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# CMS Manual System

## Pub. 100-02 Medicare Benefit Policy

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Department of Health &  
Human Services (DHHS)  
Centers for Medicare &  
Medicaid Services (CMS)

Transmittal 42

Date: DECEMBER 16, 2005

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CHANGE REQUEST 4259

**SUBJECT: January 2006 Update of the Hospital Outpatient Prospective Payment System (OPPS) Manual Instruction: Changes to Coding and Payment for Observation**

**I. SUMMARY OF CHANGES:** This transmittal deletes outdated §70.4 found in the Medicare Benefit Policy Manual, Pub 100-02, Chapter 6, and replaces it with a new §20.5. This manual update reflects changes included in the January 2006 OPPS OCE and the January 2006 OPPS PRICER.

**NEW/REVISED MATERIAL - EFFECTIVE DATE\*:** January 01, 2006

**IMPLEMENTATION DATE:** January 03, 2006

*Disclaimer for manual changes only: The revision date and transmittal number apply to the red italicized material only. Any other material was previously published and remains unchanged. However, if this revision contains a table of contents, you will receive the new/revised information only, and not the entire table of contents.*

**II. CHANGES IN MANUAL INSTRUCTIONS: (N/A if manual not updated.)**  
**(R = REVISED, N = NEW, D = DELETED) – (Only One Per Row.)**

R/N/D	CHAPTER/SECTION/SUBSECTION/TITLE
R	6/Table of Contents
N	6/20.5/Outpatient Observation Services
D	6/70.4/Outpatient Observation Services

**III. FUNDING:** No additional funding will be provided by CMS; contractor activities are to be carried out within their FY 2006 operating budgets.

**IV. ATTACHMENTS:**

	Business Requirements
X	Manual Instruction
	Confidential Requirements
	One-Time Notification
	Recurring Update Notification

\*Unless otherwise specified, the effective date is the date of service.

# **Medicare Benefit Policy Manual**

## **Chapter 6 - Hospital Services Covered Under Part B**

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### **Table of Contents**

*(Rev.42, 12-16-05)*

*20.5 – Outpatient Observation Services*

## ***20.5 - Outpatient Observation Services***

***(Rev.42, Issued: 12-16-05, Effective: 01-01-06, Implementation: 01-03-06)***

### ***A. Outpatient Observation Services Defined***

*Observation care is a well-defined set of specific, clinically appropriate services, which include ongoing short term treatment, assessment, and reassessment before a decision can be made regarding whether patients will require further treatment as hospital inpatients or if they are able to be discharged from the hospital. Observation status is commonly assigned to patients who present to the emergency department and who then require a significant period of treatment or monitoring before a decision is made concerning their admission or discharge.*

*Observation services are covered only when provided by the order of a physician or another individual authorized by State licensure law and hospital staff bylaws to admit patients to the hospital or to order outpatient tests. In the majority of cases, the decision whether to discharge a patient from the hospital following resolution of the reason for the observation care or to admit the patient as an inpatient can be made in less than 48 hours, usually in less than 24 hours. In only rare and exceptional cases do reasonable and necessary outpatient observation services span more than 48 hours.*

*Hospitals may bill for patients who are “direct admissions” to observation. A “direct admission” occurs when a physician in the community refers a patient to the hospital for observation, bypassing the clinic or emergency department (ED). Effective for services furnished on or after January 1, 2003, hospitals may bill for patients directly admitted for observation services.*

*See Pub. 100-04, Medicare Claims Processing Manual, Chapter 4, §290, at <http://www.cms.hhs.gov/manuals/downloads/clm104c04.pdf> for billing and payment instructions for outpatient observation services.*

### ***B. Coverage of Outpatient Observation Services***

*When a physician orders that a patient be placed under observation, the patient’s status is that of an outpatient. The purpose of observation is to determine the need for further treatment or for inpatient admission. Thus, a patient in observation may improve and be released, or be admitted as an inpatient (see Pub. 100-02, Medicare Benefit Policy Manual, Chapter 1, §10 “Covered Inpatient Hospital Services Covered Under Part A” at <http://www.cms.hhs.gov/manuals/Downloads/bp102c01.pdf>).*

### ***C. Notification of Beneficiary***

*All hospital observation services, regardless of the duration of the observation care, that are medically reasonable and necessary are covered by Medicare, and hospitals receive OPSS payments for such observation services. A separate APC payment is made for outpatient observation services involving three specific conditions: chest pain, asthma, and congestive heart failure (see the Medicare Claims Processing Manual, §290.4.2) for additional criteria which must be met. Payments for all other reasonable and necessary observation services are packaged into the payments for other separately payable services provided to the patient on the same day. An ABN should not be issued in the context of reasonable and necessary observation services, whether packaged or paid separately.*

*If a hospital intends to place or retain a beneficiary in observation for a noncovered service, it must give the beneficiary proper written advance notice of noncoverage under limitation on liability procedures (see Pub. 100-04, Medicare Claims Processing Manual; Chapter 30, “Financial Liability Protections,” §20, at <http://www.cms.hhs.gov/manuals/downloads/clm104c30.pdf> for information regarding Limitation On Liability (LOL) Under §1879 Where Medicare Claims Are Disallowed). “Noncovered,” in this context, refers to such services as those listed in paragraph D, below.*

***D. Services That Are Not Covered as Outpatient Observation***

*The following types of services are not covered as outpatient observation services:*

- Services that are not reasonable or necessary for the diagnosis or treatment of the patient.*
- Services that are provided for the convenience of the patient, the patient’s family, or a physician, (e.g., following an uncomplicated treatment or a procedure, physician busy when patient is physically ready for discharge, patient awaiting placement in a long term care facility).*
- Services that are covered under Part A, such as a medically appropriate inpatient admission, or services that are part of another Part B service, such as postoperative monitoring during a standard recovery period, (e.g., 4-6 hours), which should be billed as recovery room services. Similarly, in the case of patients who undergo diagnostic testing in a hospital outpatient department, routine preparation services furnished prior to the testing and recovery afterwards are included in the payment for those diagnostic services. Observation should not be billed concurrently with therapeutic services such as chemotherapy.*
- Standing orders for observation following outpatient surgery.*

*Claims for the preceding services are to be denied as not reasonable and necessary, under [§1862\(a\)\(1\)\(A\)](#) of the Act.*