Alabama's Hospitals Paid Significantly Less for Caring for Medicare Patients:
The Impact of the Wage Index

Hospitals care for Alabama's 880,000 Medicare eligibles, yet they are typically paid less than hospitals in other states providing the same care. The difference is caused by a formula used to calculate Medicare payments called the wage index. This fact sheet explains the inequities.

What is the Wage Index?

- The wage index is a complicated formula used nationwide to determine how much a hospital is paid for providing care to Medicare patients.
    - The original intent was to provide Medicare payments to hospitals based on market-to-market differences in hospital labor costs nationwide.

- Hospitals update their wage information each year to reflect the average salaries of their staff. If wages go up, the wage index goes up.
    - The wage index formula is budget neutral, meaning when the wages of hospitals go up in one part of the country, payments to these hospitals increase and payments to hospitals in other areas decrease.

Why is it inequitable?

- While the goal of the wage index was to reflect variations in the country's labor markets, the formula has been manipulated.
    - The greatest reason for the failure of this system is the multitude of exceptions and political fixes, meaning the wage index is not a true comparison of labor markets.

- Since the wage index factors are budget neutral, a self-perpetuating cycle develops for states like Alabama.
    - As a state like California receives higher payments, it has more resources to increase wages, driving its wage index higher and small rural states' wage index lower.
    - Low wage index states typically have lower margins, decreasing their ability to add staff or increase wages in order to increase their wage index.

- The range of wage indexes is too great and the way wages are reported can be skewed
    - The formula is unnecessarily complex and there are inconsistencies in data collection.
    - This results in some hospitals in other states being paid almost twice as much for providing the exact same care as Alabama's hospitals.

<u>What is the impact in Alabama?</u>

- Alabama has always been at the bottom in terms of payments and, currently, rural Alabama hospitals have the lowest reimbursement rate in the country.
  - The efficiency of Alabama's hospitals means they have lower staffing needs. This keeps cost low for consumers, but penalizes hospitals with lower Medicare reimbursements.

- Forty percent of all hospital care in Alabama is covered by Medicare, so for every dollar lost to another state in reduced Medicare payments, the cost is spread to patients who have private pay insurance.

- Hospitals have already cut their costs to the bone in order to survive financially.
  - Hospitals that are heavily Medicare dependent are struggling to survive as payments from the federal government are reduced more and more each year.
  - Without a more equitable wage index, some hospitals will be forced to close their doors, cut jobs or reduce services.

<u>The Bottom Line</u>

- The wage index does not encourage efficiency.
  - Higher wages = higher payments, regardless of services provided or outcomes.
  - Lower wages = lower payments, regardless of services provided or outcomes.

- The wage index formula needs to be recalculated to remove the inherent inequalities and to provide reasonable payment to all hospitals for the services they provide.

Alabama's hospitals are some of the most efficient providers in the nation. Please urge Congress to level the wage index playing field and not penalize hospitals for keeping costs low for patients.