

PUBLICATION

Court Allows 'Retroactive' Application of 2005 Wage Index Rule Limiting Reimbursement for Pension Plan Costs [Ober|Kaler]

2016

On February 22, 2016, in *Regents of the University of California v. Burwell*, the U.S. District Court for the District of Columbia granted summary judgment in favor of the Secretary of Health and Human Services (the Secretary) and denied a challenge lodged by over 100 hospitals whose wage indices were adjusted downward based on their claimed costs associated with pension and other benefit plans. The hospitals unsuccessfully challenged the retroactive effect of a 2005 rule that allowed fiscal intermediaries to use previously-filed cost report data to limit reimbursement in fiscal years 2007 and 2008.

Court's Analysis

As an initial matter, the Secretary asserted that the hospitals' failure to object to the new rule during the notice-and-comment rulemaking period was a bar to the hospitals' pursuit of the present case. The court rejected that argument, stating that "'as a general matter,' failure to present an issue during the notice-and-comment process is not a jurisdictional bar to judicial review."

The hospitals then argued that application of the 2005 rule violated the Administrative Procedure Act and the Medicare statute in the following respects:

- Because the relevant cost data was generated before 2005, the rule constitutes a retroactive rulemaking;
- The rule is inconsistent with the purposes of the wage index provision of the Medicare statute;
- The rule is not applied in a consistent manner; and
- There is no reason the rule should apply to fully-funded pension plans.

Addressing the retroactivity issue first, the court determined that the rule did not constitute an impermissible retroactive rulemaking. Namely, the court found that there were no vested rights impaired or taken away by the rule, as hospitals do not have a vested right to receive payment for costs incurred in 2004 and 2005 under GAAP standards. The new method of calculating the wage index simply uses historical data, including historical pension costs, to calculate the prospective payment rate, but it does not alter the compensation that hospitals received for services they already provided. All the 2005 rule accomplished was requiring that pension costs that were actually and timely liquidated, and not merely accrued for accounting purposes, now will be used going forward to calculate the wage index.

Further, the 2004 and 2005 cost reports were not suddenly incorrect and did not require resubmission after the enactment of the 2005 changes, because fiscal intermediaries simply used previously submitted information to adjust wage indices for 2007 and 2008. As a more general comment, the court reiterated that the wage index is not used to reimburse hospitals for labor costs incurred in earlier years, but rather it is used to determine a fair rate for prospective compensation. In that regard, the court held the 2005 rule is not retroactive even if it requires the fiscal intermediaries to rely on 2004 and 2005 data. Further, if anything, the court noted the hospitals were asserting that the rule has *secondary* retroactivity despite its future effect on past transactions,

but the hospitals failed to carry their burden of showing how this rose to the level of being arbitrary and capricious.

Because the Medicare statute requires the Secretary to update the wage index at least annually, with broad discretion, and because an agency is free to change its mind with good reasoning, the court found that the 2005 rule was not an impermissibly retroactive rule.

The hospitals also argued that the 2005 rule is inconsistent with the objectives of the wage index provisions of the Medicare statute and thus remains arbitrary and capricious. Using the traditional *Chevron* two-step analysis, the court reasoned that where the Secretary is given broad discretion to implement the accounting methodology for the wage index, and has done so reasonably and with an eye to correcting the unanticipated consequences of the 1994 rule (inconsistent pension plan reporting under GAAP standards), the Secretary is within her proper judgment and discretion. The hospitals failed to carry the burden of establishing that the rule was arbitrary and capricious as inconsistent with the Medicare statute.

Similarly, the hospitals argued that the 2005 rule was not being applied consistently by fiscal intermediaries nationwide. The court found that the hospitals' only evidence, however, was the expert testimony of an accountant and health-care consultant, whose testimony was based on "speculation" and "conversations with these hospitals" about their experiences with the fiscal intermediaries. Such "speculation," as the court deemed it, failed to carry the burden of establishing that the agency action was arbitrary and capricious due to its disparate treatment of hospitals.

Finally, some of the hospitals involved had fully-funded pension plans, and they argued that there is no basis to exclude the actuarially-determined pension costs for wage reporting purposes. The court, however, citing established D.C. Circuit precedent, noted that the Secretary was "not required to choose the best solution, only a reasonable one," and she had done so here.

Ober|Kaler's Comments

Providers that filed 2004 and 2005 cost reports, using GAAP standards or otherwise accounting for costs that were not actually and timely liquidated, had no way of knowing that a 2005 rule would use their prior cost reports against them in 2007 and 2008, to adjust the wage indices downward. A number of providers adversely affected by the 2005 rule are currently appealing the adjustments. There is every reason to believe the providers in this case will appeal this lower court's decision to the Court of Appeals for the D.C. Circuit. Other providers who have protected this issue in appeals to the PRRB should continue to maintain their appeals until the issue is fully resolved, likely at the next level of appeal.