Appendix B

Financial Methodology
(Non-LDO CEC Model)

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TABLE OF EXHIBITS

GLOSSARY

Term	Definition
Aggregation Pool	A group of Medicare beneficiaries, as determined by CMS in accordance with this Appendix, that includes ESCO Beneficiaries and Medicare beneficiaries that have been aligned to one or more CEC Non-LDO Entities , and grouped together for financial calculation purposes.
Annualize	To adjust expenditures to allow the summation of cost data from beneficiaries with less than one year of eligibility to reflect a full year of expenditures.
Base Year (BY)	The three years prior to the start of the CEC Initiative. BY1, BY2, and BY3 correspond to calendar years 2012, 2013, and 2014, respectively.
Beneficiary-Month	One month of time for which a beneficiary is aligned to the ESCO, a CEC LDO Entity, or a CEC Non-LDO Entity, or is a Reference Group Beneficiary.
Beneficiary-Year	The sum of twelve Beneficiary-Months.
CEC Initiative	Comprehensive End-Stage Renal Disease Care Initiative.
CEC LDO Entity	An entity that: (1) has executed a CEC participation agreement with CMS; (2) has Dialysis Facility Participants that are owned in whole or in part by one or more LDOs; and (3) is not the same legal entity as the ESCO.
CEC Non-LDO Entity	An entity that: (1) has executed a CEC participation agreement with CMS; (2) has Dialysis Facility Participants that are owned in whole or in part by one or more non-LDOs; and (3) is not the same legal entity as the ESCO.
CEC Non-LDO Entity Beneficiaries	A Medicare beneficiary who has been aligned to a CEC Non-LDO Entity.
Completion Factor	Total expenditures for all CY2012 Medicare Part A and Part B claims with processing dates before April 1, 2013, divided by total expenditures for CY2012 claims that were processed as of the date that the Government runs its report. The Completion Factor will be applied separately to each Eligibility Category's Annualized and Truncated expenditures.
Continuously Aligned ESCO Beneficiary	An ESCO Beneficiary aligned to the ESCO in a given year and in the previous year.
Dialysis Facility	An entity that provides outpatient maintenance dialysis services (including Hospital-Based Dialysis Facilities and Home Dialysis training and support services) either as a Medicare-enrolled entity or as an operating division of a Medicare-enrolled entity that is owned in whole or in part by the Company.
Effective Date	The date specified in Section II.A of the participation agreement.
Eligibility Category	One of five groups of Medicare beneficiaries (for purposes of calculating Historical Expenditure Baselines) or ESCO Beneficiaries (for purposes of calculating Performance Year Expenditure Benchmarks) that are combined according to their reason for Medicare entitlement and, if applicable, Medicaid enrollment status.
Eligible Beneficiary-Months	Months in which a beneficiary was enrolled in Medicare Parts A and B and met all other CEC eligibility criteria.
Eligible BY Beneficiary	A beneficiary who would have been aligned to the ESCO during BY1, BY2, or BY3 had the CEC Initiative been operating at that time because the beneficiary meets the eligibility requirements (listed in Section 1.1.1) and receives a "first touch" dialysis treatment (discussed in Section 1.1.2) from a Dialysis Facility on the ESCO Participant List. Information for Eligible BY Beneficiaries will be used to produce the Historical Expenditure Baseline.
ESCO Beneficiary	A Medicare beneficiary who has been aligned to the ESCO according to the methodology outlined in Section 1.1 below.

Term	Definition
ESCO Participant List	The list of the Participants that are approved by CMS for participation in CEC, as updated from time to time in accordance with paragraphs 3-5 of Section IV.B. of the Participation Agreement. The initial ESCO Participant List is attached as Appendix A.
ESCO Provider/Supplier	An individual or entity that (1) is a Medicare-enrolled provider or supplier identified by an NPI or CCN; (2) bills for items and services furnished to Medicare beneficiaries under a Medicare billing number assigned to the TIN of a Participant Owner or Participant Non-Owner; (3) has agreed to participate in the CEC pursuant to a written agreement with the ESCO; (4) may, but is not required, to receive Shared Savings Payments; and (5) is included on the ESCO Participant List.
ESCO Total Revenue	The total Medicare Part A and Part B claims paid to all providers or suppliers for the items and services furnished to all ESCO Beneficiaries (and any Medicare beneficiaries aligned to any CEC Non-LDO Entities in the Aggregation Pool, if applicable) in a given Performance Year.
Established Beneficiary	A Medicare beneficiary with 12 months of Medicare enrollment during the calendar year preceding the current Performance Year.
Financial Reconciliation	The process occurring after the end of the PY where alignment is finalized and Shared Savings is calculated using the full PY of claims data plus the run-out.
Government	The federal executive, legislative, and judicial branches of the United States of America.
Historical Expenditure Baseline	A dollar amount calculated by CMS according to the methodology set forth in Section 2 of this Appendix to establish the average annual Medicare Part A and Part B expenditures for Medicare beneficiaries who would have been aligned to the ESCO (as well as all Medicare beneficiaries who would have been aligned to the CEC Non-LDO Entities in the Aggregation Pool during this period, if applicable) in an Eligibility Category during any of the three years prior to the start of the first Performance Year under the alignment methodology described in this Appendix.
Home Dialysis	Peritoneal or hemodialysis performed by an appropriately trained ESCO Beneficiary (and/or the ESCO Beneficiary's caregiver) at the home of the ESCO Beneficiary.
Initial Term	The period of time beginning on the Effective Date of this Agreement and concluding at the end of the third Performance Year.
Large Dialysis Organization (LDO)	An entity that, as of the Effective Date, owns, directly or indirectly, 200 or more Dialysis Facilities.
Market	A geographic area consisting of no more than two contiguous Medicare core-based statistical areas ("CBSA") in which one or more Dialysis Facilities listed in Appendix A are located, except that inclusion is allowed of contiguous rural counties that are not included in a Medicare CBSA. If the ESCO is rural and not included in any Medicare CBSA, the Market will be defined by CMS based on a geographic unit no larger than a state.
Minimum Savings Rate (MSR)	The minimum percentage of the Total Performance Year Expenditure Benchmark that the ESCO must achieve in Preliminary Shared Savings to be eligible to receive Shared Savings.
New Beneficiary	A Medicare beneficiary with fewer than 12 months of Medicare enrollment during the calendar year preceding the current Performance Year.
Newly-Aligned ESCO Beneficiary	An ESCO Beneficiary aligned to the ESCO in a given year and not also aligned to the ESCO in the previous year.
Non-LDO	An entity that is not owned directly or indirectly, in whole or in part by an LDO and, as of the Effective Date, either wholly owns at least one but fewer than 200 Dialysis Facilities, or jointly owns at least one but fewer than 200 Dialysis Facilities with another entity that is not owned directly or indirectly, in whole or in part by an LDO.

Term	Definition
Participant	An individual or entity that is a Participant Owner, a Participant Non-Owner, or an ESCO Provider or Supplier.
Participant Non-Owner	An individual or entity that (1) is a Medicare-enrolled provider or supplier identified by a TIN and either a NPI or a CCN; (2) does not have any direct or indirect ownership or investment interest in the ESCO; (3) has agreed to participate in the CEC pursuant to a written agreement with the ESCO; (4) may, but is not required to, receive Shared Savings Payments; and (5) is included on the ESCO Participant List.
Participant Owner	An individual or entity that (1) is a Medicare-enrolled provider or supplier identified by a TIN and either a NPI or a CCN; (2) has a direct ownership or investment interest in the ESCO; (3) has agreed to participate in the CEC Initiative pursuant to a written agreement with the ESCO; (4) may, but is not required to, receive Shared Savings Payments; and (5) is included on the ESCO Participant List.
Per-Beneficiary-Per-Year (PBPY)	A measurement of expenditures calculated by dividing expenditures by Beneficiary-Years. This differs from a per capita basis, which is expressed in per beneficiary terms.
Performance Year (PY)	The 12-month period beginning on January 1 of each year during the term of the Participation Agreement, except that the first Performance Year of this Agreement will begin on July 1, 2015 and end on December 31, 2016. The second Performance Year will begin on January 1, 2017 and end on December 31, 2017. The third Performance Year will begin on January 1, 2018 and end on December 31, 2018. If this Agreement is renewed, the fourth Performance Year will begin on January 1, 2019 and end on December 31, 2019, and the fifth Performance Year will begin on January 1, 2020 and end on December 31, 2020.
Performance Year Expenditure Benchmark	The ESCO's expected Medicare Part A and Part B expenditures for ESCO Beneficiaries (and any Medicare beneficiaries aligned to any CEC Non-LDO Entities in the Aggregation Pool, if applicable) in an Eligibility Category during the applicable Performance Year, as determined by CMS according to the parameters set forth in this Appendix. The Performance Year Expenditure Benchmarks reflect adjustments to the Historical Expenditure Baselines made using Trending and Risk Adjustment.
Preliminary Shared Savings	The difference between the ESCO's Total Performance Year Expenditure Benchmark and ESCO Total Revenue when ESCO Total Revenue is less than the ESCO's Total Performance Year Expenditure Benchmark. This number represents an interim value and is not the final estimate of Shared Savings.
Reference Group Beneficiaries	Beneficiaries nationwide who would be eligible for the CEC Initiative according to the eligibility requirements (listed in Section 1.1.1) but who do not have a "first touch" dialysis treatment with the ESCO, a CEC-Non-LDO Entity, or a CEC LDO Entity.
Risk Adjustment	The process of adjusting for diagnoses and demographic factors that are expected to affect Medicare Part A and Part B expenditures
Shared Savings	The amount owed to the ESCO by CMS due to ESCO Total Revenue below the ESCO's Total Performance Year Expenditure Benchmark for the applicable Performance Year as determined by CMS in accordance with this Appendix. This number represents the final amount paid to the ESCO.
Shared Savings Cap	Maximum amount of Preliminary Shared Savings, equal to 5% of the Total PY Expenditure Benchmark.
Shared Savings Payments	The portion of Shared Savings distributed by the ESCO to a Participant or by a Participant Owner or Participant Non-Owner to an ESCO Provider/Supplier.

Term	Definition
Shared Savings Percentage	The maximum proportion of Preliminary Shared Savings the ESCO can receive, equal to 50% of the difference between Total ESCO Revenue and Total Performance Year Benchmark
TIN	A federal taxpayer identification number, which in some cases may be a Social Security Number.
Total Performance Year Expenditure Benchmark	The ESCO's expected combined Medicare Part A and Part B expenditures for ESCO Beneficiaries (and any Medicare beneficiaries aligned to any CEC Non-LDO Entities in the Aggregation Pool, if applicable) in all Eligibility Categories during the applicable Performance Year, as determined by CMS according to the parameters set forth in this Appendix. There is one Total Performance Year Expenditure Benchmark, expressed at the ESCO level rather than the Eligibility Category Level, for each Performance Year.
Trending	The process by which expenditures are adjusted to account for national changes in expenditures over time.
Truncating	The process by which Annualized expenditures are capped to limit financial risk to the ESCO.

LIST OF ACRONYMS

Term	Definition
ACO	Accountable care organization
BY	Base year
CEC Initiative	Comprehensive End-Stage Renal Disease Care Initiative
DME	Durable medical equipment
DRS	Demographic risk score
DSH	Disproportionate share hospital
ESCO	End-Stage Renal Disease Seamless Care Organization
ESRD	End-stage renal disease
FFS	Fee for service
FRS	Full risk score
HCC	Hierarchical Condition Category
HHA	Home health agency
IME	Indirect medical education
LDO	Large dialysis organization
MS-DRG	Medicare Severity Diagnosis-Related Group
MSR	Minimum Savings Rate
MSSP	Medicare Shared Savings Program
Non-LDO	Non-Large Dialysis Organization
PBPY	Per-beneficiary-per-year
PY	Performance Year
PPS	Prospective payment system
SNF	Skilled nursing facility

1. INTRODUCTION

This appendix describes the financial methodology that CMS will use to calculate Shared Savings for the End-Stage Renal Disease Comprehensive Care Organization (ESCO) that has executed a Participation Agreement with CMS to participate in the Comprehensive ESRD Care (CEC) Initiative. The methodology is adapted from those used for the Medicare Shared Savings Program (MSSP) and the Pioneer Accountable Care Organization (ACO) Model.[1,2]

Section 1 of this document discusses the process by which CMS identifies beneficiaries who are eligible for the CEC Initiative and assigns them to the ESCO and provides a high-level overview of the financial methodology. Section 2 includes the methodology used to calculate the Historical Expenditure Baseline for the ESCO. Section 3 explains how the Historical Expenditure Baseline is adjusted to establish the ESCO's specific Performance Year Expenditure Benchmarks that CMS will use to calculate Shared Savings. Section 4 describes the methodology used to calculate the expenditures required to compute ESCO Total Revenue. Section 5 explains how the ESCO Beneficiaries can be grouped in an Aggregation Pool to achieve the minimum number of beneficiaries required to participate in the CEC Initiative. Section 6 describes how Total Performance Year Expenditure Benchmarks and ESCO Total Revenue are compared to determine Shared Savings. CMS will provide regular reports to the ESCO. The attachment lists examples of the types of reports that the ESCO will receive and provides an overview of the content of each report.

Exhibit 1 contains a flow chart that provides a comprehensive overview of the key calculation components and sequence in which historic expenditures will be adjusted and compared to ESCO Total Revenue to calculate Shared Savings.[3] This document also contains an example that traces the inputs and outputs of key computational steps for a hypothetical Performance Year for the ESCO.

1.1 Identifying and Aligning Eligible Beneficiaries to the ESCO

CMS will use the process described below to identify eligible beneficiaries – both during Base Years and Performance Years – prior to aligning them to the ESCO operating in the Market in which they receive the majority of their dialysis care.

There are three groups of beneficiaries considered in the financial calculations:

1. *ESCO Beneficiaries* are beneficiaries who meet the eligibility requirements (listed in Section 1.1.1) and are aligned to the ESCO during the Performance Years per the first touch matching methodology (listed in Section 1.1.2).

[1] http://www.cms.gov/Medicare/Medicare-Fee-for-Service-Payment/sharedsavingsprogram/Downloads/Shared-Savings-Losses-Assignment-Spec-v2.pdf
[2] http://innovation.cms.gov/files/x/pioneeracobmarkmethodology.pdf
[3] For simplicity, the exhibit shows only the initial three-year performance period.

2. *Eligible BY Beneficiaries* are beneficiaries who would have been aligned to the ESCO during BY1, BY2, or BY3 had the CEC Initiative been operating at that time because they meet the eligibility requirements (listed in Section 1.1.1) and receive a "first touch" dialysis treatment (discussed in Section 1.1.2) from a Dialysis Facility on the ESCO Participant List. Information for Eligible BY Beneficiaries will be used to produce the Historical Expenditure Baseline.
3. *Reference Group Beneficiaries* are beneficiaries who would be eligible for the CEC Initiative according to the eligibility requirements (listed in Section 1.1.1) but who do not have a "first touch" dialysis treatment (discussed in Section 1.1.2) with the ESCO, a CEC-Non-LDO Entity, or a CEC LDO Entity. Preliminary figures indicate that this nationally representative population of Reference Group Beneficiaries included approximately 317,400 individuals in 2013. Information for Reference Group Beneficiaries will be used to develop Truncation and Trending factors described in Sections 2.4, 2.7, and 3.1.

The paragraphs below describe in greater detail the key concepts and methods used to identify these three categories of beneficiaries.

1.1.1 Identifying Eligible Beneficiaries

To become aligned to the ESCO or another CEC Non-LDO Entity, ESCO Beneficiaries, Eligible BY Beneficiaries, and Reference Group Beneficiaries must meet the following criteria at the time alignment is performed:

- Must be enrolled in Medicare Parts A and B
- Must not be enrolled in a Medicare Advantage plan, cost plan, or other non-Medicare Advantage Medicare managed care plan at the time alignment is performed
- Must be receiving maintenance dialysis services, identified using type of bill 72x
- Must be at least 18 years of age
- Must reside in the United States
- Must not be aligned to another existing Medicare shared savings program (unless otherwise determined by CMS)
- Must not have had a kidney transplant in the last 12 months
- Must have Medicare as the primary payer

1.1.2 Alignment Methodology and Timeline

Alignment through "First Touch." Beneficiaries will be aligned to the ESCO based on their first visit (identified by submission of a 72x claim) to a Dialysis Facility that is affiliated with the ESCO as documented in the claims data. This first touch approach means that a beneficiary's first visit to a given Dialysis Facility will prospectively align that beneficiary to the ESCO in which the Dialysis Facility is a Participant. Beneficiaries will be added to the ESCO via first touch even if the beneficiary has visited another Dialysis Facility previously in the PY that is not participating in a

CEC-Non-LDO Entity or a CEC LDO Entity. The beneficiary will be aligned for the Performance Year and for the life of CEC Initiative, assuming that the beneficiary does not lose eligibility status and the ESCO does not withdraw from the CEC Initiative. If eligible, the beneficiary will remain aligned to the ESCO for the Initial Term even if the beneficiary visits another Dialysis Facility after alignment.

Alignment Prior to the First Performance Year. All beneficiaries who meet eligibility requirements will be prospectively aligned. For the first Performance Year, prior to the Effective Date for the CEC Initiative, the ESCO will receive a list of all of its Eligible BY Beneficiaries. This list will include beneficiaries who meet the eligibility requirements (listed in Section 1.1.1) and who visited the ESCO Dialysis Facility between January 1, 2014 and December 31, 2014 with a three-month claims run-out.

Alignment During the Performance Years. On a monthly basis, eligible beneficiaries will be prospectively added to the aligned population for the ESCO according to the first touch rule. This will occur when a beneficiary first receives maintenance dialysis services from a Dialysis Facility participating in the ESCO and the beneficiary's first claim with that Dialysis Facility is submitted for dialysis services via a 72x claim. CMS will provide an updated list of aligned beneficiaries to the ESCO on a monthly basis. After the end of each Performance Year, CMS will finalize the ESCO's list of aligned beneficiaries for that Performance Year during the reconciliation process described below.

Financial Reconciliation. To be accurate, the alignment process needs to account for circumstances where beneficiaries initially aligned to the ESCO are partially or fully excluded due to death or because the majority of their dialysis care occurred outside of the ESCO's Market area. Alignment will be retrospectively finalized as part of Financial Reconciliation after the first quarter of the following Performance Year to allow for three months of claim run-out (i.e., time after the end of the PY for providers to submit claims for services provided during the PY). For example, the reconciliation process for Performance Year 1 will occur after the first quarter of Performance Year 2.

During reconciliation, CMS will identify the final aligned population for the ESCO, including each beneficiary's aligned months of service within the performance period, as incurred through the end of the Performance Year and allowing for a three month claim run-out. In certain cases, a beneficiary may be removed from the ESCO's list of aligned beneficiaries for the entire performance period or selected Beneficiary-Months may be removed from settlement.

Beneficiaries will be excluded for some or all months in a given Performance Year for the following reasons:

1. Medicare as a secondary payer. All the months during which a patient identifies Medicare as a secondary payer will be removed during Financial Reconciliation. In other

words, the ESCO will not be held fiscally responsible for beneficiary costs during months where Medicare is a secondary payer.

2. Kidney transplant. The month in which a beneficiary receives a kidney transplant will be removed during Financial Reconciliation. In addition, the 12 months following transplant will be removed. In other words, the ESCO will not be held fiscally responsible for the costs of the transplant (evaluation, typing, organ acquisition, execution of transplant) and post-transplant care during the month of the transplant and for at least 12 months post-transplant. However, the ESCO will be fiscally responsible for all non-transplant-related costs the beneficiary incurred prior to the transplant. The beneficiary will be removed from the ESCO's list of aligned beneficiaries in the following Performance Year. After 12 months, if a beneficiary is still receiving dialysis services (indicating graft failure) and satisfies all other eligibility requirements, the beneficiary will be eligible for the CEC Initiative.

3. Geographic Exclusions. A beneficiary will be removed from the ESCO's list of aligned beneficiaries for the entire Performance Year if the patient received more than 50 percent of his or her dialysis services from one or more Dialysis Facilities outside of the Market of the ESCO during the Performance Year. The ESCO's Market is defined for the entire duration of the CEC Initiative as no more than two contiguous Medicare core-based statistical areas with permissible inclusion of contiguous rural counties that are not included in a Medicare CBSA. If the ESCO's Dialysis Facilities are not included in any CBSA, the Market is defined as no larger than a state.

1.2 Overview of Financial Calculations

This is an overview and actual calculations will be made in accordance with Sections 2 to 6. To calculate Shared Savings, CMS will use a multi-step process to assess each ESCO's financial performance annually following the close of each Performance Year.[4] This annual assessment involves a comparison of ESCO Total Revenue and the Total Performance Year Expenditure Benchmark.

The target population for the CEC Initiative is FFS Medicare beneficiaries with ESRD for whom Medicare is the primary payer. Within this population, expenditure calculations will be stratified for each of the following Medicare Eligibility Categories:

- Aged dual: ESRD beneficiaries who are aged and eligible for Medicaid
- Aged non-dual: ESRD beneficiaries who are aged but not eligible for Medicaid
- Disabled dual: ESRD beneficiaries who are disabled and eligible for Medicaid
- Disabled non-dual: ESRD beneficiaries who are disabled but not eligible for Medicaid

- ESRD: ESRD beneficiaries who are not aged or disabled, regardless of whether they are eligible for Medicaid

The calculations underlying this comparison are performed in four major steps that are described in detail below. If the ESCO does not satisfy the 350 minimum ESCO Beneficiary threshold, its ESCO Beneficiaries will be included in an Aggregation Pool for Financial Reconciliation purposes. If the ESCO has at least 350 ESCO Beneficiaries, it will have the option of being evaluated independently or requesting to have its ESCO Beneficiaries included in an Aggregation Pool. Aggregation Pools are discussed in more detail in Section 5.

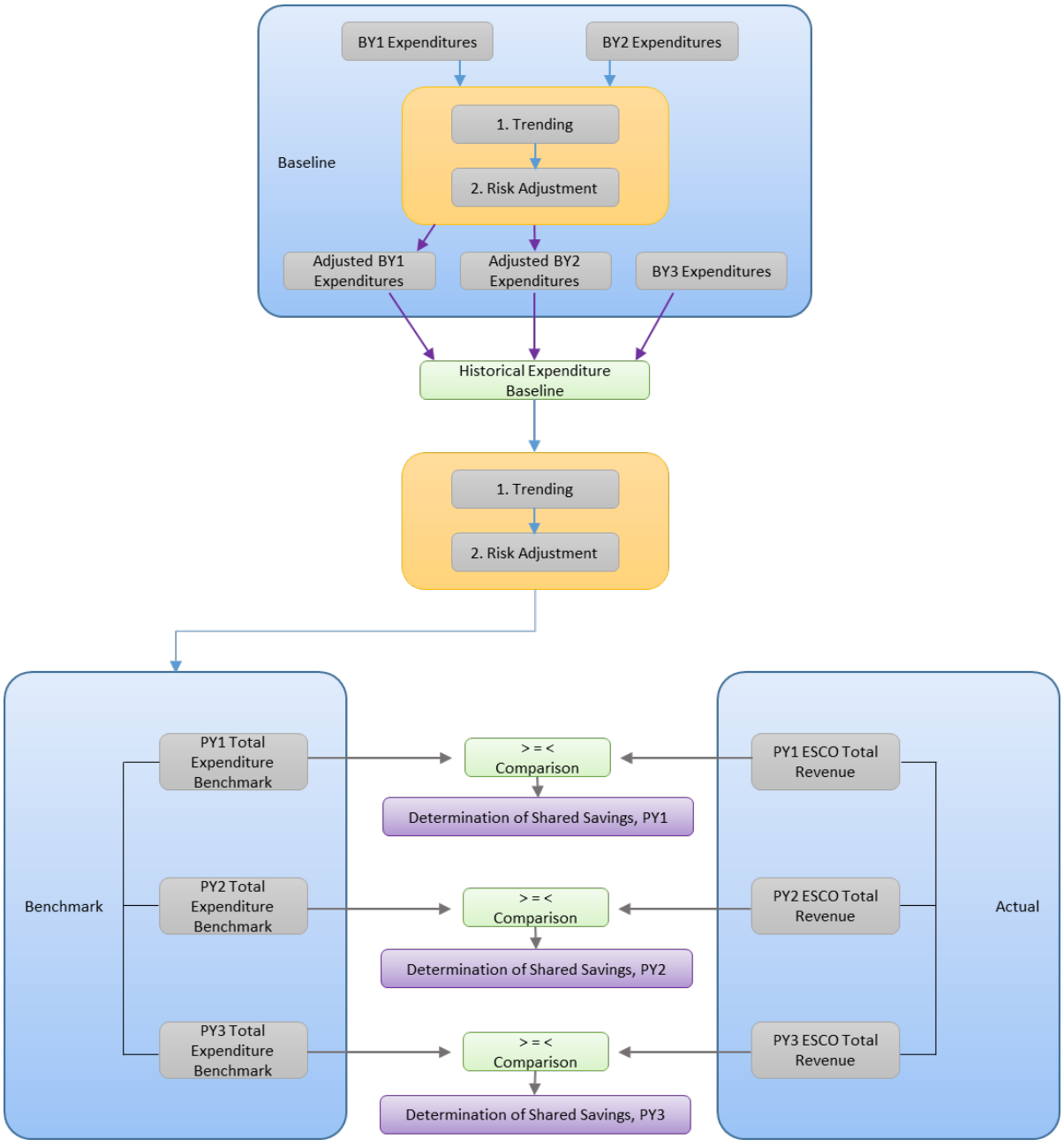
1. **Calculate the Historical Expenditure Baseline.** This involves adjusting Base Year (BY) 1 and 2 expenditures in a number of ways—exclusion of certain payment amounts (described in Section 2.2), adjustment for sequestration reductions, Annualization, Truncation of outliers, accounting for late-arriving claims, accounting for Eligible BY Beneficiaries with less than a full year of alignment, Trending, accounting for geographic variation in prices, and Risk Adjustment—to make them comparable to BY3 expenditures. BY3 expenditures are also subject to the same adjustments with the exception of Trending and Risk Adjustment. Next, BY1 and BY2 expenditures are averaged with BY3 expenditures to produce a Historical Expenditure Baseline for each ESCO. All expenditure information will be Annualized and expressed on a Per-Beneficiary-Per-Year (PBPY) basis. Adjustments are made separately for each of five Eligibility Categories. Section 2 explains this process in detail.

2. **Determine Performance Year Expenditure Benchmark.** For each Performance Year, update the Historical Expenditure Baseline (using Trending and Risk Adjustment) to derive the PY Expenditure Benchmark for each Performance Year. CMS will calculate an aggregated Performance Year Expenditure Benchmark for CEC Non-LDO Entities with fewer than 350 aligned beneficiaries and for CEC Non-LDO Entities which, despite having at least 350 aligned beneficiaries, have requested to have their ESCO Beneficiaries included in an Aggregation Pool. Section 3 details this process.

3. **Calculate ESCO Total Revenue.** Actual Performance Year expenditures are adjusted to exclude certain claims, Annualize expenditures for beneficiaries with partial years of eligibility, Truncate outliers, and account for late-arriving claims. CMS will calculate ESCO Total Revenue. Section 4 details this process.

4. **Determine Shared Savings.** ESCO Total Revenue is then compared to the Total Performance Year Expenditure Benchmark to calculate Preliminary Shared Savings in a given PY. Adjustments are made to the Preliminary Shared Savings to account for the MSR, quality scores, Shared Savings Cap, and sequestration. Section 5 and Section 6 detail the methodologies for Aggregation Pools and calculating Shared Savings, respectively.

Exhibit 1. Overview of ESCO Financial Performance Assessment Methodology



2. CALCULATING THE HISTORICAL EXPENDITURE BASELINE

The Historical Expenditure Baseline for each Eligibility Category is calculated using Medicare claims data for services delivered during Base Years 1, 2 and 3 (calendar years 2012, 2013, and 2014, respectively) and is expressed on a Per-Beneficiary-Per-Year (PBPY) basis, for each ESCO. The following steps will be used to calculate the Historical Expenditure Baseline:

1. Gather all claims data for Eligible BY Beneficiaries for BY1, BY2, and BY3.
2. Apply adjustments and exclusions to BY1, BY2, and BY3 claims (Sections 2.1 and 2.2).
3. Annualize, Truncate, and apply a Completion Factor to claims and compute weighted average PBPY expenditures for each Baseline Year (Sections 2.3 through 2.6).
4. Trend and Risk Adjust BY1 and BY2 expenditures to be comparable with BY3 expenditures (Sections 2.7 and 2.8).
5. Calculate the simple average of the Risk Adjusted, Trended BY1, BY2, and BY3 expenditures to produce the Historical Expenditure Baseline (Section 2.8, Step 3)

2.1 Dialysis Claims Adjustments

ESRD PPS[5] dialysis claims (billed via 72x) will be handled differently from other types of claims used in the financial calculations. In particular, rather than using the full claim payment amount included in the claims data, which is the adjusted ESRD PPS payment rate, the CEC Initiative will use the ESRD PPS base rate amount for each dialysis treatment. Doing so removes from the financial calculations all of the adjustments to the base rate that CMS uses to calculate dialysis payments under the ESRD PPS. Among other adjustments, this includes geographical price variation and payment reductions under the Quality Incentive Program. The ESRD PPS base rate changes annually and is publicly available from the ESRD PPS final rule.[6]

2.2 Exclusions and Sequestration Adjustment

The financial calculations will exclude four types of payments — those related to indirect medical education (IME), disproportionate share hospitals (DSH), uncompensated care

[5] Beginning January 1, 2011, the Medicare Improvements for Patients and Providers Act mandated the implementation of a bundled payment system for outpatient maintenance dialysis services. This ESRD PPS bundled payment covers a set of dialysis-related items and services routinely required for dialysis treatments. It consists of a base (unadjusted) rate modified by several adjustments at the provider, patient, and claim levels (http://www.usrds.org/2012/pres/USDialysisBundle_impact_NKFCM2012.pdf). Additional information about the ESRD PPS is available from the ESRD PPS final rule: http://www.cms.gov/Medicare/Medicare-Fee-for-Service-Payment/ESRDpayment/End-Stage-Renal-Disease-ESRD-Payment-Regulations-and-Notices.html.

[6] Dialysis claims are the only claim type from which the CEC Initiative removes geographical variation in expenditures. In the future, CMS may choose to remove geographical variation from other claim types.

payments, and those for kidney transplant-related services — and will adjust claim payment amounts for sequestration reductions.[7] Aside from the adjustments discussed throughout this appendix, all other payment information included in the seven Medicare Parts A and B claims files (inpatient, outpatient, carrier, DME, hospice, SNF, and HHA) will be included in the financial calculations. These exclusions and adjustments are described below.

2.2.1 Indirect Medical Education, Disproportionate Share Hospital, and Uncompensated Care Payments

The CEC Initiative's financial calculations will exclude both the capital and operating components of IME and DSH payments applicable to inpatient claims. The uncompensated care payments will also be excluded from the financial calculations.[8]

2.2.2 Kidney Transplant-Related Services

All financial calculations will exclude expenditures related to kidney transplant services in order to avoid creating an incentive for the ESCO to limit kidney transplant services. These services fall into each of the following stages:

1. Evaluation of the recipient and donor
2. Blood and tissue typing of the recipient and donor
3. Organ acquisition
4. Execution of the transplant itself
5. Services following the transplant

Medicare ESRD beneficiaries are excluded from the CEC Initiative once they receive a transplant. The only exception is individuals who still require maintenance dialysis 12 months following the transplant.

2.2.3 Sequestration Adjustment

As part of the Budget Control Act of 2011, payments to Medicare providers were reduced by 2 percent beginning on April 1, 2013. This reduction applies both to claim payments and to Shared Savings calculated under the CEC Initiative. To avoid "double jeopardy," in which Shared Savings would first be calculated using sequestration-adjusted claim payment amounts and then the Shared Savings amounts would also be subject to the 2 percent reduction, the following adjustments will be made:

[7] In addition to these exclusions, in the future CMS may decide to exclude material changes to provider reimbursement, such as care management fees and quality payments.

[8] Additional information on the uncompensated care payment is available from http://www.medpac.gov/documents/reports/mar14_ch03_appendix.pdf?sfvrsn=0

1. The amount of the sequestration adjustment will be added back to the claim payment amount prior to calculating Shared Savings.
2. The Preliminary Shared Savings will be subject to the 2 percent sequestration reduction, as discussed in Section 6. The resulting amount will be the Shared Savings.

2.3 Annualization

Eligible Beneficiary-Months are months in which a beneficiary was enrolled in Medicare Parts A and B and met all other CEC eligibility criteria. Eligible Beneficiary-Months will be allocated to each Eligibility Category in order to calculate total Medicare FFS expenditures (or Medicare paid amounts) as the sum of expenditures for eligible months for all FFS claims. All expenditure information will be Annualized and expressed as PBPY amounts.

Annualization is required to allow the summing of cost data from Eligible BY Beneficiaries with differing numbers of months of service and to produce PBPY estimates. To implement Annualization, spending is multiplied at the beneficiary level by an Annualization factor, which is equal to 12 divided by the number of eligible Beneficiary-Months. If the ESCO has an Eligible BY Beneficiary with 6 months of alignment, the Annualization factor would equal 12/6 or 2.

Annualized expenditures are calculated separately for each Eligibility Category so that an ESCO Beneficiary can contribute experience to multiple Eligibility Categories in the same year.

2.4 Truncation

Annualized expenditures will then be Truncated to limit financial risk to the ESCO posed by high-cost beneficiary outliers. Outlier Annualized expenditures will be Truncated by capping expenditures at a specific maximum value known as the Truncation threshold or stop-loss limit. The threshold is equal to the 99th percentile of expenditures for non-ESRD FFS Medicare beneficiaries plus the difference between average expenditures for Medicare ESRD beneficiaries (the Reference Group Beneficiaries, discussed in Section 1.1) and average expenditures for non-ESRD FFS Medicare beneficiaries. Similar to Annualization, expenditures are Truncated separately for each Eligibility Category. If an Eligible BY Beneficiary changes Eligibility Categories during a BY, the Eligible BY Beneficiary will contribute experience to multiple Eligibility Categories in the same year.

2.5 Completion Factor

Because the CEC Initiative relies on three months of claims run-out for most financial calculations, expenditure amounts will be adjusted using a Completion Factor to account for claims that may not have been processed as of 3 months after the end of a PY. The Completion Factor will be calculated based on CY2012 incurred claims data and applied to all years. The incurred claims data would include claims for all Eligible BY Beneficiaries, and beneficiaries who

would have been aligned to a CEC Non-LDO Entity or a CEC LDO-Entity or who would have been a Reference Group Beneficiary.

The Completion Factor will be equal to total Medicare expenditures for CY2012 claims with processing dates before April 1, 2013, divided by total expenditures for CY2012 services that were processed as of the date that the Government runs its report. The Completion Factor will be applied separately to each Eligibility Category's Annualized and Truncated expenditures.

For example, a Completion Factor of 0.94 would indicate that, for any calendar year, the total expenditure amount available with a three-month run-out period represents 94 percent of the total expenditure amount observed after all claims have been processed. Following with this example, expenditures would be multiplied by 1.06 (that is, 1 ÷ 0.94) to obtain an estimate of the complete expenditure amount.

2.6 Weighted Average of Truncated Expenditures

This section discusses the computation of PBPY expenditures for each of the three BYs, which involves weighting each beneficiary's expenditures to account for partial years of eligibility and then averaging across beneficiaries in each Eligibility Category.

Step 1: Calculate weighting factor. The weighting factor is equal to the number of Beneficiary-Months during which each beneficiary was aligned (in the case of Eligible BY Beneficiaries) or eligible (in the case of Reference Group Beneficiaries) divided by 12.

Step 2: Apply weighting factor. The weighting factor will be multiplied by the Annualized, Truncated, and Completed expenditures resulting from the calculations described in Sections 2.1 through 2.5 to produce weighted expenditures.

Step 3: Calculate weighted average of Truncated expenditures. Weighted expenditures from Step 2 will be added within each of the five Eligibility Categories. Each sum will be divided by total Beneficiary-Years in the Eligibility Category, which is equal to the sum of the weighting factors (from Step 1) within the Eligibility Category.

The weighted average of Truncated expenditures produces PBPY figures by Eligibility Category. Unless specified otherwise, *PBPY* below refers to expenditures that have had the adjustments in Sections 2.1 through 2.6 applied. Exhibit 2 provides hypothetical data produced by these adjustments. This information will be used in the example provided throughout this document.

Exhibit 2. Annualized, Truncated, Completed, and Weighted Base Year PBPY Expenditures

Eligibility Category	BY1 PBPY [1]	BY2 PBPY [2]	BY3 PBPY [3]
Aged dual	$75,000	$80,000	$86,000
Aged non-dual	$65,000	$67,000	$70,000

Disabled dual	$80,000	$82,000	$102,000
Disabled non-dual	$70,000	$73,000	$80,000
ESRD	$50,000	$55,000	$65,000

All values are hypothetical.

2.7 Trending for the Historical Expenditure Baseline

This adjustment consists of Trending BY1 and BY2 PBPY spending forward to be comparable with BY3 spending. This process requires two steps.

Step 1: Use Reference Group Beneficiaries to compute Trending factors. Trending factors will be calculated using PBPY expenditures incurred by the Reference Group Beneficiaries (described in Section 1.1). There will be separate Trending factors for expenditures for beneficiaries in each Eligibility Category. A BY-specific Trending factor is equal to PBPY BY3 expenditures for the Reference Group Beneficiaries divided by the PBPY expenditures for the BY that will be Trended. For example, the Trending factor for BY1 expenditures for ESRD, aged dual beneficiaries will be equal to PBPY BY3 expenditures for ESRD, aged dual Reference Group Beneficiaries divided by PBPY BY1 expenditures for ESRD, aged dual Reference Group Beneficiaries.

Hypothetical Trending factors (*T*) are calculated in columns 4–6 of Exhibit 3. As described earlier, calculations will be stratified by Eligibility Category to capture national trends specific to each group.

Exhibit 3. Trending Factors for Base Years Derived from Reference Group Expenditures

	Hypothetical PBPY Spending for Reference ESRD Population			Trending Factors (Using BY3 as Baseline)		
Eligibility Category	$PBPY^{N}_{BY1}$ [1]	$PBPY^{N}_{BY2}$ [2]	$PBPY^{N}_{BY3}$ [3]	$T_{BY1,BY3}$ [4]	$T_{BY2,BY3}$ [5]	$T_{BY3,BY3}$ [6]
Aged dual	$100,000	$110,000	$120,000	1.20	1.09	1.00
Aged non-dual	$55,000	$60,000	$65,000	1.18	1.08	1.00
Disabled dual	$71,000	$85,000	$90,000	1.27	1.06	1.00
Disabled non-dual	$76,000	$80,000	$85,000	1.12	1.06	1.00
ESRD	$150,000	$170,000	$200,000	1.33	1.18	1.00

Step 2: Apply Trending factors. Trended amounts will be calculated by multiplying PBPY expenditures by the Trending factors calculated in Step 1. This is illustrated in
Exhibit 4, which multiplies the Trending factors from the previous step by the PBPY figures in Exhibit 2.

Exhibit 4. Trended BY Expenditures for Eligible BY Beneficiaries

Eligibility Category	Trending Factors (Using BY3 as Base Year)			Trended Expenditures (Using BY3 as Base Year)		
	$T_{BY1,BY3}$ [1]	$T_{BY2,BY3}$ [2]	$T_{BY3,BY3}$ [3]	*Trended BY1 PBPY* [4]	*Trended BY2 PBPY* [5]	*Trended BY3 PBPY* [6]
Aged dual	1.20	1.09	1.00	$90,000	$87,200	$86,000
Aged non-dual	1.18	1.08	1.00	$76,700	$72,360	$70,000
Disabled dual	1.27	1.06	1.00	$101,600	$86,920	$102,000
Disabled non-dual	1.12	1.06	1.00	$78,400	$77,380	$80,000
ESRD	1.33	1.18	1.00	$66,500	$64,900	$65,000

[4] = [1] × column 1 from Exhibit 2; [5] = [2] × column 2 from Exhibit 2; [6] = [3] × column 3 from Exhibit 2.

2.8 Risk Adjustment of BY Expenditures

This section describes the Risk Adjustment procedure used to adjust BY1 and BY2 expenditures to be comparable to BY3 expenditures.

Step 1: Renormalize Hierarchical Condition Category (HCC) risk scores. The Government calculates prospective HCC risk scores for all Medicare beneficiaries. These HCC risk scores—also known as full risk scores (FRS)—will be divided by a renormalization factor for each applicable beneficiary for every year. This procedure will ensure that all CMS risk scores are scaled so that the average risk score is 1.0 every year. The renormalization factor is the average risk score at the Eligibility Category level.

Step 2: Calculate weighted average risk scores for New Beneficiaries and Established Beneficiaries in every Eligibility Category. After renormalization, for each Eligibility Category, separate weighted average risk scores will be calculated for New Beneficiaries (those who were not enrolled in Medicare during all 12 months of the prior calendar year) and Established Beneficiaries (those who were enrolled for all 12 months of the prior calendar year). For Established Beneficiaries, FRS will be used. For New Beneficiaries, demographic risk scores (DRS) – a risk score calculated using a separate model that incorporates information on beneficiary demographic and entitlement eligibility – will be used. The weight for each beneficiary will be calculated as the number of Beneficiary-Months for the beneficiary divided by the total number of Beneficiary-Months for the Eligibility Category. The same procedure applies to BY2. Hypothetical weighted averages for BY1 appear in columns 1 and 2 of Exhibit 5 and those for BY3 appear in columns 1 and 2 of Exhibit 6.

Step 3: Calculate weighted average risk score for each Eligibility Category. This step calculates an overall average risk score for each Eligibility Category based on the average risk scores for both New Beneficiaries and Established Beneficiaries. The weights that will be used are the Eligibility Category's proportions of New Beneficiary and Established Beneficiary Beneficiary-Months. In other words, the weight for the New Beneficiary group will be calculated by adding all New Beneficiary Beneficiary-Months and dividing by the total number of Beneficiary-Months

for both New Beneficiaries and Established Beneficiaries. Column 4 of Exhibit 5 and Exhibit 6 illustrate for BY1 and BY3, respectively.

Exhibit 5. Weighted Average BY1 Risk Scores by Eligibility Category

Eligibility Category	BY1 Average DRS for New Beneficiaries [1]	BY1 Average FRS for Established Beneficiaries [2]	Proportion of New Beneficiary Beneficiary-Months [3]	Weighted Average Risk Score [4]
Aged dual	1.22	1.80	0.30	1.62
Aged non-dual	1.35	1.40	0.20	1.39
Disabled dual	1.84	1.90	0.40	1.88
Disabled non-dual	0.90	1.70	0.40	1.38
ESRD	1.57	1.20	0.30	1.31

[1] and [2] are hypothetical weighted average risk scores with weights based on Beneficiary-Years.
[3] represents a hypothetical proportion.
[4] = [1] × [3] + [2] × (1 – [3])

Exhibit 6. Weighted Average BY3 Risk Scores by Eligibility Category

Eligibility Category	BY3 Average DRS for New Beneficiaries [1]	BY3 Average FRS for Established Beneficiaries [2]	Proportion of New Beneficiary Beneficiary-Months [3]	Weighted Average Risk Score [4]
Aged dual	1.70	1.90	0.40	1.82
Aged non-dual	1.35	1.40	0.30	1.39
Disabled dual	1.90	2.00	0.30	1.97
Disabled non-dual	1.50	1.60	0.40	1.56
ESRD	1.30	1.20	0.20	1.22

[1] and [2] are hypothetical weighted average risk scores with weights based on Beneficiary-Years.
[3] represents a hypothetical proportion.
[4] = [1] × [3] + [2] × (1 – [3])

Step 4: Convert risk scores into risk score ratios. The overall Eligibility Category weighted average risk scores will be converted into risk score ratios, which are equal to the average risk score for the later year divided by that of the earlier year. Exhibit 7 illustrates the calculation of the BY1/ BY3 risk score ratios.

Exhibit 7. BY1, BY3 Risk Score Ratios

Eligibility Category	BY1 Weighted Average Risk Score [1]	BY3 Weighted Average Risk Score [2]	BY3,BY1 Risk Score Ratio [3]
Aged dual	1.62	1.82	1.12
Aged non-dual	1.39	1.39	1.00
Disabled dual	1.88	1.97	1.05

Disabled non-dual	1.38	1.56	1.13
ESRD	1.31	1.22	0.93

[1] is from Exhibit 5, and [2] is from Exhibit 6.
[3] = [2] ÷ [1]

Step 5: Risk Adjust Trended baseline expenditures. Next, Risk Adjustment is applied to Trended expenditures in Exhibit 4, as illustrated in Exhibit 8. Columns 4 and 5 of the exhibit provide BY1 and BY2 expenditures that are comparable to BY3 expenditures, given in column 6. The figures in columns 4, 5, and 6 form the basis for the Historical Expenditure Baseline calculation in the next step.

Exhibit 8. Risk-Adjusted Base Year Expenditures

Eligibility Category	BY3/BY1 Risk Score Ratio [1]	BY3/BY2 Risk Score Ratio [2]	BY3/BY3 Risk Score Ratio [3]	BY1 Risk-Adjusted PBPY [4]	BY2 Risk-Adjusted PBPY [5]	BY3 Risk-Adjusted PBPY [6]
Aged dual	1.12	1.03	1.00	$100,800	$89,816	$86,000
Aged non-dual	1.00	0.95	1.00	$76,700	$68,742	$70,000
Disabled dual	1.05	1.02	1.00	$106,680	$88,658	$102,000
Disabled non-dual	1.13	0.97	1.00	$88,592	$75,059	$80,000
ESRD	0.93	1.00	1.00	$61,845	$64,900	$65,000

[1], [2], and [3] are hypothetical risk score ratios. [1] comes from Exhibit 7.
[4] = [1] × column 4 from Exhibit 4; [5] = [2] × column 5 from Exhibit 4; [6] = [3] × column 6 from Exhibit 4.

Step 3: Average BY1, BY2, and BY3 Risk-Adjusted PBPY. The Historical Expenditure Baseline for each Eligibility Category is the simple average[9] of the figures in columns 4, 5, and 6 of Exhibit 8, which are the BY3-comparable PBPY expenditures in each year. Column 4 of Exhibit 9 provides the Historical Expenditure Baseline.

Exhibit 9. Historical Expenditure Baseline

Eligibility Category	BY1 Risk-Adjusted PBPY [1]	BY2 Risk-Adjusted PBPY [2]	BY3 Risk-Adjusted PBPY [3]	Historical Expenditure Baseline PBPY [4]
Aged dual	$100,800	$89,816	$86,000	$92,205
Aged non-dual	$76,700	$68,742	$70,000	$71,814
Disabled dual	$106,680	$88,658	$102,000	$99,113
Disabled non-dual	$88,592	$75,059	$80,000	$81,217

[9] The simple average already incorporates weights to account for the number of aligned Beneficiary-Months, as described in Section 2.6.

ESRD	$61,845	$64,900	$65,000	$63,915

[1], [2], and [3] are Risk-Adjusted expenditures from Exhibit 8.
[4] = ([1] + [2] + [3]) ÷ 3

3. CALCULATING THE PERFORMANCE YEAR EXPENDITURE BENCHMARKS

This section describes the calculation of the Performance Year Expenditure Benchmarks that are generated at the close of the PY and used as a basis for assessing whether the ESCO reduced Medicare expenditures. The Performance Year Expenditure Benchmarks are calculated by adjusting the Historical Expenditure Baseline using Trending (Section 3.1) and Risk Adjustment (Section 3.2). The Performance Year Expenditure Benchmarks for the ESCO whose ESCO Beneficiaries are included in the Aggregation Pool will be a Beneficiary-Month weighted average of each CEC Non-LDO Entity's PBPY expenditures at Eligibility Category level for any CEC Non-LDO Entity Beneficiaries in the Aggregation Pool, as discussed in Section 3.3.

3.1 Trending for the Performance Year Expenditure Benchmarks

To calculate the PY Expenditure Benchmarks, the Historical Expenditure Baseline for each Eligibility Category will be Trended forward based on the sum of 50% of the average percentage of the national growth rate for Reference Group Beneficiary PBPY expenditures (defined in Section 1.1) and 50% of the absolute dollar amount of that growth. Trending for the PY Expenditure Benchmarks requires three steps.

Step 1: Calculate absolute difference in Reference Group Beneficiary Spending. The absolute difference in spending (*D*) is equal to the difference between PBPY Historical Expenditure Baseline for the Reference Group Beneficiaries and PBPY expenditures in the PY for the Reference Group Beneficiaries. Exhibit 10 illustrates using PY1: column 4 calculates the absolute difference in spending between the Historical Expenditure Baseline and PY1 for the Reference Group Beneficiaries.

Step 2: Calculate the Reference Group Beneficiary Trending factor. Trending factors will be calculated using PBPY expenditures for Reference Group Beneficiaries in each Eligibility Category. PY Trending factors are equal to PBPY PY expenditures for the Reference Group Beneficiaries divided by PBPY Historical Expenditure Baseline for the Reference Group Beneficiaries. Column 3 of Exhibit 10 provides hypothetical figures.

Step 3: Trend Historical Expenditure Baseline to PY. The Historical Expenditure Baseline for Eligible BY Beneficiaries will be Trended to be comparable to PY figures by adjusting PBPY using the Trending factor and absolute difference as shown in Exhibit 10. Column 7 of Exhibit 10 shows that PBPY PY1 Trended expenditures are equal to the Historical Expenditure Baseline (Column 1), plus 50 percent of the Trend factor minus one (Column 5) multiplied by the Historical Expenditure Baseline, plus 50 percent of the absolute difference in spending between PY3 and the Historical Expenditure Baseline (Column 6).

Exhibit 10. Trending Historical Expenditure Baseline to PY1

Eligibility Category	Historical Expenditure Baseline PBPY		Reference Group Beneficiaries		Weighted Trending Components Based on Reference Group Beneficiaries		Historical Expenditure Baseline PBPY Trended to PY1
	$PBPY_B$ [1]	$PBPY_{PY1}$ [2]	$T_{B,PY1}$ [3]	$D_{B,PY1}$ [4]	$0.5(T_{B,PY1} - 1)$ [5]	$0.5D_{B,PY1}$ [6]	$Expend_B^{PY1}$ [7]
Aged dual	$92,205	$109,538	1.05	$16,000	0.025	$8,000	$102,510
Aged non-dual	$71,814	$74,359	1.02	$7,000	0.01	$3,500	$76,032
Disabled dual	$99,113	$99,113	0.99	$3,000	–0.005	$1,500	$100,117
Disabled non-dual	$81,217	$94,059	1.06	$4,000	0.03	$2,000	$85,654
ESRD	$63,915	$63,915	1.04	$2,500	0.02	$1,250	$66,443

[1] comes from Exhibit 9.
[2] represents hypothetical PBPY expenditures for PY1 from Exhibit 14.
[3]–[6] are components of the Trending factor, based on the Reference Group Beneficiaries.
[7] is Trended PBPY spending, equal to [1] + [1] × [5] + [6] .

3.2 Risk Adjustment for the Performance Year Expenditure Benchmarks

This section explains the approach used to Risk Adjust the Historical Expenditure Baseline to produce the Performance Year Expenditure Benchmarks.

The Risk Adjustment approach requires the following steps:

Step 1: Choose risk score to be used for Newly-Aligned ESCO Beneficiaries. Newly-Aligned ESCO Beneficiaries can be either new to Medicare (with fewer than 12 months of claims history) or established (with 12 or more months of claims history).

- Demographic risk scores will be used for Newly-Aligned ESCO Beneficiaries who are newly aligned in the Performance Years.
- Full risk scores will be used for established, Newly-Aligned ESCO Beneficiaries in the Performance Years. As described in Section 2.8, full risk scores will be divided by a renormalization factor to ensure that the average risk score is 1.0 every year. The renormalization factor will be calculated as the average risk score across the entire reference population, regardless of Eligibility Category.

Step 2: Choose risk score to be used for Established Beneficiaries who are also Continuously Aligned ESCO Beneficiaries. For Continuously Aligned ESCO Beneficiaries, either the FRS or a demographic-adjusted version of the BY3 FRS will be used. In the case of the PY1 Expenditure Benchmark, the FRS will be used if the PY1/BY3 average FRS ratio for Continuously Aligned ESCO Beneficiaries is lower than 1. Such a ratio would imply that, on average, the PY1 FRS is lower than the BY3 FRS. However, if the ratio is higher than 1 — implying that, on average, the

PY1 FRS is higher than the BY3 FRS — a demographic-adjusted version of the BY3 FRS will be used. The demographic adjustment adjusts the BY3 FRS to account for changes in demographics between BY3 and PY1. The same process will be used for the PY2 and PY3 Expenditure Benchmarks.

Step 3: Calculate weighted average risk score for each Eligibility Category. Similar to Step 3 in Section 2.8, this step calculates an overall weighted average risk score for each Eligibility Category based on the average risk scores separately selected in Step 1 and Step 2. The weights used to produce the average are the Beneficiary-Months of New Beneficiaries and Established Beneficiaries in each Eligibility Category.

Step 4: Convert risk scores into risk score ratios. Similar to Step 4 in Section 2.8, the overall Eligibility Category weighted average risk scores resulting from Step 3 will be converted into risk score ratios, which are equal to the average risk score for the later year divided by that of the earlier year. In this case, the later year is the PY for which the Expenditure Benchmark is being formed, and the earlier year is always BY3.

Step 5: Perform Risk Adjustment. Similar to Step 5 in Section 2.8, the Historical Expenditure Baseline will be multiplied by the risk score ratios. Exhibit 11 illustrates the Risk Adjustment calculations. The Trended expenditures in column 7 of Exhibit 10, reproduced in column 2 of Exhibit 11, are multiplied by the risk score ratios in column 1. The result is shown in column 3, which provides Trended and Risk Adjusted Historical Expenditure Baseline figures.

Exhibit 11. Risk Adjustment of Historical Expenditure Baseline

Eligibility Category	PY1,HB Risk Score Ratio [1]	HB PBPY Spending Trended to PY1 [2]	Trended and Risk-Adjusted PY1 Expenditure Benchmark PBPY [3]
Aged dual	1.12	$102,510	$114,811
Aged non-dual	1.00	$76,032	$76,032
Disabled dual	1.05	$100,117	$105,123
Disabled non-dual	1.13	$85,654	$96,788
ESRD	0.93	$66,443	$61,792

[1] represents hypothetical PY1/HB (Historical Expenditure Baseline) risk score ratios.
[2] shows Historical Expenditure Baseline PBPY Trended to PY1 from Exhibit 10, column [7].
[3] shows Risk-Adjusted expenditures, equal to [1] × [2].

3.3 Performance Year Expenditure Benchmarks

As described in Section 1.2 and Section 5, if the Non-LDO ESCO has fewer than 350 ESCO Beneficiaries, it will have its ESCO Beneficiaries included in an Aggregation Pool with the Medicare beneficiaries who have been aligned to one or more CEC Non-LDO Entities and for financial calculation purposes. If the Non-LDO ESCO satisfies the 350 ESCO Beneficiary threshold, it will have the option of having its ESCO Beneficiaries included in an Aggregation

Pool. This section uses hypothetical PY2 figures to provide examples for two cases. In the first case, shown in Exhibit 12, Aggregation Pool A is composed of the ESCO and one CEC Non-LDO Entity (labeled A1 and A2) that do not separately satisfy the 350 aligned beneficiary threshold. The exhibit shows how the ESCO A1 and CEC Non-LDO Entity A2 figures are aggregated to arrive at a single aggregated Aggregation Pool A PY2 Expenditure Benchmark. In another example, the ESCO, referred to as ESCO B in this example, satisfies the 350 aligned beneficiary threshold and chooses not to have its ESCO Beneficiaries in an Aggregation Pool. Because ESCO B is not required to have its ESCO Beneficiaries included in an Aggregation Pool, Exhibit 13 simply provides PY2 Expenditure Benchmark figures that will be used in the examples in Section 6.

Exhibit 12. PY2 Expenditure Benchmark for Aggregation Pool A

Eligibility Category	PY2 Expenditure Benchmark (PBPY), ESCO A1	PY2 Bene-Years, ESCO A1	PY2 Expenditure Benchmark (PBPY), CEC Non-LDO Entity A2	PY2 Bene-Years, CEC Non-LDO Entity A2	PY2 Expenditure Benchmark (PBPY), Aggregation Pool A
	[1]	[2]	[3]	[4]	[5]
Aged dual	$107,524	53	$105,783	33	$106,856
Aged non-dual	$88,267	38	$82,180	33	$85,438
Disabled dual	$101,258	57	$96,299	62	$98,674
Disabled non-dual	$98,214	29	$94,422	42	$95,971
ESRD	$85,354	25	$68,706	19	$78,165

[1], [2], [3], and [4] are hypothetical figures.
[5] is an average of [1] and [3], weighted by Beneficiary-Years in [2] and [4].

Exhibit 13. PY2 Expenditure Benchmark for ESCO B

Eligibility Category	PY2 Expenditure Benchmark (PBPY)	PY2 Beneficiary-Years
Aged dual	$113,248	166
Aged non-dual	$79,875	331
Disabled dual	$104,263	414
Disabled non-dual	$94,713	530
ESRD	$65,332	215

4. PERFORMANCE YEAR EXPENDITURES

Similar to the Historical Expenditure Baseline process described in Sections 2.1 through 2.6, the following steps will be used to calculate Performance Year expenditures on a PBPY basis:

- Gather all claims data for ESCO Beneficiaries for PY1, PY2, and PY3.
- Apply adjustments and exclusions to PY1, PY2, and PY3 claims (Sections 4.1 and 4.2)[10]
- Annualize, Truncate, and apply a Completion Factor to PY1, PY2, and PY3 claims and compute weighted average PBPY expenditures for each PY (Sections 4.3 through 4.6)
- Aggregate combined Performance Year expenditures for the ESCO if the ESCO Beneficiaries are included in an Aggregation Pool (Section 4.7)

Unlike the Historical Expenditure Baseline, the Performance Year PBPY figures will not be Trended or Risk Adjusted.

4.1 Dialysis Claims Adjustments

As described in Section 2.1, ESRD PPS[11] dialysis claims will be handled differently from other types of claims used in the financial calculations. In particular, rather than the claim payment amount observed in the claims data, the CEC Initiative will use the base rate amount for each dialysis treatment. Doing so removes from the financial calculations all of the adjustments to the base rate that CMS uses to calculate dialysis payments under the ESRD PPS. Among other adjustments, this includes geographical price variation and payment reductions under the Quality Incentive Program. The ESRD PPS base rate changes annually and is publicly available from the ESRD PPS final rule.[12]

4.2 Exclusions and Sequestration Adjustment

The financial calculations will exclude four types of payments — indirect medical education (IME), disproportionate share hospitals (DSH), uncompensated care, and kidney transplant-related services — and will adjust claim payment amounts for sequestration reductions. Additional detail on these exclusions and adjustments is available in Section 2.2. All other

[10] In addition to the exclusions listed in Section 4.2, in the future CMS may decide to exclude material changes to provider reimbursement, such as care management fees and quality payments.

[11] Beginning January 1, 2011, the Medicare Improvements for Patients and Providers Act mandated the implementation of a bundled payment system for outpatient maintenance dialysis services. This ESRD PPS bundled payment covers a set of dialysis-related items and services routinely required for dialysis treatments. It consists of a base (unadjusted) rate modified by several adjustments at the provider, patient, and claim levels (http://www.usrds.org/2012/pres/USDialysisBundle_impact_NKFCM2012.pdf). Additional information about the ESRD PPS is available from the ESRD PPS final rule: http://www.cms.gov/Medicare/Medicare-Fee-for-Service-Payment/ESRDpayment/End-Stage-Renal-Disease-ESRD-Payment-Regulations-and-Notices.html.

[12] Dialysis claims are the only claim type from which the CEC Initiative removes geographical variation in payments.

expenditure information included in the seven Medicare Parts A and B claims files (inpatient, outpatient, carrier, DME, hospice, SNF, and HHA) will be included in the financial calculations.

4.3 Annualization

Annualization is required to allow the summing of cost data from ESCO Beneficiaries with differing numbers of months of service and to produce PBPY estimates. To implement Annualization, spending is multiplied by an Annualization factor, which is equal to 12 divided by the number of Eligible Beneficiary-Months. Annualized expenditures are calculated separately for each Eligibility Category so that an ESCO Beneficiary can contribute experience to multiple Eligibility Categories in the same year. If an ESCO Beneficiary has 6 months of alignment, the Annualization factor would equal 12/6 or 2.

Annualized expenditures are calculated separately for each Eligibility Category so that an ESCO Beneficiary can contribute experience to multiple Eligibility Categories in the same year.

4.4 Truncation

As described in Section 2.4, Annualized expenditures will be Truncated to limit financial risk to the ESCO posed by high-cost beneficiary outliers. Outlier Annualized expenditures will be Truncated by capping expenditures at a specific maximum value known as the Truncation threshold or stop-loss limit. The threshold is equal to the 99th percentile of expenditures for non-ESRD FFS Medicare beneficiaries plus the difference between average expenditures for Medicare ESRD beneficiaries (the reference group, discussed in Section 1.1) and average expenditures for non-ESRD FFS Medicare beneficiaries. Similar to Annualization, expenditures are Truncated separately for each Eligibility Category. If an ESCO Beneficiary changes Eligibility Categories during a PY, the ESCO Beneficiary will contribute experience to multiple Eligibility Categories in the same Performance Year.

4.5 Completion Factor

Because the CEC Initiative relies on three months of claims run-out for most financial calculations, expenditure amounts will be adjusted using a Completion Factor to account for claims that may have not been processed as of 3 months after the end of a PY. As described in Section 2.5, the Completion Factor will be estimated based on CY2012 data and applied to all years. The Completion Factor will be applied separately to each Eligibility Category's Annualized and Truncated expenditures.

4.6 Weighted Average of Truncated Expenditures

This section discusses the computation of PBPY expenditures, which involves weighting each beneficiary's expenditures to account for partial years of eligibility and then averaging across

beneficiaries in each Eligibility Category. The process is the same as that described in Section 2.6.

Step 1: Calculate weighting factor. The weighting factor is equal to the number of Beneficiary-Years during which each beneficiary was aligned (in the case of ESCO Beneficiaries) or eligible (in the case of Reference Group Beneficiaries), divided by 12.

Step 2: Apply weighting factor. The weighting factor will be multiplied by the Annualized, Truncated, and Completed expenditures resulting from the calculations described in Sections 4.1 through 4.5 to produce weighted expenditures.

Step 3: Calculate weighted average of Truncated expenditures. Weighted expenditures from Step 2 will be added within each of the five Eligibility Categories. Each sum will be divided by total Beneficiary-Years in the Eligibility Category, which is equal to the sum of the weighting factors (from Step 1) within the Eligibility Category.

The weighted average of Truncated expenditures produces PBPY figures by Eligibility Category. Exhibit 14 provides hypothetical PY1, PY2, and PY3 PBPY expenditures that have been Annualized, Truncated, Completed, and weighted. These expenditures will be used to estimate Shared Savings by comparing them to their respective PY Expenditure Benchmarks. The last row of the exhibit provides an average, weighted by the Beneficiary-Years in Exhibit 15.

Exhibit 14. Hypothetical Performance Year PBPY Expenditures

Eligibility Category	PY1 PBPY	PY2 PBPY	PY3 PBPY
Aged dual	$109,538	$113,568	$120,673
Aged non-dual	$74,359	$76,257	$82,862
Disabled dual	$99,113	$100,839	$106,831
Disabled non-dual	$94,059	$96,287	$101,398
ESRD	$63,915	$65,823	$69,271
Average	**$91,900**	**$91,187**	**$98,456**

All values are hypothetical. Averages are weighted by Beneficiary-Years in Exhibit 15.

Exhibit 15. Hypothetical Performance Year Beneficiary-Years

Eligibility Category	PY1 Beneficiary-Years	PY2 Beneficiary-Years	PY3 Beneficiary-Years
Aged dual	291	166	263
Aged non-dual	260	331	316
Disabled dual	383	414	439
Disabled non-dual	444	530	526
ESRD	153	215	210
Total	**1,532**	**1,656**	**1,754**

4.7 Performance Year Expenditures for Aggregation Pools

As described in Sections 1.2 and Section 5, if the ESCO has fewer than 350 ESCO Beneficiaries, its ESCO Beneficiaries will be grouped in an Aggregation Pool with CEC Non-LDO Entity Beneficiaries for financial calculation purposes and deemed to have met the minimum 350 aligned beneficiary requirement. If the ESCO satisfies the 350 ESCO Beneficiary threshold, it will also have the option of having its ESCO Beneficiaries grouped in an Aggregation Pool. This section uses PY2 figures to provide examples for two cases. In the first case, shown in Exhibit 16, Aggregation Pool A is composed of the ESCO and a CEC Non-LDO Entity (labeled A1 and A2, respectively) that do not separately satisfy the 350 aligned beneficiary threshold. The exhibit shows how the ESCO A1 and CEC Non-LDO Entity A2 figures are aggregated to arrive at a single Aggregation Pool A PY2 expenditure amount. CMS will use a weighted average of PY expenditures for ESCO A1 and CEC Non-LDO Entity A2 to produce Aggregation Pool A PY2 expenditures. Beneficiary-Years are used as the weights. If the ESCO satisfies the 350 ESCO Beneficiary threshold, it can choose not to have its ESCO Beneficiaries grouped in an Aggregation Pool (ESCO B in this example). Because ESCO B does not need to have its ESCO Beneficiaries included in an Aggregation Pool, Exhibit 17 simply provides PY2 expenditure figures that will be used in the examples in Section 6.

Exhibit 16. PY2 Expenditures for Aggregation Pool A

Eligibility Category	PY2 Expenditures (PBPY), ESCO A1 [1]	PY2 Bene-Years, ESCO A1 [2]	PY2 Expenditures (PBPY), CEC Non-LDO Entity A2 [3]	PY2 Bene-Years, CEC Non-LDO Entity A2 [4]	PY2 Expenditures (PBPY), Aggregation Pool A [5]
Aged dual	$98,265	53	$100,589	33	$99,157
Aged non-dual	$80,325	38	$80,354	33	$80,338
Disabled dual	$96,175	57	$99,214	62	$97,758
Disabled non-dual	$90,354	29	$87,523	42	$88,679
ESRD	$68,423	25	$69,534	19	$68,903

[1] and [3] provide hypothetical PBPY expenditures for PY2.
[2] and [4] are from Exhibit 12.

Exhibit 17. PY2 Expenditures for ESCO B

Eligibility Category	PY2 PBPY	PY2 Beneficiary-Years
Aged dual	$105,983	166
Aged non-dual	$75,631	331
Disabled dual	$100,839	414
Disabled non-dual	$93,421	530
ESRD	$65,823	215
Average	**$91,187**	**1,656**

PY2 PBPY values are hypothetical.
PY2 Beneficiary-Years are from Exhibit 15.

5. AGGREGATION POOL METHODOLOGY

In order to produce statistically valid figures for Financial Reconciliation, CMS requires that the ESCO have a minimum of 350 ESCO Beneficiaries or have its ESCO Beneficiaries included in an Aggregation Pool with Medicare beneficiaries who have been aligned to a CEC Non-LDO Entity so that the combined number of beneficiaries in the Aggregation Pool is at least 350.

However, CMS, in its sole discretion, may allow the ESCO to participate under a Corrective Action Plan without including its ESCO Beneficiaries in an Aggregation Pool if all of the conditions described in Section 5.2 are met. In such an instance, CMS may raise the ESCO's MSR to greater than 4.75% using the methodology described in Section 6.1.

This section discusses the approaches for including ESCO Beneficiaries in an "Aggregation Pool" (Section 5.1) and an exception to the requirement to include ESCO Beneficiaries into an Aggregation Pool (Section 5.2).

5.1 Combining ESCO Beneficiaries into an Aggregation Pool

If at the start of a Performance Year CMS determines that fewer than 350 ESCO Beneficiaries are aligned to the ESCO and the exception described in Section 5.2 does not apply, CMS will include these ESCO Beneficiaries in an Aggregation Pool for that Performance Year for two purposes only:

(i) Satisfying the minimum number of ESCO Beneficiaries required for participation in the CEC; and
(ii) Calculating the Total PY Expenditure Benchmarks (as described in Section 3.3), ESCO Total Revenue (as described in Section 4.7), and any Shared Savings (as described in Section 6)

CMS will determine the composition of any Aggregation Pool or Pools in its sole discretion. If the ESCO has its ESCO Beneficiaries included in an Aggregation Pool, the ESCO:

(i) Will be subject to the MSR that characterizes that Aggregation Pool; and
(ii) Will otherwise remain independent from the CEC Non-LDO Entities whose CEC Non-LDO Entity Beneficiaries are included in the Aggregation Pool and will continue to be an independent legal entity under this Agreement.

If the ESCO chooses to have its ESCO Beneficiaries included in an Aggregation Pool even though the ESCO satisfies the 350 beneficiary requirement, the ESCO will likely benefit from a lower MSR, as described in Section 6. The following discussion is organized into three scenarios:

(i) ESCO satisfying the minimum ESCO Beneficiary threshold and having its ESCO Beneficiaries included in an Aggregation Pool;
(ii) ESCO satisfying the minimum ESCO Beneficiary threshold and not having its ESCO Beneficiaries included in an Aggregation Pool; and
(iii) ESCO with fewer than 350 ESCO Beneficiaries whose ESCO Beneficiaries are included in an Aggregation Pool.

ESCO with 350 or more ESCO Beneficiaries with its ESCO Beneficiaries included in an Aggregation Pool. If CMS finds that 350 or more ESCO Beneficiaries are aligned to the ESCO at the start of a Performance Year, the ESCO may request to, but is not required to, have its ESCO Beneficiaries included in an Aggregation Pool for that Performance Year. The ESCO must notify CMS of its request to participate in an Aggregation Pool within 30 days of the start of the Performance Year and cannot withdraw from the Aggregation Pool at any point during the Performance Year.

If for any reason, including the termination of one of the ESCO's Dialysis Facilities, the number of ESCO Beneficiaries falls below 350 during the Performance Year, CMS may take action against the ESCO. Such action could include placing the ESCO on a Corrective Action Plan for failing to maintain at least 350 ESCO Beneficiaries. Under this specific Corrective Action Plan, the ESCO may add Dialysis Facilities so that the Aggregation Pool meets the minimum number of ESCO Beneficiaries.

ESCO with 350 or more ESCO Beneficiaries with its ESCO Beneficiaries not included in an Aggregation Pool. If the ESCO with 350 or more ESCO Beneficiaries does not have its ESCO Beneficiaries included in an Aggregation Pool, and if for any reason, including the termination of one of the ESCO's Dialysis Facilities, the number of ESCO Beneficiaries falls below 350 during the Performance Year, CMS may take action against the ESCO. Such action could include

(i) Grouping the ESCO Beneficiaries in an Aggregation Pool; or
(ii) Placing the ESCO on a Corrective Action Plan for failing to maintain at least 350 ESCO Beneficiaries. Under this specific Corrective Action Plan, the ESCO may add Dialysis Facilities in order for the ESCO to meet the minimum number of ESCO Beneficiaries.

ESCO with fewer than 350 aligned beneficiaries. As described previously, if the ESCO has fewer than 350 ESCO Beneficiaries and the exception described in Section 5.2 does not apply, its ESCO Beneficiaries will be included in an Aggregation Pool. If for any reason, including the termination of a CEC Non-LDO Entity in the Aggregation Pool, CMS determines that the number of ESCO Beneficiaries and CEC Non-LDO Entity Beneficiaries in an Aggregation Pool falls below 350 during the Performance Year, CMS may take appropriate action for non-compliance with the Agreement, including placing the ESCO on a Corrective Action Plan. Under this Corrective Action Plan, CMS may permit or require the ESCO to add Dialysis Facilities in order for either the ESCO itself or the CEC Non-LDO Entities whose CEC Non-LDO Entity Beneficiaries are included in the Aggregation Pool to meet the minimum number of ESCO Beneficiaries.

5.2 Exception to Requirement to Include ESCO Beneficiaries in an Aggregation Pool if the ESCO has Fewer than 350 ESCO Beneficiaries

Even if the ESCO has fewer than 350 ESCO Beneficiaries, CMS, in its sole discretion, may allow the ESCO to participate in the CEC Initiative if there is no Aggregation Pool that includes at least 350 ESCO Beneficiaries. Under such circumstances, the ESCO shall be subject to a Corrective Action Plan and may be subject to an MSR of greater than 4.75% (as calculated using the methodology described in Section 6.1).

6. DETERMINATION OF SHARED SAVINGS

Shared Savings will be calculated at the end of each Performance Year based on a comparison of each year's Total PY Expenditure Benchmark (from Section 3.3) to the same year's ESCO Total Revenue (from Section 4.7). Section 6.1 provides two examples to illustrate how Shared Savings will be calculated for the ESCO. The example for ESCO A1 and CEC Non-LDO Entity A2 illustrates the calculations if the ESCO's ESCO Beneficiaries are included in an Aggregation Pool either because the ESCO has fewer than 350 ESCO Beneficiaries or because it requests to have its ESCO Beneficiaries included in an Aggregation Pool even though it meets the aligned beneficiary minimum. The example for ESCO B illustrates the calculations if the ESCO chooses not to have its ESCO Beneficiaries grouped in an Aggregation Pool (an option the ESCO can request if it satisfies the 350 minimum ESCO Beneficiary threshold). Both examples use figures for PY2, and the discussion refers to Exhibit 19 (which contains information for Aggregation Pool A) and

Exhibit 20 (which contains information for ESCO B). Section 6.2 discusses reconciliation for the ESCO with ESCO Beneficiaries in an Aggregation Pool where a CEC Non-LDO Entity with CEC Non-LDO Beneficiaries in the same Aggregation Pool terminates participation in the CEC Initiative.

6.1 Shared Savings Calculations if the ESCO Participates in the CEC Initiative for a Full Performance Year

The following steps will be used to conduct Financial Reconciliation for the ESCO when it participates for a full Performance Year:

- Calculation of Total PY Expenditure Benchmark, ESCO Total Revenue, and Preliminary Shared Savings (Steps 1, 2, and 3).
- Comparison of Preliminary Shared Savings to the MSR (Step 4).
- Application of the Shared Savings Percentage (Step 5).
- If the ESCO Beneficiaries are included in an Aggregation Pool:
    - The Shared Savings Cap will be applied (Step 6A).
    - Aggregated Preliminary Shared Savings will be apportioned to the ESCO and any CEC Non-LDO Entities whose CEC Non-LDO Entity Beneficiaries are included in the Aggregation Pool (Step 7A).
    - Preliminary Shared Savings will be adjusted for quality and sequestration (Steps 8A and 9A).
- If the ESCO Beneficiaries are not included in an Aggregation Pool:
    - Preliminary Shared Savings will be adjusted for quality (Step 6B).
    - The Shared Savings Cap will be applied (Step 7B).
    - Preliminary Shared Savings will be adjusted for sequestration (Step 8B).

Step 1: Calculate Total PY Expenditure Benchmark. Multiply the Performance Year Expenditure Benchmark PBPY by Beneficiary-Years for the Performance Year for each Eligibility Category, and then sum across all Eligibility Categories. If the ESCO Beneficiaries are included in an Aggregation Pool, the ESCO's Performance Year Expenditure Benchmark will be the combined Performance Year Expenditure Benchmarks for the ESCO and any CEC Non-LDO Entity whose CEC Non-LDO Entity Beneficiaries who are included in the Aggregation Pool. Exhibit 19 and

Exhibit 20 provide the Total PY2 Expenditure Benchmark for Aggregation Pool A. The PBPY Expenditure Benchmarks are from Exhibit 12 (ESCO A1 and CEC Non-LDO Entity A2) and Exhibit 13 (ESCO B).

Aggregation Pool A Total PY2 Expenditure Benchmark =	**$37,251,121**
ESCO B PY2 Total PY2 Expenditure Benchmark =	**$152,646,945**

Step 2: Calculate ESCO Total Revenue. Multiply Performance Year PBPY expenditures by Beneficiary-Years and sum across Eligibility Categories. Similar to the PY Expenditure Benchmark in the previous step, for ESCO Beneficiaries included in the Aggregation Pool, the ESCO Total Revenue and the revenue for any CEC Non-LDO Entities whose CEC Non-LDO Entity Beneficiaries are included in the Aggregation Pool will be combined and will be considered the ESCO Total Revenue for financial calculation purposes. Column 5 of Exhibit 19 and

Exhibit 20 provides the ESCO Total Revenue for each scenario:

Aggregation Pool A PY2 ESCO Total Revenue =	**$35,192,643**
ESCO B PY2 ESCO Total Revenue =	**$148,039,460**

Step 3: Calculate ESCO Preliminary Shared Savings. Subtract ESCO Total Revenue from the PY Total Expenditure Benchmark. This produces the following results:

Aggregation Pool A Preliminary Shared Savings	=	$37,251,121 - $35,192,643
	=	**$2,058,478**
ESCO B Preliminary Savings	=	$152,646,945 - $148,039,460
	=	**$4,607,485**

If these calculations resulted in negative numbers, the Aggregation Pool or the ESCO would have produced losses. However, the ESCO is a non-LDO entity and therefore is only subject to one-sided risk and will not be held fiscally responsible for shared losses.

Step 4: Compare Preliminary Shared Savings to MSR. The MSR is designed to ensure the statistical validity of any Preliminary Shared Savings that may be achieved by the ESCO. As a result, the MSR varies based on the number of ESCO Beneficiaries and CEC Non-LDO Entity Beneficiaries in an Aggregation Pool if the ESCO's Beneficiaries are included in an Aggregation Pool or the number of ESCO Beneficiaries if the ESCO Beneficiaries are not included in an Aggregation Pool.

Exhibit 18 provides MSRs for the ESCO (or the Aggregation Pool) based on the number of ESCO Beneficiaries or ESCO Beneficiaries and CEC Non-LDO Entity Beneficiaries in an Aggregation Pool. If the number of ESCO Beneficiaries (or the number of the Aggregation Pool's aligned beneficiaries) falls between the endpoints, it will have an MSR equal to a weighted average of the upper and lower MSRs for the category. For the purpose of this example, it is assumed that Aggregation Pool A has **488** ESCO Beneficiaries and CEC Non-LDO Entity Beneficiaries and ESCO B has **2,070** ESCO Beneficiaries. Aggregation Pool A's MSR is given by the following equation:

Aggregation Pool A's MSR = 4.20% × (499 – 488)/(499 – 450) + 4.00% × (488 – 450)/(499 – 450) = **4.04%**

Exhibit 18. MSR by Number of ESCO Beneficiaries

Number of ESCO Beneficiaries	MSR at low end of ESCO Beneficiary range	MSR at high end of ESCO Beneficiary range
350-399	4.75%	4.40%
400-449	4.40%	4.20%
450-499	4.20%	4.00%
500-599	4.00%	3.60%
600-799	3.60%	3.10%

800-999	3.10%	2.80%
1000-1199	2.80%	2.60%
1200-1399	2.60%	2.40%
1400-1599	2.40%	2.20%
1600-1799	2.20%	2.10%
1800-1999	2.10%	2.00%
2000+	2.00%	2.00%

To remain eligible for Shared Savings, the Preliminary Shared Savings amount must meet or exceed the MSR.

Aggregation Pool A PY2 minimum savings = .0404 × $37,251,121 = **$1,504,945**
ESCO B PY2 minimum savings = .02 × $152,646,945 = **$3,052,939**

Because both Aggregation Pool A's and ESCO B's Preliminary Shared Savings exceed their minimum savings requirements, both remain eligible for Shared Savings. Where the Preliminary Shared Savings of the ESCO or the Aggregation Pool does not meet the MSR, the ESCO or the Aggregation Pool will not be eligible to receive Shared Savings.

CMS may specify a higher MSR if the ESCO has fewer than 350 ESCO Beneficiaries for a Performance Year.

Step 5: Apply Shared Savings Percentage. The ESCO will receive up to 50 percent of Preliminary Shared Savings. CMS will multiply Preliminary Shared Savings by this proportion.

Aggregation Pool A Preliminary Shared Savings with Shared Savings Percentage applied
= 0.5 × $2,058,478 = **$1,029,239**

ESCO B Preliminary Shared Savings with Shared Savings Percentage applied
= 0.5 × $4,607,485 = **$2,303,743**

Note: The financial calculations for ESCO Beneficiaries will slightly differ depending on whether the ESCO Beneficiaries are included in an Aggregation Pool. Consequently, Aggregation Pool A's and ESCO B's shared savings are discussed separately. The steps for Aggregation Pool A are indicated with an "A" in the step numbering while the steps for ESCO B are indicated with a "B."

<u>Aggregation Pool A (Group of ESCO Beneficiaries and CEC Non-LDO Entity Beneficiaries)</u>

Step 6A: Apply the Shared Savings Cap. Preliminary Shared Savings are capped at 5 percent of the PY Expenditure Benchmark for each Performance Year. The cap is applied to the Total PY Expenditure Benchmark.

Aggregation Pool A's PY2 Shared Savings Cap = 0.05 × $37,251,121 = **$1,862,556**

Aggregation Pool A's Preliminary Shared Savings (from Step 5) of $1,029,239 fall below its PY2 Shared Savings Cap. Therefore, ESCO A1 and CEC Non-LDO Entity A2 remain eligible to share the full Shared Savings amount.

Step 7A: Apportion aggregated Preliminary Shared Savings by Beneficiary-Year counts. After applying the Shared Savings Percentage and Shared Savings Cap, CMS will distribute the Preliminary Shared Savings according to the proportion of Beneficiary-Years contributed to the Aggregation Pool by the ESCO Beneficiaries and the CEC Non-LDO Entity Beneficiaries. From Exhibit 16, total aggregated Beneficiary-Years were 391, with ESCO A1 contributing 202 and CEC Non-LDO Entity A2 contributing 189. Therefore, ESCO A1 will be allocated 202 ÷ 391 = 51.7 percent of savings and CEC Non-LDO Entity A2 will be allocated 48.3 percent of savings.

ESCO A1's savings, apportioned by Beneficiary-Years =
.517 × $1,029,239 = **$532,117**

CEC Non-LDO Entity A2's savings, apportioned by Beneficiary-Years =
.483 × $1,029,239 = **$497,122**

Step 8A: Adjust allocated Preliminary Shared Savings for quality. To be eligible for Shared Savings, the ESCO must satisfy a minimum quality threshold, which will be determined by CMS. If the ESCO satisfies the minimum quality threshold, Preliminary Shared Savings will be adjusted for quality in order to provide the ESCO with a financial incentive to deliver quality care. In PY1, the ESCO will be paid for complete reporting on quality measures. There will be two reporting periods for PY1: the first six months of PY1 (July 1, 2015 – December 31, 2015) and the latter 12 months of PY1 (CY 2016). The ESCO will not be required to submit quality data during the first reporting period because it is a Non-LDO. During the second reporting period, if the ESCO reports all requested quality data and if the ESCO submits these data in a timely fashion, the PY1 quality score will be treated as "1" for the purpose of quality adjusting Preliminary Shared Savings. If the ESCO does not report all data in a timely fashion during the second reporting period, the quality score will be treated as a "0" for the purpose of quality adjusting Preliminary Shared Savings and the ESCO will be ineligible to receive Shared Savings.

In PY2 and later years, however, the ESCO's Preliminary Shared Savings will be adjusted for quality achievement. The ESCO's quality score will be calculated as a percentage. For this example, the PY2 quality score is assumed to be 85 percent for ESCO A1 and 75 percent for CEC Non-LDO Entity A2. To adjust for quality, savings will be multiplied by the ESCO's quality score.

ESCO A1's quality-adjusted Preliminary Shared Savings =
0.85 × $532,117 = **$452,299**

CEC Non-LDO Entity A2's quality-adjusted Preliminary Shared Savings =
0.75 × $497,122 = **$372,842**

Step 9A: Apply the sequestration adjustment to Preliminary Shared Savings. As described in Section 2.2.3, Preliminary Shared Savings amounts are subject to the 2 percent sequestration reduction. Therefore, the Shared Savings from Financial Reconciliation are:

ESCO A1's Shared Savings	= .98 × $452,299 =	**$443,253**
CEC Non-LDO Entity A2's Shared Savings	= .98 × $372,842 =	**$365,385**

As noted in Step 8A, PY1 uses pay-for-reporting and there is no quality adjustment in this year. Therefore, if the example used PY1 figures, the amount to which the sequestration adjustment is applied would be different from the amounts in the equations above.

ESCO B (ESCO Beneficiaries Not Included in an Aggregation Pool)

Step 6B: Adjust Preliminary Shared Savings for quality. As described previously, Preliminary Shared Savings will be adjusted for quality in order to provide the ESCO with a financial incentive to deliver quality care. In PY1, the ESCO will be paid for complete reporting on quality measures. There will be two reporting periods for PY1: the first six months of PY1 (July 1, 2015 – December 31, 2015) and the latter 12 months of PY1 (CY 2016). The ESCO will not be required to submit quality data during the first reporting period because it is a Non-LDO. During the second reporting period, if the ESCO reports all requested quality data and if the ESCO submits these data in a timely fashion, the PY1 quality score will be treated as "1" for the purpose of quality adjusting Preliminary Shared Savings. If the ESCO does not report all data in a timely fashion during the second reporting period, the quality score will be treated as a "0" for the purpose of quality adjusting Preliminary Shared Savings and the ESCO will be ineligible to receive Shared Savings.

In PY2 and later years, however, the ESCO's Preliminary Shared Savings will be adjusted for quality achievement. The ESCO's quality score will be calculated as a percentage and Preliminary Shared Savings will be multiplied by that percentage to adjust for quality. For this example, the PY2 quality score is assumed to be 80 percent for ESCO B.

ESCO B's quality-adjusted Preliminary Shared Savings = 0.8 × $2,303,743 = **$1,842,994**

Step 7B: Apply the Shared Savings Cap. Preliminary Shared Savings are capped at 5 percent of the Total PY Expenditure Benchmark for each Performance Year.

ESCO B's PY2 Shared Savings Cap = 0.05 × $152,646,945 = **$7,632,347**

ESCO B's Preliminary Shared Savings (from Step 5B) of $1,842,994 falls below its PY2 Shared Savings Cap. Therefore, ESCO B remains eligible to share the full Shared Savings amount.

Step 8B: Apply the sequestration adjustment to Preliminary Shared Savings. As described in Section 2.2.3, Preliminary Shared Savings amounts are subject to the 2 percent sequestration reduction. Therefore, the final results (the Shared Savings) from the determination process are:

ESCO B's Shared Savings = .98 × $1,842,994 = **$1,806,134**

Exhibit 19. Calculation of Preliminary Shared Savings for Aggregation Pool A

Eligibility Category	PY2 Benchmark PBPY Spending	PY2 Actual PBPY Spending	PY2 Bene-Years	PY2 Benchmark Total Spending	PY2 Actual Total Spending	Preliminary Shared Savings
	[1]	[2]	[3]	[4]	[5]	[6]
Aged dual	$106,856	$99,157	86	$9,189,616	$8,527,502	$662,114
Aged non-dual	$85,438	$80,338	71	$6,066,098	$5,703,998	$362,100
Disabled dual	$98,674	$97,758	119	$11,742,206	$11,633,202	$109,004
Disabled non-dual	$95,971	$88,679	71	$6,813,941	$6,296,209	$517,732
ESRD	$78,165	$68,903	44	$3,439,260	$3,031,732	$407,528
Total				**$37,251,121**	**$35,192,643**	**$2,058,478**

[1] comes from Exhibit 12.
[2] comes from Exhibit 16.
[3] is the sum of [2] and [4] from Exhibit 16.
[4] = [1] × [3]; [5] = [2] × [3]; [6] = [4] - [5]

Exhibit 20. Calculation of Preliminary Shared Savings for ESCO B

Eligibility Category	PY2 Benchmark PBPY Spending [1]	PY2 Actual PBPY Spending [2]	PY2 Bene-Years [3]	PY2 Benchmark Total Spending [4]	PY2 Actual Total Spending [5]	Preliminary Shared Savings [6]
Aged dual	$113,248	$105,983	166	$18,799,168	$17,593,178	$1,205,990
Aged non-dual	$79,875	$75,631	331	$26,438,625	$25,033,861	$1,404,764
Disabled dual	$104,263	$100,839	414	$43,164,882	$41,747,346	$1,417,536
Disabled non-dual	$94,713	$93,421	530	$50,197,890	$49,513,130	$684,760
ESRD	$65,332	$65,823	215	$14,046,380	$14,151,945	($105,565)
Total				**$152,646,945**	**$148,039,460**	$4,607,485

[1] comes from Exhibit 13.
[2] and [3] come from Exhibit 17.
[4] = [1] × [3]; [5] = [2] × [3]; [6] = [4] – [5]

6.2 Shared Savings Determination if the ESCO Does Not Participate in the CEC Initiative for a Full Performance Year

Because participation in the CEC Initiative is voluntary, the ESCO may choose to end its participation in the CEC Initiative at any time. In addition, there are circumstances under which CMS will terminate the ESCO's participation in the CEC Initiative. This section describes Financial Reconciliation when the ESCO leaves the CEC Initiative before a PY's completion. Section 6.1 describes Financial Reconciliation where the ESCO participates in the CEC Initiative for a full PY. If the ESCO only participates in the CEC Initiative for a partial PY, it will not be eligible to receive Shared Savings.

The remainder of this section describes the impact on Financial Reconciliation for the ESCO whose ESCO Beneficiaries are included in an Aggregation Pool when a CEC Non-LDO Entity whose CEC Non-LDO Entity Beneficiaries are in the Aggregation Pool drops out of the CEC Initiative after only a partial PY. Because a CEC Non-LDO Entity's voluntary and involuntary termination have different implications, this section is organized according to these two cases. CMS reserves the right to unilaterally adjust the approach described herein, especially in the event that multiple CEC Non-LDO Entities with CEC Non-LDO Entity Beneficiaries in an Aggregation Pool are terminated.

6.2.1 Voluntary Partial-Year Termination

If a CEC Non-LDO Entity that has its CEC Non-LDO Entity Beneficiaries included in an Aggregation Pool voluntarily leaves the CEC Initiative after a partial PY, Financial Reconciliation of the ESCO and any remaining CEC Non-LDO Entities in the Aggregation Pool would include the partial-year CEC Non-LDO Entity's financial performance only for services delivered during the portion of the year during which the CEC Non-LDO Entity participated (i.e., on or after the first

day of the Performance Year and prior to the date on which the CEC Non-LDO Entity discontinues participation).

Among other requirements (discussed in Section 6.1), to be eligible to receive Shared Savings, savings must exceed the MSR. For the ESCO and any CEC Non-LDO Entity with CEC Non-LDO Entity Beneficiaries included in the Aggregation Pool, the MSR will be based on the total number of ESCO Beneficiaries and CEC Non-LDO Entity Beneficiaries in the Aggregation Pool during the Performance Year. This count will include the number of CEC Non-LDO Entity Beneficiaries aligned to the partial-year CEC Non-LDO Entity during the portion of the year during which it participated.

Once CMS determines that Preliminary Shared Savings have exceeded the MSR, CMS will distribute the Preliminary Shared Savings among the ESCO and any CEC Non-LDO Entities with CEC Non-LDO Entity Beneficiaries in the Aggregation Pool who have participated in the CEC Initiative for the full PY according to the proportion of Beneficiary-Years that the ESCO and each CEC Non-LDO Entity contributed to the Aggregation Pool. When calculating the ESCO and each CEC Non-LDO Entity's contribution, CMS will exclude the partial-year CEC Non-LDO Entity's aligned Beneficiary-Years from the Aggregation Pool's total number of aligned Beneficiary-Years.

6.2.2 Involuntary Partial-Year Termination

If before the end of the Performance Year, CMS terminates a CEC Non-LDO Entity that has CEC Non-LDO Entity Beneficiaries in an Aggregation Pool, the terminated CEC Non-LDO Entity's financial performance would be completely excluded from reconciliation. Excluding the partial-year CEC Non-LDO Entity's Beneficiaries from the Aggregation Pool would result in a reduction in the number of unique aligned beneficiaries in the Aggregation Pool. The smaller size of the pool would likely result in a higher MSR for the ESCO and any remaining CEC Non-LDO Entities.

If CMS terminates the ESCO before the end of the Performance Year, and ESCO Beneficiaries are in an Aggregation Pool, the ESCO's financial performance would be completely excluded from reconciliation. Excluding the partial-year ESCO Beneficiaries from the Aggregation Pool would result in a reduction in the number of unique aligned beneficiaries in the Aggregation Pool. The smaller size of the pool would likely result in a higher MSR for any remaining CEC Non-LDO Entities.

CMS will mitigate the financial impact on the ESCO and any remaining CEC Non-LDO Entities. If termination of one CEC Non-LDO Entity causes the Aggregation Pool's MSR to increase by less than 0.5 percentage points, CMS will not increase the MSR and the MSR will remain at the original level (i.e., the MSR that would have prevailed, had the CEC Non-LDO Entity not been terminated). If, as a result of CEC Non-LDO Entity's termination, the MSR faced by the ESCO and any remaining CEC Non-LDO Entities increases by at least 0.5 percentage points, CMS will reduce the MSR by 0.5 percentage points.

For example, suppose the Aggregation Pool has 1,000 ESCO Beneficiaries and CEC Non-LDO Beneficiaries with a corresponding MSR of 2.8 percent. Further, suppose that one of the CEC Non-LDO Entities is terminated mid-year, resulting in the Aggregation Pool having only 600 ESCO Beneficiaries and CEC Non-LDO Entity Beneficiaries and a corresponding MSR of 3.6 percent. Because the MSR after the CEC Non-LDO Entity's termination is at least 0.5 percentage points higher than the original MSR, CMS will reduce the MSR by 0.5 percentage points and the ESCO and any CEC Non-LDO Entities remaining in the Aggregation Pool will face a final MSR of 3.1 percent. If the Aggregation Pool had instead fallen from 1,000 ESCO Beneficiaries and CEC Non-LDO Entity Beneficiaries (MSR of 2.8 percent) to 800 ESCO Beneficiaries and CEC Non-LDO Entity Beneficiaries (MSR of 3.1 percent), the MSR would remain at 2.8 percent.

ATTACHMENT: FINANCIAL REPORTING TO THE ESCO

CMS plans to report to the ESCO on a continuous basis to support care improvement efforts. Exhibit 21 outlines examples of the types of reports that CMS plans to share with the ESCO. CMS intends to work with the ESCO to better understand reporting needs; hence, the information reported may change over the course of the CEC Initiative.

Exhibit 21. Examples of Financial Reporting

Report	Frequency	Overview of Content
Historical Expenditure Baseline report	Prior to the start of PY1	▪ Information on BY1, BY2, and BY3 ▪ Number of ESCO Beneficiaries and aligned Beneficiary-Years ▪ ESCO Beneficiary expenditures by Eligibility Category ▪ ESCO Beneficiary per capita expenditures ▪ ESCO Beneficiary Per Beneficiary Per Year expenditures ▪ Trending and Risk Adjustment information
Quarterly expenditure report	Quarterly (Including a three month claims run-out)	▪ Number of ESCO Beneficiaries and aligned Beneficiary-Years for the current PY quarter ▪ ESCO Beneficiary expenditures for the current quarter ▪ Historical Expenditure Baseline amount by Eligibility Category, repeated from the Historical Expenditure Baseline report ▪ Aligned beneficiary proportions for the current PY quarter
Utilization report	Quarterly (Including a three month claims run-out)	▪ Use rates for ESCO Beneficiaries ▪ Use metrics cover inpatient, emergency, post-acute, diagnostic, laboratory, outpatient, vascular access, dialysis, physician, durable medical, and ambulance services.
Monthly expenditure report	Monthly (Does not include a three month claims run-out)	▪ Number of ESCO Beneficiaries and aligned Beneficiary-Years for the current PY month ▪ Actual expenditures per ESCO Beneficiary by Eligibility Category ▪ Actual expenditures per ESCO Beneficiary, disaggregated by: - Part A: Inpatient, skilled nursing facility (SNF), home health agency (HHA), hospice - Part B: Carrier, outpatient, durable medical equipment (DME)
Initial beneficiary list	Once (Prior to beginning of PY1)	▪ The ESCO prospectively aligned list of beneficiaries for the start of PY1 ▪ Includes each ESCO Beneficiary's identifier (HICN), last name, first name, state of residence, ZIP code of residence, birth date, and first-touch Dialysis Facility name
Monthly beneficiary list	Monthly	▪ Cumulative list of ESCO Beneficiaries provided to the ESCO monthly during the Performance Year ▪ Beneficiaries who lose eligibility throughout the Performance Year will remain on the list ▪ Includes each aligned beneficiary's identifier (HICN), last name, first name, state of residence, ZIP code of residence, birth date, and first-touch Dialysis Facility name

Report	Frequency	Overview of Content
Performance Year beneficiary list	Annually (In April of each PY starting in PY2)	▪ List of aligned beneficiaries with whom the ESCO will begin the Performance Year ▪ Beneficiaries who lose eligibility in the previous Performance Year will be excluded from the list ▪ Includes each ESCO Beneficiary's identifier (HICN), last name, first name, state of residence, ZIP code of residence, birth date, and first-touch Dialysis Facility name
Reconciled beneficiary list	Annually (In April after the three month claim run-out)	▪ Finalized list of aligned beneficiaries for the previous Performance Year. ▪ Beneficiaries who lose eligibility in the previous Performance Year will be excluded from the list ▪ The reasons for beneficiary exclusions will be specified ▪ Includes each ESCO Beneficiary's identifier (HICN), last name, first name, state of residence, ZIP code of residence, birth date, and first-touch Dialysis Facility name
Monthly claims lag report	Monthly	▪ Actual expenditures using debit-credit methodology ▪ Total calendar-year-to-date expenditures ▪ Total uncapped expenditures ▪ Comparison of the month in which a payment was made vs. the month in which the service was delivered, disaggregated by inpatient, SNF, HHA, hospice, carrier, outpatient, and DME
Claim and claim-line feeds	Monthly	▪ Claims for all services covered by Part A and Part B that were provided to beneficiaries who agreed to data sharing and were processed during the prior month ▪ The ESCO will receive one Part A claim header file including Part A diagnosis and Part A procedure codes; a claim line file consisting of the line details from Parts A, B, and D; a beneficiary demographics file; and one beneficiary Health Insurance Claim Number cross-reference file.
Expenditure Benchmark report	Annually (Includes a three month claims run-out)	▪ Historical Expenditure Baseline information (repeated from the Historical Expenditure Baseline Report) ▪ Trend and Risk Adjustment factors ▪ ESCO Beneficiaries and Beneficiary-Years ▪ Performance Year Expenditure Benchmark to be used in Financial Reconciliation
Annual settlement reports	Annually (Includes a three month claims run-out)	▪ Number of ESCO Beneficiaries and aligned Beneficiary-Years ▪ Per capita and Per Beneficiary Per Year ESCO Beneficiary expenditures and per capita and Per Beneficiary Per Year PY Expenditure Benchmarks ▪ Total ESCO Beneficiary expenditures and PY Expenditure Benchmarks ▪ Shared Savings, MSR, and Preliminary Shared Savings calculations