

## **Memorandum (February 28, 2013)**

TO: Office of Health Policy, NHPCO  
FROM: The Moran Company  
SUBJECT: Profit Margin Analysis for the Hospice Industry, 2012-2023

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Over the past three years, several policies have been established which will reduce Medicare payments for hospice services:

- The annual hospital market-basket update applied to hospice payment rates will be reduced by 0.3% from 2013-2019;<sup>1</sup>
- A productivity factor will be applied to Medicare payments, reducing hospice payments by an estimated 1% in 2014 and is expected to reduce hospice payments by 0.6-1.5% over the next 8-10 years;<sup>2</sup>
- The Budget Neutrality Adjustment Factor (BNAF) will continue to be phased out from 2012-2015;<sup>3</sup> and,
- An additional two percent reduction of Medicare payments will be applied pursuant to the 2011 Budget Control Act (Sequestration) beginning in 2013.

The National Hospice and Palliative Care Organization (NHPCO) asked The Moran Company to estimate the effect of these changes on profit margins for Medicare-certified hospices. The estimates reflect what hospice margins would be if hospices are unable to reduce their operating costs sufficiently to offset significant revenue reductions:

- We estimate that the median Medicare profit margin for the hospice industry could decrease from 6% in 2012 to -11% by 2023.
- We estimate that 67% of hospices could have negative Medicare profit margins by 2023.

### **Summary of Analysis**

Using the 2011 Medicare hospice cost reports and claims data, we calculated Medicare profit margins per patient day for 2,328 free-standing hospices and estimated 2012-2023 profit margins for those providers (Table 1).<sup>4</sup> The analysis was conducted using data from community-based hospice programs whose claims data are considered most complete for purposes of determining the margin impacts of changes in reimbursement policy. To estimate changes in revenues, we applied all policies affecting Medicare hospice reimbursement (columns 1-4) plus a 2% sequester of Medicare payments beginning in 2013. To estimate costs, we used the market basket update adjusted by increases in productivity to the non-labor portion of hospice services (column 1 and non-labor portion of column 3).<sup>5</sup> The March 2012 CBO baseline estimated productivity factors were used from 2014 to 2022. The 2022 hospital

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<sup>1</sup> Social Security Act: Sec.1814(i)(1)(c) as amended by the Patient Protection and Affordability Care Act of 2010.

<sup>2</sup> Social Security Act: Sec 1886(b)(3)(B)(xi)(II).

<sup>3</sup> See Code of Federal Regulations for 2012Hospice Wage Index: 42 CFR Part 418 p. 47302.

<sup>4</sup> Profit Margin calculation includes Medicare revenue per patient day as well as total costs per day. Costs include reimbursable costs, as well as statutorily required services (bereavement and volunteer costs). We do not account for hospice repayments associated with the “cap” policy, or “other” costs that are not reimbursable or required reported on the cost report. Additionally, this analysis relies upon Medicare hospice cost reports which may contain errors and variations in the completeness of reporting.

<sup>5</sup> Labor portion of hospice services: 68.7%, non-Labor portion: 31.1%.

market-basket increase and estimated productivity factor were used in 2023 since 2023 data are not yet available.

We estimate that median Medicare profit margins for all hospices would decrease from 6% in 2012 to -11% by 2023.<sup>6</sup> We estimate that the percent of hospices with negative profit margins would increase from 39% in 2012 to 67% in 2023 (Figure 1).

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<sup>6</sup> We report median profit margins rather than mean profit margins because of considerable variability and incompleteness in cost report data which result in extreme high and low values.

**Table 1: Assumptions for Calculating Annual Hospice Profit Margins and Estimated Median Profit Margin, 2012-2023**

	Assumptions				Revenue Analysis			Cost Analysis <sup>6</sup>	
Column	1	2	3	4	1 + 2 + 3 + 4			1 + 3	
	Hospital Market-Basket Increase <sup>1</sup>	Hospice Market-Basket Adjustment <sup>2</sup>	Estimated Productivity Factor <sup>3</sup>	Annual Percent Reduction for BNAF Phase-Out <sup>4</sup>	Annual Change in Revenue	Additional Reduction in Revenue Due to Sequestration <sup>5</sup>	Net After Sequestration	Annual Change in Costs	Estimated Median Profit Margin
2023	3.2%		-0.9%		2.3%	-2.0%	0.3%	2.9%	-11%
2022	3.2%		-0.9%		2.3%	-2.0%	0.3%	2.9%	-10%
2021	3.3%		-1.3%		2.0%	-2.0%	0.0%	2.9%	-9%
2020	3.4%		-1.5%		1.8%	-2.0%	-0.2%	2.9%	-8%
2019	3.5%	-0.3%	-1.5%		1.6%	-2.0%	-0.4%	3.0%	-7%
2018	3.4%	-0.3%	-1.3%		1.7%	-2.0%	-0.3%	3.0%	-5%
2017	3.2%	-0.3%	-1.2%		1.7%	-2.0%	-0.3%	2.8%	-4%
2016	3.2%	-0.3%	-1.1%	-0.6%	1.1%	-2.0%	-0.9%	2.9%	-2%
2015	3.1%	-0.3%	-1.0%	-0.6%	1.2%	-2.0%	-0.8%	2.8%	-1%
2014	3.0%	-0.3%	-1.0%	-0.6%	1.1%	-2.0%	-0.9%	2.7%	1%
2013	2.5%	-0.3%		-0.6%	1.6%	-2.0%	-0.4%	2.5%	4%
2012	3.0%			-0.6%	2.4%		2.4%	3.0%	6%

<sup>1</sup> CBO March 2012 Baseline

<sup>2</sup> ACA Policy Adjustment, 1814(i)(1)(C).

<sup>3</sup> 2013: Actual CMS estimated productivity factor, 2014-2022: CBO March 2012 Baseline

<sup>4</sup> BNAF reduction, 7 year reduction applied to the labor portion of the hospice rate (68.71%).

<sup>5</sup> Medicare 2% Sequestration from 2011 Budget Control Act.

<sup>6</sup> Increase in costs adjusted by application of productivity factor to non-labor portion of costs (market basket + productivity factor \* 31.3%).

**Figure 1: Estimated Median Profit Margin and Percent of Hospices with Negative Profit Margins, 2012-2023**

