

## PFS Practice Expense RVU Algorithm

This draft Technical Memo expands on the *Federal Register* description of the algorithm used to create practice expense (PE) relative value units (RVUs) under the Medicare Physician Fee Schedule (PFS). It describes the current algorithm, without analysis or reference to when specific elements were added or modified.

CMS uses the PE RVU algorithm to develop PE RVUs for PFS services based on variation in direct costs and indirect costs, scaled to maintain the ratio between total work RVUs and total PE RVUs. This algorithm is described in the *Federal Register* and uses current RVUs and the five input files (direct costs, physician time, physician work, utilization, and PE per hour (PE/HR) data by specialty) published as public use files (PUFs) with each proposed (NPRM) and final rule (FR). This Technical Memo aims to provide more detail about the steps of the algorithm to support analysis of PE RVUs and proposed changes by stakeholders and other interested parties. The method described is based on policies as implemented in the 2026 FR. A brief section at the end shows modifications to the method associated with particular proposals in the 2027 NPRM. An updated version of this memo will be issued with the 2027 FR that reflects all policies finalized in that rule.

### Overview of the Method

The method used to establish PE RVUs is, at its core, fairly straightforward and aims to distribute the pool of PE RVUs across all services to reflect differences in *relative* resources used to provide each service. Reflecting accounting norms that separate costs into *direct costs* attributable to a particular product or service and *indirect costs* inherent in having the capacity to produce *any* products or services, the PE RVU pool is split into two pools: a direct costs pool, associated with providing a particular service to a particular patient, and an indirect costs pool, associated with maintaining a medical practice. These two pools of RVUs are then allocated across services based on different bases. The direct cost pool is allocated based on CMS's direct cost data and the indirect cost pool is allocated based on direct costs and physician work (or clinical labor when the service does not involve physician work), adjusted for specialty-specific differences in practice expense per hour. For both cost types, once the target RVU pool is established, the process involves calculating the allocation basis and then *rescaling* it to create preliminary estimates of RVUs that have a volume-weighted sum equal to the target pool. Specifically, the process of "rescaling the basis to fit the pool" means:

1. Calculate the volume-weighted sum of the allocation basis across all services.
2. Calculate a scaling adjuster as the ratio of the target RVU pool to the sum of the allocation basis (Step 1).
3. Establish preliminary RVUs equal to the product of the allocation basis at the service level and the scaling adjuster (Step 2).

This simple scheme applies to both direct and indirect costs, but the latter has some additional steps to incorporate specialty-specific adjustments. The resulting preliminary indirect RVU estimates are adjusted through two additional policies – the 'cognitive floor' for indirects and the 'transition policy' for total RVUs – to establish final PE RVUs, which also involve rescaling to maintain budget neutrality.

Each proposed and final rule includes a PUF that provides the steps in the calculation of RVUs for several example HCPCS codes. The NPRM26 version of this PUF is in Appendix B, limited to the first two services for space considerations. The PUF is designed to show the values of key measures in the course of developing PE RVUs, some of which are evident from the data for each HCPCS code. However, some key measures require weighted sums across codes, sometimes by specialty. These are reported in the PUF with a footnote briefly

explaining the calculation underlying the measure. This Technical Memo explains the PE RVU algorithm and clarifies the calculation of these measures.

## Key Data

There are six data sources used to estimate PE RVUs:

- *Service-level direct costs.* For each service, CMS establishes both the quantities of specific direct inputs (clinical labor, medical supplies, medical equipment) used to provide each service and the prices of these inputs. Total clinical labor, supply, and equipment costs per service are calculated and serve as the allocation basis for the direct PE RVU pool. Level of measure: **HCPCS MODIFIER<sup>1</sup>(MOD) FACILITY**
- *Utilization.* Service volume is summarized from claims data to the service level by service setting (facility vs. non-facility) and specialty. For some calculations, utilization is further summarized across specialties. Level of measure: **HCPCS MOD FACILITY SPECIALTY**
- *Physician work.* Defined for each service, the physician work values play two roles in establishing PE RVUs: (1) they are used to establish the size of the PE RVU pool and (2) they are part of the allocation basis for allocating the indirect PE RVU pool. Level of measure: **HCPCS MOD**
- *Practice expense per hour (PE/HR).* Total, direct, and indirect PE/HR measures by specialty are used: (1) to separate the total PE RVU pool into direct and indirect pools and (2) to adjust the indirect allocator. Level of measure: **SPECIALTY**
- *Physician service time.* Defined for each service, the measure of provider minutes is used, along with utilization, to weight the PE/HR data by specialty. Level of measure: **HCPCS MOD**
- *Current RVUs.* The work and PE RVU measures that underlie the current year's PFS are needed to establish the size of the PE RVU pool for next year's values. Level of measure: **HCPCS MOD FACILITY**

## Universe of Services Included, Rounding and “Adding Up”, and Policy Exceptions

*Universe of services and final budget neutrality.* The PE RVU algorithm establishes values for the upcoming year's HCPCS codes included in the PFS, which typically differs from the current year's values as codes are created and deleted over time. The current year's values serve to create the target PE RVU pool based on the previous year's service volume, crosswalked as necessary for new codes. As described in the *Federal Register*, claims for some providers are not used in establishing relative values but are included for the final budget neutrality calculation. As a result, the PE RVU values estimated through the process described above are used in a final budget neutrality calculation, wherein the newly calculated PE RVUs are multiplied by *all* utilization, including the utilization from the claims excluded from the ratesetting process, and rescaled as necessary to ensure that the newly calculated values' total matches that of the target values .

*Rounding and “Adding Up”.* PE RVUs are rounded to the hundredths place before the final budget neutrality adjustment is made. Similarly, current policy requires that the global value for codes billable with modifiers 26 and TC be equal to the sum of the two modified cases. This ‘adding up’ constraint is imposed after PE RVU values are rounded to the second decimal. As a result, it is virtually impossible for the newly derived values’

<sup>1</sup> The PFS establishes different payment rates for three modifiers: 26, TC, and 53. Rates for Modifier 53 are only established for a few specific HCPCS codes: 44388, 45378, G0105, G0121 .

total, when multiplied by millions of services, to equal the target pool exactly.

*Policy Exceptions.* Over the years, CMS has described a number of policy exceptions that lead to special treatment of specific HCPCS codes or other cases. For example, physical therapy services are treated in the ratesetting process as if they are provided by Physical Therapists. The utilization data reports services provided by a mix of billing specialties, but for the purpose of the algorithm and, in particular, the specialty-specific elements of the indirect cost allocation, they are all treated as if they were provided by Physical Therapists. These specific exceptions affect specific services and are implemented at various points of the PE estimation process to achieve policy decisions described in the PFS rule text.

## Key Elements of the PE Algorithm

The PE RVU pool and values both are derived from the updated work RVUs for the next year. Once these work RVUs are established, the key elements in the PE RVU algorithm are<sup>2</sup>:

### A. Create total, direct, and indirect PE RVU pools:

- a. Calculate [total target PE RVU pool](#) as the volume-weighted sum of current, or base, PE RVUs times the ratio of the target work RVU pool (i.e., the volume-weighted sum of the target work RVUs) to current work RVU pool.
- b. Calculate [direct share of total PE](#), based on specialty-level expenses by category, as the ratio of the weighted average of direct and total costs across specialties, where the weight is the product of service-level physician time and service volume.
- c. Multiply direct share of total PE by target PE RVU pool to establish [target direct PE RVU pool](#); subtract this from target PE RVU pool to establish [target indirect PE RVU pool](#).

### B. Allocate the direct pool across services:

- a. Calculate service-level [direct PE cost](#) which will serve as the allocation basis for direct costs.
- b. Rescale the direct allocation basis by the direct scaling adjustment, which is equal to the ratio of the target direct RVU pool to the volume-weighted sum of the direct PE cost, to calculate the [direct PE RVU](#).

### C. Allocate indirect pool across services:

- a. Calculate the service-level [indirect allocator](#) as the sum of two parts:
  - i. [Indirect basis due to direct costs](#), defined as the direct RVU scaled by the ratio of the service's indirect and direct shares, which are calculated as the service-level volume-weighted share of costs that are direct and indirect, respectively, across the specialties that provide the service
  - ii. [Indirect basis due to work or clinical labor](#), defined as larger of service-level clinical labor costs rescaled by the direct adjustment, and physician work RVUs<sup>3</sup>. This part of indirect allocator is reduced

<sup>2</sup> References in parentheses are used in the algebraic representation found in Table 1.

<sup>3</sup> For services billable with Modifiers 26 and TC, this part of the indirect allocator is the SUM of work and scaled clinical labor for the unmodified, or global, case, since its RVUs are the sum of the two modified cases. The Modifier=26 case will have this part of allocator equal to work and the Modifier=TC case will have the scaled clinical labor.

- by 50 percent for facility-based services.
- b. Calculate [scaled indirect allocator](#) prior to adjustment due to specialty mix, by rescaling the indirect base by the ratio of the target indirect pool to the volume-weighted sum of the indirect base.
- c. Develop [service-level indirect practice cost index](#) as the service's volume-weighted average of the specialty-specific indirect practice cost index.
  - i. Calculate a specialty-specific [indirect cost scalar](#) as the ratio of their respective indirect target pool based on time-volume weighted PE per hour to the volume-weighted sum of their scaled indirect allocator and a national scalar of the same two pools across all specialties
  - ii. Calculate [specialty indirect practice cost index](#) as the ratio of each specialty's scalar to the national scalar.
  - iii. Calculate [service indirect practice cost index](#) as the volume-weighted average of specialty indirect practice cost index
- d. Calculate [preliminary indirect PE RVU](#) as the product of the scaled indirect allocator and service indirect practice cost index and adjust value for services eligible for the **cognitive services floor**:
  - i. For eligible services, establish [cognitive service floor](#) as the service's work RVU times the ratio of preliminary indirect PE RVU for HCPCS 99213 to work RVU for HCPCS 99213
  - ii. If [cognitive service floor](#) is greater than the preliminary indirect PE RVU, increase the preliminary indirect PE RVU by a quarter of the difference between the preliminary indirect PE RVU and the cognitive service floor
- e. Create [indirect PE RVU](#) by rescaling the preliminary indirect PE RVU by the ratio of the initial target indirect RVU pool and the volume-weighted sum of preliminary indirect PE RVUs

#### D. Create final PE RVU

- a. Calculate the [pre-transition PE RVU](#) for each service as the sum of the preliminary direct RVU and preliminary indirect RVU, rescaled to ensure that the volume-weighted sum equals the target PE RVU pool.
- b. Calculate the difference between the pre-transition total RVU, i.e., the sum of proposed work, pre-transition PE, and MP, and 81 percent of the service's current total RVU.
  - i. If the pre-transition total RVU is less than 81 percent of the current total RVU, the transition policy applies: set [final PE RVU](#) equal to pre-transition PE plus this difference in total RVUs
  - ii. For all other services, set [final PE RVU](#) equal to the pre-transition PE RVU

rescaled to account for the RVUs added to services that had their values increased due to the transition policy.

The final section of this memo provides more details about the calculations described above in the context of the service-level PUF that shows the steps in deriving values for several services.

## Details of Key Calculations

The Example Calculation PUF that is released with each PFS NPRM and FR shows each step in the calculation for selected codes, with reference to the corresponding steps in the PE algorithm as described in the *Federal Register*. Because it is designed to show service-level values, the calculations described above that involve summing across services, whether to the specialty or national level, are not shown but their resulting values are reported. The table includes footnotes for these lines that describe the relevant calculation. This section presents a more detailed description of the various calculations that are not explicitly shown in that PUF. In particular, it presents an algebraic representation of those calculations.

This table presents the PE RVU algorithm described above in more technical detail. The first column of the table refers to the approach as described above and the second refers to the algorithm as described by CMS in the annual fee schedule rule announcement in the Federal Register, an excerpt of which is included as an Appendix.

**Table 1: Detailed Description of CMS PE RVU Algorithm based on FR2026 Policies**

This table refers to both the above description of the algorithm and the Example PUF elements. Please note that the terminology used in the text above and Table 1 may differ slightly from that in the Example PUF. This deviation was necessary to clarify some of the intermediary steps present in the methodology but not explicitly called out in the PUF.

The equations below use the following subscripts:

$h$  denotes a particular service at the HCPCS level, with a total of  $n$  in the target year and  $m$  in the current year

$f$  denotes a particular service at the HCPCS MOD FACILITY level, with a total of  $w$  in the target year and  $v$  in the current year

$s$  denotes a particular specialty, with a total of  $j$  specialties

$t$  denotes the time period – since most calculations are with regard to the target period ( $t+1$ ), that subscript is NOT used; the subscript  $t$  is only used to identify the few instances when values from current period are used

| A: CREATE TOTAL, DIRECT, AND INDIRECT PE RVU POOLS |                         |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               |
|----------------------------------------------------|-------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Step in Above Description                          | Step in the Example PUF |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               |
| Aa                                                 | -                       | <p><b>Goal:</b> Establish <a href="#">Total Target PE RVU Pool</a></p> <p><b>Approach:</b> Multiply each service's current PE RVU and its total volume and sum these across all services; multiply this pool by the ratio of volume-weighted target work RVUs to current volume-weighted work RVUs</p> <p><b>Target PE RVU Pool</b> = Base PE RVU Pool <math>\times</math> Work Pool Ratio</p> $\text{Base PE RVU Pool} = \sum_{f=1}^v \text{PE RVU}_{f,t} \times \text{Volume}_{f,t}$ $\text{Work Pool Ratio} = \frac{\sum_{f=1}^w \text{Work RVU}_f \times \text{Volume}_f}{\sum_{f=1}^v \text{Work RVU}_{f,t} \times \text{Volume}_{f,t}}$ |

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| Ab                                                       | -   | <p><b>Goal:</b> Establish the <a href="#">share of the Target PE RVU pool</a> that is due to direct costs, based on specialty cost/hr data and create the Direct PE RVU pool</p> <p><b>Approach:</b> Create pool of all direct costs incurred as the product of each service's physician time, volume, and direct PE cost for the specialty that provided it and divide this by the pool of all costs incurred based on total PE costs/hour</p> $\text{Direct PE Share} = \frac{\text{Total Direct PE Costs}}{\text{Total PE Cost}} = \frac{(\sum_{s=1}^j (\sum_{h=1}^n (\frac{\text{Time}_h}{60} \times \text{Volume}_{s,h}) \times \text{Direct PE Costs per Hour}_s))}{(\sum_{s=1}^j (\sum_{h=1}^n (\frac{\text{Time}_h}{60} \times \text{Volume}_{s,h}) \times \text{Total PE Costs per Hour}_s))}$ |
| Ac                                                       | -   | <p><b>Goal:</b> Create the <a href="#">Target Direct and Indirect PE RVU pools</a></p> <p><b>Approach:</b> Calculate Direct Pool as percent of Total Pool; create Indirect Pool as different between Total and Direct Pools</p> $\text{Target Direct PE RVU Pool} = \text{Direct PE Share (Ab)} \times \text{Target PE RVU Pool (Aa)}$ $\text{Target Indirect PE RVU Pool} = \text{Target PE RVU Pool (Aa)} - \text{Target Direct PE RVU Pool}$                                                                                                                                                                                                                                                                                                                                                         |
| <b>STEP B: ALLOCATION OF DIRECT POOL ACROSS SERVICES</b> |     |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
| Ba                                                       | (4) | <p><b>Goal:</b> Create <a href="#">service-level estimate of direct PE cost</a></p> <p><b>Approach:</b> Sum the three direct cost elements from the Direct Practice Expense Inputs (DPEI) database for each service</p> $\text{Direct PE Cost}_f = \text{Clinical Staff}_f + \text{Medical Supplies}_f + \text{Medical Equipment}_f$                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |

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| Bb                                                  | (5),(9),<br>(14) | <p><b>Goal:</b> Calculate adjusted <a href="#">direct PE RVUs</a></p> <p><b>Approach:</b> Multiply service-level direct costs by the Direct Scaling Adjustment and divide by the conversion factor</p> $\text{Direct PE RVU}_f = \frac{\text{Adjusted Direct Cost}_f}{\text{Conversion Factor}_t}$ $\text{Adjusted Direct Cost}_f = \text{Direct PE Cost}_f(\text{Ba}) \times \text{Direct Scaling Adjustment}$ $\text{Direct Scaling Adjustment(DSA)} = \frac{\text{Target Direct PE Cost Pool}}{\text{Total Direct PE Costs}}$ $\text{Total Direct PE Costs} = \sum_{f=1}^w \text{Direct PE Costs}_f(\text{Ba}) \times \text{Volume}_f$ |
| STEP C: ALLOCATION OF INDIRECT POOL ACROSS SERVICES |                  |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |
| Ca                                                  | (16),<br>(17)    | <p><b>Goal:</b> Establish <a href="#">service-level indirect allocation basis</a></p> <p><b>Approach:</b> Sum the two parts of the indirect allocator: (i)directs adjusted by ratio of indirect share of PE to direct share of PE and (ii) indirect basis due to work or clinical labor.</p> $\begin{aligned} \text{Indirect Allocator}_f &= \text{Indirect Basis due to Direct Costs}_f(\text{Cai}) \\ &+ \text{Indirect Basis due to Work or Clinical Labor}_f(\text{Caii}) \end{aligned}$                                                                                                                                              |

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|    |               | <p>i. <a href="#">Indirect basis due to direct costs</a>: multiply service-level directs by the ratio of the service's indirect to direct shares</p> $\text{Indirect Basis due to Direct Costs}_f = \left( \text{Direct PE RVU}_f(Bb) \times \frac{\text{Indirect Cost } \%_h}{\text{Direct Cost } \%_h} \right)$ $\text{Indirect Cost } \%_h = \frac{\left( \sum_{s=1}^j \text{Volume}_{h,s} \times \left( \frac{\text{Indirect Costs per hour}_s}{\text{Total Costs per hour}_s} \right) \right)}{\sum_{s=1}^j \text{Volume}_{h,s}}$ $\text{Direct Cost } \%_h = 1 - \text{Indirect Cost } \%_h$ <p>ii. <a href="#">Indirect basis due to work or clinical labor</a></p> $\text{Indirect Basis due to Work or Clinical Labor}_f$ $= \text{Indirect Facility Adjustment} \times \text{Max} \left( \text{Work RVU}_f, \frac{\text{Clinical Labor Costs}_f}{\text{ConversionFactor}_t} \times \text{DSA}(Bb) \right)$ <p>where <i>Indirect Facility Adjustment</i> equals 0.5 for facility services and 1 for nonfacility services</p> <p>*In the case of services billable with TC and 26 modifiers, the global value is based on the SUM rather than MAX of work and scaled clinical labor</p> |
| Cb | (23),<br>(24) | <p><b>Goal:</b> <a href="#">Rescale the indirect allocation</a> basis so that it sums to the Target Indirect PE RVU Pool</p> <p><b>Approach:</b> Calculate the Indirect Scaling Adjustment as the ratio of the Target Indirect RVU Pool (Ac) to the weighted sum of the Indirect Base (Ca) and multiply the Indirect Base for each service (Ca) by this adjustment factor</p> $\text{Scaled Indirect Allocator}_f = \text{Indirect Allocator}_f(Ca) \times \text{Indirect Scaling Adjustment}$ $\text{Indirect Scaling Adjustment} = \frac{\text{Target Indirect PE RVU Pool (Ac)}}{\sum_{f=1}^w \text{Indirect Allocator}_f(Ca) \times \text{Volume}_f}$                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |

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| Cc | (25) | <p><b>Goal:</b> Create <a href="#">service-level indirect practice cost index</a></p> <p><b>Approach:</b> Calculate specialty and national indirect cost scalars as ratio of pooled indirect costs per hour to pooled scaled indirect allocator to create specialty-level indirect cost index; take vol-weighted average of specialty indirect cost index to create service-level index</p> <p>i. <a href="#">Indirect cost scalars</a>: by specialty and national</p> $\text{Indirect Cost Scalar}_s = \frac{\sum_{f=1}^w \text{Volume}_{f,s} \times \text{Time}_f \times \text{Indirect Costs per Hour}_s}{\text{ConversionFactor}_t}$ $\text{Indirect Cost Scalar}_{\text{national}} = \frac{\sum_{s=1}^j \frac{\sum_{f=1}^w \text{Volume}_{f,s} \times \text{Time}_f \times \text{Indirect Costs per Hour}_s}{\text{ConversionFactor}_t}}{\sum_{s=1}^j (\sum_{f=1}^w \text{Volume}_{f,s} \times \text{Scaled Indirect Allocator}_f(Cb))}$ <p>ii. <a href="#">Specialty indirect practice cost index</a></p> $\text{Specialty Indirect Practice Cost Index (IPCI)}_s = \frac{\text{Indirect Cost Scalar}_s (Cci)}{\text{Indirect Cost Scalar}_{\text{national}} (Cci)}$ <p>iii. <a href="#">Service indirect practice cost index</a></p> $\text{Service Indirect Practice Cost Index (IPCI)}_h = \frac{\sum_{s=1}^j \text{IPCI}_s (Ccii) \times \text{Volume}_{h,s}}{\sum_{s=1}^j \text{Volume}_{hs}}$ |
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| Cd                                                      | (26),<br>(27)          | <p><b>Goal:</b> Create <a href="#">preliminary indirect PE RVU</a> by adjusting the Scaled Indirect Allocator by the service-level IPCI and adjust, for eligible services, by the cognitive services floor.</p> <p><b>Approach:</b> Multiply the Scaled Indirect Allocator (Cb) by the IPCI (Cc); for eligible services, calculate cognitive services floor based on the ratio of indirect PE to work for HCPCS 99213 and adjust preliminary indirect PE RVU as appropriate</p> <p><b>Preliminary Indirect PE RVU<sub>f</sub></b> = <i>Scaled Indirect Allocator<sub>f</sub> (Cb) × IPCI<sub>h</sub> (Cciii)</i></p> <p>i. <a href="#">For eligible services</a> (on list of eligible services and preliminary PE RVU/work ≤ 0.4, nonfacility setting only):</p> $\text{Cognitive Service Floor}_f = \text{Work RVU}_f \times \frac{\text{Preliminary Indirect PE RVU}_{99213,NF}}{\text{Work RVU}_{99213}}$ <p>ii. <a href="#">If Cognitive Service Floor<sub>f</sub> &gt; Preliminary Indirect PE RVU<sub>f</sub> then</a></p> <p>redefine <b>Preliminary Indirect PE RVU<sub>f</sub></b></p> $= \text{Preliminary Indirect PE RVU}_f + \frac{\text{Cognitive Services Floor}_f - \text{Preliminary Indirect PE RVU}_f}{4}$ |
| Ce                                                      |                        | <p><b>Goal:</b> Create <a href="#">final indirect PE RVU</a></p> <p><b>Approach:</b> Calculate and apply budget neutrality adjustment to preliminary indirect PE RVU</p> <p><b>Final Indirect PE RVU<sub>f</sub></b> = <i>Preliminary Indirect PE RVU<sub>f</sub> (Cdii) × Indirect PE RVU Budget Neutrality Adjustment</i></p> $\text{Indirect PE RVU Budget Neutrality Adjustment} = \frac{\frac{\text{Target Indirect PE RVU Pool (Ac)}}{CF_t}}{\sum_{f=1}^w \text{Volume}_f \times \text{Preliminary Indirect PE RVU}_f (Cd)}$                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |
| <b>STEP D: FINAL SERVICE-LEVEL PRACTICE EXPENSE RVU</b> |                        |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               |
| Da                                                      | (28),<br>(29),<br>(30) | <p><b>Goal:</b> Create <a href="#">pre-transition PE RVU</a></p> <p><b>Approach:</b> Sum the direct (Bb) and indirect (Ce) values to create a preliminary final PE value for each service and then adjust these values to ensure budget-neutrality relative to the Total PE RVU Pool</p> <p><b>Pre Tran PE RVU<sub>f</sub></b> = <i>Budget Neutrality Adjustment Pre Transition × Preliminary Final PE RVU<sub>f</sub></i></p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |



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|           |      | $\text{Budget Neutrality Adjustment Pre Transition} = \frac{\text{Target PE RVU Pool (Aa)}}{\sum_{f=1}^w (\text{Volume}_f \times \text{Preliminary Final PE RVU}_f)}$ $\text{Preliminary Final PE RVU}_f = \left( \text{Direct PE RVU}_f (Bb) + \text{Final Indirect PE RVU}_f (Ce) \right)$                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
| <b>Db</b> | (31) | <p><b>Goal:</b> Establish <a href="#">Final PE RVU</a> that ensures that total RVU is no less than 81 percent of previous total RVU for service</p> <p><b>Approach:</b> Take difference between sum(work RVU, Pre-Transition PE RVU, MP RVU) and .81*(base total RVU) for each service. (i) For any service where the difference is &lt;0, add absolute value of the difference to the Pre-T PE RVU. (ii) Sum total PE RVUs for transitioned services and subtract it from the PE pool, and (iii) rescale all non-transitioned values to the remaining pool, so total PE pool remains correct.</p> <p>(i) <a href="#">If Change in Total RVU Relative to Transition Minimum<sub>f</sub> &gt; 0, transition applies so increase PE,</a></p> $\text{Final PE RVU}_f = \text{Pre Tran PE RVU}_f (Da) + \text{Change in Total RVU Relative to Transition Minimum}_f$ $\text{Change in Total RVU Relative to Transition Minimum}_f = .81 \times \text{Total RVU}_{f,t} - \text{Preliminary Total RVU}_f$ $\text{Preliminary Total RVU}_f = \text{Work RVU}_f + \text{Pre Tran PE RVU}_f (Da) + \text{MP RVU}_f$ <p>(ii) Adjust all non-transition services to preserve pool – denote the number of these services as W-T and those subject to the transition as T in number. Apply adjustment to non-transition codes only to preserve PE pool as well as work-to-PE RVU pool ratio. <a href="#">Create final PE RVUs for non-transition services</a></p> $\text{Final PE RVU}_f = \text{Budget Neutrality Adjustment Post Transition} \times \text{Pre Tran PE RVU}_f (Da)$ $\text{Budget Neutrality Adjustment Post Transition} = \frac{\text{Target PE RVU Pool (Aa)} - \sum_{f=1}^T (\text{Volume}_f \times \text{Final PE RVU}_f (Dbi))}{\sum_{f=1}^{W-T} (\text{Volume}_f \times \text{Pre Tran PE RVU}_f (Da))}$ |

## Proposed Changes in 2027 PFS NPRM

Some of the proposed PFS changes call for changes to the algorithm as it existed for FR2026, described above. This section describes those specific NPRM proposals and the specific changes to elements of the algorithm that they call for. In the 2027 PFS Final Rule, CMS will issue an updated version of this document that incorporates all finalized policies in the algorithm.

The three specific proposals requiring changes to the algorithm as described above are:

- Modifying the second part of the indirect cost allocation basis to reflect the SUM, rather than MAX, of physician work and scaled clinical labor for services that are not billable with technical and professional components and that do not have 10- or 90-day global periods.
- Removing the indirect cost practice index from the calculation of the indirect cost over two years, reducing variation reflected in NPRM27 by 50 percent; and
- Introducing a PE stabilization factor for PE RVUs for services that are not new, revised, or revalued to ensure that the pre-target PE RVU does not change by more than 5 percent relative to the previous year.

| Proposal                                                              | Revised algorithm calculation for NPRM27                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 |
|-----------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| SUM(work, clinical labor)                                             | <p>Ca ii. Indirect basis due to work or clinical labor (excluding codes billable with technical and professional modifiers and 10- and 90-day global period):</p> $\text{Indirect Basis due to Work or Clinical Labor}_f = \text{Indirect Facility Adjustment} \times \text{Sum} \left( \text{Work RVU}_f, \frac{\text{Clinical Labor Costs}_f}{\text{ConversionFactor}_t} \times \text{DSA}(Bb) \right)$ <p>*In the case of services billable with TC and 26 modifiers, values for these modifiers are based on the MAX (not SUM) of work and scaled clinical labor</p> |
| Reflect half of IPCI variation                                        | <p>Cc ii. Specialty indirect practice cost index</p> $\text{Specialty Indirect Practice Cost Index (IPCI)}_s = 1 + .5 * \left( \frac{\text{Indirect Cost Scalar}_s (\text{Cci})}{\text{Indirect Cost Scalar}_{\text{national}} (\text{Cci})} - 1 \right)$                                                                                                                                                                                                                                                                                                                |
| Limit PE change to 5 percent, except new, revised, and revalued codes | <p>Da Additional element to adjust Pre Transition PE RVU as necessary, if new value is more than 5 percent larger or smaller than current year's value</p> <p><i>if Pre Tran PE RVU<sub>f,t+1</sub> &lt; 0.95 × Pre Tran PE RVU<sub>f,t</sub></i><br/> <i>then Pre Tran PE RVU<sub>f,t+1</sub> = 0.95 × Pre Tran PE RVU<sub>f,t</sub></i></p> <p><i>if Pre Tran PE RVU<sub>f,t+1</sub> &gt; 1.05 × Pre Tran PE RVU<sub>f,t</sub></i><br/> <i>then Pre Tran PE RVU<sub>f,t+1</sub> = 1.05 × Pre Tran PE RVU<sub>f,t</sub></i></p>                                         |



## APPENDIX A: Example Calculation of PE RVUs for Selected Services

Every PFS Notice of Proposed Rulemaking and Final Rule includes a Public Use File (PUF) that shows the calculation of PE RVUs for several codes. An example of this table is included here for reference. It was taken from the 2026 NPRM that was issued in July 2025; it only includes the first few codes due to space constraints.

| CALCULATION OF PE RVUS UNDER METHODOLOGY FOR SELECTED CODES |            |                        |                 |                                              |                                                |
|-------------------------------------------------------------|------------|------------------------|-----------------|----------------------------------------------|------------------------------------------------|
|                                                             | Step       | Source                 | Formula         | 99213<br>Office visit,<br>est<br>Nonfacility | 33533<br>CABG, arterial,<br>single<br>Facility |
| (1) Labor cost (Lab)                                        | Step 1     | AMA                    |                 | 19.44                                        | 115.50                                         |
| (2) Supply cost (Sup)                                       | Step 1     | AMA                    |                 | 5.54                                         | 14.52                                          |
| (3) Equipment cost (Eqp)                                    | Step 1     | AMA                    |                 | 0.34                                         | 1.10                                           |
| (4) Direct cost (Dir)                                       | Step 1     |                        | =(1)+(2)+(3)    | 25.31                                        | 131.10                                         |
| (5) Direct Scaling<br>Adjustment (Dir. Adj.)                | Steps 2-4  | See footnote*          |                 | 0.4242                                       | 0.4242                                         |
| (6) Adjusted Labor                                          | Steps 2-4  | =Labor * Dir Adj       | =(1)*(5)        | 8.25                                         | 49.00                                          |
| (7) Adjusted Supplies                                       | Steps 2-4  | =Eqp * Dir Adj         | =(2)*(5)        | 2.35                                         | 6.16                                           |
| (8) Adjusted Equipment                                      | Steps 2-4  | =Sup * Dir Adj         | =(3)*(5)        | 0.14                                         | 0.47                                           |
| (9) Adjusted Direct                                         | Steps 2-4  |                        | =(6)+(7)+(8)    | 10.74                                        | 55.63                                          |
| (10) Conversion Factor<br>(CF)                              | Step 5     | PFS                    |                 | 32.3465                                      | 32.3465                                        |
| (11) Adj. labor cost<br>converted                           | Step 5     | =(Lab * Dir<br>Adj)/CF | =(6)/(10)       | 0.25                                         | 1.51                                           |
| (12) Adj. supply cost<br>converted                          | Step 5     | =(Sup * Dir<br>Adj)/CF | =(7)/(10)       | 0.07                                         | 0.19                                           |
| (13) Adj. equipment cost<br>converted                       | Step 5     | =(Eqp * Dir<br>Adj)/CF | =(8)/(10)       | 0.00                                         | 0.01                                           |
| (14) Adj. direct cost<br>converted                          | Step 5     |                        | =(11)+(12)+(13) | 0.33                                         | 1.72                                           |
| (15) Work RVU                                               | Setup File | PFS                    |                 | 1.30                                         | 32.91                                          |
| (16) Dir_pct                                                | Steps 6,7  | Surveys                |                 | 0.25                                         | 0.17                                           |
| (17) Ind_pct                                                | Steps 6,7  | Surveys                |                 | 0.75                                         | 0.83                                           |
| (18) Ind. Alloc. Formula<br>(1st part)                      | Step 8     | See Step 8             |                 | (14)/(16)*(17)                               | (14)/(16)*(17)                                 |
| (19) Ind. Alloc.(1st part)                                  | Step 8     |                        | See 18          | 1.01                                         | 8.30                                           |
| (20) Ind. Alloc. Formula<br>(2nd part)                      | Step 8     | See Step 8             |                 | (15)                                         | (15)                                           |
| (21) Ind. Alloc.(2nd part)                                  | Step 8     |                        | See 20          | 1.30                                         | 16.45                                          |
| (22) Indirect Allocator (1st<br>+ 2nd)                      | Step 8     |                        | =(19)+(21)      | 2.31                                         | 24.75                                          |

|                                                                          |             |                           |            |        |        |
|--------------------------------------------------------------------------|-------------|---------------------------|------------|--------|--------|
| (23) Indirect Scaling Adjustment (Ind. Adj.)                             | Steps 9-11  | See Footnote**            |            | 0.4476 | 0.4476 |
| (24) Adjusted Indirect Allocator                                         | Steps 9-11  | =Ind Alloc * Ind Adj      |            | 1.03   | 11.08  |
| (25) Ind. Practice Cost Index (IPCI)                                     | Steps 12-16 | See Footnote***           |            | 1.13   | 0.92   |
| (26) Adjusted Indirect                                                   | Step 17     | = Adj.Ind Alloc * PCI     | =(24)*(25) | 1.17   | 10.23  |
| (27) Adjusted Indirect for high work/low direct PE office-based services | Step 17 Cog | See Footnote****          |            | 1.16   | 10.13  |
| (28) Sum of Direct and Indirect PE                                       | Step 18     | =Adj Dir + Adj Ind        | =(14)+(27) | 1.48   | 11.85  |
| (29) Budget Neutrality Adjustment (BN Adj.)                              | Step 18     |                           |            | 0.9975 | 0.9975 |
| (30) Adjusted Sum of Direct and Indirect PE                              | Step 18     |                           | =(28)*(29) | 1.48   | 11.82  |
| (31) Final PE RVU (with Phase-In)                                        | Step 19     | Apply Phase-In Transition |            | 1.46   | 11.66  |

Notes: 1) PE RVUs may not match Addendum B due to rounding. 2) The use of any particular conversion factor (CF) to illustrate the PE Calculation has no effect on the resulting RVUs, because the same conversion factor is used to calculate the direct and indirect scaling adjustments.

\*The direct adj = [current pe rvus \* CF \* avg dir pct]/[sum direct inputs] = [step2]/[step3]

\*\*The indirect adj = [current pe rvus \* avg ind pct]/[sum of ind allocators] = [step9]/[step10]

\*\*\* Step 12: Volume-weighted sum of [Step11] across all services within the specialty

Step 13: Volume-weighted sum of specialty indirect PE/HR\*service MD\_TIME, across all services within the specialty

Step 14: (a) for each specialty: [Step13]/[Step 12] (b) national: (sum of [Step13] across all specialties)/(sum of [Step 12] across all specialties)

Step 15: for each specialty: [Step 14a]/[Step 14b]

Step 16: for each service, average of [Step 15] for all specialties that provide service, weighted by the volume of the service that the specialty provides and divided by the service's total volume across all specialties

\*\*\*\* The adjusted high work/low direct PE office-based services has two steps: (A) Indirect PE Floor = Work RVU\* [Ratio of Indirect PE to work RVU for CPT 99213] = step15\*[step17 CPT 99213/step15 CPT 99213], (B) Indirect PE Adjustment = Indirect PE + [Indirect PE Floor - Indirect PE]/4 = step17a + [Indirect PE Floor-step17]/4

Note: The use of any particular conversion factor (CF) to illustrate the PE Calculation has no effect on the resulting RVUs.

SOURCE: <https://www.cms.gov/medicare/payment/fee-schedules/physician/federal-regulation-notice/cms-1832-p>