

# **PROVIDER REIMBURSEMENT REVIEW BOARD**

## **HEARING DECISION**

99-D17

### **PROVIDER -**

Deaconess Medical Center  
St. Louis, Missouri

Provider No. 26-0021

**vs.**

### **DATE OF HEARING-**

April 24, 1998

Cost Reporting Periods Ended -  
September 30, 1989 & September 30,  
1990 & September 30, 1991

### **INTERMEDIARY -**

Mutual of Omaha

### **CASE NOS.**

91-2308  
94-2352 (On The Record)  
94-1066 (On The Record)

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**ISSUE:**

Was the Intermediary's reclassification of the Provider's nursing school library costs from the nursing school cost center to the administrative and general cost center proper?

**STATEMENT OF THE CASE AND PROCEDURAL HISTORY:**

Deaconess Medical Center ("Provider") is a 527-bed hospital located in St. Louis, Missouri. The Provider is a nonprofit, general acute care hospital subject to Medicare's prospective payment system ("PPS"). The Provider also operated an approved nursing education program. For cost reporting periods at issue in these appeals, the Provider claimed medical library costs in the nursing school cost center. During the audit of the Provider's cost reports, Aetna Life Insurance Company ("Intermediary")<sup>1</sup> identified these costs and reclassified them from the nursing school to the administrative and general cost center. The Intermediary also reclassified the salary statistic for the allocation of employee benefit costs associated with the medical library from the nursing school to the administrative and general cost center.

The Medicare reimbursement effect, for each of the years in dispute, is approximately:

9/30/89	\$60,000. <sup>2</sup>
9/30/90	\$90,000 <sup>3</sup>
9/30/91	\$70,000 <sup>4</sup>

The Provider timely appealed the NPRs to the Provider Reimbursement Review Board ("Board") and has met the jurisdictional requirements of 42 C.F.R. §§ 405.1835-.1841. All other issues in the original appeals have either been settled or withdrawn.

A hearing on PRRB Case No. 91-2308 (FYD 6/30/89) was held before the Board on April 24, 1998. The Provider was represented by Ronald N. Sutter, Esquire, of Powers, Pyles, Sutter & Verville, P.C. The Intermediary was represented by Tom Bruce, Senior Consultant, Research and Appeals, Mutual of Omaha.

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<sup>1</sup> The current Intermediary that presented the case at the hearing is Mutual of Omaha.

<sup>2</sup> 1989 Provider Position Paper at 7; 1989 Intermediary Position Paper at 1.

<sup>3</sup> 1990 Provider Position Paper at 5; 1990 Intermediary Position Paper at 1

<sup>4</sup> 1991 Provider Position Paper at 3; 1991 Intermediary Position Paper at 1 indicates Medicare reimbursement effect is \$21,000.

Subsequent to the above hearing, the Board received joint stipulations from the parties requesting that the decisions for PRRB Case Nos. 94-2352 (9/30/90) and 94-1066 (9/30/91) be based solely on 1) the materials previously filed in these cases, and 2) the record for case PRRB Case No.91-2308 (9/30/89). The sole issue remaining in the 6/30/90 and 6/30/91 cases is the same as in the 6/30/89 case which was heard before the Board.<sup>5</sup> Unless otherwise noted, all footnotes in this decision will refer to the record for 6/30/89.

#### BACKGROUND:

The Provider's nursing school has a library located on its premises.<sup>6</sup> According to the Provider, the library specializes in nursing studies and is used primarily by the students and faculty of the nursing school and is managed and operated by the nursing school.<sup>7</sup>

The Provider has always claimed the costs of the nursing school library as nursing education costs.<sup>8</sup> Prior to 1989, the Intermediary had allowed the costs of the nursing school library as nursing education costs,<sup>9</sup> including 1981, the base year used for the PPS federal rate, and 1982, the base year used for the PPS hospital-specific rate.<sup>10</sup> During the Provider's 1989 fiscal year, the Intermediary made interim payments which the Provider presumed to allow the nursing school library costs as nursing education costs.<sup>11</sup>

When the Intermediary audited the Provider's 1989 fiscal year in 1991, the Intermediary departed from its prior audit determinations and recharacterized the Provider's nursing school library costs as operating costs.<sup>12</sup> The Provider maintains that the nursing school library

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<sup>5</sup> In the 1991 appeal, the Provider added the issue of the adequacy of its outlier payments. The parties agree, however, that the Board lacks the authority to decide the outlier issue and that expedited judicial review is therefore appropriate for the outlier issue.

<sup>6</sup> Tr. at 29-30, 92.

<sup>7</sup> Provider Exhibit 13; Transcript (hereinafter “Tr.”) at 30, 33-34, 44-50.

<sup>8</sup> Tr. at 35-37, 113.

<sup>9</sup> Id.

<sup>10</sup> Tr. at 41, 113-114.

<sup>11</sup> Tr. at 43, 100.

<sup>12</sup> Tr. at 36-37, 113.

operated in 1989 as it had always operated in the past, and there were no changes in the operation of the nursing school library during 1989.<sup>13</sup>

Based on 42 C.F.R. § 413.85(d)(4), the Intermediary made a determination that the "maintenance of a medical library" required that the costs of the nursing school library be recharacterized as operating costs. The Provider maintains that the Intermediary's reclassification of these costs as operating costs for the Provider's 1989, 1990, and 1991 fiscal years is inconsistent with the Intermediary's classification of these costs as nursing education costs for all prior years, including 1981 and 1982, the base years used to establish the PPS rates for operating costs.<sup>14</sup>

#### LEGISLATIVE HISTORY:

Effective with cost reporting years beginning on or after October 1, 1983, Congress adopted a Prospective Payment System ("PPS") to reimburse most hospitals for inpatient operating costs. PPS does not apply to capital costs or education costs, both of which continued to be reimbursed under "reasonable cost" payment principles. 42 U.S.C. § 1395ww(d) (1)(A).

For the first four years of PPS (1984-1987), Medicare paid hospitals a blend of two rates for operating costs -- the "hospital-specific rate" and the "federal rate." Georgetown Univ. Hosp. v. Bowen, 698 F. Supp. 290, 292-93 (D.D.C. 1987), aff'd, 862 F.2d 323 (D.C. Cir. 1988) (Georgetown II); 42 C.F.R. § 412.70. The hospital specific rate was established for each hospital based on the hospital's operating costs per patient discharge for a base year (1982). 42 C.F.R. § 412.73(a). The federal rate was an amount per patient discharge based on average national and regional costs during a base year (1981). Since 1988, hospitals have been paid for operating costs solely on the basis of the federal rate. Georgetown II, 698 F. Supp. at 292; 42 U.S.C. § 1395ww(d)(1)(A)(iii).

From the beginning of the program, Medicare has reimbursed a provider's "net cost of approved educational activities" on a "reasonable cost" basis. 20 C.F.R. § 405.421(a) (1966); 42 C.F.R. § 413.85(a) (1997). Such "activities" include "training programs for nurses." 20 C.F.R. § 405.421(c)(1966); 42 C.F.R. § 413.85(c)(1997). Even after the enactment of PPS, nursing education costs have continued to be reimbursed on a "reasonable cost" basis.

The Secretary first published the Provider Reimbursement Manual ("HCFA Pub. 15-1") in 1968.<sup>15</sup> Chapter 4 of the HCFA Pub. 15-1 governs educational costs. From 1968 to the

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<sup>13</sup> Tr. at 36-37.

<sup>14</sup> Tr. at 35-42, 113-114.

<sup>15</sup> Provider Exhibit 30; Tr. at 104.

present, HCFA Pub. 15-1§ 416.1 has provided that "the expenses of a medical library" are allowable as an "educational" cost.<sup>16</sup>

On September 1, 1983, HCFA amended the regulation governing reimbursement of education costs (then 42 C.F.R. § 405.421; currently 42 C.F.R. § 413.85), effective "with cost reporting periods that begin on or after October 1, 1983."<sup>17</sup> As amended, 42 C.F.R. § 413.85(d)(4) characterizes "maintenance of a medical library" as an operating expense.<sup>18</sup>

#### PROVIDER'S CONTENTIONS:

The Provider explains that it has historically claimed the costs of the nursing school library as a nursing education cost and that the Intermediary has historically reimbursed the costs of the nursing school library as a nursing education cost. The Provider contends that this was true during 1981, the base year used to establish the federal rate for PPS for operating costs. The Provider further contends this was also true during 1982, the base year used to establish the hospital-specific rate for PPS. Thus, the Provider's nursing school library costs were excluded from the costs used to establish the PPS rates for operating costs.

For its 1989, 1990, and 1991 fiscal years, the Provider explains that it claimed its nursing school library costs as it had done for all prior years -- it claimed them as nursing education costs. During the Provider's 1989 fiscal year, the Intermediary reimbursed the Provider's nursing school library costs as nursing education costs in the interim rates paid to the Provider. However, when it settled the 1989 cost report in 1991, the Intermediary recharacterized the nursing school library costs as operating costs. The Intermediary also reclassified these costs in the 1990 and 1991 cost report years. The Provider maintains that the practical effect of the recharacterization was to deny it reimbursement for these clearly allowable costs because the costs had been excluded from the operating costs used to establish the PPS rates.

The Provider argues that the Intermediary's disallowance is clearly illegal or erroneous for several reasons:

(1) it violates the expressed prohibition in the Omnibus Budget Reconciliation Act of 1990 ("OBRA 1990") against recouping alleged overpayments relating to nursing education costs; (2) it violates 42 C.F.R. § 413.85, which requires Medicare reimbursement of the net costs of a provider's approved educational programs,

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<sup>16</sup> Provider Exhibit 10; Tr. at 69-70, 102-103.

<sup>17</sup> 48 Fed. Reg. 39,752 (1983) (Provider Exhibit 7); Tr. at 105-107.

<sup>18</sup> Provider Exhibit 6.

including nursing education programs,  
(3) the Intermediary's interpretation of 42 C.F.R. § 413.85 (d)(4) is erroneous; and  
(4) it violates the proscription against cross-subsidization in 42 U.S.C. § 1395x(v)(1)(A) and the fairness principle in 42 C.F.R. § 413.9(c)(1).

The Provider asserts that the Intermediary based its disallowance on 42 C.F.R. § 413.85(d)(4). The Provider notes that this provision was added by HCFA in September 1983 without using the advance notice and comment procedures of the Administrative Procedure Act ("APA") 5 U.S.C. § 553. HCFA did not first publish the amendment as a proposed rule; it published the amendment as an "interim final rule."<sup>19</sup> That provision characterizes the costs of maintaining a "medical library" as an operating cost, rather than as an education cost.

The Provider asserts that the Intermediary's reliance on 42 C.F.R. § 413.85(d)(4) is misplaced. The Provider contends that the evidence in this case clearly demonstrates that the Provider's library is a "nursing school library," not a "medical library."<sup>20</sup> The Provider contends that the Intermediary's interpretation of section 413.85(d)(4) conflicts with both the Medicare statute and the APA and, therefore, would be invalid. The Provider argues that the Board should construe section 413.85(d) in accordance with its plain meaning and reject the Intermediary's inequitable nonliteral construction.

As noted above, the Provider argues that the Intermediary's adjustment was illegal for several reasons. Following, is a summary of the Provider's arguments in each of areas mentioned above.

(1) Violation of the expressed prohibition in the Omnibus Budget Reconciliation Act of 1990 ("OBRA 1990") against recouping alleged overpayments relating to nursing education costs.

The Provider contends that OBRA 1990 enacted a provision, section 4004(b)(3), that barred HCFA from recouping "alleged overpayments" relating to "approved nursing . . . education programs" for "cost reporting periods beginning on or after October 1, 1983, and before October 1, 1990."<sup>21</sup> OBRA 1990, § 4004(b)(3)(A) provides:

The Secretary of Health and Human Services may not recoup payments from (or otherwise reduce or adjust payments under Part A of title XVIII of the Social Security Act to) a hospital because of alleged overpayments to such

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<sup>19</sup> Id.

<sup>20</sup> Provider Post Hearing Brief (hereinafter "Provider PHB") at 2-3.

<sup>21</sup> Provider Exhibit 12. Section 4004(b)(3) applies to Part A of Medicare. Section 4159(b)(3) of OBRA 1990 is identical to Section 4004(b)(3) but applies to Part B of Medicare. Provider Exhibit 24

hospital under such title due to a determination that costs which were reported by the hospital on its Medicare cost report for cost reporting periods beginning on or after October 1, 1983, and before October 1, 1990, relating to approved nursing and allied health education programs did not meet the requirements for allowable nursing and allied health education costs (as developed by the Secretary pursuant to section 1861(v) of such Act [42 U.S.C. § 1395x(v)]).

Id.

The Provider argues that the congressional prohibition in OBRA 1990 clearly applies to this case. The Intermediary witness acknowledged that the Intermediary was recouping alleged overpayments relating to nursing education costs for a cost reporting year that began "after October 1, 1983, and before October 1, 1990."<sup>22</sup> The Provider points out that the Intermediary witness also conceded that the plain words of section 4004(b)(3) preclude the recoupment effected by the Intermediary in this case.<sup>23</sup>

The Provider takes exception to the Intermediary's argument that section 4004(b)(3) must be read in light of section 4004(b)(1) of OBRA 1990. The Provider points out that Section 4004(b)(1) provides that :

"clinical training (as defined by the Secretary) conducted on the premises of the hospital under approved nursing and allied health education programs that are not operated by the hospital shall be allowable as reasonable costs . . ."

Id. Provider Exhibit 12.

Thus, the Intermediary argues, section 4004(b)(3) only bars recoupment of a particular type of nursing education cost, i.e., "clinical training . . . conducted on the premises of the hospital under approved nursing and allied health education programs that are not operated by the hospital." Id.

The Provider contends that the Intermediary clearly errs in its interpretation. The Provider maintains that sections (b)(1) and (b)(3) are entirely discrete. The Provider points out that if the Intermediary were correct, paragraph (b)(3) would reference paragraph (b)(1). However, as the Intermediary's witness conceded, it does not.<sup>24</sup>

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<sup>22</sup> Tr. at 98-101.

<sup>23</sup> Id. at 101.

<sup>24</sup> Tr. at 101.

The Provider contends that the wording of paragraph (b)(1) is narrow and refers to a specific type of nursing education costs, clinical training. In contrast, as the Intermediary witness acknowledged, the wording of paragraph (b)(3) is "quite broad."<sup>25</sup> The Provider maintains that Paragraph (b)(3) refers to "alleged overpayments . . . relating to approved nursing and allied health education programs," without any qualification whatsoever.<sup>26</sup>

The Provider points out that the Supreme Court has held that the words of the Medicare statute must be construed in accordance with their "plain meaning." Bethesda Hosp. Assn. v. Bowen, 485 U.S. 399, 403-05 (1988). As the Intermediary witness conceded, if the words of section 4004(b)(3) are construed in accordance with their plain meaning, they clearly bar the recoupment effected by the Intermediary in this case.<sup>27</sup> Therefore, the Provider believes that the Intermediary's recoupment is contrary to law and must be reversed.

(2) The Intermediary's disallowance violates 42 C.F.R. § 413.85.

The Provider notes that from the beginning of the program, Medicare has required reimbursement of a provider's "net cost of approved educational activities" on a "reasonable cost" basis. 20 C.F.R. § 405.421(a) (1966); 42 C.F.R. § 413.85(a) (1997). Such "activities" include "training programs for nurses." 20 C.F.R. § 405.421(c)1966); 42 C.F.R. § 413.85(c)1997). The net costs of approved education activities include "direct and indirect costs of the activities." 42 C.F.R. § 413.85(g).

The Provider contends that the costs it incurs for the nursing school library are necessary and proper costs of its nursing education program; thus, they are clearly reimbursable as education costs under Medicare principles. The Provider further contends that the evidence in this case clearly demonstrates that the nursing school library is an integral part of its nursing school. The evidence shows:

- (1) The College of Nursing is the Provider's only school of education. Tr. at 28-29.
- (2) The nursing school library is located on the premises of the nursing school. Tr. at 29.
- (3) The library is named after the individual who was the chancellor of the nursing school when the library opened in 1942. Tr. at 30.
- (4) The nursing school library is operated by the nursing school. Tr. at 30-33. The librarian reports directly to the chancellor of the nursing school. Id. at 33.

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<sup>25</sup> Id.

<sup>26</sup> Provider PHB at 9.

<sup>27</sup> Tr. at 101.

- (5) Nursing students work in the nursing school library. Tr. at 33.
- (6) The nursing school library specializes in nursing studies. Tr. at 33-34. Approximately two-thirds of the books specifically relate to nursing studies. Id. at 33. All other materials are relevant to the nursing students' education. Id. at 33-34.
- (7) The nursing school must have a library to meet accreditation standards. Tr. at 34. The Provider's nursing school files reports with accreditation agencies regarding the nursing school library. Id.; Provider Exhibit 18.
- (8) The chief librarian of the nursing school library serves on the resources and facilities committee of the nursing school. Tr. at 34-35.
- (9) The Provider has always viewed the nursing school library as a cost of its nursing education program and has always claimed the nursing school library costs on its Medicare cost reports. Tr. at 35-36. Prior to 1989, the Medicare Intermediary always viewed the nursing school library as a cost of the Provider's nursing education program and always treated the nursing school library costs in its Medicare audits of the Provider. Tr. at 36, 113. The nursing school library operated during the Provider's 1989 fiscal year as it had always operated in the past. Tr. at 36-37. There was no change in operations in the Provider's 1989 fiscal year that warranted a change in the classification of the costs relating to the nursing school library. Tr. at 36. There was also no relevant change in law in 1989. The Provider notes that the regulatory provision relied on by the Intermediary was promulgated in 1983 and that prior to the 1991 audit of the Provider's 1989 fiscal year, the Intermediary never construed this provision to require a reclassification of the costs of the Provider's nursing school library.
- (10) The nursing school library is used primarily by the nursing students and the nursing school faculty. Tr. at 44-53; Exhibit 13. The Provider points out that a four-week study conducted by the Provider demonstrates that the nursing students and faculty account for 61.23 percent of the usage of the nursing school library. Id. The Provider also points out that the Intermediary witness, who observed the study while it was being conducted, "agreed to the study" and to "the way it was conducted" and also agreed that the study was "thorough" and the Provider had done a "good job." Tr. at 124; see also Tr. at 55. During 1989, only two percent of the hospitals in the country had nursing schools. Tr. at 57-59; Provider Exhibits 29, 31. Thus, as the Intermediary witness acknowledged, for 98 percent of the hospitals in the country, nursing students account for zero percent usage of whatever library facilities are available. Tr. at 58-59; 110-111. That contrasts sharply with the 61.23 percent nursing student usage at the Provider's nursing school library.

The Provider contends that an intermediary that seeks to change a long-standing classification of costs, where there has been no change in circumstances and no change in law (as is the

case here), must bear a heavy burden of proof. The Provider argues that the Intermediary has presented no evidence at all, much less compelling evidence, to justify reclassifying the Provider's nursing school library costs as operating costs. To the contrary, the evidence overwhelmingly demonstrates the inextricable connection of the nursing school library to the Provider's nursing school and the correctness of Medicare's long-standing classification of the Provider's nursing school library costs as nursing education costs.

The Provider contends that under the Medicare regulations, the Provider is entitled to Medicare reimbursement of all the "direct and indirect costs" of its nursing education program on a "reasonable cost" basis. 42 C.F.R. § 413.85(g). The Provider maintains that the expenses of the nursing school library are clearly such costs. Thus, the Intermediary's disallowance violates the governing Medicare regulations.

(3) The Intermediary's interpretation of 42 C.F.R. § 413.85 (d)(4) is erroneous.

The Provider asserts that the Intermediary is relying exclusively on 42 C.F.R. §413.85(d)(4) as the basis for its disallowance. The Provider contends that section 413.85(d)(4) was added to the Medicare regulations in 1983 without using the advance notice and comment procedures of the APA. The Provider points out that this section provides that costs relating to the "maintenance of a medical library" are "recognized as normal operating costs," not as education costs.

The Provider argues that the exact wording of section 413.85(d)(4) is important. The Provider contends that the provision does not refer to "maintenance of a library associated with an approved educational program." Instead, it refers to "maintenance of a medical library." *Id.* (Emphasis in original.)

The Provider points out that in the accompanying preamble to the amendment, HCFA explained that "it is important that we clearly differentiate between approved educational activities in which a hospital may be engaged and other training costs a hospital may incur."<sup>28</sup> It is the Provider's position that this clearly indicates that the intent of the amendment was not to reclassify costs relating to "approved educational activities."

The Provider also points out that from the beginning of the Medicare program, HCFA Pub. 15-1 § 416.1 has provided that "the expenses of a medical library" are allowable as "educational expenses." HCFA has never repealed HCFA Pub. 15-1§ 416.1, which remains in the Manual today. According to the Provider, nothing in the chapter suggests that educational costs attributable to a medical library should be allowable as anything other than educational costs. The Provider believes that the only logical conclusion to be drawn from the retention of § 416.1 is that the costs of a library are allowable as an education cost if the

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<sup>28</sup>

48 Fed. Reg. 39,797; Provider Exhibit 7.

library is operated as part of an approved educational program, rather than as a general medical library.

The Provider contends that HCFA has acknowledged that the "other educational expenses" listed in HCFA Pub. 15-1 § 416 historically were allowed as education costs. The Provider points out that in a notice of proposed rulemaking published in the Federal Register in 1992, HCFA stated:

The types of costs that were allowable as costs of approved educational activities early in the Medicare program were set forth in both the applicable regulation and in Chapter 4 of the Provider Reimbursement Manual (HCFA-Pub. 15-1). The original regulation specifically excluded "orientation" and "on-the-job training" from the definition of approved educational activities (20 CFR 405.421 (d)). Further, as early as 1971, Chapter 4 of the Provider Reimbursement Manual stated that "any costs of usual patient care" are also excluded from that definition (§ 404.2). The Provider Reimbursement Manual specified that the costs of usual patient care were allowable, but only as normal operating costs and not as educational costs. On the other hand, during this time, the Provider Reimbursement Manual did include within the scope of allowable educational activities, such other educational expenses as costs associated with refresher and postgraduate programs, part-time education for bona fide employees of the provider, travel expenses for educational workshops, and training in the use of medical appliances for patients or their care-givers.

57 Fed. Reg. 43,661 (Sept. 22, 1992) (emphasis added) (Provider Exhibit 6, 1990 & 1991 Position Papers).

The Provider argues that, those "other educational expenses" are described as being "within the scope of allowable educational activities." Further, those "other educational expenses" (mentioned in the last sentence quoted above) are listed in the same section of the manual as medical library expenses, and nothing in that section of the manual indicates that medical library expenses are treated differently than the other educational expenses listed therein.

The Provider argues that the evidence here demonstrates that its library was a nursing school library, not a "medical library." The Provider points out that the Intermediary witness acknowledged at the hearing that the Provider's nursing school library differs from a general medical library in numerous important respects.<sup>29</sup>

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<sup>29</sup> Tr. at 110-113.

Therefore, the Provider contends that by its plain terms, section 413.85(d)(4) applies only to a "medical library." The Provider maintains its library has always been classified as a nursing school library, not a medical library, and the evidence in the record amply demonstrates the correctness of this historic treatment. The Provider believes that the Intermediary's interpretation of section 413.85(d)(4) contravenes the plain words of the provision and is therefore invalid. See Bethesda Hosp. Assn. 485 U.S. 399 at 403-05.

The Provider argues that the Intermediary's reliance of section 413.85(d)(4) is also invalid because HCFA issued this section without following the mandatory notice and comment procedures of the APA. HCFA published section 413.85(d)(4) as an interim final rule.<sup>30</sup> It did not first publish a proposed rule and invite and evaluate comments on the proposed rule, as required by the APA.

In summary, the Provider believes that the Board should construe section 413.85(d)(4) by applying the regulation's plain wording and reject the Intermediary's unfair non-literal construction. By its plain terms, section 413.85(d)(4) applies only to a "medical library." The Provider maintains it does not apply to a nursing school library. Consequently, because the Provider's library is a nursing school library, section 413.85(d)(4) is inapplicable to this case.

(4) It violates the proscription against cross-subsidization in the Medicare statute and the fairness principle in Medicare regulations.

The Provider points out that the Medicare statute directs the Secretary to pay Medicare's fair share of necessary costs so that Medicare costs are not shifted to other payers -- a principle known as the "proscription against cross-subsidization." 42 U.S.C. § 1395x(v)(1)(A)(I). The Provider also points out that the Secretary's regulations establish the fairness principle. Specifically, they provide that "[i]t is the intent of Medicare that payments to providers of services should be fair to the providers, to the contributors to the Medicare trust funds, and to other patients." 42 C.F.R. § 413.9(c)(1) (Provider Exhibit 28). The Provider cites numerous cases in its post hearing brief that support the cross-subsidization and fairness principles.<sup>31</sup>

The Provider contends that the evidence in this case clearly demonstrates that the Intermediary's adjustment contravenes these bedrock principles of the Medicare program. The base years used to establish the PPS rates for operating costs were 1981 and 1982, during which years both operating costs and nursing education costs were reimbursed on a "reasonable cost" basis.<sup>32</sup> During 1981 and 1982, the Medicare Intermediary classified the

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<sup>30</sup> 48 Fed. Reg. 39,752; Provider Exhibit 7; Tr. at 107-108.

<sup>31</sup> See Provider PHB at 14-16.

<sup>32</sup> Tr. at 39-41.

Provider's nursing school library costs as nursing education costs.<sup>33</sup> Therefore, it is the Provider's position that nursing school library costs were not included in the costs used to establish the PPS rates.<sup>34</sup>

The Provider points out that during the Provider's 1989 fiscal year, nursing education costs were reimbursed on a "reasonable cost" basis, just as they had been in 1981 and 1982. However, operating costs were no longer reimbursed on a "reasonable cost" basis as they had been in 1981 and 1982. Instead, they were reimbursed through the PPS rates.<sup>35</sup>

Consequently, as the Provider's witness accurately testified, the Intermediary's reclassification of these costs as operating costs in 1989 placed the Provider in a "Catch-22."<sup>36</sup> Because of the reclassification, the Provider was not reimbursed for these costs on a pass-through basis because operating costs are no longer reimbursed as pass-through costs. However, the Provider was not reimbursed for these costs through the PPS rates because these costs had not been regarded as operating costs in 1981 and 1982 when the PPS rates were established. Therefore, the Provider contends that the practical effect of the Intermediary's inconsistent classifications is that a clearly allowable cost, whether classified as either nursing education or operating, has been converted almost entirely into a non-allowable cost.<sup>37</sup>

The Provider points out that the Intermediary's witness acknowledged at the hearing that this inconsistency resulted in unfair treatment to the Provider.<sup>38</sup> In addition, when asked whether Medicare was paying "its fair share," the witness responded, "Probably not. No."<sup>39</sup>

The Provider contends that both the Medicare statute and the Medicare regulations require Medicare to pay its fair share. 42 U.S.C. § 1395x(v) (1)(A); 42 C.F.R. § 413.9(c)(1). The fact that Medicare is not doing so in this case, as the Intermediary witness admitted, clearly proves that the Intermediary's adjustment is invalid and must be overturned.

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<sup>33</sup> Tr. at 35-36, 113-114.

<sup>34</sup> Tr. at 40-41.

<sup>35</sup> Tr. at 37-38.

<sup>36</sup> Tr. at 38-42.

<sup>37</sup> The Intermediary's reclassification of these costs as an administrative and general cost resulted in a very small portion (1.7%) being stepped down to the Provider's nursing education cost center. See Provider Exhibit 27; Tr. at 56-57.

<sup>38</sup> Tr. at 116-117.

<sup>39</sup> Tr. at 120-121.

INTERMEDIARY'S CONTENTIONS:

The Intermediary contends there is no dispute that the regulation at 42 C.F.R. §413.85(d)(4) states that the costs of maintaining a medical library are not medical education costs. The Intermediary asserts that the question before the Board is whether the library is a medical or nursing school library.

The Intermediary maintains that it properly reclassified medical library costs, along with the associated Worksheet B-1 salary statistic for the allocation of employee benefit costs, from the Provider's nursing school cost center to the administrative and general cost center.

The Intermediary acknowledges that nursing educational training programs are allowable as educational activities and consequently, providers can be reimbursed for these costs outside the prospective payment system's predetermined rate.

The Intermediary points out that allowable costs of approved educational activities are further defined within the regulations. Relevant to this appeal, 42 C.F.R. §413.85(d)(4) specifically excludes the maintenance of a medical library from the definition of an educational activity, meaning that the costs of maintaining a medical library are normal operating costs of a hospital and are considered paid through the prospectively determined rate. In other words, with respect to inpatient services, there is no additional payment outside the prospective payment system's predetermined rate for the costs of maintaining the medical library.

It is the Intermediary's position that medical library costs are general service costs and are most appropriately classified in the administrative and general cost center. The Intermediary contends that all hospitals are required to maintain a medical library as a condition of their accreditation. The Provider is not exempt from this requirement.

The Intermediary also points to testimony at the hearing that established that the library is physically connected to the hospital and accessible to all hospital personnel.<sup>40</sup> The Intermediary's witness also testified that, in addition to the nursing students, the Provider's physicians, interns and residents, and administrative staff used the library. It is the Intermediary's position that even though the library may have a nursing school orientation, it remains a medical library that is used by various hospital personnel and benefits the Provider as a whole and not just the nursing school program. Along with other costs that benefit the entire hospital, the costs of the library are properly included in the administrative and general cost center and allocated to the benefiting cost centers using the accumulated cost statistic.

The Intermediary refers to HCFA Pub. 15- 1, §2302.9 which defines a general service cost center as, "[t]hose organizational units which are operated for the benefit of the institution as a whole." Id. The Intermediary contends that costs that benefit the Provider as a whole are best

recorded in a general service cost center and allocated to the benefiting cost centers, through the step-down method, as actual services are rendered. The Intermediary contends that in this way, the costs of maintaining the medical library can be appropriately spread among all of those who benefit from its existence.

The Intermediary contends that the Provider should not be permitted to directly assign any portion of the costs of the medical library to the nursing school cost center. The Intermediary refers to HCFA Pub. 15-1, § 2307A, which defines the direct assignment of cost as follows:

"[d]irect assignment of cost is the process of assigning directly allocable costs of a general service cost center (see §2302.9) to all cost centers receiving service from that cost center based upon actual auditable usage. Hours worked by hourly wage or metered utility consumption are examples of measures of actual usage. Estimates, including a statistical surrogate such as square feet, are not acceptable. Time studies are considered statistical surrogates and, thus, may not be used as a basis for direct assignment of costs.....

Id. (Intermediary Exhibit 1-6)

The Intermediary rejects the Provider's argument that, should the Board decide that 100 percent of the Provider's library costs may not be included in the nursing school cost center, then the Board should direct the Intermediary to directly assign 61.23% of the library costs to the nursing school cost center. The Intermediary acknowledges that this percentage is consistent with the results of the Provider's library use study. As stated above, HCFA Pub. 15-1, §2307A prohibits the direct assignment of general service costs based on estimates. The Intermediary contends that the library use study, which was conducted during a two-month period approximately eight years after the 1989 cost reporting period, is clearly an estimate. In addition, the Intermediary points out that the results of the study are at odds with the librarian's more contemporaneous estimate of 35% nursing school usage. (See Intermediary Exhibit 1-7).

To the Intermediary's knowledge, the Provider does not have any other auditable records of the use of the medical library by the nursing school students. The Intermediary asserts that even if the Provider had these records, it would also have to have records of the use of the library by its physicians, interns and residents, therapists, and nursing staff so that all of the directly allocable medical library costs could be directly assigned to the appropriate cost centers. It is the Intermediary's position that if the nursing school were the only cost center to receive a direct allocation of medical library costs with the remaining medical library costs recorded in the administrative and general cost center, then the nursing program would receive a disproportionate allocation of medical library costs through its accumulated cost statistic.

The Intermediary also refers to two cases in which the Board has decided that the costs of a medical library are most appropriately included in the administrative general cost center. Los Angeles County Medical Library Group Appeal, PRRB Dec. 88-D13, January, !3, 1988, Medicare & Medicaid Guide (CCH), ¶36,814, (Intermediary Exhibit I-3), aff'm HCFA Adm., March 11, 1988, Medicare & Medicaid Guide (CCH) ¶37,025, (Intermediary Exhibit I-5), and Good Samaritan Hospital and Health Center, PRRB Dec.93-D30 April 1, 1993, Medicare & Medicaid Guide (CCH) ¶41,399, (Intermediary Exhibit 1-4).

The Intermediary rejects the Provider's contention that § 4004(b)(3)(A) of OBRA 90<sup>41</sup> prohibits the recoupment of any overpayments resulting from the reclassification of library costs from the nursing school to the administrative and general cost center. The Intermediary contends that all of §4004(b) must be read in context.

The Intermediary asserts that Section 4004(b)(1) clearly refers to nursing education programs that are not operated by a hospital. The Intermediary contends that the prohibition against recoupment in §4004(b)(3) also refers only to overpayments resulting from a determination that the nursing education program was not operated by a hospital. The Intermediary further contends that its reclassification of the library costs did not result from a determination that the Provider's nursing education program was not operated by the hospital, but rather that the library was a medical library. The Intermediary asserts that Section 4004(b)(3)(A) does not prohibit the collection of the overpayment resulting from this determination.

In conclusion, the Intermediary maintains that the Provider's library is a medical library that benefits the entire hospital. Therefore, the reclassification of the library's costs from the nursing school to the administrative and general cost center was in accordance with 42 C.F.R. §413.85(d)(4).

#### CITATION OF LAW, REGULATIONS, AND PROGRAM INSTRUCTIONS:

1. Laws-42 U.S.C.:  
§ 1395x(v)(1)(A)et seq  
§ 1395ww(d)(1)(A) et seq
  - Reasonable Cost
  - Exceptions and adjustments to PPS
2. Regulations-42 C.F.R.:  
§ 405.1835-.1841
  - Board Jurisdiction  
§ 412.70
  - Determination of Transition Period
  - Payment Rates-General Description
  - Determination of the Hospital
  - Specific rate based on the Federal fiscal year 1982 base period- Costs  
§ 412.73(a)

on a per discharge basis  
§ 413.9(c)(1) - Costs related to patient care  
§ 413.85 et seq (formally 42 C.F.R. §405.421(1966))-Cost of Educational Activities

3. Provider Reimbursement Manual (HCFA Pub. 15-1):

§ 404.2 et seq - Costs of Approved Nursing and Paramedical Education Programs  
§ 416 et seq - Other Educational Expenses  
§ 2302.9 - General Service Cost Centers  
§ 2307A - Direct Assignment of Cost

4. Cases:

Georgetown Univ. Hosp.v- Bowen, 698 F. Supp. 290, (D.D.C. 1987), aff'd, 862 F.2d 323 (D.C. Cir. 1988)

Bethesda Hosp. Assn. v. Bowen, 485 U.S. 399, 403-05 (1988)

Los Angeles County Medical Library Group Appeal, PRRB Dec. 88-D13, January 13, 1988, Medicare & Medicaid Guide (CCH), ¶36,814, aff'm HCFA Adm., March 11, 1988, Medicare & Medicaid Guide (CCH) ¶37,025

Good Samaritan Hospital and Health Center, PRRB Dec.93-D30 April 1, 1993, Medicare & Medicaid Guide (CCH) ¶41,399

5. Other:

Administrative Procedures Act, U.S.C. § 553

OBRA 1989 § 6205(b)(1)  
OBRA 1990 § 4004(b)(1)  
OBRA 1990 § 4004(b)(3)et seq.  
OBRA 1990 § 4159(b)(3)  
48 Fed. Reg. 39,752; 39,797 (1983)  
57 Fed. Reg. 43,661, (Sept. 22, 1992).

FINDINGS OF FACT, CONCLUSIONS OF LAW AND DISCUSSION:

The Board, after consideration of the facts, parties' contentions, evidence presented, testimony given at the hearing and post-hearing briefs, finds and concludes as follows:

The Intermediary had historically considered the costs of the nursing school library as nursing education costs, and accordingly, the Provider was reimbursed reasonable costs for these activities. Even after the enactment of PPS, these costs were considered educational costs by the Intermediary and paid on a “pass-through” basis, outside the PPS rates. In 1991, during the audit of the Provider’s 1989 cost report, the Intermediary, citing 42 C.F.R. § 413.85(d)(4) reclassified these costs from the nursing school to the administrative and general cost center. The Intermediary made similar reclassification adjustments for the 1990 and 1991 cost reporting years. The Medicare reimbursement impact to the Provider was substantial.

In support of its position, the Provider argued that section 413.85(d)(4) did not apply since its library was a nursing school library and not a medical library as referred to in the regulation. The Intermediary argued that the library was in fact a medical library and that section 413.85(d)(4) did apply.

The Provider also argued that section 4004(b)(3)(A) of OBRA 1990 precluded the Intermediary from recouping payments because of adjustments made in its approved nursing program. The Intermediary’s position was that the prohibition against recoupment, in section 4004(b)(3)(A), refers only to overpayments resulting from a determination that nursing education programs were not operated by a hospital.

The Board was first tasked with analyzing section 4004 of OBRA 1990 to try and determine what Congress intended this section to convey. As a starting point, the Board looked HCFA Pub. 15-1 § 404.2E for guidance on the intent. Section 404.2 E states in part:

E. [m]oratorium on Recoupment of Overpayments Attributable to Nursing and Allied Health Education Costs Section 6205(b)(1) of OBRA 1989(P.L. 101-239) imposed a moratorium on the recoupment of Medicare overpayments to hospitals for pass-through costs related to approved nursing and allied health education programs. Section 4004(b)(3)(A) of OBRA 1990 (P.L. 101-508) indefinitely prohibits the recoupments of these overpayments. The prohibition of recoupment applies to all hospital reporting periods beginning on and after October 1, 1983 and before October 1, 1990.

The moratorium on recoupment applies to overpayments attributable to the costs of approved nursing and allied health education programs that were determined not to meet the definition of allowable costs for pass-through because the programs were not operated by the hospital.

Id. (emphasis added)

Based on its review of OBRA 1990, and on its review of the manual, the Board opines that the intent of the moratorium, established in section 4004(b)(3)(A) of OBRA 1990, was to protect payments, for a period of time, to outside parties operating education programs. In

other words, the intent of this section was to protect those programs that were not hospital run. Therefore, the Board finds that nursing education costs are not protected from recoupment when the programs are operated by the provider. The Board concludes that section 4004(b)(3)(A) of OBRA 1990 does not apply in this case since no outside organization or company was operating the nursing school. The nursing school was operated by the Provider.

Next, the Board turned to 42 C.F.R. §413.85(d)(4) which states that the costs for, “[m]aintenance of a medical library,” are normal operating costs of a hospital and consequently are paid through a prospectively determined rate, i.e. medical library costs are not pass-through costs. The Board finds that the fact that only (2) two percent of hospitals in the United States operate nursing programs (1989) makes this case unique. Based on evidence in the record, the Board finds that a portion of the Provider’s library was used by hospital staff as a medical library and in fact, could replicate medical libraries in hospitals throughout the country. The Board also finds that a significant portion of the library was used by nursing students specifically for educational purposes. Therefore, the Board concludes that the Provider’s library was in fact a “dual purpose library.” It served as both a medical library and a nursing school library. Based on this conclusion, the Board finds that only part of 42 C.F.R. §413.85(d)(4) would apply in this case.

Because the Board considered the Provider’s library a dual purpose library, the Board looked to the best evidence in the record to split the library costs between educational (i.e. pass-through) and normal operating costs. The Board finds that the best evidence in the record to accomplish the split was a four-week study conducted by the Provider which demonstrated that the nursing students and faculty accounted for 61.23 percent of the usage of the nursing school library.<sup>42</sup> The Board notes that the Intermediary’s witness testified that she had observed the study and agreed that it was "thorough" and the Provider had done a "good job."<sup>43</sup>

The Intermediary argued that the Board should not rely on the study since HCFA Pub. 15-1 § 2307.A prohibits direct costing based on estimates. The Board finds that using the study, as a basis for allocating 61.23 percent of the library costs to the nursing school cost center and the remainder to A & G, would not violate section 2307.A because the costs in question are not part of a general service cost center, and therefore, do not have to be allocated to the institution as a whole. The Board notes that the costs claimed in the nursing school cost center were previously allowed as pass-through costs. If these costs had been A & G costs, they would not have been allowed as pass-through costs.

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<sup>42</sup> Tr. at 44-53; Provider Exhibit 13.

<sup>43</sup> Tr. at 124; see also Tr. at 55.

The Board also refers to the issue of whether the library costs were included in the base year when PPS operating cost rates were developed. The Board notes that since only 2 (two) percent of United States hospitals had nursing school programs, it is questionable whether the costs were included. Even if they were, the Board believes they would be inadequately represented.

**DECISION AND ORDER:**

The Intermediary improperly reclassified total library costs from the nursing school cost center to the A & G cost center. Based on the Provider's study, the Intermediary is directed to modify its adjustment by returning 61.23 percent of the reclassified library costs to the nursing school cost center. The remaining 38.77 percent of these costs should remain, as adjusted, in the A & G cost center.

**Board Members Participating:**

Irvin W. Kues

James G. Sleep

Henry C. Wessman, Esq.

Martin W. Hoover, Jr. Esq.

Charles R. Barker

**Date of Decision:** December 09, 1998

**FOR THE BOARD:**

Irvin W. Kues  
Chairman