.

HOSPICE = 0%

Rec #1: MedPAC discussed recommending that Congress eliminate the update for 2025. Commissioners were supportive of the recommendation, particularly in light of the poor performance of a significant number of hospices and the positive margins for providers. The overall Medicare margin for hospices was +13.3% for all provider types.

Hospice quality of care continues to be a major concern. Commissioners noted that hospice performance continues to be lacking with around half of hospices in the 1,2,3, star range. Commissioners discussed solutions including recommending a MA model for star rating or redesigning the CAPS survey to more align with patient goals of care. Link to the slides are [here](#).

Increase in non-hospice spending by hospice patients warrants a policy solution. CMS expects “virtually all” care needed by a hospice patient to be covered by hospice but spending outside of hospice amounted to \$1.5 B in program payments. MedPAC introduced three possible approaches to align all hospice patient spend. These approaches include an administrative approach that requires CMS to more concretely define “related”, a bundled payment approach that would bundle unrelated services into the hospice benefit with a base rate increase, and the payment penalty that could apply to hospice providers whose patients have a high nonhospice spending.

DIALYSIS = +1.8% UPDATE IN '25

REC #1: MedPAC discussed recommending that Congress update the Medicare ESRD base rate by the rate determined under current law for 2025 (+1.8%). Commissioners were supportive of the recommendation.

MedPAC predicts a 2024 Medicare margin of 0% (up from -1.1% in 2021) for outpatient dialysis services. In 2022, higher labor and capital costs growth than historical norms contributed to a decline in margin. Medicare margin for dialysis services in 2021 was -1.1%. All-payer margin in 2021 of +14%.

The dialysis market saw a slowdown in growth due to increased use of home dialysis, among other factors. MedPAC noted a decline in dialysis capacity due to excess COVID mortality, decline in ESRD incidence rates, decline in total number of treatments by freestanding dialysis facilities and an increase in use of home dialysis. Link to slides [here](#).

Increased enrollment in MA by ESRD patients is driving a decline in fee for service dialysis treatments. Between December 2020 and December 2022, the share of beneficiaries on dialysis enrolled in MA climbed from 27% to 47%. During the same period FFS dialysis treatment declined by -14%. The significant switch to Medicare Advantage is likely being driven by the availability of supplemental benefits and the lower cost sharing liability.

HOME HEALTH = -7%

Recommendation #1: For CY 2025, MedPAC discussed recommending Congress reduce the 2024 Medicare base payment rate for home health agencies by -7%. Commissioners supported the recommendation.

MedPAC predicts a 2024 Medicare margin of +18% (down from +22.2% in 2022) for home healthcare services. Decline is attributed to an assumed cost growth of 3% which is higher than historic rate of cost growth). Margins for 2024 could be higher if cost growth is lower than current projections.

Medicare margin for home healthcare services in 2022 was +22.2%. Average payment per 30-day period increased 3% for freestanding home health agencies while cost per 30-day period increased +4% in 2022. All-payer margin for 2022 was +7.9%. Link to slides is [here](#).

Medicare marginal profit for home healthcare services was +23%. Per-capital volume of home health utilization was lower in 2021. While rate of home health use remains above pre-pandemic levels, the share of

discharges from inpatient setting to home health share has declined with increase SNF discharges rebounding.

PE firms own just 5.7% of home health agencies, but the size of firms and their market share is not known. MedPAC also noted the increasing investments by MA insurers with 3 of the largest publicly traded HHA (Amedisys, LHC, Signify Health) recently being purchased by MA insurers (UNH, CVS). Some commissioners noted that vertical integration by MA may be a positive for the sector in creating a prepaid, integrated environment that could improve home health service delivery.

INPATIENT REHAB FACILITIES (IRFs) = -5%

Recommendation #1: MedPAC recommends that Congress reduce the Medicare base payment rate for inpatient rehabilitation facilities by -5% for 2025. Non-partisan commissioners largely supported the recommendation. Link to slides is [here](#)

MedPAC predicts a 2024 Medicare margin of +14% (+13.7% in 2022) for IRF services. Growth is attributed to an assumed increase in payment that will be more than cost growth from current market basket projections.

Medicare margin for inpatient rehab services in 2022 was +13.7%. Medicare margin for freestanding facilities was +23.3%, significantly higher compared to +0.9% for hospital-based IRFs. Fee for service Medicare patients made up 51% of all IRF discharges. All-payer margin for 2022 for freestanding facilities was +9%.

Marginal profit for IRF was +39% for freestanding facilities, +18% for hospital-based. It was noted that most new IRFs were freestanding and for profit, but hospital-based providers continue to make up 71% of IRF providers in Medicare. Hospital based united were impacted by the all-payer operating margin decline for hospitals in IPPS. It was noted that patient selection differences and specialty mix may also be contributing to the margin differences between freestanding and hospital-based facilities.

Commissioners discussed the role of MedPAC recommendations light of 5 years of recommended cuts not taken up by Congress. Commissioners Greg Poulsen noted the importance of making recommendations without bringing in political implications, and Betty Rambur highlighted that the recommendations often have broad impacts that go beyond Medicare reimbursement.

SKILLED NURSING FACILITIES (SNF) = -3%

Recommendation #1: MedPAC recommends that Congress reduce the base rate for skilled nursing facilities by -3% in 2025. This is the same % that the Commission put forth earlier this year for 2024. Non-partisan commissioners generally agreed with the recommendation with some Commissioners suggesting SNFs be offered the opportunity to earn back some percentage based on improved quality metrics and staffing measures. However, MedPAC cannot make an “earn back” recommendation in the rate update without making changes to their standing SNF value incentive program (VIP) recommendation.

MedPAC predicts a 2024 Medicare margin of +16% (down from 18.4% in 2022) for SNF services. Costs are expected to increase more than payment rate updates, the sequester was reinstated in 2022, and there is an adjustment for overpayments resulting from a new case mix. See slides [here](#).

Medicare margin for SNF services in 2022 was +18.4%. This is the 23rd consecutive year where margins are above 10%. For for-profit providers, Medicare margins were +22%. “All-payer margin” for freestanding SNFs in 2022 fell to -1.4% with half of SNF having negative total margins from low Medicaid base rates. At the median, Medicaid base rates were 86% of SNF costs.

Low staffing continues to impact access and may be exacerbated by rebounding demand for SNFs. The median facility total nurse and RN staffing ratio decline slightly, and employment levels continue to remain below pre-pandemic levels in 2023. Notably, SNFs continued to see high turnover with a 53% nurse turnover rate. Commissioners discussed their concerns about the influence of staffing on limiting access and how to measure the actual capacity of SNFs in a more granular way.

Ipsita Smolinski
Managing Director | Capitol Street
ipsita@capitol-street.com

202.250.3741 | www.capitol-street.com

900 19th St NW 6th Fl
Washington, D.C. 20006

CAPITOL STREET

Copyright 2023 Capitol Street.

This communication, including this broadcast and any attachments hereto, is intended solely for the original recipient(s) and may not be redistributed without the written consent of Capitol Street. This communication is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of any financial instruments, nor is it intended as advice to purchase or sell such instruments