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*CMCS Informational Bulletin*

**DATE:** August 18, 2020

**FROM:** Calder Lynch, Deputy Administrator and Director  
Center for Medicaid and CHIP Services (CMCS)

**SUBJECT: Treatment of Third Party Payers (TPP) in Calculating Uncompensated Care Costs (UCC)**

This Center for Medicaid and CHIP Services Informational Bulletin (CIB) provides guidance to states on treatment of third party payers (TPP) in determining the hospital-specific Medicaid disproportionate share hospital (DSH) payment limits for the state plan rate year (SPRY) 2017 DSH audits. The CIB recommends using one of two approaches to properly report uncompensated care costs (UCC) if states decide not to include TPP payments as an offset for purposes of calculation of the hospital-specific DSH limit prior to the June 2, 2017, effective date of the “Medicaid Program; Disproportionate Share Hospital Payments—Treatment of Third Party Payers in Calculating Uncompensated Care Costs” final rule, 82 Fed. Reg. 16114 (April 3, 2017) (DSH TPP final rule). This guidance will be most relevant for state Medicaid personnel responsible for the DSH program and submission of the annual independent certified audit.

In the April 3, 2017 issue of the *Federal Register*, the Centers for Medicare & Medicaid Service (CMS) published the DSH TPP [final rule](#)<sup>1</sup>. This rule (codified at 42 C.F.R. § 447.299(c)(10)) clarifies federal requirements regarding the treatment of TPP payments in determining the hospital-specific Medicaid DSH payment limit, which is set by statute in section 1923(g) of the Social Security Act as a hospital’s “uncompensated costs” incurred in providing inpatient and outpatient hospital services to Medicaid beneficiaries and uninsured patients.

The DSH TPP final rule clarifies that for purposes of Medicaid DSH, the total cost of uncompensated care is the costs of inpatient and outpatient hospital services remaining after accounting for all third party revenues, including but not limited to, payments by Medicare and private insurance, associated with Medicaid eligible or uninsured individuals. The final rule took effect on June 2, 2017.

Some states and hospitals have challenged our requirements in the final rule regarding the treatment of TPP payments in determining UCC for purposes of Medicaid DSH. Following the district court decision in *Children’s Hosp. Ass’n of Texas v. Azar* (“CHAT”), which vacated the DSH TPP final rule, we advised states that we would not be enforcing that rule as long as that district court decision remained operative. Additionally, CMS withdrew FAQs 33 & 34 from the Medicaid DSH guidance that was issued in January 2010 titled “[Additional Information on the DSH Reporting and Audit Requirements](#)”<sup>2</sup>, which provided instructions to states for offsetting

TPP payments for services provided prior to June 2, 2017. On August 13, 2019, the United States Court of Appeals for the D.C. Circuit issued an opinion reversing the district court in *CHAT, reinstating the final rule, and remanding the case for further proceedings. Children’s Hosp. Ass’n of Texas v. Azar*, No. 18-5135 (D.C. Cir. 2019). Additionally, we have received favorable rulings from two other appellate courts—namely, the Fifth and Eighth Circuits. See *Baptist Mem’l Hosp.-Golden-Triangle, Inc. v. Azar*, 18-60592 (5th Cir. 2020); *Missouri Hosp. Ass’n v. Azar*, No. 18-1778 (8th Cir. 2019).

Based on these court rulings, CMS will be enforcing the DSH TPP final rule as it applies to all hospital services furnished on or after June 2, 2017. To assist in complying with the applicable requirements, this bulletin provides states with guidance on how to properly report UCC for 2017 if states decide not to include TPP payments as an offset for purposes of calculating the hospital-specific DSH limit for periods before the June 2, 2017 effective date of the DSH TPP final rule.

CMS suggests one of two general approaches to comply with the requirements of the DSH TPP final rule for a portion of the 2017 SPRY, which is a similar recommendation to [FAQ #21](#)<sup>3</sup> on cost report proration in our [Additional Information of the DSH Reporting and Audit Requirements – Part 2](#).

**Method #1:**

The state can determine each hospital’s Medicaid and uninsured costs and TPP payments for services within the SPRY prior to June 2, 2017 and then separately determine the hospital’s Medicaid and uninsured costs and TPP payments for services within the SPRY on and after June 2, 2017. For the UCC computation for the partial SPRY prior to June 2, 2017, if the state does not offset TPP payments in view of the withdrawal of FAQs 33 & 34, it nonetheless must include the TPP payments as an offset for the UCC computation for the partial SPRY on or after June 2, 2017, consistent with the DSH TPP final rule. The sum of the two partial periods’ UCC will equal the hospital’s UCC for the SPRY.

**Method #2:**

The state can determine each hospital’s Medicaid and uninsured costs as it otherwise would for the entire SPRY. The state will also determine each hospital’s TPP payments for the entire SPRY. If the state chooses to not use TPP payments as a cost offset in view of CMS’s withdrawal of FAQs 33 & 34, then the state would pro-rate the TPP payments for the entire SPRY to reflect the partial SPRY period on or after June 2, 2017, based on the percentage of the SPRY occurring on or after June 2, 2017. A reasonable percentage can be computed based on the number of days within the SPRY that occur on or after June 2, 2017, divided by the total number of days within the entire SPRY; the resulting fraction would be multiplied by TPP payments for the entire SPRY to obtain the pro-rated TPP payment amount attributable to the partial SPRY period on or after June 2, 2017. The hospital’s Medicaid and uninsured costs for the entire SPRY would then only be offset by the portion of the TPP payments attributed to the period on or after June 2, 2017.

Regardless of the method used, the state must submit the reporting required under by 42 CFR 447.299(c), including total SPRY amounts for each data element in the order in which they are specified in regulation. The state should not modify the official data element report to include

support for its total SPRY calculations or include additional columns. However, states may provide additional modified versions of the data element report to provide support for its calculations in determining total SPRY UCC amounts. Any methodology necessary to implement the TPP payments offset effective June 2, 2017 for a partial SPRY must be described either in the audit report itself or as part of supporting documentation submitted in addition to the audit report and the official data element report.

If you have any questions or need additional information, please contact Richard Cuno at 410-786-1111 or [Richard.Cuno@cms.hhs.gov](mailto:Richard.Cuno@cms.hhs.gov) .

1. <https://www.govinfo.gov/content/pkg/FR-2017-04-03/pdf/2017-06538.pdf>
2. <https://www.medicaid.gov/medicaid/downloads/part-1-additional-info-on-dsh-reporting-and-auditing.pdf>
3. <https://www.medicaid.gov/medicaid/downloads/part-2-additional-info-on-dsh-reporting-and-auditing.pdf>