All Patient Refined Diagnosis Related Group (APR DRG)

Presented by

Carmen A. Lliteras, CPA, CGMA, CHCRS
Consulting Director – Galíndez LLC

Héctor M. Vázquez, CPA, CGMA
Audit Partner – Galíndez LLC

August 7, 2025

Galíndez LLC TRUSTworthy

Member of Nexia

Important Disclaimers

Legal Advice Disclaimer

This presentation does not constitute legal advice. It is intended for informational purposes only and should not be relied upon as a substitute for professional legal counsel. Always consult a qualified attorney regarding your specific legal concerns.

Tax Advice Disclaimer

This presentation does not constitute tax advice. It is intended for informational purposes only and should not be relied upon as a substitute for professional tax advice. Always consult a qualified tax professional regarding your specific tax concerns.

Copyright Disclaimer

Topics to be discussed

- How Did We Get Here?
- Implementation of APR-DRG for IPD Services in Plan Vital
- Key Questions and Answers
- Implementation Schedule
- Recommendations
- Accounting and reporting considerations
- Closing

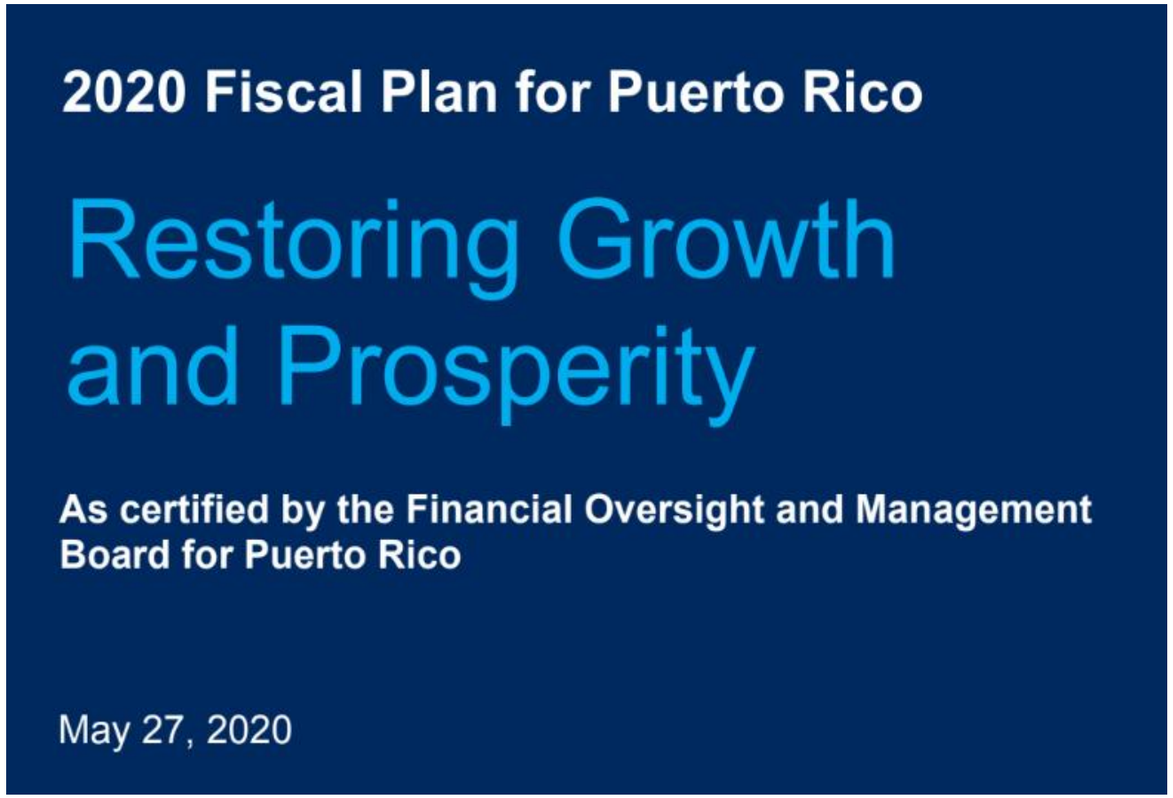
How Did We Get Here?

Introductions – Roles

ASES	ADMINISTRACIÓN DE SEGUROS DE SALUD DE PUERTO RICO ASES	The Government Entity administering the health insurance system and the transition to an APR-DRG methodology.
Mercer	Mercer	Actuarial firm contracting with ASES to design, develop, and implement the APR-DRG system in Plan Vital. Providing consulting support through implementation.
Solventum (formerly 3M)	solventum	An organization that develops state or territory specific APR-DRG reimbursement software, including testing the APR-DRG software that is used by agencies, hospitals and health plans for inpatient hospital payment.

Adoption of APR-DRG Methodology in Plan Vital

Guiding Principles –
FOMB Fiscal Plan Regarding DRGs



As stated in the 2020 Fiscal Plan, ASES began development of a Diagnosis Related Group (DRG)-based payment model for the following purposes:

- Reimburse hospitals a fixed amount to fully treat a patient with a given medical condition.
- Help control medical costs by incentivizing providers to deliver cost-effective care without sacrificing quality.
- Improve the effectiveness of Medicaid service delivery by standardizing the measurement of patient acuity across providers and reducing the administrative burden associated with reimbursements.

ASES will begin testing this payment model in 2020 ahead of a launch in July 2021.

Source: 2020 Fiscal Plan for Commonwealth of Puerto Rico, Page 210, https://oversightboard.pr.gov/fiscal-plans/

Fundamentals of the All Patients Refined – Diagnosis Related Groups (APR-DRG) System

Puerto Rico Plan Vital

Important facts about the APR-DRG Methodology

- Applicable to all inpatient services of the medical plan Vital.

Important facts about the APR-DRG Methodology

What are DRGs?

- DRGs are a classification system that categorizes medical cases into similar groups to help standardize resource intensity and cost reimbursement across hospitals in an equitable manner.
- The purpose of DRGs is to create a standardized system to evaluate patient conditions and asses the level of resources typically required to treat like cases.
- DRGs help hospitals improve treatment efficiency, discourage overtreatment, improve patient safety by standardizing patient care, and provide a comparison of costs across different hospitals.

Important facts about the APR-DRG Methodology

APR DRG versus MS-DRG

- Both classification systems are used to group patients based on like conditions and other factors for payment purposes.
- Both use relative weights to indicate resource intensity for treatment within the respective DRGs.

Major differences are listed below:

APR DRGs:

- Clinical model used in development.
- Relative weights reflect all payer experience.
- Considers SOI, mortality risks, and multiple diagnoses/comorbidities.
- More granular categorizations (four levels of severity for every DRG, with differing weights).
- Have additional DRGs for non-Medicare populations (such as newborn and psychiatric care).

MS DRGs:

- Statistical model used in development.
- Relative weights reflect Medicare payer experience.
- Considers complications, comorbidities, age, sex, and discharge status, but doesn't account for severity of a patient's condition.
- Primarily used for Medicare population.

APR – DRG Payment Formula:

Each inpatient hospital discharge receives a base payment:

DRG Base Payment = Base Rate x DRG Relative Weight

- **Base Rate** – Standard dollar amount developed in program design. Can be a statewide rate, hospital-specific rates or peer group rates.
- **Other dispositions as:**
  - Outliers
  - Transfer of patients
  - Short stays
  - Eligibility provisions
  - STAC payments transition provisions
  - Etc.

Important facts about the APR-DRG Methodology

- **Clinically Meaningful:** Classifies inpatient services based on clinical similarities and use of hospital resources by severity of illness and risk of mortality.
- **All Populations:** Developed to work across all populations including newborns, pediatrics, maternity, complexity and behavioral health.
- **Flexible:** Integrates with payment, quality and cost-efficiency programs to drive improvements in clinical outcomes and operational efficiencies.
- **Accurate:** Clinical categorical approach allows for accurate prospective payment that align with resource utilization.
- **Transparent:** Detailed clinical logic, hierarchies and specifications are published in APR-DRG definitions manual which is updated regularly by 3M's clinical experts

Important Questions and Answers

Questions and Answers – Transitional Payment Pool

Question:

Explain the Transitional Payment Pool and how it will operate.

Answer:

ASES will be adopting a transition payment pool for Year 1 of the APR DRG implementation to ease the conversion on hospitals from the current per diem system. This transition payment pool will ensure that no hospital is disproportionally harmed in transition from the current per diem methodology to an APR DRG system due to coding and documentation changes.

The transition payment pool will be created by setting aside a portion of the STAC directed payments. For Year 1 of the APR DRG system, this is a portion of the funding traditionally allocated for STAC directed payments that hospitals have received since January 2020. The estimated amount of the transition payment pool for Year 1 of the APR DRG implementation is $60 million.

Questions and Answers – Transfer Payments

Question:

What are the various payments made under the APR DRG reimbursement system and what is the reasoning for each of the payments?

Answer:

Transfer Payment

A special payment is made to a hospital that admits a patient and subsequently transfers that patient to another hospital. Claims with a patient discharge status code of 02, 05, 07, or 82 will be paid the transfer payment as opposed to the DRG base payment. The payment made is the lessor of a per diem payment times the number of days, or the DRG base payment. The per diem payment is calculated as follows:

$$\left(\left(\text{Hospital Base Rate} \times \text{DRG/SOI Relative Weight}\right) \div \text{DRG/SOI ALOS}\right) \times \text{Inpatient Days} = \text{Transfer Payment}$$

Questions and Answers – Outlier Payments

Question:

What are the various payments made under the APR DRG reimbursement system and what is the reasoning for each of the payments?

Answer:

Outlier Payment

A day outlier payment is available on discharges with an exceptionally high number of days in relation to the Average Length of Stay (ALOS) for the assigned DRG/SOI. Outlier payments are made in addition to the DRG base payment that the hospital receives. In order for a claim to qualify for an outlier payment, the greater of the following must be met:

- The geometric trimmed ALOS plus 10 days
- The geometric trimmed ALOS plus two times the untrimmed standard deviation of the DRG/SOI.

$$\left(\left(\text{Hospital Base Rate} \times \text{DRG/SOI Relative Weight}\right) \div \text{DRG/SOI ALOS}\right) \times \text{Inpatient Days Above Threshold} \times \text{80\% Payment Adjustment} = \text{Outlier Payment}$$

Questions and Answers – Short Stay Payment

Question:

What are the various payments made under the APR DRG reimbursement system and what is the reasoning for each of the payments?

Answer:

Short Stay Payment

The DRG reimbursement system being adopted for Plan Vital will include a short-term payment for certain inpatient stays that are significantly less than the ALOS for the DRG/SOI. This payment is being adopted to allow for more funds to be included in the calculation of hospital specific base rates and maintain budget neutrality based on the claims data used to calculate base rates trended to the implementation date of October 1, 2025. The threshold for a short stay payment is where a patient is discharged with a length of stay less than one standard deviation of the ALOS of the associated DRG. The calculation of the short stay payment is as follows:

$$\left(\left(\text{Hospital Base Rate} \times \text{DRG/SOI Relative Weight}\right) \div \text{DRG/SOI ALOS}\right) \times \text{Inpatient Days} = \text{Short Stay Payment}$$

Questions and Answers – Payment for a Patient that loses Medicaid Coverage

Question:

Please discuss the payment made for an individual that loses Medicaid coverage during the hospital stay.

Answer:

For discharges that occur after the expiration of eligibility, the hospital shall receive a full APR DRG payment if the length of stay under Medicaid eligibility is greater than the trimmed geometric ALOS for the DRG. Outlier provisions will apply for length of stay under Medicaid eligibility. For discharges for which the length of stay for Medicaid eligibility is less than the trimmed geometric ALOS for the DRG, a per diem will be paid for each day under Medicaid eligibility.

For example, if the ALOS of the DRG/SOI is 7 days and the patient loses Medicaid eligibility 5 days into the hospital stay, the hospital would receive a per diem payment using the following calculation:

If the patient was in the hospital 8 days before losing Medicaid eligibility, the hospital will receive the full DRG payment for the claim.

Questions and Answers –

Question:

Provide information regarding how each discharge was converted to APR DRG and classified into each SOI (diagnosis used).

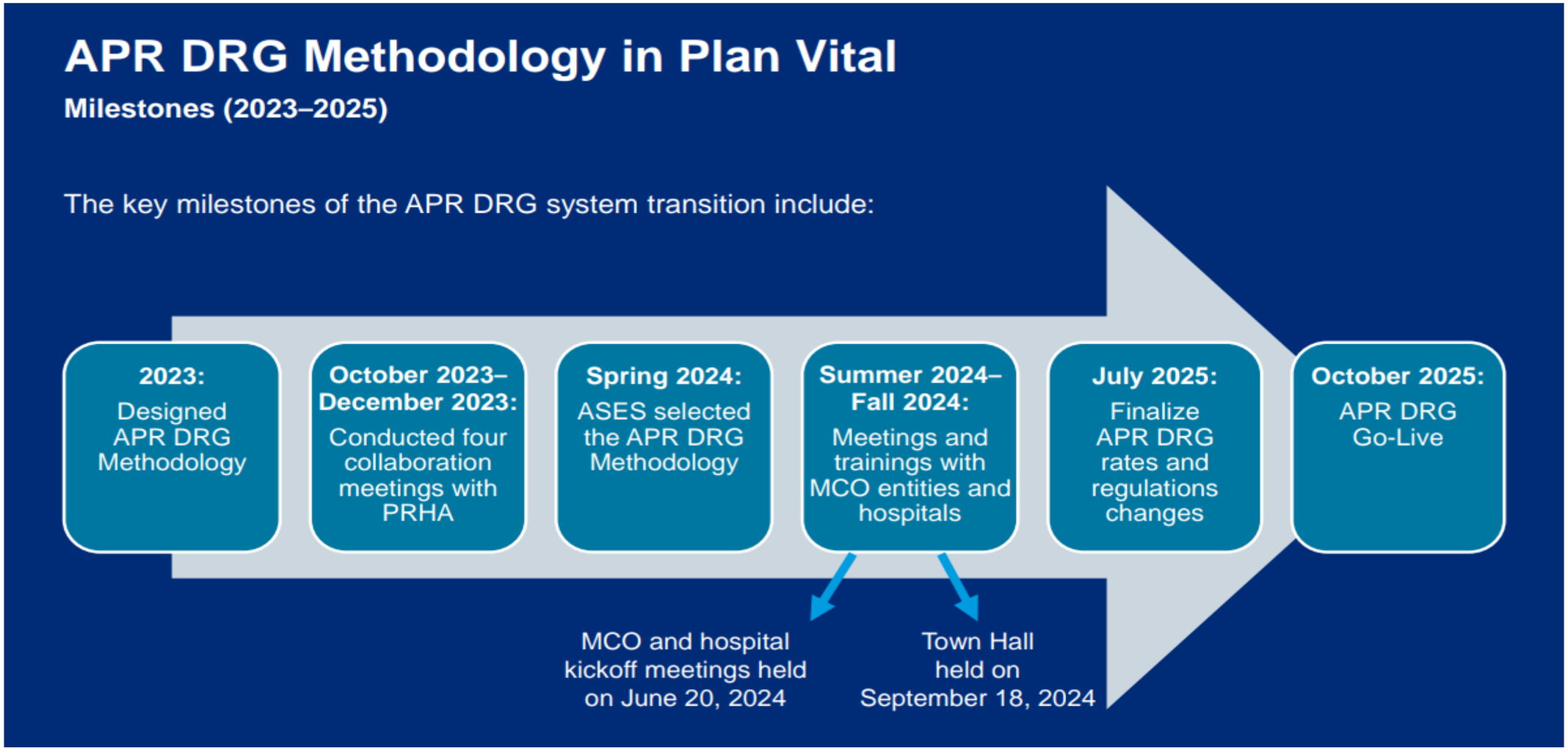
Answer:

Mercer Response: The assignment of a specific DRG is driven by the following:

1. Principal diagnosis
2. Procedures performed
3. Most additional or secondary diagnoses
4. Patient age
5. Patient gender

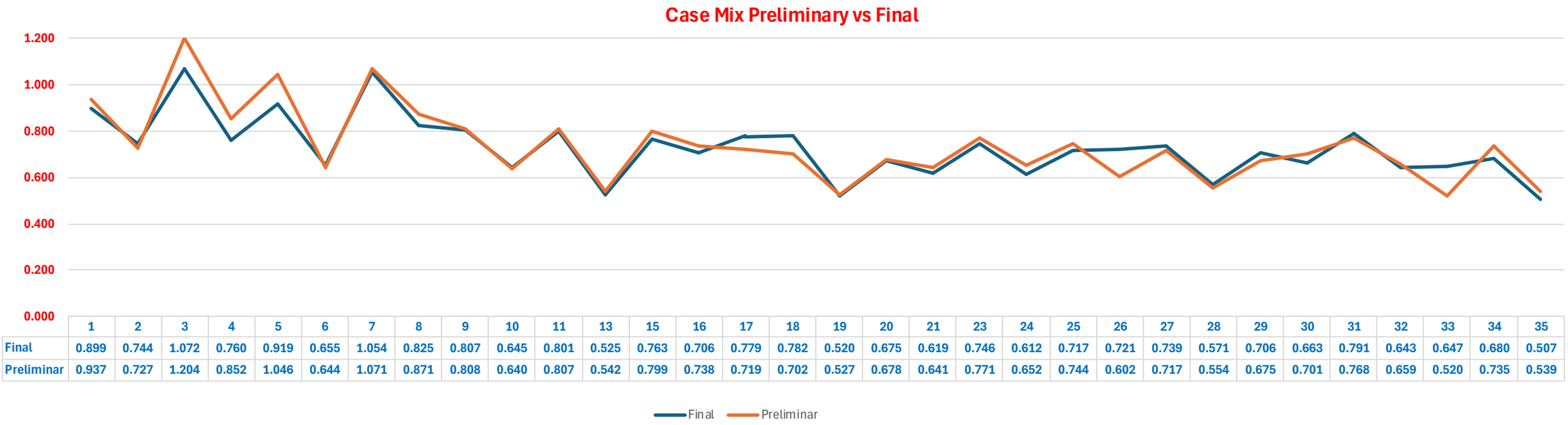
The above information is submitted on the UB04 paper claim form or the 837I electronic claim form.

Implementation Timeline



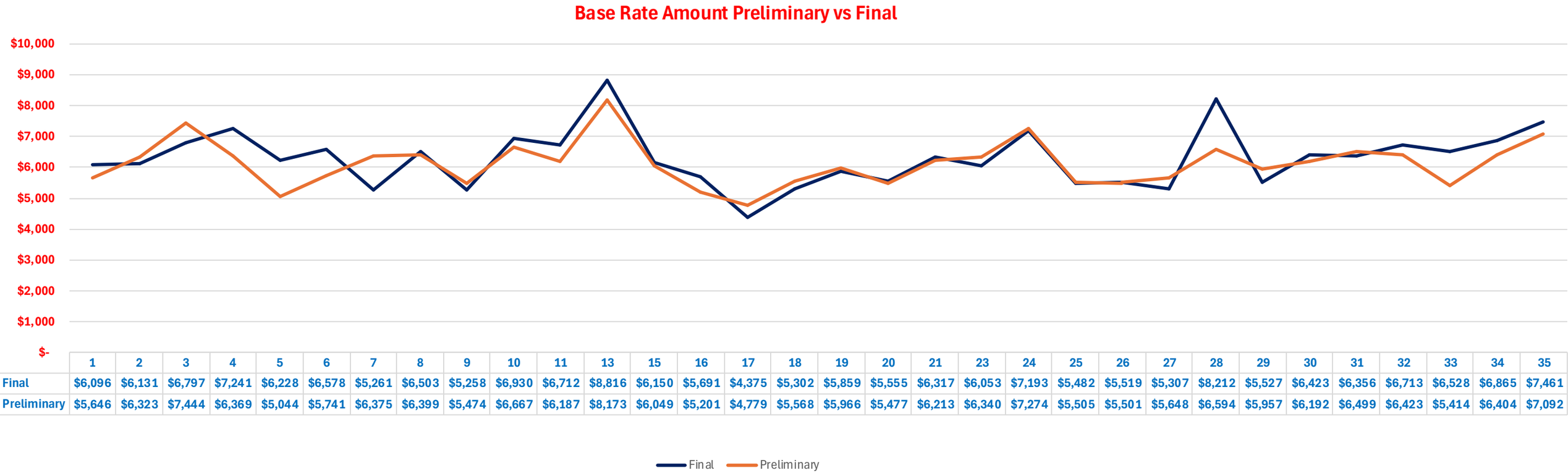
GRAPHICS

Case Mix Comparison: Preliminary vs Final



	1	2	3	4	5	6	7	8	9	10	11	13	15	16	17	18	19	20	21	23	24	25	26	27	28	29	30	31	32	33	34	35
Final	0.899	0.744	1.072	0.760	0.919	0.655	1.054	0.825	0.807	0.645	0.801	0.525	0.763	0.706	0.779	0.782	0.520	0.675	0.619	0.746	0.612	0.717	0.721	0.739	0.571	0.706	0.663	0.791	0.643	0.647	0.680	0.507
Preliminar	0.937	0.727	1.204	0.852	1.046	0.644	1.071	0.871	0.808	0.640	0.807	0.542	0.799	0.738	0.719	0.702	0.527	0.678	0.641	0.771	0.652	0.744	0.602	0.717	0.554	0.675	0.701	0.768	0.659	0.520	0.735	0.539

Base Rate Amount Comparison: Preliminary vs Final



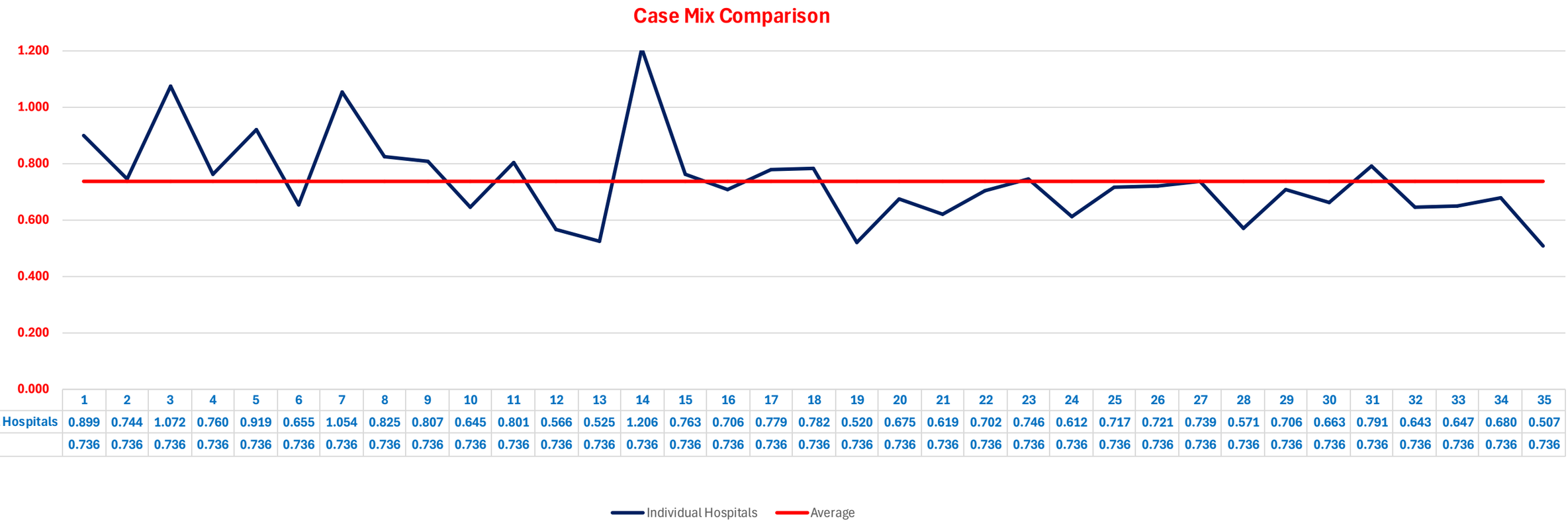
	1	2	3	4	5	6	7	8	9	10	11	13	15	16	17	18	19	20	21	23	24	25	26	27	28	29	30	31	32	33	34	35
Final	$6,096	$6,131	$6,797	$7,241	$6,228	$6,578	$5,261	$6,503	$5,258	$6,930	$6,712	$8,816	$6,150	$5,691	$4,375	$5,302	$5,859	$5,555	$6,317	$6,053	$7,193	$5,482	$5,519	$5,307	$8,212	$5,527	$6,423	$6,356	$6,713	$6,528	$6,865	$7,461
Preliminary	$5,646	$6,323	$7,444	$6,369	$5,044	$5,741	$6,375	$6,399	$5,474	$6,667	$6,187	$8,173	$6,049	$5,201	$4,779	$5,568	$5,966	$5,477	$6,213	$6,340	$7,274	$5,505	$5,501	$5,648	$6,594	$5,957	$6,192	$6,499	$6,423	$5,414	$6,404	$7,092

Galíndez LLC TRUSTworthy Member of Nexia

SOI Level PR VS National

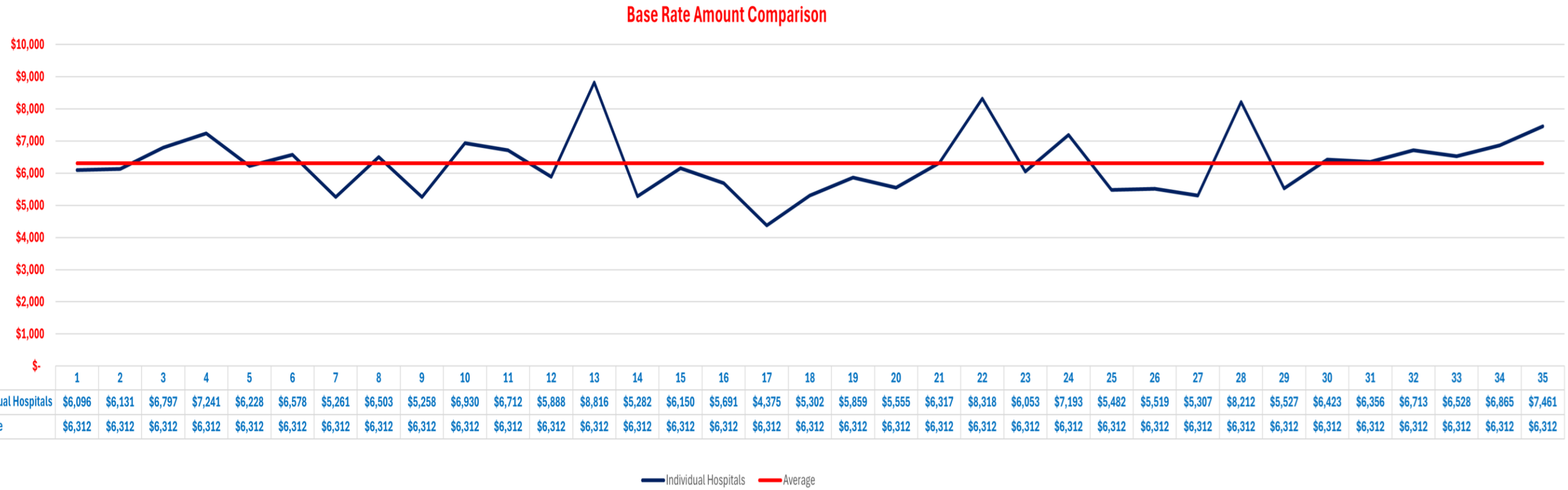
SOI Level	Puerto Rico	National
1	61%	36%
2	30%	36%
3	7%	22%
4	2%	7%

Case Mix Comparison –Sample of 35 hospitals



	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	34	35
Individual Hospitals	0.899	0.744	1.072	0.760	0.919	0.655	1.054	0.825	0.807	0.645	0.801	0.566	0.525	1.206	0.763	0.706	0.779	0.782	0.520	0.675	0.619	0.702	0.746	0.612	0.717	0.721	0.739	0.571	0.706	0.663	0.791	0.643	0.647	0.680	0.507
Average	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736	0.736

Base Rate Amount –Sample of 35 hospitals



	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	34	35
Individual Hospitals	$6,096	$6,131	$6,797	$7,241	$6,228	$6,578	$5,261	$6,503	$5,258	$6,930	$6,712	$5,888	$8,816	$5,282	$6,150	$5,691	$4,375	$5,302	$5,859	$5,555	$6,317	$8,318	$6,053	$7,193	$5,482	$5,519	$5,307	$8,212	$5,527	$6,423	$6,356	$6,713	$6,528	$6,865	$7,461
Average	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312	$6,312

Galíndez LLC TRUSTworthy

Member of Nexia

Recommendations

APR-DRG Implementation Recommendations

- What is next in the following months?
  - Create an implementation team in your hospital and include a representation of the physicians on it
  - Obtain from ASES the information as to your hospital base amount, and if possible, the supporting documentation as to how such amount was calculated.
  - Reconcile such information with your records ***(note: ASES worked with claims not with your billings)***
  - Recruit medical coders or outsource the services
  - Acquire the APR-DRG software and related IT systems

APR-DRG Implementation Recommendations (continued)

- What is next in the following months?
  - Run test of billings under the new payment method and compare with the actual payment method to identify the winners and losers' diagnosis
  - Perform projections as to the effect of the APR-DRG implementation in your financials: budget, compliance with covenants, projected cash flows, etc.
  - Analyze the medical protocols, and introduce changes if applicable, in those services where the payment amount does not provide to cover the medical costs.
  - Monitor intensively the implementation process.

All Patient Refined Diagnosis Related Group (APR DRG)

- **REMEMBER:**

  - Goes live the new methodology of APR DRG payment for discharges after 10/01/2025.
  - Importance of MEDICAL DOCUMENTATION and CODING.
  - Excel file prepared by MERCER on behalf of ASES as a valuable tool.

Accounting and reporting considerations

All Patients Refined – Diagnosis Related Groups (APR-DRG) System

Puerto Rico Plan Vital

For Profit and Non-For-Profit Hospitals –Vital Revenue

	For Profit Hospitals (19)		Non-for-Profit Hospitals (14)	
	2023	**2024**	**2023**	**2024**
Net Patient Service Revenue	$ 1,097,897,470	$ 1,135,329,959	$ 980,847,300	$ 1,063,559,495
Net Income (loss)	(30,706,796)	(3,371,225)	205,552,015	91,452,081
Net Revenue -Vital	308,987,602	283,167,882	186,751,490	196,361,060
% Vital to Net Patient Service Revenue	28%	25%	19%	18%
95% Vital	293,538,222	269,009,488	177,413,916	186,543,007
Cut	(15,449,380)	(14,158,394)	(9,337,575)	(9,818,053)

Includes audited financial data and unaudited financial data from the Medicare Cost Report.

Accounting & reporting challenges

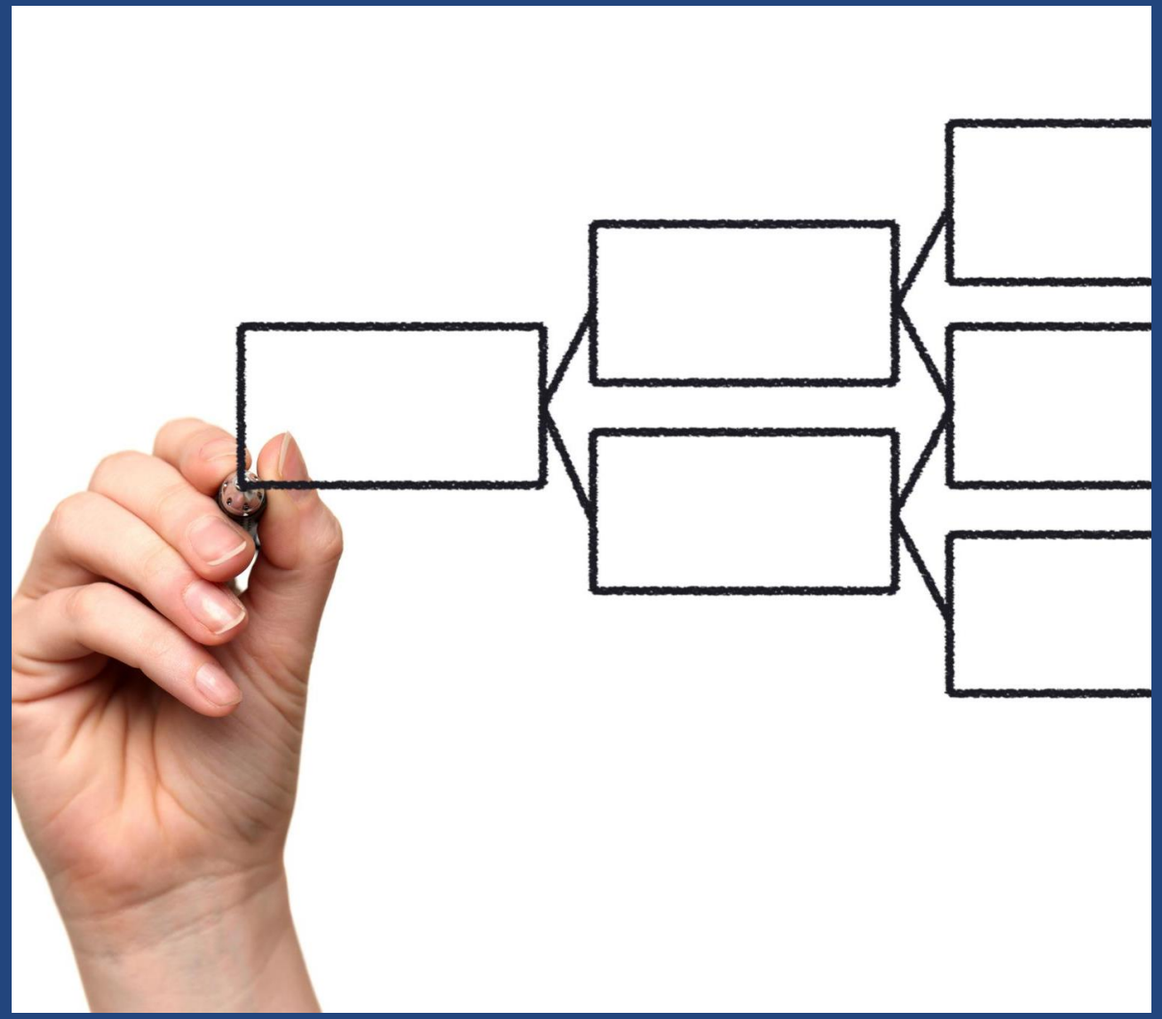
- **Training and Education**:
  - Educate **finance and coding teams** on the mechanics of APR-DRG to ensure comprehensive understanding of the new payment model and its effects.
  - Provide **continuous training and resources** to keep teams informed about any modifications or updates to the APR-DRG system.
- **System Updates**:
  - Modify revenue cycle systems to accommodate DRG-based billing, guaranteeing alignment with the updated payment structure.
  - Deploy necessary software and hardware enhancements to support the transition to APR-DRG.
- **Internal Controls**:
  - Strengthen internal controls over clinical documentation to maintain accuracy and adherence to APR-DRG standards
  - Implement rigorous controls over coding and billing processes to minimize errors and ensure precise revenue recognition.
- **Policy Review**:
  - Assess and update financial reporting policies to ensure alignment with ASC 606 and ASC 954 standards.
  - Conduct regular policy evaluations and revisions to address new challenges or changes within the APR-DRG framework.

Overview of ASC 606 in Healthcare

- ASC 606: Revenue from Contracts with Customers
- Establishes a 5-step model for revenue recognition
- Applies to all entities entering contracts with customers
- Focus on transfer of control rather than risk and rewards
- Requires enhanced disclosures and judgment in estimates

Visualizing the 5-Step Revenue Recognition Model

- Step 1: Identify the contract with a customer.
- Step 2: Identify the performance obligations in the contract.
- Step 3: Estimate the transaction price accurately.
- Step 4: Allocate the transaction price to each performance obligation.
- Step 5: Recognize revenue as the obligations are satisfied.

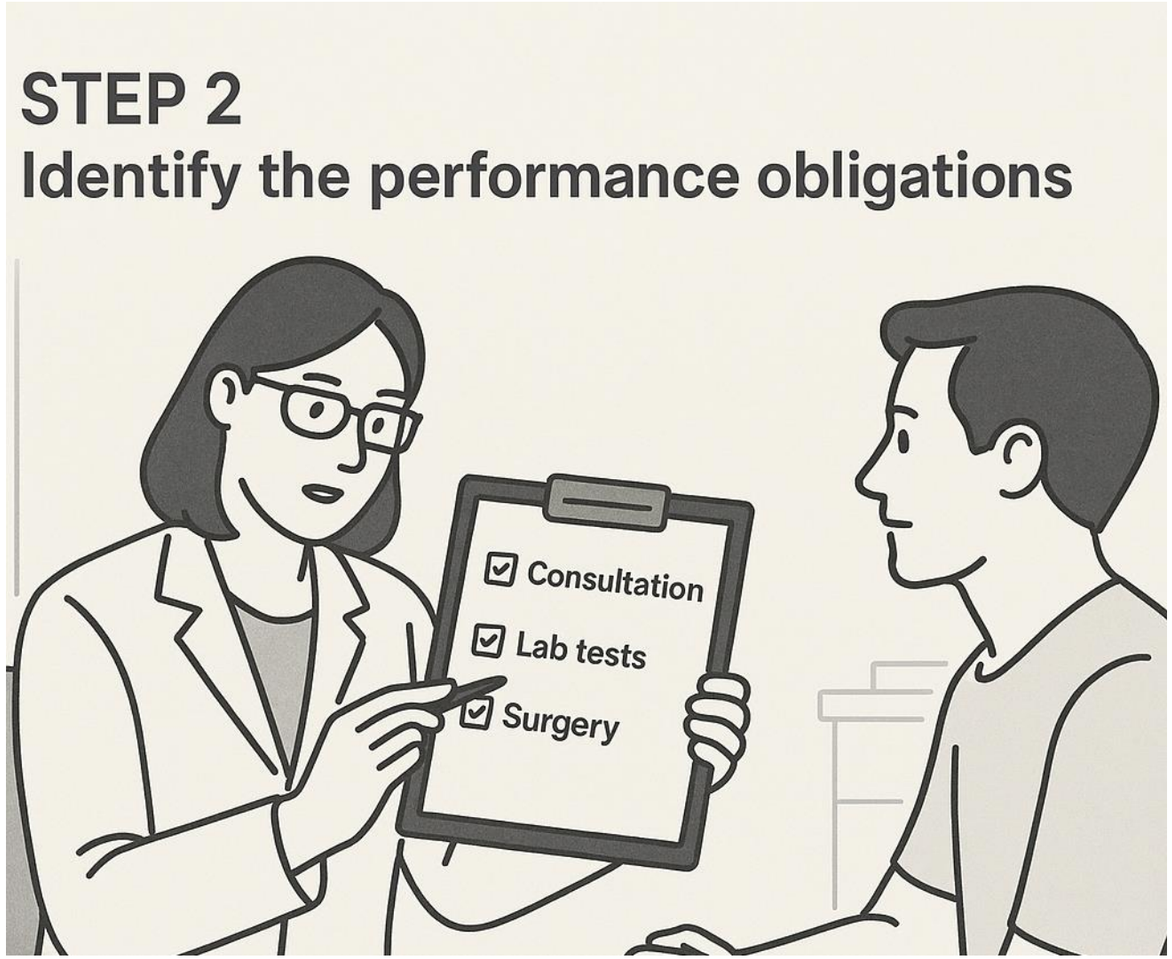


Step 1: Identify the Contract

ASC 606-10-25: “Identify contract criteria”

- Under ASC 606-10-25-1(d), a contract must have **commercial substance** to be accounted for under the revenue recognition standard. This means:
  - “The risk, timing, or amount of the entity’s **future cash flows** is **expected to change** as a result of the contract.”
  - If a contract does **not alter the entity’s future cash flows**, it lacks commercial substance and **should not be recognized** for revenue purposes.
- In healthcare, commercial substance is typically present when:
  - A patient receives services that trigger billing to third-party payors.
  - A provider enters into a managed care agreement that changes reimbursement timing or rates.
  - Medicaid or Medicare adjustments (e.g., STAC, APR-DRG) affect the amount or timing of revenue.
- These arrangements change the risk profile and timing of cash flows, satisfying the commercial substance criterionAPR-DRG contracts are typically between the hospital and Medicaid (Plan Vital).
- The “**reimbursement**” contract encompasses the full episode of inpatient care.

Step 2: Identify Performance Obligations



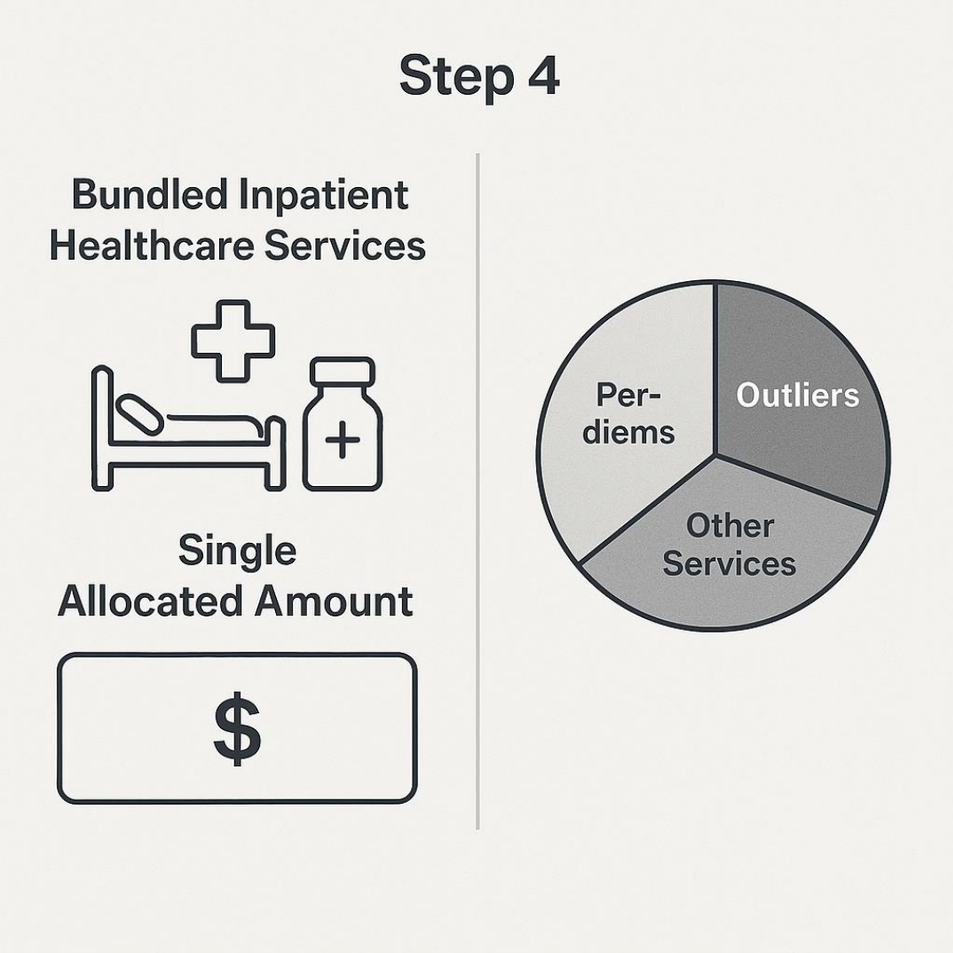
ASC 606-10-25-14 to 22: “Performance obligation guidance”

- The performance obligation is the entire episode of care for a patient admission.
- Under APR-DRG, services are bundled and not treated as separate “single” obligations.
- Obligation is satisfied upon patient discharge.
- Requires accurate documentation and coding.

Step 3: Determine Transaction Price

- Fixed payment under APR-DRG simplifies transaction price
- Adjustments may be needed for denials, audits, or quality penalties
- Estimate variable consideration using historical data and apply constraint to avoid significant revenue reversal.
- Estimate **variable consideration** using expected value or most likely amount
    - "**The expected value**" sum of probability-weighted amount (*For large number of contracts with similar characteristics) Portfolio approach*
    - *"**The most likely amount**" – single most likely amount in a range. Two possible outcome. N/A*
- Apply constraint to avoid significant revenue reversal

Step 4: Allocate Transaction Price

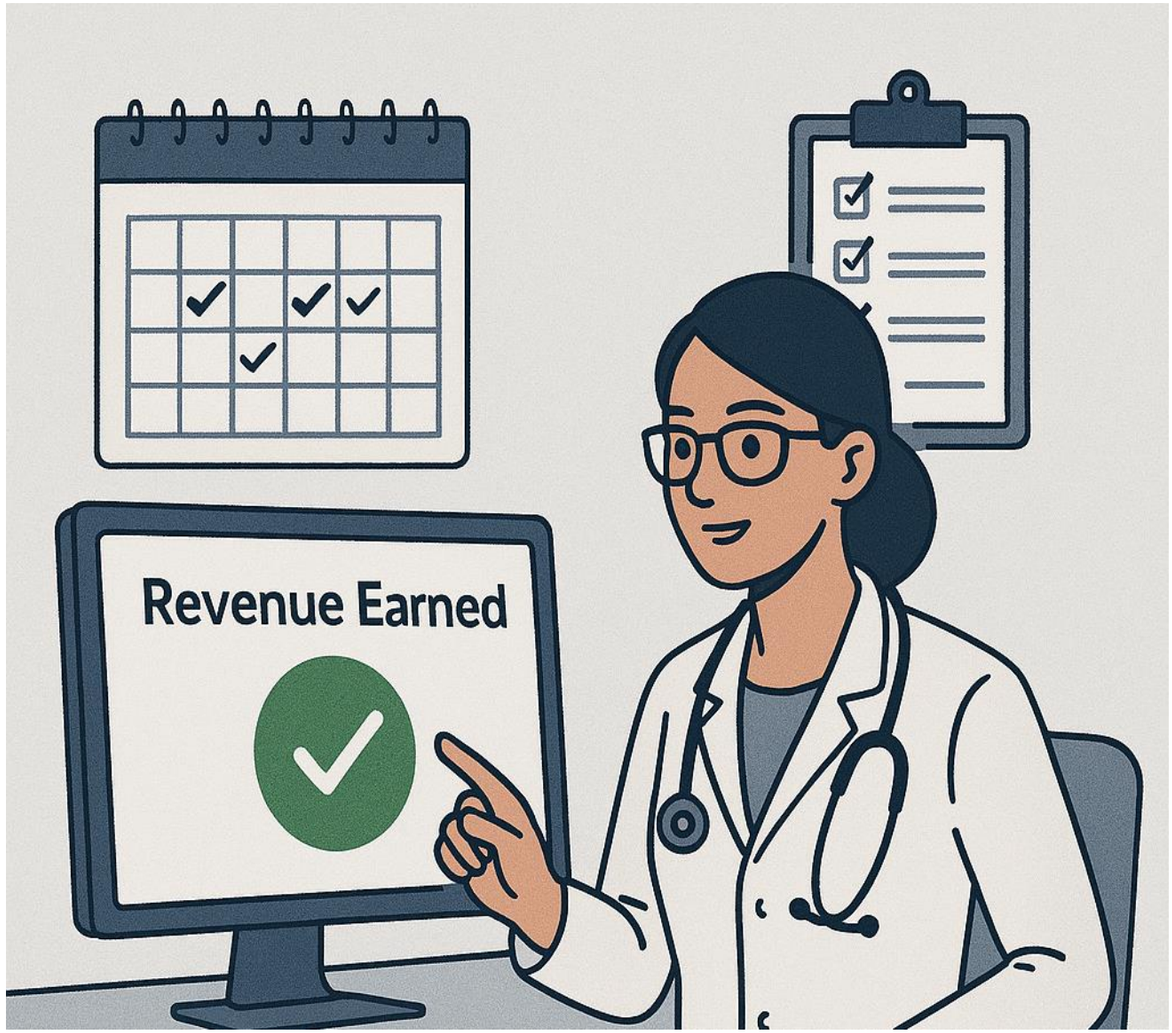


- Since the performance obligation is a bundled episode, the full transaction price is allocated to it.
- No need to allocate across multiple obligations.
- Allocation is straightforward under APR-DRG.

Step 5: Recognize Revenue

ASC 606-10-25-23 to 30: **Recognize revenue** when or **as performance obligations are satisfied:**

- Revenue is **recognized over time** when the patient simultaneously receives and **consumes the benefits** of the services provided (e.g., inpatient stays, outpatient visits)
- **Inpatient services** are typically treated as **a single performance obligation**, satisfied over the duration of care—from admission to discharge.
- Outpatient services may be recognized at a point in time or over time, depending on whether the services are distinct and separately identifiable.
- **Input methods** (e.g., charges incurred relative to total expected charges) and **output methods** (e.g., units of service delivered) are used to measure progress toward satisfying the obligation.
- **Revenue** is recorded **as services are provided**, not when payment is received. This aligns with the accrual basis of accounting and reflects the transfer of control to the customer.
- Contract assets and liabilities are recognized when payment timing differs from service delivery:
  - **Contract asset**: Unbilled receivable when services are rendered before payment.
  - **Contract liability**: Deferred revenue when payment is received before services.
- Requires strong internal controls over coding and documentation.



Disclosure Requirements:

Disclosure Requirement	Codification Ref.	Healthcare Context
Disaggregation of revenue by type (e.g., inpatient, outpatient, payor class)	ASC 606-10-50-5	Revenue sources and variability
Information about **contract balances** (**assets and liabilities**)	ASC 606-10-50-8	Unbilled receivables and deferred revenue
Significant judgments in applying the standard	ASC 606-10-50-17	Timing and variable consideration
Methods used to **recognize revenue** (e.g., input/output methods)	ASC 606-10-50-18	Inpatient services billed over time

Disclosure Requirement	Codification Ref.	Healthcare Context
Optional exemption for contracts < 1 year duration	ASC 606-10-50-14A	Short-term healthcare contracts
Performance obligations and **when** they are typically **satisfied**	ASC 606-10-25-23 to 25-30	Inpatient: over time; Outpatient: point in time
Policies for estimating variable consideration	ASC 606-10-32-5 to 32-14	Final payments and audit settlements

Impact on Revenue Recognition

- APR-DRG changes how hospitals receive Medicaid / Vital payments.
- Providers need to adjust for variable consideration in payment estimates.
- Historical data is essential for accurate revenue predictions.

Thanks!

This and other presentations are available on our website: **galindezllc.com/presentations**

If you have any questions,
please contact us at (787) 725-4545
or by e-mail at **info@galindezllc.com**

Galíndez LLC TRUSTworthy Member of Nexia