

TABLE 2(A).—PROPOSED EXCLUDED HOSPITAL WITH CAPITAL INPUT PRICE INDEX (FY 1997) VINTAGE WEIGHTS

Year from farthest to most recent	Fixed assets (23-year weights)	Movable assets (11-year weights)	Interest: capital-related (23-year weights)
1 .....	0.018	0.063	0.007
2 .....	0.021	0.068	0.009
3 .....	0.023	0.074	0.011
4 .....	0.025	0.080	0.012
5 .....	0.026	0.085	0.014
6 .....	0.028	0.091	0.016
7 .....	0.030	0.096	0.019
8 .....	0.032	0.101	0.022
9 .....	0.035	0.108	0.026
10 .....	0.039	0.114	0.030
11 .....	0.042	0.119	0.035
12 .....	0.044	.....	0.039
13 .....	0.047	.....	0.045
14 .....	0.049	.....	0.049
15 .....	0.051	.....	0.053
16 .....	0.053	.....	0.059
17 .....	0.057	.....	0.065
18 .....	0.060	.....	0.072
19 .....	0.062	.....	0.077
20 .....	0.063	.....	0.081
21 .....	0.065	.....	0.085
22 .....	0.064	.....	0.087
23 .....	0.065	.....	0.090
Total	1.0000	1.0000	1.0000

NOTE: Weights may not sum to 1.000 due to rounding.

Table 2(B) below compares the 1992-based excluded hospital with capital market basket to the proposed 1997-based excluded hospital with capital market basket. As shown below, the rebased and revised market basket grows slightly faster over the 1999 through 2001 period than the 1992-based market basket. The main reason for this growth is the switching of the wage and benefit proxy to the ECI for hospital workers from the previous occupational blend. This revision had a similar impact on the hospital inpatient prospective payment system and excluded hospital market baskets, as described in the final rule published in the **Federal Register** on August 1, 2002 (67 FR 50032 through 50041).

TABLE 2(B).—PERCENT CHANGES IN THE 1992-BASED AND PROPOSED 1997-BASED EXCLUDED HOSPITAL WITH CAPITAL MARKET BASKETS, FYS 1999 THROUGH 2004

Fiscal year	Percent change, 1992-based market basket	Percent change, proposed 1997-based market basket
1999 .....	2.3	2.7

TABLE 2(B).—PERCENT CHANGES IN THE 1992-BASED AND PROPOSED 1997-BASED EXCLUDED HOSPITAL WITH CAPITAL MARKET BASKETS, FYS 1999 THROUGH 2004—Continued

Fiscal year	Percent change, 1992-based market basket	Percent change, proposed 1997-based market basket
2000 .....	3.4	3.1
2001 .....	3.9	4.0
Average historical:	3.2	3.3
2002 .....	2.7	3.6
2003 .....	3.0	3.5
2004 .....	3.0	3.3
Average forecast:	2.9	3.5

Source: Global Insights, Inc., 4th Qtr 2002, @USMARCO.MODTREND@CISSIM/TL1102.SIM. Historical data through 3rd Qtr 2002.

Based upon the analysis mentioned below, we believe the excluded hospital with capital market basket provides a reasonable measure of the price changes facing IPFs. However, we have also been researching the feasibility of developing a market basket specific to IPF services. This research includes analyzing data sources for cost category weights, specifically the Medicare cost reports, and investigating other data sources on cost, expenditure, and price information specific to IPFs.

Our analysis of the Medicare cost reports indicates that the distribution of costs among major cost report categories (wages, pharmaceuticals, and capital) for IPFs is not substantially different from the 1997-based excluded hospital with capital market basket we propose to use. In addition, the only data available to us for these cost categories (wages, pharmaceuticals, and capital) presented a potential problem since no other major cost category weights would be based on IPF data. Based on the research discussed below, at this time, we are not proposing to develop a market basket specific to IPF services.

We conducted an analysis of annual percent changes in the market basket when the weights for wages, pharmaceuticals, and capital in IPFs were substituted into the excluded hospital with capital market basket. Other cost categories were recalibrated using ratios available from the hospital inpatient prospective payment system hospital market basket. On average, between 1995 and 2002, the excluded hospital with capital market basket increased at nearly the same average annual rate (3.4 percent) as the market

basket with IPF weights for wages, pharmaceuticals, and capital (3.5 percent). This difference is less than the 0.25 percentage point criterion that determines whether a forecast error adjustment is warranted under the hospital inpatient prospective payment system update framework.

Based upon this analysis, we believe that the excluded hospital with capital market basket is doing an adequate job of reflecting the price changes facing IPFs. We will continue to solicit comments about issues particular to IPFs that should be considered in our development of the proposed 1997-based excluded hospital with capital market basket, as well as encourage suggestions for additional data sources that may be available. Our hope is that the additional cost data being collected under the proposed IPF prospective payment system will eventually allow for the development of a market basket based primarily on IPF data. We welcome comments on issues particular to IPFs that should be considered in our use of the proposed 1997-based excluded hospital with capital market basket, as well as on suggestions for additional data sources that may be readily available on the cost structure of IPFs.

As discussed more fully in section IV of this proposed rule, we are proposing to implement the proposed IPF prospective payment system for IPF cost reporting periods that begin on or after April 1, 2004. The first update, however, would not be until July 1, 2005. This extends the first year for 3 additional months in order to adjust the update cycle for this proposed payment system. As a result, the effective period for this proposed rule is April 1, 2004 through June 30, 2005. To update payments between FY 2003 and the effective period, the update must reflect the market basket increase over this period, which is currently estimated at 5.3 percent. This would represent the proposed increase in the excluded hospital with capital market basket for FY 2004 and the first 9 months of FY 2005.

#### B. Development of the Proposed Case-Mix Adjustment Regression

In order to ensure that the proposed IPF prospective payment system would be able to account adequately for each IPF's case-mix, we performed an extensive regression analysis of the relationship between the per diem costs and both patient and facility characteristics to determine those characteristics associated with statistically significant cost differences. For characteristics with statistically