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Reductions Continue To Be  
Needed In Medicare's End Stage  
Renal Dialysis Rates



OFFICE OF INSPECTOR GENERAL

OFFICE OF AUDIT SERVICES

A-14-90-00215



# Memorandum

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Date

From

Richard P. Kusserow  
Inspector General *for Bryan Mitchell*

Subject

Management Advisory Report - Reductions Continue To Be Needed in Medicare's End Stage Renal Dialysis Rates (A-14-90-00215)

To

Gail R. Wilensky, Ph.D.  
Administrator  
Health Care Financing Administration

Since 1986 the Office of Inspector General (OIG) has been involved in periodic audits of costs for end stage renal disease (ESRD) dialysis treatments. This work clearly indicates that the average cost for performing dialysis treatments for Medicare beneficiaries has been decreasing, with no correlating decreases in the Medicare prospective rates. Our audits also indicate that most of the dialysis providers are being overpaid for ESRD services for nonroutine drugs and blood which are reimbursed by Medicare outside the composite rate. Additionally, a recent OIG report issued on the Medicare payments for the drug Epogen shows the average gross profit to facilities for administering this drug is in excess of 40 percent.

### BACKGROUND

In Fiscal Year (FY) 1989, payments under the ESRD program totaled \$2 billion for kidney dialysis treatments provided to Medicare beneficiaries. These payments were made to 1,830 providers of services, including 1,164 freestanding facilities and 666 hospital based facilities. The Health Care Financing Administration's (HCFA) data shows that in FY 1989 these dialysis payments averaged \$125.05 per treatment for freestanding facilities and \$129.11 for hospitals. These rates were constructed from FY 1980 audited costs for in-facility treatments with a median cost of \$125.98 per treatment.

Providers also receive additional payments for nonroutine drugs and blood, and an add-on amount for administering the drug Epogen. Our audits show that freestanding facilities

also received over \$40 million in 1989 for payments relating to nonroutine drugs and blood. These facilities are earning substantial profits from these related ESRD services. Many Medicare contractors have been paying for nonroutine drugs and blood to the facilities at their submitted charges resulting in substantial profits for these services. We found numerous instances where payments for certain nonroutine drugs and blood generated over a 100 percent profit to the facilities. Additional profits are being earned by providers for administering the drug Epogen. Our report dated May 9, 1990 shows the average profit margin for administering Epogen is in excess of 40 percent with facilities earning profits of over \$100 million annually.

#### DIFFERENCES IN COSTS FOR DIALYSIS TREATMENTS

Medicare pays for each dialysis treatment through a composite rate. Each treatment includes a package of dialysis services that takes into account the mix of patients that receive dialysis at a facility or at home and the relative cost of providing the services in these settings. Our analysis of the services rendered to beneficiaries shows that treatment costs for in-facility services vary among facilities. These cost variances are primarily due to differences in the areas of direct salaries (\$15 per treatment), supplies (\$15 per treatment), administrative and general costs (\$13 per treatment). The following practice policies may explain why differences occur among facilities:

- o some facilities may be utilizing a higher proportion of licensed practical nurses rather than more expensive registered nurses;
- o facilities which reuse dialyzers have a lower supply cost; and
- o general and administrative costs vary based on the cost allocation method used for calculating overhead costs. Additionally, members of affiliated chain operations are able to allocate costs over member operations resulting in lower costs per individual facility.

Conclusion

We believe that both the 1985 and the current 1988 audited data justifies a decrease in the payment rate. Facilities have become more efficient in their operations which has enabled them to reduce treatment costs since 1980. Efficient operations such as NMC have been able to reduce treatment costs from \$117 in 1980 to \$89 in 1988 or \$28. Medicare in lowering the rates would be recognizing both the current efficiencies and economies in the marketplace.

Should you or your staff wish to discuss the issues raised by this report, please let me know or contact Thomas D. Roslewicz, Deputy Inspector General for Audit Services. We would appreciate receiving your comments within 60 days from the date of this memorandum.