

portion of the Federal rate attributable to wage-related costs by a wage index.

The Federal rate also incorporates adjustments to account for facility case-mix, using a classification system that accounts for the relative resource utilization of different patient types. This classification system, Resource Utilization Groups, version III (RUG—III), uses beneficiary assessment data from the Minimum Data Set (MDS) completed by SNFs to assign beneficiaries to one of 44 RUG—III groups. The May 12, 1998 interim final rule (63 FR 26252) included a complete and detailed description of the RUG—III classification system, and a further discussion appears in section II.B of this preamble.

The Federal rates in this proposed rule reflect an update to the rates that we published in the July 31, 2002 **Federal Register** (67 FR 49798) equal to the full change in the SNF market basket index. According to section 1888(e)(4)(E)(ii)(IV) of the Act, for FY 2004, we would update the rate by adjusting the current rates by the full SNF market basket index.

2. Payment Provisions—Initial Transition Period

The SNF PPS included an initial, phased transition from a facility-specific rate (which reflected the individual facility's historical cost experience) to the Federal case-mix adjusted rate. The transition extended through the facility's first three cost reporting periods under the PPS, up to, and potentially including, the one that began in FY 2001. Furthermore, pursuant to section 102 of BBRA, a facility could nonetheless elect to be paid entirely under the Federal rates.

Accordingly, starting with cost reporting periods beginning in FY 2002, we base payments entirely on the Federal rates and, as mentioned previously in this preamble, we no longer include adjustment factors

related to facility-specific rates for the coming fiscal year.

F. Skilled Nursing Facility Market Basket Index

Section 1888(e)(5) of the Act requires us to establish a SNF market basket index that reflects changes over time in the prices of an appropriate mix of goods and services included in the covered SNF services. The SNF market basket index is used to update the Federal rates on an annual basis, and is discussed in greater detail in section III of this preamble.

II. Update of Payment Rates Under the Prospective Payment System for Skilled Nursing Facilities

A. Federal Prospective Payment System

This proposed rule sets forth a schedule of Federal prospective payment rates applicable to Medicare Part A SNF services beginning October 1, 2003. The schedule incorporates per diem Federal rates that provide Part A payment for all costs of services furnished to a beneficiary in a SNF during a Medicare-covered stay.

1. Costs and Services Covered by the Federal Rates

The Federal rates apply to all costs (routine, ancillary, and capital-related costs) of covered SNF services other than costs associated with approved educational activities as defined in § 413.85. Under section 1888(e)(2) of the Act, covered SNF services include post-hospital SNF services for which benefits are provided under Part A (the hospital insurance program), as well as all items and services (other than those services excluded by statute) that, before July 1, 1998, were paid under Part B (the supplementary medical insurance program) but furnished to Medicare beneficiaries in a SNF during a Part A covered stay. (These excluded service categories are discussed in greater detail

in section V.B.2 of the May 12, 1998 interim final rule (63 FR 26295–97)).

2. Methodology Used for the Calculation of the Federal Rates

The proposed FY 2004 rates would reflect an update using the full amount of the latest market basket index. The FY 2004 market basket increase factor is 2.9 percent. Consistent with previous years, this factor may be revised in the final rule when later forecast data are available. For a complete description of the multi-step process, see the May 12, 1998 interim final rule (63 FR 26252). We note that in accordance with section 101(a) of the BBRA and section 314 of the BIPA, the existing, temporary increase in the per diem adjusted payment rates of 20 percent for certain specified RUGs (and 6.7 percent for certain others) remains in effect until the implementation of case-mix refinements. As we discuss elsewhere in this proposed rule, while we are proceeding with our ongoing research in this area, we are not proposing to implement case-mix refinements in this proposed rule.

We used the SNF market basket to adjust each per diem component of the Federal rates forward to reflect cost increases occurring between the midpoint of the Federal fiscal year beginning October 1, 2002, and ending September 30, 2003, and the midpoint of the Federal fiscal year beginning October 1, 2003, and ending September 30, 2004, to which the payment rates apply. In accordance with section 1888(e)(4)(E)(ii)(IV) of the Act, the payment rates for FY 2004 are updated by a factor equal to the market basket index percentage increase to determine the payment rates for FY 2004. The rates would be further adjusted by a wage index budget neutrality factor, described later in this section. Tables 1 and 2 reflect the updated components of the unadjusted Federal rates for FY 2004.

TABLE 1.—UNADJUSTED FEDERAL RATE PER DIEM: URBAN

Rate component	Nursing— case-mix	Therapy— case-mix	Therapy—non- case-mix	Non-case-mix
Per Diem Amount	\$125.15	\$94.27	\$12.42	\$63.87

TABLE 2.—UNADJUSTED FEDERAL RATE PER DIEM: RURAL

Rate component	Nursing— case-mix	Therapy— case-mix	Therapy-non- case-mix	Non-case-mix
Per Diem Amount	\$119.57	\$108.70	\$13.26	\$65.06