Accounting for Contractual Allowances

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Definition of Contractual Allowance

Contractual Allowance:

• is the difference between what hospitals bill and what they receive in payment from third party payers, most commonly government and managed care programs; also known as contractual adjustment.

• is the difference between Total Charges and the Covered Plan Benefit.
CFO asks “Why are contractuals up?”

- Changes in the hospital’s charge structure, utilization patterns and payor mix can cause significant fluctuations in this difference.
- Most commonly, contractuals are increasing due to non-covered line items, late charges, duplicate posting of contractual adjustments, keying errors, and claim payment errors.

How Much Do You Have at Risk?

- Patient claims are always paid in accordance with the contract terms by all payors.
- All contractual adjustments AND non-covered items indicated on a payors remittance advice should be posted only upon receipt of payment.

*Healthcare industry analysts estimate that hospitals may regularly be losing between 2% and 4% of their contracted managed care revenue each year due to overpayments and denials.*
What To Do?

• Calculate the Plan Benefit expected from all major payors and compare that expected benefit to the actual payment(s) received.
• Identify all Payment Differences and facilitate adjudication follow-up.
• Collect every dollar due.
• Record your monthly Contractual Allowance for unbilled and in-house charges

In the Perfect World

• Have a contract modeling system that
  • Accurately models the payor contractual terms
  • Compares the expected contractual to actual contractual posted

• Compare profitability by payor, by product line, by physician.... Drill down to the individual claim level detail
What Can I do in My World?

- Create standards to review a variation of reports to determine underpayment / overpayment of accounts
- Post contractuals at time of billing when possible with your current hospital reimbursement system
- Avoid late charges – identify departments not in compliance
- Educate cash posting on Managed Care agreements and importance of accurate contractual posting. Cash posting can be key to initial identification of underpayment / denials issue
- Use companies specializing in overpayment / underpayment reviews to identify issues and recovery lost dollars

Variance Reports

- Review Credit Balance reports – are contractuals overstated due to posting errors
  - Daily review of credit balances created from previous day posting activity
  - Reports to identify duplicate contractuals or contractual posted for more than total charges.
  - Prior to month-end review of high dollar credit balances
- REVIEW your remittances for non-covered line item charges
- Create a Medicare DRG Model and apply to inpatient Medicare accounts
- Create a Medicaid DRG Model and apply to inpatient Medicaid accounts
Reimbursement Systems

- Most hospital systems have a reimbursement module that supports DRG payment reimbursement and percent of charges
- Spend the time to understand your system and upload your major contracts
- Variance reports should be a part of the system OR create your own Sequel or NPR reports to identify issues

Collect EVERY Dollar Due

- Identify & Appeal denied claims & line item denials
- Rebill underpaid claims – send adjudication letters
- Develop relationships with payor representatives in your area
- Understand the value of trending data & correct processes upstream
- Utilize companies that specialize in contract reviews to recovery dollars