

Next Generation ACO Model Financial Operations Overview of Benchmarking Method for Performance Years 4 & 5

March 23, 2018

Revision: 1.01.11

Document Number: RTI.NGACO.BNCH.PY4.1.01.11
Contact Number: HHSM-500-2014-0037I/HHSM-500-T0001

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Acronyms

ACO	Accountable Care Organization
CMMI	Center for Medicare & Medicaid Innovation
CMS	Centers for Medicare & Medicaid Services
NGACO	Next Generation ACO

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1.0 Introduction

This document provides a non-technical description of the methods that will be used by the Next Generation Accountable Care Organization (NGACO) Model to calculate the expenditure benchmarks in Performance Years 4 & 5.

The refinements in the methods used to calculate the benchmark are intended to accomplish several objectives:

1. Recognize attained performance of the NGACO during the baseline period.
2. Increase the reliability of the NGACO baseline and the measurement of attained performance.
3. Increase the comparability of the beneficiaries aligned to the NGACO in the performance-year and base year(s).
4. Strengthen incentives for participation in an ACO over the long run.
5. Preserve incentives for participation in the NGACO model by organizations with both high and low baseline costs.
6. More fully recognize regional differences in expenditure growth in the benchmark.
7. Allow the NGACO to participate in savings achieved by reducing expenditures incurred by beneficiaries incurring very high costs.
8. Strengthen incentives to improve quality of care.

An additional objective is to reduce uncertainty as to developing financial performance over the course of the performance year.

2.0 Overview of Principal Features

The Performance Year 4 (PY4) Benchmark will include an adjustment that reflects the attained performance of the NGACO during a 2-year baseline period. Conceptually, the attained performance adjustment will be similar to blending the NGACO's baseline expenditure with the average baseline expenditure in the region served by the NGACO. An NGACO with a baseline expenditure that is less than the average expenditure incurred by beneficiaries in its region will have an amount added to its baseline. An NGACO with a baseline expenditure that is higher than the average expenditure in its region have an amount deducted from its baseline. The maximum upward adjustment to the NGACO's baseline will be 10% of the baseline. The maximum reduction to the NGACO's baseline will be 2% of the baseline.

The PY4 Benchmark will be based on the experience of NGACO-aligned beneficiaries during a 2-year baseline period. The purpose of replacing a single base year with a 2-year baseline period is to increase the reliability of the baseline experience of the NGACO.

The 2-year baseline period used to calculate the NGACO baseline will be the two most recent calendar years for which experience is complete. The first baseline year, therefore, will be the calendar year three years prior to the performance year. The second baseline year will be the calendar year two years prior to the performance year. The NGACO baseline will be the simple average of the trended baseline expenditure for these two years.

The discount that is applied to the benchmark will depend on the shared savings rate that is selected by the NGACO. The performance-adjusted benchmark will be discounted by 0.5% if an NGACO chooses a shared savings rate of 80%. It will be discounted by 1.25% if an NGACO chooses a shared savings rate of 100%.

The PY4 Benchmark will continue to use a prospective regional trend based on the adjusted United States Per Capita Cost (USPCC).

The PY4 Benchmark will be risk adjusted to reflect the difference between the baseline risk score and the average risk score of the performance-year aligned beneficiaries. A prospective coding adjustment will be applied to performance-year risk scores. The benchmark risk score for the performance year will be not less than 100% and not more than 103% of the baseline risk score.

Under the PY4 financial methodology, the stop-loss arrangement offered by CMS will be modified in four ways. First, it will include a single set of stop-loss attachment points regardless of the benchmark to which the beneficiary accrues experience (i.e., Aged/Disabled or ESRD). Second, multiple attachment points will be established with the percentage of the expenditure that is “ceded” to CMS increasing at each attachment point. Third, the attachment points will be the same whether a beneficiary accrues a single month of experience or 12 months of experience. Forth, the attachment points will be set prospectively and will be adjusted to reflect the geographic adjustments applied by Medicare when calculating provider payments.

Under the PY4 financial methodology, alignment-eligibility and service-area exclusion procedures will be modified to allow an aligned beneficiary to accrue a partial-year of experience. Specifically, a beneficiary will remain aligned and will accrue experience through the last month of continuous eligibility. For example, the fee-for-service experience accrued by a beneficiary who enrolls in a Medicare Advantage plan in August would accrue to the NGACO for months in which the beneficiary was aligned (January through July) and that experience would be included in the financial settlement. The baseline expenditure will, similarly, reflect the experience of beneficiaries with a partial year of eligibility. Partial year eligibility will also apply to beneficiaries excluded by the service area requirements.

2.1 Recognition of Attained Performance

2.1.1 Policy

The PY4 Benchmark will include an adjustment to the baseline that reflects the “attained performance” of the NGACO during the 2-year baseline period. “Attained performance” refers to the difference between the average cost Per Beneficiary Per Month (PBPM) of the NGACO’s baseline aligned beneficiaries and the average cost (PBPM) of all NGACO-eligible beneficiaries living in the area served by the NGACO.

An NGACO with a baseline expenditure that is **less** than the average expenditure incurred by beneficiaries in its region will have an amount added to its baseline. An NGACO with a baseline expenditure that is **higher** than the average expenditure in its region will be required to reduce spending. The **maximum add-on** to the NGACO’s baseline will be 10% of the baseline. The **maximum reduction in** the NGACO’s baseline will be 2% of the baseline.

2.1.2 Illustration

Table 2.1.1 illustrates how the “attained performance” adjustment will work.

Table 2.1.1. Calculation of the NGACO Attained Performance Adjustment to the Baseline

	Case A	Case B	Case C	Case D
National Standardized Operating Cost PBPM ¹	\$800.00	\$800.00	\$800.00	\$800.00
Regional Standardized Operating Cost PBPM ¹	\$768.00	\$832.00	\$832.00	\$768.00
... Regional Standardized Operating Cost Ratio ²	0.9600	1.0400	1.0400	0.9600
NGACO Standardized Operating Cost PBPM ¹	\$721.92	\$782.08	\$881.92	\$814.08
...NGACO Standardized Operating Cost Ratio ³	0.9400	0.9400	1.0600	1.0600
Regional Blend Percentage ⁴	37.00%	33.00%	13.50%	11.50%
Blended Standardized Operating Cost PBPM ⁵	\$738.97	\$798.55	\$875.18	\$808.78
Performance adjustment to NGACO Baseline ⁶	1.0236	1.0211	0.9924	0.9935
Performance adjustment (percentage)	2.36%	2.11%	-0.76%	-0.65%

¹ See Appendix A for a definition of the Standardized Operating Cost. Standardization removes the effect of differences in risk (expected cost) and the geographic adjustments that Medicare applies when calculating fee-for-service provider payments.

² The Regional Standardized Operating Cost PBPM divided by the National Standardized Operating Cost PBPM.

³ The NGACO Standardized Operating Cost PBPM divided by the Regional Standardized Operating Cost PBPM.

⁴ The calculation of the blend percentage is discussed below and in more technical detail in Appendix B.

⁵ The product of the Regional Standardized Operating Cost PBPM and the Regional Blend Percentage plus the product of the NGACO Standardized Operating Cost PBPM and the complement of the Regional Blend Percentage.

⁶ The Blended Standardized Operating Cost PBPM divided by the NGACO Standardized Operating Cost PBPM.

In **Case A** the NGACO is “low cost” (i.e., NGACO Standardized Operating Cost Ratio is less than 1) operating in a “low cost” region (i.e., Regional Standardized Operating Cost Ratio is less than 1).

- The region’s costs are 4% below the national average (\$768.00 is 4% less than \$800.00).
- The NGACO has baseline costs that are 6% below the region (\$721.92 is 6% less than \$768.00).

The “attained performance” adjustment will be calculated by blending 37% of the Regional Standardized Operating Cost with 63% of the NGACO standardized Operating cost, and then dividing the result by the NGACO Standardized Operating Cost. In this case the performance adjustment will increase the NGACO Standardized Baseline by 2.36%.

In **Case B** the NGACO is “low cost” (i.e., NGACO Standardized Operating Cost Ratio is less than 1) operating in a “high cost” region (i.e., Regional Standardized Operating Cost Ratio is greater than 1).

- The region’s costs are 4% above the national average (\$832.00 is 4% higher than \$800.00).
- The NGACO has baseline costs that are 6% below the region (\$782.08 is 6% less than \$832.00).

The “attained performance” adjustment will be calculated by blending 33% of the Regional Standardized Operating Cost with 67% of the NGACO standardized Operating cost, and then dividing the result by the NGACO Standardized Operating Cost. In this case the performance adjustment will increase the NGACO Standardized Baseline by 2.11%.

In **Case C** the NGACO is “high cost” (i.e., NGACO Standardized Operating Cost Ratio is greater than 1) operating in a “high cost” region (i.e., Regional Standardized Operating Cost Ratio is greater than 1).

- The region’s costs are 4% above the national average (\$832.00 is 4% greater than \$800.00).
- The NGACO has baseline costs that are 6% above the region (\$881.92 is 6% is greater than \$832.00).

The “attained performance” adjustment will be calculated by blending 13.5% of the Regional Standardized Operating Cost with 86.5% of the NGACO standardized Operating cost, and then dividing the result by the NGACO Standardized Operating Cost. In this case the performance adjustment will reduce the NGACO Standardized Baseline by 0.76%.

In **Case D** the NGACO is “high cost” (i.e., NGACO Standardized Operating Cost Ratio is greater than 1) operating in a “low cost” region (i.e., Regional Standardized Operating Cost Ratio is less than 1).

- The region’s costs are 4% above the national average (\$768.00 is 4% lower than \$800.00).
- The NGACO has baseline costs that are 6% above the region (\$814.08 is 6% is greater than \$768.00).

The “attained performance” adjustment will be calculated by blending 11.5% of the Regional Standardized Operating Cost with 88.5% of the NGACO standardized Operating cost, and then dividing the result by the NGACO Standardized Operating Cost. In this case the performance adjustment will reduce the NGACO Standardized Baseline by 0.65%.

2.1.3 Implementation

The adjustment to the NGACO standardized baseline will be based on a percentage of the difference between the NGACO’s standardized baseline and the NGACO’s regional standardized baseline. The percentage of the difference that is added to (or deducted from) the NGACO’s standardized baseline will be determined by 1) whether the NGACO’s standardized baseline is above or below the NGACO’s standardized regional baseline and 2) whether the NGACO’s standardized regional baseline is above or below the NGACO standardized national baseline. The national baseline is the average standardized operating cost for all NGACO alignment-eligible beneficiaries.

For an NGACO with a standardized baseline that is **below** the standardized regional baseline, the percentage of the difference that will be added to the NGACO’s baseline will be between 30% and 40%. The percentage will be as high as 40% if the regional standardized baseline is 90% or less of the national standardized baseline, or as low as 30% if the regional standardized baseline is 110% or more of the national standardized baseline.

For an NGACO with a standardized baseline that is **above** the standardized regional baseline, the percentage of the difference that will be deducted from the NGACO’s baseline will be between 10% and 15%. The percentage will be as low as 10% if the regional standardized baseline is 90% or less of the national standardized baseline, or as high as 15% if the regional standardized baseline is 110% or more of the national standardized baseline.

Table 2.1.2 describes the variation in the regional blend percentages under the PY4 method as the NGACO’s standardized operating cost PBPM varies relative to its regional standardized operating cost PBPM.

Table 2.1.2. Regional Blend Percentages used to calculate the Attained Performance Adjustment

	Regional PBPM as percentage of National PBPM ¹				
	≤ 90%	95%	100%	105%	≥ 110%
NGACO PBPM below Region PBPM²					
Regional blend percentage	40%	37.5%	35%	32.5%	30%
Maximum adjustment to baseline	+10%	+10%	+10%	+10%	+10%
NGACO PBPM above Region PBPM²					
Regional blend percentage	10%	11.25%	12.5%	13.75%	15%
Maximum adjustment to baseline	-2%	-2%	-2%	-2%	-2%

¹ The Regional Standardized Operating Cost PBPM as a percentage of the National Standardized Operating Cost PBPM.

² The NGACO Standardized Operating Cost PBPM is above (greater) or below (less) than the Regional Standardized Operating Cost PBPM.

Table 2.1.3 describes the variation in the performance adjustment to the NGACO standardized baseline under the PY4 method as the NGACO's standardized operating cost PBPM varies relative to its regional standardized operating cost PBPM. In practical terms, the attained performance adjustment for the NGACO would increase the NGACO's standardized baseline by 3.89% if a "low cost" NGACO had a standardized baseline equal to 90% of the standardized regional baseline in an "average" region. It would decrease the NGACO's standardized baseline by 1.14% if a "high cost" NGACO had a standardized baseline equal to 110% of the standardized regional baseline in an "average" region.

Table 2.1.3. Regional performance adjustments to the NGACO standardized baseline

	Regional PBPM as percentage of National PBPM ¹				
	≤ 90%	95%	100%	105%	≥ 110%
NGACO PBPM below Region PBPM²					
NGACO 20% below Region	+10.00%	+9.38%	+8.75%	+8.13%	+7.50%
NGACO 15% below Region	+7.06%	+6.62%	+6.18%	+5.74%	+5.29%
NGACO 10% below Region	+4.44%	+4.17%	+3.89%	+3.61%	+3.33%
NGACO 5% below Region	+2.11%	+1.97%	+1.84%	+1.71%	+1.58%
NGACO 2% below Region	+0.82%	+0.77%	+0.71%	+0.66%	+0.61%
NGACO PBPM above Region PBPM²					
NGACO 2% above Region	-0.20%	-0.22%	-0.25%	-0.27%	-0.29%
NGACO 5% above Region	-0.48%	-0.54%	-0.60%	-0.65%	-0.71%
NGACO 10% above Region	-0.91%	-1.02%	-1.14%	-1.25%	-1.36%
NGACO 15% above Region	-1.30%	-1.47%	-1.63%	-1.79%	-1.96%
NGACO 20% above Region	-1.67%	-1.88%	-2.00%	-2.00%	-2.00%

¹ The Regional Standardized Operating Cost PBPM as a percentage of the National Standardized Operating Cost PBPM.

² The NGACO Standardized Operating Cost PBPM is above (greater) or below (less) than the Regional Standardized Operating Cost PBPM.

2.1.2 Rationale

The purpose of recognizing attained performance is to create an incentive for continued participation in an ACO over the long term. By recognizing attained performance, an NGACO that has achieved substantial savings will continue to retain a portion of those savings and will have an incentive for continuous improvements in operational "efficiency". It also creates or preserves an incentive to participate in the program by an organization whose aligned beneficiaries have historically incurred low operating costs.

The requirement that an organization with high historical operating costs achieve savings that are not greater than 2% of the baseline similarly creates an attainable objective for achieving savings that does not discourage participation in the program by an ACO whose aligned beneficiaries have historically incurred above average costs.

This same principle is embodied in the final regulations for the Shared Savings Program that were published in CY2016. The NGACO implementation of that principle reflects the current operational status of the NGACO Model.

Varying the baseline adjustment based on the ratio of the regional standardized baseline to the national standardized baseline is intended to increase the attained performance adjustment for a “low cost” NGACO in a historically “low cost” region and to reduce the attained performance adjustment for a “low cost” NGACO in a historically “high cost” region. Conversely, it is intended to require slightly greater improvements in performance for a “high cost” NGACO in a historically “high cost” region and to require slightly smaller improvements in performance for a “high cost” NGACO in a historically “low cost” region. This variation recognizes that improvements in operating efficiency are likely to be more difficult to achieve in low cost regions, while high cost regions are likely to present more opportunities to improve operating efficiency.

2.2 2-Year Baseline

2.2.1 Policy

The PY4 Benchmark will be based on the experience of NGACO-aligned beneficiaries during a 2-year baseline period. The purpose of replacing a single base year with a 2-year baseline period is to increase the reliability of the baseline experience of the NGACO. The alignment algorithm for the performance year and the two base years will be the same in PY4 and PY5 as in the third performance year.

2.2.2 Rationale

Adopting a 2-year baseline period has two purposes. First, it will increase the stability and reliability of the NGACO benchmark by increasing the number of beneficiaries who contribute experience to the baseline. Second, because the baseline is continuously updated, it means that higher costs incurred in the base by an NGACO that has consistently improved its performance will be partially reflected in the performance period benchmark for two performance years.

The 2-year baseline will be implemented by conducting an alignment for each base year (e.g., CY2016 and CY2017) using the performance-year (e.g., CY2019) Participant list. The average expenditure PBPM for each base year will be risk-standardized, standardized for the impact of the geographic adjustment factors that were used in the base year(s) to calculate fee-for-service provider payments, and trended to the performance year. The NGACO’s 2-year baseline is the simple average of the standardized, trended expenditure PBPM for each base year. The benchmark will then be risk-adjusted and GAF-adjusted to reflect the geographic payment adjustment factors used to calculate fee-for-service payments in the performance year. A schematic overview of 2-year baseline period is included in Appendix C.

2.3 Continuously Updated (Rolling) 2-Year Baseline Period

2.3.1 Policy

The 2-year baseline period used to calculate the NGACO baseline will always be the two most recently completed calendar years. The first baseline year will be the calendar year three years prior to the performance year. The second baseline year will be the calendar year two years prior to the performance year. For example, for PY4, the baseline period will extend from January 1, 2016 to December 31, 2017. The NGACO baseline will be the simple average of the trended baseline expenditure for these two years.

2.3.2 Rationale

The adoption of a 2-year, continuously updated (rolling) baseline period has two purposes. First, it maximizes the comparability of the beneficiaries who are included in the baseline alignment and the beneficiaries who are included in the performance year alignment. Second, it therefore reduces the amount of work that risk adjustment is required to perform.

2.4 NGACO Discount Tied to Shared Savings Rate Election

2.4.1 Policy

The discount that is applied to the NGACO benchmark will depend on the shared savings rate. The performance-adjusted benchmark will be discounted by 0.5% if an NGACO chooses a shared savings rate of 80%. It will be discounted by 1.25% if an NGACO chooses a shared savings rate of 100%.

2.4.2 Rationale

Under the Shared Savings Program, savings achieved by the ACO are shared between the Medicare Trust Funds and the ACO starting with the first dollar of savings (assuming the minimum savings requirement is attained). Under the NGACO model the proportion of the gross savings that accrue to the Medicare Trust Funds is lower than in the SSP. Consequently, if an NGACO electing partial risk sharing achieves the same level of savings as an SSP ACO, a smaller proportion of savings would accrue to the Medicare Trust Funds. If an NGACO assumed full risk, no savings would accrue to the Trust Funds. The discount formula is intended to ensure that the Trust Funds will participate in savings, although it allows a higher proportion of total savings for a highly effective ACO to be retained by the NGACO.

Unlike in the PY3 NGACO benchmarking method, the PY4 method adjusts the NGACO baseline to reflect the attained performance of the NGACO. As a result, it is not necessary to adjust the discount to reflect baseline performance. Similarly, in PY3 the discount was used as the mechanism to recognize quality performance. In the PY4 methods, the quality bonus is handled as a withhold independent of the discount. Therefore, the sole determinant of the discount is whether the NGACO accepts full risk (100% shared savings rate) or partial risk (80% shared savings rate).

2.5 Prospective Trend with Regional GAF Adjustment

2.5.1 Policy

The PY4 Benchmark will continue to use a prospective regional trend based on the adjusted United States Per Capita Cost (USPCC).

2.5.2 Rationale

The prospective trend in the NGACO model will continue to be based on the projected (i.e., prospective) USPCC trend. The national trend will be adjusted to reflect the anticipated impact of changes in the Geographic Adjustment Factors applied by the Medicare Fee-for-Service Payment systems on spending.

It should be noted that risk adjustment will reflect the impact of changing beneficiary characteristics on regional spending. In addition, one benefit of the “rolling baseline” is that it will reflect regional differences in expenditure trends that result from changing utilization and risk.

2.6 Risk Adjustment

2.6.1 Policy

The PY4 Benchmark will be risk adjusted to reflect the difference between the baseline risk score and the average risk score of the performance-year aligned beneficiaries. A prospective coding adjustment will be applied to performance-year risk scores. The benchmark risk score for the performance year will be not less than 100% and not more than 103% of the baseline risk score.

2.6.2 Rationale

The need for risk adjustment will be reduced in the PY4 methods due to the adoption of the “rolling” two-year baseline. As noted above, the use of a continuously updated baseline period increases the comparability of the baseline and the performance year aligned population and therefore reduces the importance of risk adjustment.

Nonetheless, given ongoing changes in information technology, coding practices, and the expanded use of quality measures in calculating provider payments, it is expected that risk scores will continue to increase, reflecting increasingly comprehensive coding on claims. As a result, the PY4 method will continue to include an explicit coding adjustment.

2.7 Stop-Loss Arrangement

2.7.1 Policy

Under the PY4 financial methodology, the stop-loss arrangement offered by CMS will be modified in four ways. First, a single set of stop-loss attachment points will be used regardless of the benchmark to which the beneficiary accrues experience. Second, multiple attachment points will be established with the percentage of the expenditure that is “ceded” to CMS increasing at each attachment point. Third, the attachment points will be the same whether a beneficiary accrues a single month of experience or 12

months of experience. Forth, the attachment points will be set prospectively and will be geographically adjusted.

2.7.2 Rationale

The PY3 stop-loss arrangement has four principal deficiencies. First, it applies a uniform attachment point in all areas, regardless of regional differences in spending resulting from both utilization and Medicare FFS payment policies. Second, the NGACO receives no credit for successful efforts to improve care and manage costs for beneficiaries incurring very high costs. Third, the NGACO has no economic incentive to manage costs or improve care once a beneficiary's annual expenditure exceeds the attachment point. And finally, it is extremely complex determining the attachment point for a beneficiary with varying factors such as mortality or transitions of the beneficiary between the ESRD and Aged & Disabled benchmarks.

The purpose of the refinements in the PY4 stop-loss arrangement is to address all four of these deficiencies and to make it easier for NGACOs to track and understand the impact of the stop-loss arrangement on financial performance.

2.8 Partial Year Experience

2.8.1 Policy

Under the PY4 financial methodology, alignment-eligibility and service-area exclusion procedures will be modified to allow an aligned beneficiary to accrue a partial-year of experience. Specifically, a beneficiary will remain aligned and will accrue experience through the last month of continuous eligibility. For example, the fee-for-service experience accrued by a beneficiary between January and July before the beneficiary enrolled in a Medicare Advantage plan in August would accrue to the NGACO and that experience would be included in the financial settlement. The baseline expenditure will, similarly, reflect the experience of beneficiaries with a partial year of eligibility. Partial year eligibility will also apply to beneficiaries excluded by the service area requirements.

2.8.2 Rationale

Under the PY3 quarterly exclusion process, a beneficiary who becomes ineligible for alignment to the NGACO during the performance year is removed from all financial calculations. For example, a beneficiary who elects to enroll in a Medicare managed care plan mid-way through the year is removed *in toto* from the calculation of the NGACO's shared savings. As a result, the NGACO does not receive credit for its efforts to improve care and manage costs for that beneficiary. In addition, the complete removal of ineligible beneficiaries makes it difficult to track developing financial performance.

Under the PY4 policy, a beneficiary will accrue experience to the NGACO in months when the beneficiary is alignment eligible. Once a beneficiary becomes ineligible, the beneficiary will be removed *prospectively* from the aligned population (e.g., a beneficiary who enrolls in a managed care plan but subsequently returns to traditional Medicare would be removed permanently from the aligned population effective with the month in which the beneficiary enrolled in the managed care plan). These changes will increase the predictive value of the quarterly benchmark reports by reducing the impact of exclusions, particularly the year-end exclusions, on financial performance.

The NGACO will continue to be notified on a quarterly basis of the beneficiaries who have become ineligible and will be provided with data identifying the period of time in which the beneficiary was aligned to and accrued experience to the NGACO.

This change means that there will be two reasons for a beneficiary to have a partial year of experience. The first reason is the death of the beneficiary. The second is the occurrence of an event that terminates the beneficiary's eligibility.

The reasons a beneficiary will lose eligibility will continue to be loss of Part A or Part B coverage, enrollment in a Medicare managed care plan, Medicare not being the primary payer for the beneficiary, residence outside the United States, and moving out of the service area of the NGACO.

2.9 Quality Component

The quality component of the financial methodology for PY4 is under development and will be announced as part of the updated quality strategy for PY4.

Appendix A. Definitions

B.1 Shared Savings Expenditure

The NGACO benchmark applies to the Shared Savings Expenditure incurred by the NGACO. The Shared Savings Expenditure for a covered service is defined as:

1. The Claim Payment made to a provider
2. PLUS: The Budget Sequestration amount that is withheld from the provider payment
3. PLUS: The Population-Based Payment (PBP) Reduction that was applied to the provider payment
4. LESS: Uncompensated Care Payments under the Inpatient Prospective Payment System (IPPS)

The PBP Reduction would occur on claims for services that are subject to PBP or All-Inclusive PBP.

B.2 Operating Cost

The Operating Cost is used to calculate the Attained Performance adjustment to the NGACO benchmark. The Operating Cost is defined as:

1. The Shared Savings Expenditure for a covered service
2. LESS: The Operating Indirect Medical Education (IME) Payment under the IPPS
3. LESS: The Capital IME Payment under the IPPS
4. LESS: The Operating Disproportionate Share Hospital (DSH) Payment under the IPPS
5. LESS: The Capital DSH Payment under the IPPS

The IME and DSH payments occur only on inpatient claims that are paid under the IPPS.

B.3 Standardized Operating Cost PBPM

The Standardized Operating Cost Per Beneficiary Per Month (PBPM) is the Operating Cost PBPM after removing or controlling for the impact of the risk of the beneficiary (or beneficiaries) and removing or controlling for the impact of the Geographic Adjustment Factors (GAFs) that Medicare applies when calculating provider payments.

The difference in the Standardized Operating Cost PBPM for two groups of beneficiaries will not reflect the impact of differences in the average risk (or expected cost) of those beneficiaries or differences in the geographic adjustments that Medicare made to provider payments.

Appendix B. Calculation of the Regional Blend Percentage

The Regional Blend Percentage is a linear interpolation between the minimum and maximum blend percentage based on the Regional Standardized Operating Cost Ratio of the NGACO. The Regional Blend Percentage is given by:

$$B_a = \begin{cases} B_{hiACO}^{loReg} + \left[(B_{hiACO}^{hiReg} - B_{hiACO}^{loReg}) \times \left(\frac{OCR_a^r - OCR_{min}^r}{OCR_{max}^r - OCR_{min}^r} \right) \right], & OCR_a > 1 \\ B_{loACO}^{loReg} + \left[(B_{loACO}^{hiReg} - B_{loACO}^{loReg}) \times \left(\frac{OCR_a^r - OCR_{min}^r}{OCR_{max}^r - OCR_{min}^r} \right) \right], & OCR_a \leq 1 \end{cases}$$

and

$$OCR_a^r = \begin{cases} 0.9, & \frac{SOC_a^r}{SOC^n} < 0.9 \\ \frac{SOC_a^r}{SOC^n}, & 0.9 \leq \frac{SOC_a^r}{SOC^n} \leq 1.1 \\ 1.1, & \frac{SOC_a^r}{SOC^n} \geq 1.1 \end{cases}$$

$$OCR_a = \frac{SOC_a}{SOC_a^r}$$

where:

- B_a = Regional blend percentage for NGACO a
- B_{hiACO}^{hiReg} = Regional blend percentage for a high-cost NGACO in a high-cost Region
- B_{hiACO}^{loReg} = Regional blend percentage for a high-cost NGACO in a low-cost Region
- B_{loACO}^{hiReg} = Regional blend percentage for a low-cost NGACO in a high-cost region
- B_{loACO}^{loReg} = Regional blend percentage for a low-cost NGACO in a low-cost region
- OCR_a^r = Regional Standardized Operating Cost Ratio for NGACO a
- OCR_{min}^r = The minimum Regional Standardized Operating Cost Ratio (0.9)
- OCR_{max}^r = The maximum Regional Standardized Operating Cost Ratio (1.1)
- OCR_a = Standardized Operating Cost Ratio for NGACO a
- SOC_a^r = Regional Standardized Operating Cost PBPM for NGACO a
- SOC^n = National Standardized Operating Cost PBPM

$$SOC_a = \text{Standardized Operating Cost PBPM for NGACO } a$$

Examples are included below to assist in interpreting these formulas.

Table A.1. Assumptions (from Table 2.1.1)

	Case A	Case B	Case C	Case D
National Standardized Operating Cost PBPM	\$800.00	\$800.00	\$800.00	\$800.00
Regional Standardized Operating Cost PBPM	\$768.00	\$832.00	\$832.00	\$768.00
NGACO Standardized Operating Cost PBPM	\$721.92	\$782.08	\$881.92	\$814.08
Regional Standardized Operating Cost Ratio	0.9600	1.0400	1.0400	0.9600
NGACO Standardized Operating Cost Ratio	0.9400	0.9400	1.0600	1.0600
Blend Percentage	37.00%	33.00%	13.50%	11.50%
Preliminary Performance Adjustment	1.0236	1.0211	0.9924	0.9935
Floor on the performance adjustment	0.9800	0.9800	0.9800	0.9800
Ceiling on the performance adjustment	1.1000	1.1000	1.1000	1.1000
Final performance adjustment to NGACO Baseline	1.0236	1.0211	0.9924	0.9935
Final performance adjustment (percentage)	2.36%	2.11%	-0.76%	-0.65%

The calculation of the regional blend percentage for Case A, a low cost NGACO (standardized operation cost PBPM 6% below its region) in a low cost region (standardized operating cost PBPM 4% below the nation), is given by:

$$0.3700 = \left\{ 0.40 + \left[(0.30 - 0.40) \times \left(\frac{0.96 - 0.90}{1.10 - 0.90} \right) \right] \right\}, \quad 0.94 \leq 1$$

The calculation of the regional blend percentage for Case B, a low cost NGACO (standardized operation cost PBPM 6% below its region) in a high cost region (standardized operating cost PBPM 4% above the nation), is given by:

$$0.3300 = \left\{ 0.40 + \left[(0.30 - 0.40) \times \left(\frac{1.04 - 0.90}{0.90 - 1.10} \right) \right] \right\}, \quad 0.94 \leq 1$$

The calculation of the regional blend percentage for Case C, a high-cost NGACO (standardized operation cost PBPM 6% above its region) in a high cost region (standardized operation cost PBPM 4% above the nation), is given by:

$$0.1350 = \left\{ 0.10 + \left[(0.15 - 0.10) \times \left(\frac{1.04 - 0.90}{0.90 - 1.10} \right) \right] \right\}, \quad 1.06 > 1$$

The calculation of the regional blend percentage for Case D, a high-cost NGACO (standardized operation cost PBPM 6% above its region) in a low cost region (standardized operation cost PBPM 4% below the nation), is given by:

$$0.1150 = \left\{ 0.10 + \left[(0.15 - 0.10) \times \left(\frac{0.96 - 0.90}{0.90 - 1.10} \right) \right] \right\}, \quad 1.06 > 1$$

Appendix C. Schematic Overview of 2-year Baseline Period

PY4/Base Year 1		PY4/Base Year 2		PY4
BY1/Alignment Year 1 7/1/2013 – 6/30/2014				
BY1/Alignment Year 2 7/1/2014 – 6/30/2015		BY2/Alignment Year 1 7/1/2014 – 6/30/2015		
		BY2/Alignment Year 2 7/1/2015 – 6/30/2016		
CY2016				
The CY2016 baseline is trended to CY2019 based on the 2016-to-2019 prospective trend		CY2017		PY4/Alignment Year 1 7/1/2016 – 6/30/2017
		The CY2016 baseline is trended to CY2019 based on the 2017-to-2019 prospective trend		PY4/Alignment Year 2 7/1/2017 – 6/30/2018
Projected BY1 Baseline		Projected BY2 Baseline		
				CY2019