

future physician fee schedule updates, including the update for 2003, the SGR was 3.2 percent for FY 1998 and 4.2 percent for FY 1999. This is a change of 1.7 percentage points for FY 1998 and 4.5 percentage points for FY 1999. We will make no further revisions to the SGRs for these years. We are also announcing a 1.6 percent increase to the physician fee schedule CF that will apply from March 1 to December 31, 2003. Therefore, the physician fee schedule CF from March 1 to December 31, 2003, will be \$36.7856, an increase of 1.6 percent from the 2002 CF. The anesthesia CF for this period will be \$17.05, an increase of 2.7 percent from the 2002 anesthesia CF. In our December 31, 2002 final rule (67 FR 80032), we described our calculation of the 2003 physician fee schedule and anesthesia fee schedule CFs. Any information contained in this final rule related to the 2003 physician or anesthesia fee schedule CFs replaces the information contained in the December 31, 2002, final rule. Further, we are making one revision to our estimate of the CY 2002 SGR. As described below, we are increasing our estimate of the 2002 SGR by 0.2 percentage points to reflect the costs of the new diabetes self-management training benefit. All other provisions of the December 31, 2002, final rule are unchanged by this final rule.

In the December 31, 2002, final rule, we specifically requested comments on the revision of estimates used to establish the Medicare Volume Performance Standard from 1990 through 1996 and the SGRs from FY 1998 and FY 1999. We will respond to any comments received on these issues in a future **Federal Register** publication.

## II. Physician Fee Schedule Update

### A. Calculation of the Physician Fee Schedule Update

The physician fee schedule update is determined under a methodology specified by statute. Under section 1848(d)(4) of the Act, the update is

equal to the product of 1 plus the percentage increase in the Medicare Economic Index (MEI) (divided by 100) and 1 plus the update adjustment factor. For CY 2003, the MEI is equal to 3.0 percent (1.030). The update adjustment factor is now equal to -1.1 percent (0.989). Section 1848(d)(4)(F) of the Act requires an additional -0.2 percent (0.998) reduction to the update for 2003. Thus, the product of the MEI (1.030), the update adjustment factor (0.989), and the statutory adjustment factor (0.998) equals the CY 2003 update of 1.66 percent (1.0166). As described below, we are also making an adjustment of -0.04 percent to maintain budget neutrality for the increase in anesthesia work. With the budget-neutrality adjustment, the increase in the physician fee schedule CF will be 1.62 percent (1.0162).

### B. The Update Adjustment Factor

Section 1848(d) of the Act provides that the physician fee schedule update is equal to the product of the MEI and an "update adjustment factor." The update adjustment factor is applied to make actual and target expenditures (referred to in the law as "allowed expenditures") equal. Allowed expenditures are equal to actual expenditures in a base period updated each year by the SGR. The SGR sets the annual rate of growth in allowed expenditures and is determined by a formula specified in section 1848(f) of the Act.

Under section 1848(d)(4)(A) of the Act, the physician fee schedule update for a year is equal to the product of—(1) 1 plus the Secretary's estimate of the percentage increase in the MEI for the year, divided by 100 and (2) 1 plus the Secretary's estimate of the update adjustment factor for the year. Under section 1848(d)(4)(B) of the Act, the update adjustment factor is equal to the sum of the following—

- i. *Prior Year Adjustment Component.* An amount determined by—
  - Computing the difference (which may be positive or negative) between

the amount of the allowed expenditures for physicians' services for the prior year (the year prior to the year for which the update is being determined) and the amount of the actual expenditures for such services for that year;

- Dividing that difference by the amount of the actual expenditures for such services for that year; and

- Multiplying that quotient by 0.75.

#### ii. *Cumulative Adjustment Component.*

An amount determined by—

- Computing the difference (which may be positive or negative) between the amount of the allowed expenditures for physicians' services from April 1, 1996, through the end of the prior year and the amount of the actual expenditures for such services during that period;

- Dividing that difference by actual expenditures for such services for the prior year as increased by the sustainable growth rate for the year for which the update adjustment factor is to be determined; and

- Multiplying that quotient by 0.33.

As explained above, we are making final prospective redeterminations to the FY 1998 and FY 1999 SGRs in this final rule for the purposes of determining future physician fee schedule updates. We are also making prospective redeterminations to allowed expenditures for the period from April 1, 1997, to March 31, 1999, because allowed expenditures during this period are affected by revisions to the FY 1998 and FY 1999 SGRs. Further, allowed expenditures in all subsequent periods are based on allowed expenditures from this period and are also being prospectively redetermined. Table 1 shows annual and cumulative allowed expenditures for physicians' services from April 1, 1996, through the end of the current CY, including the transition period to a CY system that occurred in 1999, incorporating the redeterminations we are making to the SGRs for FY 1998 and FY 1999.

TABLE 1

Period	Annual allowed expenditures (billion)	Cumulative allowed expenditures (billion)	FY or CY SGR (percent)
4/1/96–3/31/97 .....	\$48.9	\$48.9	N/A
4/1/97–3/31/98 .....	50.5	99.4	FY 1998=3.2%
4/1/98–3/31/99 .....	52.6	152.0	FY 1999=4.2%
1/1/99–3/31/99 .....	13.3	( <sup>1</sup> )	FY 1999=4.2%
4/1/99–12/31/99 .....	42.1	( <sup>2</sup> )	FY 2000=6.9%
1/1/99–12/31/99 .....	55.3	194.1	FY 1999/FY 2000 <sup>3</sup>
1/1/00–12/31/00 .....	59.4	253.4	CY 2000=7.3%
1/1/01–12/31/01 .....	62.0	315.5	CY 2001=4.5%
1/1/02–12/31/02 .....	67.6	383.1	CY 2002=9.0%