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# Medicare

## Provider Reimbursement Manual - Part 1

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

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**HEADER SECTION NUMBERS**

906 -906.1

**PAGES TO INSERT**

9-7 - 9-8 (2 pp.)

**PAGES TO DELETE**

9-7 - 9-8 (2pp.)

**NEW/REVISED MATERIAL--*EFFECTIVE DATE:*** *The Factors Are Applied On A Calendar Year Basis.*

Section 905.6, Inflation Factor, provides for calendar year (CY) inflation factors to update previous years' reasonable compensation ranges of compensation. The factor is from the cost category Professional fees in the CMS Prospective Payment System Hospital Input Price Index. The data in the Input Price Index is taken from actual data for the most recent year from the Employment Cost Index for Professional and Technical Workers published by the Bureau of Labor Statistics. In this transmittal, the factor for CY 2005 has been added and the factor for CY 1995 has been deleted.

**DISCLAIMER:** The revision date and transmittal number only apply to the redlined material. All other material was previously published in the manual and is only being reprinted.

There may be situations in which an individual has an ownership interest in providers serviced by different intermediaries. It is appropriate for intermediaries to inquire of the owner whether such situation does exist and, if so, to coordinate its determination with the other intermediary.

905.4 New Providers and Future Surveys.--Where a proprietary provider first enters the program, the owner's compensation is evaluated by its intermediary in terms of the ranges of compensation established for comparable institutions. After a period of time, it may be necessary for intermediaries to resurvey their providers because of changes in compensation levels and changes in the duties and responsibilities of the owners.

905.5 Few Similar Providers in an Area.--Where there are a few comparable institutions in an area, it may be difficult for an intermediary to evaluate the reasonableness of an owner's compensation. In such situations, the intermediary may need to obtain information about the ranges of compensation established for comparable institutions in nearby or similar areas. Another method is to use the ranges established for another class of institution and adjust the ranges accordingly. For example, the intermediary may, on the basis of its analysis and judgment, establish as reasonable compensation in a given skilled nursing facility (SNF) an appropriate proportion of the compensation paid to administrators of comparably sized hospitals in the same area. However, where this approach is taken, the fact that hospitals are generally more complex institutions than SNFs is reflected in the determination.

905.6 - Inflation Factor.

(Rev. 430 )

*Intermediaries apply an inflation factor to update ranges of reasonable compensation determined for previous years. The Centers for Medicare & Medicaid Services furnishes an annual calendar year (CY) inflation factor for this purpose. Following are the CY factors for recent years:*

1996 – 3.1%; 1997 – 2.6%; 1998 – 3.3%; 1999 – 2.8%; 2000 – 4.5%; 2001 – 4.7%; 2002 – 3.0%; 2003 – 3.4%; 2004 – 4.3%; 2005 -- 3.7%

906. TYPES OF COMPENSATION - CORPORATIONS

As indicated in §902.2, compensation for the necessary services of a stockholder-employee or an individual described in §901 (other than sole proprietors and partners) includes:

- o Salary amounts paid for managerial, administrative, professional, and other services;
  - o Amounts paid by the institution for the personal benefit of the owner (see §906.1);
  - o The costs of assets and services which the owner receives from the institution (see §906.1);
- and
- o Deferred compensation. (See §2140.)

Any payments to an owner in excess of a reasonable level do not constitute compensation or any other allowable cost.

906.1 Other Types of Compensation.--There may be instances in which an owner is receiving compensation in a form that without close scrutiny might not be recognized as compensation (e.g., fringe benefits). Compensation to an owner may include (1) supplies and services used for the personal use of the owner, (2) special merchandise ordered from wholesalers for the owner's personal use, (3) wages of a domestic or other employee who works in the home of the owner, (4) personal use of a car owned by the business, (5) personal insurance premiums paid for the owner, and (6) other fringe benefits as described in §2144.

Any of the above payments must be included in the owner's total compensation to determine its reasonableness when such payments meet the requirements for being categorized as fringe benefits under the definition given in §2144.1. If the requirements of that section are not met, these types of payments cannot be considered compensation.

906.2 Subchapter S Corporation.--Under Federal income tax law, certain corporations can elect to be treated for tax purposes as a partnership. This election, however, has no effect on reimbursement under the Medicare program, and an owner of a Subchapter S corporation is not considered a partner for purposes of this principle.

906.3 Director's Fees and Consultant's Fees.--All payments by a provider to an owner which are claimed as an allowable cost are included in the owner's total compensation for purposes of determining the reasonableness of the cost claimed. This includes fees received by an owner, regardless of the label placed on them, such as consultant's or director's fees. The determination as to the reasonableness of such compensation is made by comparing it with amounts paid by comparable institutions for comparable services performed by their employees, rather than by considering the amounts that outside consultants receive.

906.4 Unpaid Compensation.--See §2146.2B.

A. General.--The compensation of stockholder-employees and individuals described in §901 (other than sole proprietors and partners) is included for a cost reporting period if earned within the period, even if not paid until after the close of the period. However, payment must be made (whether by check or other negotiable instrument, cash or legal transfer of assets such as stocks, bonds, real property, etc.) within 75 days after the close of the period. Where payment is made by check or other negotiable instrument (e.g., a promissory note), these forms of payment must be liquidated through an actual transfer of the provider's assets within 75 days after the close of the period in order to meet the requirements of this section. If payment, including the liquidation of negotiable instruments, is not made within the cost reporting period, or within 75 days thereafter, the unpaid compensation is not includable in allowable costs either in the period when earned or in the period when actually paid.