DEPARTMENT OF HEALTH & HUMAN SERVICES
Centers for Medicare & Medicaid Services
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CENTERS FOR MEDICARE & MEDICAID SERVICES

TO: All Fiscal Intermediaries (FIs), Part A and Part B Medicare Administrative Contractors (A/B MACs), and Section 1886(d) Providers (i.e., Providers Paid under Medicare's Hospital Inpatient Prospective Payment System (IPPS))

SUBJECT: Guidance for Determining Defined Benefit Pension Plan Costs for the Federal Fiscal Year (FY) 2016 Wage Index

This following provides guidance for developing pension cost for the wage index. **We have also provided a spreadsheet (that is consistent with these instructions/guidance) to assist hospitals and FIs/MACs in developing pension costs for the FY 2016 wage index.** Commencing with cost reporting periods used for the FY 2013 wage index, the cost to be included in the wage index for defined benefit pension plans shall be determined in accordance with the policy adopted in the FY 2012 IPPS final rule (CMS-1518-F; 76 FR 51586 – 51590, August 18, 2011) and as discussed below. The FY 2016 wage index will be computed using wage data from cost reporting periods beginning during FY 2012 (that is, cost reporting periods beginning on or after October 1, 2011 and before October 1, 2012).

Policy

Defined Benefit Pension Plan: A defined benefit pension plan is a type of deferred compensation plan, which is established and maintained by the employer primarily to provide systematically for the payment of definitely determinable benefits to its employees usually over a period of years, or for life, after retirement. Pension plan benefits are generally measured by, and based on, such factors as age of employees, years of service, and compensation received by employees. This section applies only to defined benefit pension plans which meet the applicable requirements for a qualified pension plan under Section 401(a) of the Internal Revenue Code. A qualified pension plan is for the exclusive benefit of employees or their beneficiaries and qualifies for special tax benefits, such as tax deferral of employer contributions.

Pension Contributions: Pension costs for a defined benefit pension plan are allowable only to the extent that costs are actually incurred by the provider. Such costs are found to have been incurred only if paid directly to participants or beneficiaries under the terms of the plan or paid to a pension fund which meets the applicable tax qualification requirements under Section 401(a) of the Internal Revenue Code. For purposes of the wage index, provider pension payments shall be measured on a cash-basis without regard to §2305 of PRM, Part I. Payment must be made by check or other negotiable instrument, cash, or legal transfer of assets such as stocks, bonds, real property, etc. A contribution payment shall be deemed to occur on the date it is credited to the fund established for the pension plan, or for provider payments made directly to a plan participant or beneficiary, on the date the provider's account is debited. Contributions made under a pension plan that covers multiple providers or employers shall be allocated on a basis consistent with plan records. If the plan records do not show a separate accounting of the actuarially determined cost estimates, contribution deposits, and/or assets attributable to each participating provider or employer, the allocation basis must represent a reasonable approximation of the funding attributable to each employer.

Source of Documentation for Pension Contributions: Providers are required to obtain contribution data from the pension trustee, insurance carrier, Schedule B or SB of IRS Form 5500, and if applicable, from accounting records showing the allocation of total plan contributions to each participating provider. These records should be maintained as needed for subsequent periods.

Reasonable Compensation: In order for pension costs to be allowable, the benefits payable under the plan (attributable to employer contributions) together with all other compensation paid to the employee must be reasonable in amount.

Defined Benefit Pension Plan Costs for the Wage Index: The annual pension cost to be included in the wage index shall be the average annual employer contributions made by or on behalf of the provider (on a cash basis) to all defined benefit plans covered under this section during the averaging period. Contribution payments must satisfy the allowability requirements outlined above; see "Pension Contributions" and "Reasonable Compensation" above. A reversion of plan assets shall be treated as a negative contribution payment and a negative pension cost resulting from a reversion of plan assets shall offset a provider's other wage related costs.

The averaging period is generally the 36 consecutive calendar month period centered on the midpoint of the cost reporting period used for the wage index (the cost reporting period used for the wage index shall hereafter referred to as the wage index cost reporting period). If the midpoint of the wage index cost reporting period is not the first day of a calendar month, use the first day of the midpoint month or the first day of the following month as the midpoint. The same averaging period must be used for all defined benefit plans sponsored by a provider.

A provider who adopts a new defined benefit pension plan and has no other defined benefit plan in existence during the averaging period may elect to exclude from the averaging period all cost reporting periods ending prior to the date the new plan was adopted. No defined benefit pension cost is reportable for a wage index cost reporting period that is excluded from the averaging period in accordance with this paragraph. An election to claim costs for a newly adopted plan based on an averaging period of less than 36 months must be applied on a consistent basis for all wage index cost reporting periods for which the 36 month averaging period contains the plan effective date.

If the wage index cost reporting period does not represent a 12 month period, the annual pension cost otherwise determined in accordance with this section shall be prorated to reflect the number of months in the wage index cost reporting period.

NOTE: For the FY 2013 through FY 2022 wage index only, a provider may include a prefunding installment as a component of pension cost regardless of whether or not the plan(s) which gave rise to the prefunding balance are still in existence. The annual prefunding installment shall equal 1/10th of the prefunding balance. A prefunding installment that is not reflected in the pension cost for a wage index cost reporting period may not be reassigned and added to the pension cost reported for wage index purposes in any subsequent period. The prefunding balance equals the excess, if any, of (i) provider contributions made (on a cash-basis) to its defined benefit pension plans during the look-back period over (ii) the pension costs included in the wage-index for the same look-back period. A provider's share of the total contributions made under a pension plan that covers multiple providers or employers shall be determined on a basis consistent with the methodology used to determine the wage index pension costs for the cost reporting periods included in the prefunding balance. The look-back period shall consist of <u>consecutive</u> provider cost reporting periods commencing no earlier than October 1, 2002 and ending with the provider's cost reporting period immediately prior to the FY 2013 wage index cost reporting period. The look-back period may not include any cost reporting period for which the provider is unable to provide documentation of the contributions made or the pension costs included in the wage index; all prior cost reporting periods must also be excluded in order to satisfy the requirement that the look-back period consist of consecutive cost reporting periods. A provider who establishes a prefunding balance must submit documentation to the Medicare Contractor to support the calculation of the prefunding balance and annual prefunding installment.

Note: If a Pension Prefunding Worksheet was prepared for FY 2013, 2014 or 2015, providers should not complete a new Pension Prefunding Worksheet for FY 2016 unless they are revising the FY 2013, 2014 or 2015 prefunding worksheet along with supporting documentation.

Examples

Example 1 (prefunding balance and prefunding installment):

- *Provider's FY 2016 wage index cost reporting period is 01/01/2012-12/31/2012. The look-back period is subject up until cost reports used for the FY 2013 wage index. Therefore the look back period ends with the cost reporting period ending 12/31/2008 (immediately prior to the FY 2013 wage index cost reporting period.) Assuming the provider has always reported costs on a calendar year basis, the earliest possible cost reporting period in the look-back period is the period commencing 01/01/2003 (first cost reporting period commencing on or after 10/01/2002).*

- *The provider is able to document its pension contributions (on a cash basis) and the pension costs included in the wage index for all cost reporting periods except for the 2004 year. Therefore, 2004 and all prior cost reporting periods must be excluded from the look-back period. The data for 2005 through 2008 is as follows:*

Cost Reporting Year	*Cash Basis Contributions*	*Wage-Index Pension Costs*
2005	*$400,000*	*$500,000*
2006	*$800,000*	*$0*
2007	*$0*	*$600,000*
2008	*$650,000*	*$700,000*

- *Because the pension cost reported in the wage index for 2005 was higher than the cash contributions made during that same period, the provider may elect to drop 2005 (and all prior periods) from the look-back period.*

- *Although the contributions made in 2007 were also less than the pension cost reported for that same period, the provider cannot exclude 2007 without also excluding 2006 (look-back period must consist of consecutive cost reporting periods).*

- *Although the contributions made in 2008 were less than the pension cost reported in that same period, the provider cannot exclude 2008 since the look-back period must end with 2008 because that is the cost reporting period immediately prior to the FY 2013 wage index cost reporting period.*

- *The prefunding balance based on a 2006-2008 look-back period is $150,000*

($1,450,000 [$800,000+$0+$650,000] total contributions - $1,300,000 [$0 + $600,000 + $700,000] in wage index pension costs reported for the same period). The annual prefunding installment is $15,000 (1/10th of $150,000).

Example 2 (pension cost for a 12 month wage index cost reporting period):

- *Provider's FY 2016 wage index cost reporting period is 12 months (01/01/2012 – 12/31/2012); the midpoint of wage index cost reporting period is 07/01/2012; the 36 month averaging period is 01/01/2010 to 12/31/2012 (begins 18 months prior to midpoint and ends 18 months following the midpoint).*

- *Contributions made in wage index cost reporting period 01/01/2012 – 12/31/2012 = $500,000.*

- *Contributions made during 01/01/2011 – 12/31/2011 = $300,000.*

- *Contributions made during 01/01/2013 – 12/31/2013 = $600,000.*

- *Total contributions made during the 36 month averaging period = $1,400,000.*

- *The provider has no prefunding balance or prefunding installment.*

- *The pension cost for the FY 2016 wage index cost reporting period is $466,667 ($1,400,000 total contributions divided by 36 months in the averaging period multiplied by 12 months in the wage index cost reporting period).*

Example 3 (pension cost for a 7 month wage index cost reporting period):

- *Provider's FY 2016 wage index cost reporting period is 7 months (01/01/2012 – 07/31/2012); the midpoint of the wage index cost reporting period is 04/15/2012; since the midpoint must be adjusted to the first of the month (either preceding or following); the provider elects to use 04/01/2012 as the midpoint; the 36 month averaging period is 10/01/2010 to 09/30/2013 (begins 18 months prior to midpoint and ends 18 months following the midpoint).*

- *Contributions made in wage index cost reporting period 01/01/2012 – 07/31/2012 = $300,000.*

- *Contributions made during 10/01/2010 – 12/31/2011 = $500,000.*

- *Contributions made during 08/01/2012 – 09/30/2013 = $600,000.*

- *Total contributions made during the 36 month averaging period = $1,400,000.*

- *The provider has documented a prefunding balance of $1,000,000; the annual prefunding installment is therefore $100,000 (1/10th of prefunding balance).*

- *The pension cost for the FY 2016 wage index cost reporting period is $330,555 ($272,222 average pension cost [$1,400,000 total contributions divided by 36 months in the averaging period multiplied by 7 months in the in wage index cost reporting period] plus $58,333 pro-rata prefunding installment [$100,000 annual prefunding installment multiplied by 7/12ths to reflect a 7 month wage index cost reporting period]).*

Example 4 (pension cost for a new plan):

- *Provider's FY 2016 wage index cost reporting period is 12 months (01/01/2012 – 12/31/2012); the midpoint of the wage index cost reporting period is 07/01/2012; the 36 month averaging period is 01/01/2011 to 12/31/2013 (begins 18 months prior to midpoint and ends 18 months following the midpoint).*

- *The provider adopted a new pension plan effective 07/01/2012 and had no other pension plan in effect prior to that date; there is therefore no prefunding balance or prefunding installment.*

- *Contributions made during 01/01/2011 – 12/31/2011 =$0 (no plan in existence)*

- *Contributions made in the wage index cost reporting period 01/01/2012 – 12/31/2012 = $500,000.*

- *Contributions made during 01/01/2013 – 12/31/2013 = $1,200,000.*

- *Total contributions during the 36 month averaging period = $1,700,000.*

- *The provider did not report a pension cost attributable to the new plan based on a 36 month averaging period during any prior wage index cost reporting period, therefore it may elect to exclude cost reporting periods ending prior to the 07/01/2012 plan effective date from the averaging period; the 36 month averaging period is therefore shortened to 24 months and excludes the period 01/01/2011 to 12/31/2011. The pension cost for the FY 2016 wage index cost reporting period would then be $850,000 ($1,700,000 total contributions divided by 24 months in the averaging period multiplied by 12 months in the wage index reporting period).*

- *Alternatively, the provider may have reported a pension cost for the FY 2015 wage index (2011 wage index cost reporting period) based on a full 36 month averaging period of 01/01/2010 to 12/31/2012. The pension cost for that prior period would have been $166,667 ($500,000 total contributions divided by 36 month averaging period, multiplied by 12 months in wage index cost reporting period). If the provider reported a pension cost for the new plan based on a full 36 month averaging period for the FY 2015 wage index, it must also compute pension costs for the FY 2016 wage index (2012 wage index cost reporting period) using a 36 month averaging period. The pension cost for the 2012 wage index cost reporting period is $566,667 ($1,700,000 total contributions divided by 36 months in averaging period, multiplied* *by 12 months in the wage index cost reporting period).*

NOTE: Fees paid to external organizations (for example, actuarial fees, claim administration fees, IRS form preparation fees) for providing services that are directly associated with a provider's wage-related costs, including a provider's defined benefit pension plan(s), may be included in wage-related costs on Worksheet S-3, Part II for the period in which the expense is incurred (see Form CMS-339, Exhibit 6, Line 6). Such expenses are to be reported as additional costs only if they are paid directly by the provider and NOT out of the plan assets.