

# CENTERS FOR MEDICARE AND MEDICAID SERVICES

## *Decision of the Administrator*

**In the case of:**

**Baptist Memorial Medical Center**  
**Provider**

vs.

**Blue Cross Blue Shield Association/  
Blue Cross Blue Shield of Arkansas**

**Intermediary**

**Claim for:**

**Provider Cost Reimbursement  
Determination for Cost Reporting  
Period Ending: 12/31/91 through  
12/31/1994**

**Review of:  
PRRB Dec. No. 2004-D27  
Dated: July 07, 2004**

This case is before the Administrator, Centers for Medicare & Medicaid Services (CMS), for review of the decision of the Provider Reimbursement Review Board (Board). The review is during the 60-day period in § 1878(f)(1) of the Social Security Act (Act), as amended (42 USC 1395oo(f)). Accordingly, the parties were notified of the Administrator's intention to review the Board's decision. Comments were received from the Center for Medicare Management (formerly the Center for Health Plans and Providers (CHPP)) requesting reversal of the Board's decision. Comments were also received from the Provider. All comments were timely received. Accordingly, this case is now before the Administrator for final agency review.

### **ISSUE AND BOARD'S DECISION**

The issue on remand was whether the Provider met the criteria set forth at § 4004(b) of OBRA 1990 and whether the costs at issue met the definition of clinical training costs.<sup>1</sup> The Board reinstated its original decision holding that the Provider

<sup>1</sup> The Board originally decided this case on April 3, 2001. See Baptist Memorial Medical Center v. Blue cross and Blue Shield Association/Blue Cross and Blue Shield of Arkansas, PRRB Dec. No. 2001-D13, April 3, 2001, Medicare &

operated the School of Nursing. The Board agreed with the Provider that the Medicare regulations did not specify the degree to which a provider must participate in a program operated by another provider to also be considered as an “operator” and to qualify for pass-through reimbursement. The Board determined that since the costs were allowable at Baptist Medical Center, the allocation of these costs to all of the Providers in this group did not undermine the stated purpose of the Secretary to not have otherwise academic costs be subsidized by the Medicare program.

With respect to the Administrator’s remand order, the Board held that the Provider met the requirements of OBRA 1990 § 4004(b) since the stipulations that the parties agreed to eliminated all disputes, except whether the costs claimed qualified as “clinical training costs.”<sup>2</sup> With regards to whether the costs claimed

---

Medicaid Guide (CCH) ¶ 80,650, rev’d and remanded, HCHA Administrator, June 7, 2001, Medicare & Medicaid Guide (CCH) ¶ 80,720 (Baptist). In that decision, the Board held that the Provider was “significantly engaged” in the operation of the nursing program. The Board determined that the nursing school costs allocated to the Provider were allocated from the books of another related provider, which was a Medicare provider. Accordingly since only providers were involved, and only provider costs were involved, the Board concluded that the nursing school program could not be anything but a provider-operated program. Based on this determination, St. John’s Hickey Memorial Hospital, Inc. v. Califano, 599 f.2d 803 (7<sup>th</sup> Cir. 1979), and various other PRRB decisions, the Board concluded that the Provider had appropriately included the net direct costs associated with the nursing program and, therefore, was entitled to pass-through treatment of the costs.

The Administrator reversed the Board’s original decision, holding that the Provider was not the operator of the nursing program and thus was not entitled to treat the cost as a prospective payment system (PPS) pass-through cost. The Administrator determined that only the costs of those approved medical education programs operated directly by a hospital are to be excluded from PPS and reimbursed on a reasonable cost basis. However because of § 4004(b) of Omnibus Budget Reconciliation Act of 1990 (OBRA 1990), the Administrator vacated and remanded the Board’s decision to allow for the additional development of the facts and the law on the issue of the applicability of OBRA 1990. Specifically the Administrator requested that the Board determine whether the Provider met the criteria set forth at § 4004(b) of OBRA 1990 and did the costs at issue meet the definition of clinical training costs.

<sup>2</sup> The parties stipulated that the Provider met all of the criteria of OBRA 1990 § 4004(b)(2) except subsection (b)(2)(B). With regards to subsection (b)(2)(B) the

qualified as “clinical training costs” the Board determined that the cost represented the direct and indirect cost of faculty time spent at the Provider’s site engaged in clinical training, thus qualifying for PPS pass-through reimbursement.

### COMMENTS

The Provider submitted comments requesting that the Administrator should affirm the Board’s decision. The Provider contends that all costs are reimbursable on a pass-through basis under OBRA 1990.

The Provider contended that the clinical costs were appropriately derived based on student hours allocated from audit reports approved by the Intermediary and allocation statistics and therefore meet the definition of clinical training under OBRA 1990. The Provider also contended that all costs, clinical and classroom, of the nursing education program should be allowable on a pass-through basis. The Provider argued that to disallow pass-through reimbursement when there is no possibility of redistribution of nonprovider costs would be arbitrary, capricious, and an abuse of discretion. In addition, the Provider stated that regulations and manuals that deny pass-through of classroom or clinical costs are contrary to statute because Congress made no distinction between classroom and clinical costs.

In addition, the Intermediary improperly disallowed all costs based on a proposed regulation defining “provider operated”. The Provider contended that the nursing education program is operated by the Provider, Baptist Medical Systems, Baptist Medical Center, Memorial, and the School of Nursing are assets of Baptist Medical Systems, Inc. which hold Medicare provider numbers and are the legal entity that holds the provider agreements with Medicare. But, the Provider also argued that the proposed regulation used by the Intermediary had no legal effect at the time and cannot be applied retroactively. The regulation in effect during the pertinent costs years, 42 C.F.R. § 413.85(c), contained no reference to whether the program is provider operated. However, the Provider noted that even if Baptist

---

Intermediary stipulated that if the PRRB or the Administrator or any reviewing court determined that the costs in question qualified as “clinical costs” for purposes of Medicare pass-through reimbursement, then the Provider satisfied the criteria of subsection (b)(2)(B) of OBRA 1990. The Intermediary also stipulated that if a reviewing body did not determine that the costs in question did not qualify as “clinical costs” for purposes of Medicare pass-through reimbursement, then the Provider did not satisfied the criteria of subsection (b)(2)(B) of OBRA 1990. Finally, the Intermediary did not challenge the Provider’s method of allocation and its calculation of the costs at issue in this case.

Medical Center is a nonprovider, the Provider is entitled to pass-through reimbursement because pass-through reimbursement is allowed when a provider is engaged in the operation of an educational program even when the program is principally operated by a nonprovider. The Provider contended that it was engaged in the operation of the program to qualify for pass-through reimbursement.

### **DISCUSSION AND EVALUATION**

The entire record furnished by the Board has been examined, including all correspondence, position papers, exhibits, and subsequent submissions. All comments are included in the record and have been considered.

Under §§ 1886(a)(4) and (d)(1)(A) of the Act, the costs of approved medical education activities were specifically excluded from the definition of “inpatient operating costs” and, thus, were not included in the PPS hospital-specific, regional, or national payment rates or in the target amount for hospitals not subject to PPS. Instead, payment for approved medical education activities costs were separately identified and treated as a “pass-through,” i.e., paid on a reasonable cost of educational programs and activities, but outside of the scope of the foregoing activities, were included in the cost used to establish the PPS payment rates. Rather, for cost years subject to PPS, these costs were considered to be part of normal operating costs covered by the per case payments made under the PPS for hospitals paid under that system. This approach was similar to the treatment that these costs had received since 1979 for purposes of the cost limits.

The regulation implementing inpatient hospital PPS at 42 C.F.R. § 412.113(b) provided that the costs of “approved education activities,” including training programs for nurses and paramedical (allied health) professionals, will be paid on a reasonable cost basis, as defined in 42 C.F.R. § 413.85. The regulations at 42 C.F.R. § 413.85 set forth the applicable principles for reimbursing the reasonable cost of educational activities under the Medicare program, and explicitly defined the types of approved educational activities which are within the scope of these reimbursement principles under PPS and those activities which are outside the scope of these reimbursement principles under PPS. Notably, the September 1, 1983 Federal Register publication of the final rule for the “Prospective Payments for Medicare Inpatient Hospital Services: Interim Final Rule with Comment Period” stated that;

(d) Activities not within the scope of this principle but are recognized as normal operating costs and are reimbursed in accordance with the applicable principles ---...

(6) Other activities which do not involve the actual operation or support ... of an approved education program....<sup>3</sup>

In response to comments with respect to this provision, the Secretary clarified the circumstances under which the costs of approved educational activities would be paid on a reasonable cost basis and, thus, treated as a pass-through cost. The Secretary explained in the final rule published in the January, 3, 1984 Federal Register that:

We believe that only the costs of those approved medical education programs operated directly by a hospital be excluded from the prospective payment system. If a program is operated by another institution, such as a nearby college or university, if [it] must be noted that by far the majority of the costs of that program are borne by that other institution, and not by the hospital. While it is true that the hospital may incur some costs associated with its provision of clinical training to students enrolled in a nearby institution, the hospital also gains in return ... We do not believe that this type of relationship was what Congress intended when it provided for a pass-through of the costs of approved medical education programs. Rather we believe that Congress was concerned with those programs that a hospital operated itself, and for which it incurs substantial direct costs. We are revising 42 C.F.R. § 405.420(d)(6) [now 42 C.F.R. § 413.85(d)(6)] to clarify that the costs of clinical training for students enrolled in programs, other than the hospital, are normal operating costs.<sup>4</sup> (Emphasis added).

Consequently, pursuant to the January 3, 1984 inpatient hospital final rule, the Secretary clarified the scope of activities not within the scope of this principle as including:

Clinical training of students not enrolled in an approved program operated by the provider...

Therefore, since the implementation of PPS, effective for cost reporting periods beginning on or after October 1, 1983, only the costs of programs operated directly

---

<sup>3</sup> 49 Fed. Reg. 39752, 39810.

<sup>4</sup> 49 Fed. Reg. 267, 313 (January 3, 1994).

by a hospital are paid on a reasonable cost basis and excluded from PPS.<sup>5</sup> Activities outside the scope of this principle are not disallowed, but rather, are treated as normal operating costs and paid as part of the per case payment, consistent with the treatment of these costs in establishing the PPS payment rates.

Subsequent to the implementation of inpatient hospital PPS, Congress enacted § 6205 of Omnibus Budget Reconciliation Act of 1989 (OBRA 1989)<sup>6</sup> which created a new temporary category of “hospital-based nursing schools” in addition to those recognized under §§ 412.113(b) and 413.85.<sup>7</sup> In addition, § 6205(b)(1) of OBRA 1989 imposed a moratorium on the Secretary (December 19, 1989 until October 1, 1990) from recouping, reducing or adjusting payments to hospitals because of alleged overpayments due to a determination by a provider’s intermediary that costs claimed by a provider for the operation of a school of nursing or paramedical education are not eligible for payment on a reasonable cost basis.<sup>8</sup> Finally, § 6205(b)(2) of OBRA 1989 directed the Secretary to publish regulations clarifying the rules when the costs of approved educational activities are when those costs are eligible for pass-through under PPS.

Congress again visited the nursing education cost issue in § 4004(b) of 1990.<sup>9</sup> That section contained several provisions affecting Medicare payment of reasonable costs under Medicare Part A for nursing and paramedical education costs for

---

<sup>5</sup> Consistent with 42 C.F.R. § 413.85(d), the PRM at § 2802.2, lists several types of activities which CMS does not recognize as within the scope of approved educational activities, and, thus, must be reimbursed as operating costs through the Provider’s diagnosis-related group (DRG) payments rather than as pass-through costs. PRM § 2802.2(f) excludes clinical training of students not enrolled in an approved education program operated by the provider.

<sup>6</sup> Pub. L. 101-239.

<sup>7</sup> Id. Section 6205(a)(1)(A). CMS implemented this provision in a final rule with comment period published in the Federal Register on April 20, 1990 (55 FR 15159) and made further revisions in the final rule that implemented changes to the inpatient hospital prospective payment system for FY 1991, which was published on September 4, 1990, (55 FR 35998). In the final rule promulgated pursuant to OBRA 1989, CMS concluded that “the temporary category of “hospital-based nursing schools will expire with a hospital’s first cost reporting period beginning on or after the date the final regulations required by § 6205(b)(2)(B)(ii) of Public Law 101-239 are issued.” 55 Fed. Reg. 15150. The final rule was published April 20, 1990, with revisions published September 4, 1990.

<sup>8</sup> See also Transmittal No. A-90-9 (June 1990).

<sup>9</sup> Pub. Law No. 101-508 (November 5, 1990).

approved nursing and paramedical education programs. Section 4004(b) governs reimbursement for clinical training conducted on the premises of a hospital under approved nursing and paramedical educational programs that are not operated by the hospital. Paragraph (1) of § 4004(b) provides that effective for cost reporting periods beginning on or after October 1, 1990, if certain conditions are met, the costs incurred by a hospital (or by an educational institution related to the hospital by common ownership or control) for clinical training (as defined by the Secretary) conducted on the premises of the hospital under an approved nursing or allied health education program that is not operated by the hospital, are treated as pass-through costs and paid on the basis of reasonable costs.<sup>10</sup>

Paragraph (2) of § 4004(b), sets forth the following conditions that a hospital must meet in order to be reimbursed on a pass-through basis for the clinical training (as defined by the Secretary) conducted on its premises.

- The hospital claimed and was reimbursed for such costs during the most recent cost reporting period that ended on or before October 1, 1989;
- The proportion of the hospital's total allowable costs that is attributable to the clinical training costs of the approved program, and allowable under (b)(1) during the cost reporting period does not exceed the proportion of total allowable costs that were attributable to the clinical training costs during the cost reporting period described in subparagraph (A);
- The hospital receives a benefit for the support it furnishes to such program through the provision of clinical services by nursing or allied health students participating in such program; and

---

<sup>10</sup> In recognizing the cost of certain hospital-based nursing schools, the Conference Committee also recognized the Secretary's treatment of these costs under inpatient hospital PPS. The conference Committee stated:

The direct costs of approved medical education programs operated by hospitals are excluded from the PPS and paid on a reasonable cost basis. [CMS] has ruled that the costs of educational programs operated at a hospital but controlled by another institution, such as a college or university are not payable on a reasonable cost basis but are included in PPS payment rates. H.R Rep. No. 964, 101<sup>st</sup> Cong., 2<sup>nd</sup> Sess. 861.

- The costs incurred by the hospital for such program do not exceed the costs that would be incurred by the hospital if it operated the program itself.

Finally, for Medicare cost reporting periods beginning on or after October 1, 1983, and before October 1, 1990, paragraph (3) of § 4004(b), imposed a moratorium on the Secretary from recouping, reducing or adjusting payments to hospitals because of alleged overpayments due to a determination that costs which were reported by the hospital on its Medicare cost reports related to approved nursing and allied health programs.<sup>11</sup>

Subsequent to the cost years at issue in this case, the Secretary issued a final rule setting forth in regulation Medicare policy for the payment of costs of approved nursing and allied health education programs.<sup>12</sup> The rule clarified and restated payment policies previously stated and established, *inter alia*, in the PRM and other documents, but never specifically addressed in the regulations. The final rule also carried out the directive made in OBRA 1989 and addressed changes required by OBRA 1990.<sup>13</sup>

As stated above, the Board reinstated its original decision holding that the Provider operated the School of Nursing. The Board further held with regard to the Administrator's remand order that the Provider satisfied the requirements of OBRA 1990 § 4004(b) and that the costs in question represented clinical costs.

Applying the above provisions to the facts of this case, the Administrator reinstates and hereby incorporates by reference, that part of Administrator Decision No. 2001-D13, (June 7, 2001), which held that the costs included by the Provider as pass-through costs were not allowable because the Provider was not the operator of the nursing program. The Administrator finds that only the costs of those approved medical education programs operated directly by a hospital are to be excluded from PPS and reimbursed on a reasonable cost basis. However, the Administrator finds that, because of OBRA 1990 § 4004(b), certain costs may be reimbursed as pass-through costs if certain conditions are met. The Administrator agrees with the Board's determination that the Provider met the criteria of OBRA 1990 § 4004(b) and that the clinical costs claimed by the Provider are allowable as reasonable costs.

---

<sup>11</sup> See also Program Memorandum Transmittal No. A-91-3. The cost reporting periods at issue in this case all began after October 1, 1990.

<sup>12</sup> 66 Fed. Reg. 3358 (January 12, 2001).

<sup>13</sup> See also 66 Fed. Reg. 14342 (March 12, 2001) delaying effective date of final rule for 60 days, from March 13, 2001 to a new effective date of May 14, 2001.

