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Setting the Record Straight: Correcting 6 Misleading Conclusions from MedPAC's 2023 Report on Hospital Payment Adequacy

On March 15, the Medicare Payment Advisory Commission (MedPAC) released its annual report on the commission's recommendations for Fiscal Year 2024 Medicare payment updates. After years of once-in-a-lifetime events in the form of a global pandemic and record inflation, hospitals across the country are struggling to continue to fulfill their mission to care for their patients and communities.

Here are some misleading conclusions drawn by MedPAC's report:

MedPAC Conclusion #1: In 2021, hospital payment adequacy indicators remain positive or improved. For example, MedPAC found that hospitals' all-payer operating margin in 2021 reached a "record high" of 8.7% with federal relief funds (7.2% without federal relief funds). MedPAC compares these improved indicators against 2020's all-time low Medicare margins of -12.3%.

Fact: MedPAC's review of 2021 hospital margins is myopic – focusing exclusively on 2021 and ignoring trend data from 2022. Analyzing just this one point-in-time masks the true experience that hospitals continue to face.

In 2021, COVID cases were declining as the first vaccines were distributed. But this belies the continued stressors our country faced, as new, more contagious variants emerged. On top of that, spillover effects from the pandemic led to supply chain disruptions, worsening labor shortages, and rapidly increasing inflation.

More recent data provides a much different picture of hospital and health system finances:

- Kaufman Hall's operating margin index showed negative margins throughout 2022, with over half of the hospitals and health systems in their sample ending the year in the red. That trend continued into January 2023 according to recent data.
- MedPAC's preliminary analysis of 2022 finds that operating margins will be lower than 2021 due to several factors, including inflation higher than expected and leading to higher operating expenses; hospitals continue to see high labor costs; and declining patient acuity.

MedPAC also found that the average lengths of stay increased by 6.1% in 2021 citing to staffing constraints at skilled nursing facilities that limited the ability for hospitals to discharge patients.

MedPAC Conclusion #2: The median Medicare margin among "relatively efficient" hospitals broke-even in 2021, signaling adequate payment.

According to MedPAC, these hospitals are able to provide high quality care while constraining their costs.

Fact: "Relatively efficient" hospitals only account for 15% of all hospitals **and have had negative Medicare margins for nearly a decade.**

In addition, MedPAC projects that even for "relatively efficient" hospitals, Medicare margins will fall below break-even in 2023. Even a break-even margin, however, is not adequate. Rather, a margin that both covers costs and is adequate for capitalization is critical to allow hospitals to continue providing services.

In addition, there is substantial variation in hospitals' performance, a fact recognized by MedPAC. For example, citing the median indicates that half of even "relatively efficient" hospitals had negative Medicare margins.

Finally, MedPAC projects 2023 Medicare margins will fall below -10%, the 20th straight year of Medicare paying below costs. This is unacceptable, but unfortunately is already borne out by early data: according to data just release by Altarum, actual Medicare rates paid to providers actually fell in February compared to the prior year.

MedPAC Conclusion #3: Hospitals continue to have strong access to bond markets, citing that during 2021 and 2022, hospitals paid relatively low risk premiums (just 1 percentage point above the yield on treasury bonds by the end of 2022).

MedPAC also cites to 2023 rating outlooks, with credits agencies reporting a stable outlook for 80% of nonprofit hospitals, a negative outlook for 15%, and a positive outlook for 5%.

Fact: MedPAC has cherry picked data points to support their own argument.

For example, the three major credit reporting agencies (S&P, Fitch, and Moody's) all report more ratings downgrades than upgrades in 2022, a trend that has continued through the first quarter of 2023. And while individual hospitals may have stable outlook, all three agencies had negative 2023 sector-wide outlooks for hospitals and health systems.

As the financial conditions faced by hospitals and health systems deteriorated in 2022 and 2023, credit rating agencies and others raised concerns about the possibility that some may be in breach of bond covenants, which could have some effect on their ability to access credit markets.

Moreover, the cost of capital has increased. The Federal Reserve has raised interest rates nine times since December 2021, from 0% to a range of 4.75 to 5.0% in March, 2023. According to a March 2023 Moody's report, interest expenses will rise 20% for most low-rated health care companies in 2023.

MedPAC Conclusion #4: The supply of hospitals has been steady, and thus Medicare patients have good access to services.

MedPAC finds that the number of general acute care hospitals that closed was the same as the number that opened, both in 2021 and 2022. MedPAC contends that Medicare payment policies were not the main contributor to those that closed, but rather failure to secure a buyer or low patient volume.

Fact: A simple analysis of closure and opened hospitals is not an accurate indicator of beneficiary access.

Service line closures and reduced bed counts provide a more nuanced view of access to care. Beckers reported 15 closures or service endings between May 1 and September 1, 2021.

Additionally, rural hospital closures hit an all-time high of 19 closures in 2020, impacting access to care to some of the most vulnerable communities. Critically neededCOVID-19 relief dollars temporarily buoyed struggling hospitals in 2021, but rural closures are once again ticking up.

MedPAC Conclusion #5: For-profit hospitals continued to be able to break even or even generate a small profit on Medicare patients in 2021.

MedPAC found that for-profit Medicare margins for 2021 were 3.7% without federal relief funds (5.3% with relief funds).

Fact: Relying on cost reports to pinpoint a margin level for a specific calendar year is a flawed approach.

Even in a normal, pre-pandemic year, calculating the total aggregate margin for all U.S. hospitals can be misleading. Individual hospital margins vary widely and are driven by a range of factors, including facility or system size and type; local payer mix; geographic location; patient demographics; services provided, both clinical and non-medical; and relationships and affiliations with other entities in the community.

In addition to this, cost reports are filed for hospitals' own specific fiscal years, and because surges, relief payments and eventual expense increases happened at different times for different hospitals, these calculated margins don't necessarily provide a fully accurate picture of the financial reality in 2021.

MedPAC Conclusion #6: Patient experience indicators declined in 2021 relative to 2019.

H-CAHPS data show a 1percentage point decrease of overall hospital experience, and hospital mortality rate increased (from 8.1% to 8.6%).

Fact: Quality of care is difficult to assess due to the effects of the pandemic.

MedPAC did not use 2020 pandemic data to inform decisions about the quality of care. In 2021, hospitals continued to battle COVID surges and care for COVID patients.

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