

December 30, 2016

Mark Wong  
Division of Medicaid and Children's Health Operations  
U.S. Department of Health & Human Services  
Centers for Medicare & Medicaid Services  
90 Seventh Street, Suite 5-300 (5W)  
San Francisco, CA 94103-6707

**RE: Arizona SPA #16-013, DRG Updates**

Dear Mr. Wong:

Enclosed is State Plan Amendment (SPA) #16-013, DRG Update, which revises the State Plan to describe changes to DRG payments for inpatient hospital services, effective October 1, 2016.


If you have any questions about the enclosed SPA, please contact Kyle Sawyer at (602) 417-4211.

Sincerely,



Beth Kohler  
Deputy Director  
Arizona Health Care Cost Containment System (AHCCCS)

cc: Jessica Woodard, CMS  
Brian Zolynas, CMS

<b>TRANSMITTAL AND NOTICE OF APPROVAL OF STATE PLAN MATERIAL</b>		1. TRANSMITTAL NUMBER: 16-013	2. STATE Arizona
<b>FOR: Centers for Medicare and Medicaid Services</b>		3. PROGRAM IDENTIFICATION: TITLE XIX OF THE SOCIAL SECURITY ACT (MEDICAID)	
TO: REGIONAL ADMINISTRATOR CENTERS FOR MEDICARE AND MEDICAID SERVICES DEPARTMENT OF HEALTH AND HUMAN SERVICES		4. PROPOSED EFFECTIVE DATE October 1, 2016	
5. TYPE OF PLAN MATERIAL ( <i>Check One</i> ): <input type="checkbox"/> NEW STATE PLAN <input type="checkbox"/> AMENDMENT TO BE CONSIDERED AS NEW PLAN <input checked="" type="checkbox"/> AMENDMENT COMPLETE BLOCKS 6 THRU 10 IF THIS IS AN AMENDMENT ( <i>Separate Transmittal for each amendment</i> )			
6. FEDERAL STATUTE/REGULATION CITATION:  42 CFR Part 447		7. FEDERAL BUDGET IMPACT:  FFY 17: \$926,800 FFY 18: \$0	
8. PAGE NUMBER OF THE PLAN SECTION OR ATTACHMENT:  Att. 4.19-A, pages 18-26		9. PAGE NUMBER OF THE SUPERSEDED PLAN SECTION OR ATTACHMENT ( <i>If Applicable</i> ):  Same	
10. SUBJECT OF AMENDMENT:  Updates the State Plan to make changes to DRG payments.			
11. GOVERNOR'S REVIEW ( <i>Check One</i> ): <input checked="" type="checkbox"/> GOVERNOR'S OFFICE REPORTED NO COMMENT <input type="checkbox"/> OTHER, AS SPECIFIED: <input type="checkbox"/> COMMENTS OF GOVERNOR'S OFFICE ENCLOSED <input type="checkbox"/> NO REPLY RECEIVED WITHIN 45 DAYS OF SUBMITTAL			
12. SIGNATURE OF STATE AGENCY OFFICIAL:  		16. RETURN TO:  Beth Kohler 801 E. Jefferson, MD#4200 Phoenix, Arizona 85034	
13. TYPED NAME: Beth Kohler			
14. TITLE: Deputy Director			
15. DATE SUBMITTED:			
<b>FOR REGIONAL OFFICE USE ONLY</b>			
17. DATE RECEIVED:		18. DATE APPROVED:	
PLAN APPROVED – ONE COPY ATTACHED			
19. EFFECTIVE DATE OF APPROVED MATERIAL:		20. SIGNATURE OF REGIONAL OFFICIAL:	
21. TYPED NAME:		22. TITLE:	
23. REMARKS:			

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**VIII. INPATIENT HOSPITAL PAYMENTS EFFECTIVE OCTOBER 1, 2014**

A. Applicability

Except as specified in this paragraph, the inpatient payment method applies to all inpatient stays in all acute care hospitals. It does not apply to the following:

1. Stays in Indian Health Services (IHS) hospitals, or hospitals operated as 638 facilities, which are paid the all-inclusive rate published annually by IHS.
2. Stays in rehabilitation hospitals and long term acute care hospitals which, for the period October 1, 2014 through September 30, 2015, are paid on a per diem basis using the per diem rates that were in effect for each hospital on September 30, 2014, and thereafter are paid in accordance with Att. 4.19-A, page 27, paragraphs X and IX respectively.
3. Stays in psychiatric hospitals, which are paid on a per diem basis in accordance with the methodology described in Att. 4.19-A, page 11, paragraph V.
4. Stays associated with organ transplant services that are paid under contract, which are paid in accordance with the contract between AHCCCS and the transplant hospital.
5. Stays where the principle diagnosis is a behavioral health diagnosis, which are covered by a Regional Behavioral Health or Tribal Regional Behavioral Health Authorities in accordance with state law and which are paid on a per diem basis in accordance with the methodology described in Att. 4.19-A, page 11, paragraph V.

Comment [GT1]: Does this date need to be updated?

B. APR-DRG Reimbursement

For dates of discharge on and after October 1, 2014, inpatient hospital services will be reimbursed using the diagnosis related group (DRG) payment methodology. Each claim for an inpatient hospital stay will be assigned a DRG code and a corresponding DRG relative weight based on the All Patient Refined Diagnosis Related Group (APR-DRG) classification system established by 3M Health Information Systems. DRG payments made using this methodology shall be the sole reimbursement to the hospital for all inpatient hospital services and related supplies provided by the hospital. A hospital will not be reimbursed separately for emergency room treatment, observation hours, or other outpatient hospital services performed on an outpatient basis, if the patient is admitted as an inpatient to the same hospital directly from the emergency room, observation or other outpatient department.

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C. DRG Relative Weights

The APR-DRG methodology classifies inpatient stays into categories based on similar clinical conditions and similar levels of hospital resources required for treatment. The categories are identified using diagnosis-related group codes, each of which is assigned a relative weight appropriate to the relative amount of hospital resources expected to be used to treat the patient. Each claim is assigned to a DRG based on the patient's diagnoses, surgical procedures performed, age, gender, birth weight, and discharge status. An APR-DRG payment is determined by multiplying the DRG base rate by the DRG relative weight and any applicable policy adjusters. The DRG relative weights are posted on the AHCCCS website as of October 1, 2014 at <http://www.azahcccs.gov/commercial/ProviderBilling/rates/APRDRG.aspx>.

Comment [GT2]: Does this date and link need to be updated?

D. DRG Base Rate for Arizona Hospitals

The DRG base rate for each hospital other than those described in paragraphs 1 and 2 below is a statewide standardized amount adjusted by applying the hospital's wage index to the hospital's labor-related share. The hospital wage index and labor-related share are those used in the Medicare inpatient prospective payment system for the fiscal year October 1, 2013 through September 30, 2014, and will not be subject to annual updates. For the following described hospitals, the DRG base rate will be calculated in the same manner except that an alternative standardized amount will be used in place of the statewide standardized amount:

1. Hospitals that are licensed by the state of Arizona Department of Health Services as short-term hospitals, indicated by a license number beginning with the letters "SH." These hospitals typically practice in a limited, specialized field.
2. Hospitals that are located in a city with a population greater than one million, which on average have at least 15% of inpatient days for patients who reside outside of Arizona and at least 50% of discharges reimbursed by Medicare as reported on the hospital's Medicare Cost Report for the hospital's cost reporting period ending between January 1, 2011 and December 31, 2011.

The statewide standardized amount, the alternative standardized amount, and the DRG base rates for all hospitals are posted on the AHCCCS website as of October 1, 2014 at <http://www.azahcccs.gov/commercial/ProviderBilling/rates/APRDRG.aspx>.

Comment [GT3]: Does this date and link need to be updated?

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E. DRG Base Rate for Out-of-State Hospitals

The DRG base rate for high volume out-of-state hospitals will be calculated in the same manner as for Arizona hospitals, using the Arizona statewide standardized amount. A high volume out-of-state hospital is a hospital that is located in a county that borders the state of Arizona and had 500 or more AHCCCS-covered inpatient days for the fiscal year beginning October 1, 2010. The DRG base rate for all other out-of-state hospitals is posted on the AHCCCS website that is referenced in paragraph D.

F. Policy Adjustors

Where AHCCCS has determined that an adjustment to the base payment is appropriate to ensure access to quality care, a policy adjustor will be applied to the base payment. Firstly, AHCCCS will apply a provider policy adjustor of 1.055 times the base rate to all claims from hospitals that are high volume Medicaid providers. A high volume Medicaid provider is a hospital that had at least 46,112 AHCCCS-covered inpatient days during the fiscal year beginning October 1, 2010 and had a Medicaid utilization rate greater than 30% as reported in the hospital's Medicare Cost Report for the hospital's cost reporting period ending between January 1, 2011 and December 31, 2011. These calculations include both Fee-For-Service and Managed Care Organization data. Secondly, and in addition to the provider policy adjustor if it applies, Effective January 1, 2016, AHCCCS will apply one of seven service policy adjustors where the claim meets certain conditions. The seven service policy adjustors, the conditions to which they apply, and the adjustment values are described below:

1. Normal newborn DRG codes: 1.55
2. Neonates DRG codes: 1.10
3. Obstetrics DRG codes: 1.55
4. Psychiatric DRG codes: 1.65
5. Rehabilitation DRG codes: 1.65
6. Claims for patients under age 19 assigned DRG codes other than those described in items 1 through 5 above and with severity of illness level 1 or 2: 1.25

Comment [GT4]: Do the dates or # or adjusters need to be updated?

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G. DRG Initial Base Payment

A claim for an inpatient hospital stay will be assigned both a DRG code derived from all diagnosis and surgical procedure codes included on the claim and a DRG code derived by excluding diagnosis and surgical procedure codes associated with health care acquired conditions or other provider-preventable conditions listed in Att. 4.19-A, page 13. The DRG code with the lower relative weight will be used to process the claim. For each hospital stay, the DRG initial base payment equals the DRG base rate multiplied by the DRG relative weight and any applicable policy adjusters.

The DRG initial base payment may be subject to additional adjustments as described in the following paragraphs to produce a DRG final base payment.

H. Outlier Add-on Payments

Cases which are extraordinarily costly in relation to other cases within the same DRG due to the severity of illness or complicating conditions may qualify for an outlier add-on payment. A claim will qualify for an outlier add-on payment if the claim cost exceeds the outlier cost threshold. The claim cost is determined by multiplying the covered charges by the hospital's outlier cost-to-charge ratio. The outlier threshold is equal to the DRG base payment plus the fixed loss amount, where the DRG base payment for this purpose is the lesser of the DRG initial base payment determined under paragraph G and the DRG transfer payment determined under paragraph I. The fixed loss amounts for critical access hospitals and for all other hospitals are posted on the AHCCCS website as of October 1, 2014 at <http://www.azahcccs.gov/commercial/ProviderBilling/rates/APRDRG.aspx>. The outlier cost-to-charge ratios for all hospitals will be determined as follows:

1. For children's hospitals in Arizona, the outlier cost-to-charge ratio will be calculated by dividing the hospital's total costs by its total charges using the most recent Medicare Cost Report available as of September 1st each year.
2. For Critical Access Hospitals in Arizona, the outlier cost-to-charge ratio will be the sum of the statewide rural default operating cost-to-charge ratio and the statewide capital cost-to-charge ratio contained in the Medicare inpatient prospective payment system data file available as of September 1st each year.

**Comment [GT5]:** The public notice references Outliers so not sure if something needs updating in this section

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3. For all other Arizona hospitals and for high volume out-of-state hospitals, the outlier cost-to-charge ratio will be the sum of the operating cost-to-charge ratio and the capital cost-to-charge ratio established for the specific hospital and contained in the Medicare inpatient prospective payment system impact file available as of September 1st each year.
4. For all other out-of-state hospitals, the outlier cost-to-charge ratio will be the sum of the Arizona statewide urban default operating cost-to-charge ratio and the Arizona statewide capital cost-to-charge ratio contained in the Medicare inpatient prospective payment system data file available as of September 1st each year.

AHCCCS will update the cost-to-charge ratios annually on October 1st each year. AHCCCS will not adopt any Medicare updates that CMS publishes subsequently for that payment year. Where a claim qualifies for an outlier add-on payment, the payment is calculated by subtracting the outlier threshold from the claim cost and multiplying the result by the DRG marginal cost percentage. The DRG marginal cost percentage is 90% for claims assigned DRG codes associated with the treatment of burns and 80% for all other claims.

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I. Transfer Payments

A transfer payment adjustment applies when a patient is transferred from a hospital that is subject to DRG reimbursement to another hospital that is subject to DRG reimbursement for inpatient care. The transferring hospital will be reimbursed the lesser of the DRG initial base payment and the DRG transfer payment. The DRG transfer payment is equal to the DRG initial base payment divided by the DRG national average length of stay for the assigned DRG code, multiplied by the actual length of stay plus one day. The receiving hospital will not be impacted by the transfer payment adjustment unless it transfers the patient to another hospital.

J. Prorated Payments

When a patient has Medicaid coverage for fewer days than the actual length of stay, the DRG payment will be prorated. The proration factor is determined as follows:

1. Where the patient is ineligible for Medicaid on the first day of the inpatient stay but is eligible for subsequent days during the inpatient stay, the proration factor is equal to the number of Medicaid-eligible days divided by the DRG national average length of stay for the assigned DRG code.
2. Where the patient is eligible for Medicaid on the first day of the inpatient stay but is ineligible for one or more days prior to or on the date of discharge, the proration factor is equal to the number of Medicaid-eligible days plus one day divided by the DRG national average length of stay for the assigned DRG code.

If the calculated proration factor is greater than one, the proration factor used for the payment calculation will be one. The DRG prorated payment is equal to the DRG base payment multiplied by the proration factor, where the DRG base payment for this purpose is the lesser of the DRG initial base payment determined under paragraph G and the DRG transfer payment determined under paragraph I. The DRG prorated outlier add-on payment is equal to the outlier add-on payment determined under paragraph H multiplied by the proration factor. Notwithstanding paragraph K, for the purpose of paragraphs J.1 and J.2 above, the day of discharge is included in determining the number of Medicaid-eligible days during an inpatient stay.



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K. Length of Stay Defined

For purposes of inpatient hospital reimbursement, the length of stay is equal to the total number of calendar days of an inpatient stay beginning with the date of admission and ending with the date of discharge or transfer, but not including the date of discharge or transfer unless the patient expires. A claim for inpatient services with an admission date and discharge date that are the same calendar date will be processed and reimbursed as an outpatient claim, unless the patient expired on the date of discharge.

L. Documentation and Coding Improvement and Transition Adjustment Factors

A DCI and transition adjustment factor will be applied to each claim for an inpatient hospital stay. The DCI and transition adjustment factor is a hospital-specific value established to limit the financial impact to individual hospitals of the transition to a DRG payment methodology, by phasing in the impact over two years, with full implementation in the third year, and to account for improvements in documentation and coding that are expected as a result of the transition. The DCI and transition adjustment factors are published as part of the AHCCCS capped fee schedule and posted on the AHCCCS website as of October 1, 2015 <sup>at</sup>

<http://www.azahcccs.gov/commercial/ProviderBilling/rates/APRDRG.aspx>.

Comment [GT6]: Does this date/link need to be updated?

M. DRG Final Payment

The DRG final base payment is the lesser of the DRG initial base payment determined under paragraph G and the DRG transfer payment determined under paragraph I, multiplied by a proration factor if applicable, and further multiplied by the DCI and transition factor. The DRG final outlier add-on payment is the outlier add-on payment determined under paragraph H, multiplied by a proration factor if applicable, and further multiplied by the DCI and transition factor. The DRG final payment amount is equal to the DRG final base payment amount plus the DRG final outlier add-on payment amount.

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N. Interim Payments

For an inpatient stay with a length of stay greater than 29 days, the hospital may submit interim claims for each 30 day period during the inpatient stay. In this case, the hospital will be reimbursed for interim claims at a per diem rate of \$500 per day. Following discharge of the patient, the hospital must void all interim claims and AHCCCS will recoup the interim payments. Final payment will be determined under the DRG payment methodology.

O. New Hospitals

The DRG base rate for a new hospital is calculated in the same manner as other Arizona hospitals if the hospital's wage index and labor-related share are available in the Medicare inpatient prospective payment system; otherwise, the DRG base rate is the statewide standardized amount adjusted by applying the wage index and labor-related share appropriate to the physical location of the hospital. Likewise, the outlier cost-to-charge ratio for a new hospital is determined in the same manner as other Arizona hospitals if the hospital's operating cost-to-charge ratio is contained in the Medicare inpatient prospective payment system impact file; otherwise, the Arizona statewide urban or rural default operating cost-to-charge ratio, whichever is appropriate to the physical location of the hospital, will be added to the Arizona statewide capital cost-to-charge ratio to derive the outlier cost-to-charge ratio.

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P. Administrative Days and Readmissions

1. Administrative days are days of a hospital stay in which a patient does not meet the criteria for an acute inpatient stay, but is not discharged because an appropriate placement outside the hospital is not available or the patient cannot be safely discharged or transferred. Administrative days are reimbursed at the rate the claim would have paid had the services not been provided in an inpatient hospital setting but had been provided at the appropriate placement. In certain circumstances, a member has unique medical or behavioral health needs, and the cost of the care for those unique needs is not factored into the rate otherwise established for the appropriate non-hospital inpatient placement. In such circumstances, AHCCCS negotiates with the hospital for a rate no less than the rate for the appropriate non-hospital inpatient placement and no more than the rate that would otherwise be paid for a hospital inpatient stay, taking into consideration the comparable fee for service rate for the unique services.
2. If a patient is readmitted, without prior authorization, to the same hospital that the patient was discharged from within 72 hours and the DRG code assigned to the claim for the prior admission has the same first three digits as the DRG code assigned to the claim for the readmission, then payment for the claim for the readmission will be disallowed if a medical review determines the readmission could have been prevented by the hospital. □

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TN No. 14-009

Supersedes

TN No. N/A

Approval Date: \_\_\_\_\_

Effective Date: October 1, 2014