

\$5,000. The amount of \$3,000 would be allowable if the provider assumes obligation for the expense under a written agreement with the sisterhood or other religious order covering payment by the provider for the services.

§ 413.98 Purchase discounts and allowances, and refunds of expenses.

(a) *Principle.* Discounts and allowances received on purchases of goods or services are reductions of the costs to which they relate. Similarly, refunds of previous expense payments are reductions of the related expense.

(b) *Definitions*—(1) *Discounts.* Discounts, in general, are reductions granted for the settlement of debts.

(2) *Allowances.* Allowances are deductions granted for damage, delay, shortage, imperfection, or other causes, excluding discounts and returns.

(3) *Refunds.* Refunds are amounts paid back or a credit allowed on account of an overcollection.

(c) *Normal accounting treatment—Reduction of costs.* All discounts, allowances, and refunds of expenses are reductions in the cost of goods or services purchased and are not income. If they are received in the same accounting period in which the purchases were made or expenses were incurred, they will reduce the purchases or expenses of that period. However, if they are received in a later accounting period, they will reduce the comparable purchases or expenses in the period in which they are received.

(d) *Application.* (1) Purchase discounts have been classified as cash, trade, or quantity discounts. Cash discounts are reductions granted for the settlement of debts before they are due. Trade discounts are reductions from list prices granted to a class of customers before consideration of credit terms. Quantity discounts are reductions from list prices granted because of the size of individual or aggregate purchase transactions. Whatever the classification of purchase discounts, like treatment in reducing allowable costs is required. In the past, purchase discounts were considered as financial management income. However, modern accounting theory holds that income is not derived from a purchase but rather from a sale or an exchange and that purchase dis-

counts are reductions in the cost of whatever was purchased. The true cost of the goods or services is the net amount actually paid for them. Treating purchase discounts as income would result in an overstatement of costs to the extent of the discount.

(2) As with discounts, allowances, and rebates received from purchases of goods or services, refunds of previous expense payments are clearly reductions in costs and must be reflected in the determination of allowable costs. This treatment is equitable and is in accord with that generally followed by other governmental programs and third-party payment organizations paying on the basis of cost.

§ 413.99 Qualified and Non-Qualified Deferred Compensation Plans.

(a) *Statutory basis, scope, and definitions*—(1) *Basis.* All payments to providers of services must be based on the reasonable cost of services covered under Title XVIII in accordance with section 1861(v) of the Act and the regulations in this part.

(2) *Scope.* This section and § 413.100(c)(2)(vii) apply to Medicare's treatment of the costs incurred for Qualified and Non-Qualified Deferred Compensation Plans.

(3) *Definitions.* As used in this section the following definitions apply:

Deferred Compensation means remuneration currently earned by an employee that is not received until a subsequent period, usually after retirement.

Employee Retirement Income Security Act of 1974 (ERISA) is a Federal law that sets standards of protection for individuals in most voluntarily established, private-sector retirement plans. The law is set forth in Title 29, Chapter 18 of the U.S. Code.

Funded Plan means a plan in which assets have been irrevocably and unconditionally set aside with a third party for the payment of plan benefits (for example, in a trust or escrow account), and those assets are beyond the reach of the employer or its general creditors.

Non-Qualified Deferred Compensation Plan (NQDC) means an elective or non-elective plan, agreement, method, or arrangement between an employer and

an employee to pay the employee compensation in the future. In comparison with qualified plans, nonqualified plans do not provide employers and employees with the tax benefits associated with qualified plans because NQDC plans do not satisfy all the requirements of 26 U.S.C. 401(a).

Non-Qualified Defined Benefit Plan (NQDB) means a type of NQDC that is established and maintained by the employer primarily to provide definitely determinable benefits to its employees usually over a period of years, or for life, after retirement. Such benefits are generally measured by, and based on, such factors as age of employees, years of service, and compensation received by the employees.

Pension Benefit Guaranty Corporation (PBGC) is a Federal agency created by ERISA to protect benefits in private-sector QDBP plans described in section 3(35) of ERISA.

Qualified Defined Benefit Plan (QDBP) means a type of Qualified Deferred Compensation Plan that is established and maintained by the employer primarily to provide definitely determinable benefits to its employees usually over a period of years, or for life, after retirement. Such benefits are generally measured by, and based on, such factors as age of employees, years of service, and compensation received by the employees. A QDBP meets the applicable requirements of ERISA, as amended, and the requirements for a QDBP under 26 U.S.C. 401(a). Under a qualified plan, employers are entitled to deduct expenses in the year the employer makes contributions even though employees will not recognize income until the receipt of distributions.

Qualified Defined Contribution or Individual Account Plan (QDCP) means a type of Deferred Compensation Plan in which the employee, the employer, or both, contribute to an employee's individual account under the plan. The amount in the account at distribution includes the contributions and investment gains or losses, minus any investment and administrative fees. The value of the account changes based on contributions and the value and performance of the investments. A QDCP meets the applicable requirements of

ERISA, as amended, and the requirements set forth in 26 U.S.C. 401(a), and, if applicable 26 U.S.C. 401(k).

Unfunded Plan means a plan in which benefits are supported by assets that have not been set aside (that is, a "pay as you go" plan), or by assets that have been set aside, but remain subject to the claims of the employer's general creditors.

(b) *Principle requirements*—(1) *General*. Deferred Compensation contributions or payments must be made by a provider of services, or an employee of the provider of services, to a Qualified or Non-Qualified Deferred Compensation Plan, established and maintained by the provider of services to provide retirement income to employees or to result in the deferral of income by employees for periods extending to the termination of covered employment or beyond. Contributions or payments made by a provider of services for the benefit of its employees to a Qualified or Non-Qualified Deferred Compensation Plan are allowable, when, and to the extent that, such costs are actually incurred by the provider of services and found to be reasonable and necessary under the principles of reasonable cost.

(2) *Deferred Compensation for provider-based physicians services in a hospital or SNF*. Costs incurred by a hospital or SNF to fund a Qualified or Non-Qualified Deferred Compensation Plan for a provider-based physician must meet the following requirements to be allowable under the program:

(i) The allocation of physician compensation costs required under § 415.60 of this chapter does not attribute the provider-based physician's Deferred Compensation entirely to one category of service and his current compensation to another.

(ii) Contributions or payments toward the Qualified or Non-Qualified Deferred Compensation Plan do not include any cost excluded from the definition of physician compensation at § 415.60(a) of this chapter.

(iii) The amount of Deferred Compensation does not exceed the amount specified in the agreement required by § 415.60(g) of this chapter.

(iv) An arrangement between a physician and a provider of services under which the physician is reimbursed for

patient charges, but the provider of services does the billing as a Deferred Compensation agreement, is not allowed.

(v) The costs incurred for physician guaranteed arrangements for hospital emergency room availability services, must meet the following additional requirements:

(A) The terms of both the guarantee arrangements and the Deferred Compensation Plan establish the amounts to be included at the beginning of the hospital's cost reporting period.

(B) The amount of Deferred Compensation is included in the guaranteed amount.

(C) The hospital contributes to the Deferred Compensation Plan from its own funds.

(D) The amount of Deferred Compensation that is allowable is limited to the amount by which the guarantee, including Deferred Compensation, exceeds the total billed by the hospital to all patients for the physician's patient care services.

(E) When the physician's charges to all patients equal or exceed the amount guaranteed by the hospital, the program does not recognize a Deferred Compensation contribution/payment.

(c) *Requirements for Non-Qualified and Qualified Deferred Compensation Plans—*

(1) *NQDC requirements.* In order for contributions or payments by a provider of services to an NQDC as defined at paragraph (a)(3) of this section to be allowable under the program, the NQDC must meet the general requirements at paragraph (c)(1)(i) of this section, and it must either meet the requirements for a funded NQDC at paragraph (c)(1)(ii) of this section or the requirements for an unfunded NQDC at paragraph (c)(1)(iii) of this section, as applicable.

(i) *General requirements.* An NQDC must satisfy the requirements for document compliance and operational compliance set forth in 26 U.S.C. 409A.

(ii) *Funded NQDCs.* A funded NQDC must meet the definition of a Funded Plan in paragraph (a)(3) of this section and comply with the requirements in paragraph (c)(5) of this section.

(iii) *Unfunded NQDCs.* An NQDC that is unfunded must meet the definition of an Unfunded Plan in paragraph (a)(3) of

this section, and there must be no constructive receipt of income for employees from a NQDC as a result of contributions made by a provider of services.

(2) *QDCP requirements.* A QDCP must meet the applicable requirements of ERISA, as amended, and the requirements set forth in 26 U.S.C. 401(a), and if applicable 26 U.S.C. 401(k). A QDCP must meet the definition of a Funded Plan in paragraph (a)(3) of this section and comply with the requirements in paragraph (c)(5) of this section.

(3) *QDBP requirements.* A QDBP must meet the applicable requirements of ERISA, as amended, and the requirements for a defined benefit plan under 26 U.S.C. 401(a). A QDBP must meet the definition of a Funded Plan in paragraph (a)(3) of this section and comply with the requirements in paragraph (c)(5) of this section.

(4) *NQDB requirements.* In order for contributions or payments by a provider of services to an NQDB as defined at paragraph (a)(3) of this section to be allowable under the program, the NQDB must meet the general requirements at paragraph (c)(4)(i) of this section, and it must either meet the requirements for a funded NQDB at paragraph (c)(4)(ii) of this section or the requirements for an unfunded NQDB at paragraph (c)(4)(iii) of this section, as applicable.

(i) *General requirements.* An NQDB must satisfy the requirements for document compliance set forth in 26 U.S.C. 409A and operational compliance set forth in 26 U.S.C. 409A(a).

(ii) *Funded NQDBs.* An NQDB that is funded must meet the definition of a Funded Plan in paragraph (a)(3) of this section and comply with the requirements in paragraph (c)(5) of this section.

(iii) *Unfunded NQDBs.* An NQDB that is unfunded must meet the definition of an Unfunded Plan in paragraph (a)(3) of this section, and there must be no constructive receipt of income for employees from a NQDB as a result of contributions made by a provider of services.

(5) *Funded Plan requirements*—(i) *Acceptable funding mechanism*. Both provider of services contributions and employee contributions must be used either to purchase an insured plan with a commercial insurance company, to establish a custodial bank account, or to establish a trust fund administered by a trustee.

(ii) *Life insurance contracts*. The purchase of an ordinary life insurance contract (for example, whole life, straight life, or other) is not a deferral of compensation and is not recognized as a funding mechanism, even where it is convertible at the normal retirement date specified in the policy to an annuity payable over the remaining life of the employee.

(iii) *Sole benefit of participating employees*. Regardless of the funding mechanism utilized, all provider of services and employee contributions to the fund established under the Deferred Compensation Plan and income therefrom must be used for the sole benefit of the participating employees.

(d) *Recognition of contributions or payments to Qualified and Non-Qualified Deferred Compensation Plans*—(1) *General rule*. Except as provided for in paragraph (c)(1)(iii) of this section with respect to QDBPs and funded NQDBs, contributions to Qualified Deferred Compensation Plans or payments to plan participants from Non-Qualified Deferred Compensation Plans are recognized as allowable costs in accordance with paragraph (c)(1)(i) of this section (in the case of Unfunded Plans) and paragraph (c)(1)(ii) of this section (in the case of Funded Plans).

(i) *Unfunded Plans*. Contributions or payments made to an unfunded Deferred Compensation Plans (including unfunded NQDBs) by a provider of services on behalf of its employees are included in allowable costs only during the cost reporting period in which an actual payment is made to the participating employees (or their beneficiaries) and only to the extent considered reasonable, in accordance with § 413.100(c)(2)(vii)(A).

(ii) *Funded Plans*. Reasonable provider of services payments made under funded Deferred Compensation Plans (specifically, funded Defined Contribution Plans, but excluding QDBPs and

funded NQDBs) are included in allowable costs in accordance with § 413.100(c)(2)(vii)(B).

(iii) *Exception for QDBPs and funded NQDBs*. (A) QDBP and NQDB contributions are found to have been incurred only if paid directly to participants or beneficiaries under the terms of the plan or to the QDBP or NQDB.

(B) Payments to a QDBP or funded NQDB for a cost reporting period must be measured on a cash basis. A contribution or payment is deemed to occur on the date it is credited to the fund established for the QDBP or funded NQDB, or for provider of services payments made directly to a plan participant or beneficiary, on the date the provider of services account is debited.

(C) Payments or contributions made to fully fund a terminating QDBP or funded NQDB are to be included as funding on the date they are paid. Excess assets withdrawn from a QDBP or funded NQDB are to be treated as negative contributions on the date that they are withdrawn.

(D) QDBP and funded NQDB annual allowable costs are computed as follows:

(1) QDBP and funded NQDB costs and limits are computed in accordance with § 413.100(c)(2)(vii)(D).

(2) For purposes of determining the QDBP or funded NQDB cost limit under § 413.100(c)(2)(vii)(D)(2), provider of services contribution payments for each applicable cost reporting period must be determined on a cash basis without regard to any limit determined for the period during which the contributions were made, and excluding any contributions deposited in a prior period and treated as carry forward contributions.

(3) The averaging period used to determine the QDBP or funded NQDB cost limit must be determined without regard to a provider of services period of participation in the Medicare program. Periods that are not Medicare cost reporting periods (for example, periods prior to the hospital's participation in the Medicare program) must be defined as consecutive 12-month periods ending immediately prior to the provider of services initial Medicare cost reporting period.

(4) The averaging period used to determine the QDBP or funded NQDB cost limit must exclude all periods ending prior to the initial effective date of the plan (or a predecessor plan in the case of a merger).

(5) In general, the current period defined benefit cost and limit is computed and applied separately for each QDBP or funded NQDB offered by a provider of services. In the case of a plan merger, the contributions or payments made by a provider of services to a predecessor QDBP or funded NQDB and reflected in the assets subsequently transferred to a successor plan are treated as contribution payments made to the successor plan.

(2) [Reserved]

(e) *Documentation requirements.* Documentation must be maintained by the provider of services in accordance with § 413.20 to substantiate the allowability of contributions or payments to Qualified and Non-Qualified Deferred Compensation Plan(s) that it has included in its cost reports.

(1) *Required documentation.* The provider of services must maintain and make available, upon request by the contractor or CMS, certain specified documentation, to substantiate the allowability of the contributions or payments to its Qualified or Non-Qualified Deferred Compensation Plan(s), or both:

(i) Documentation that demonstrates that the provider of services is in compliance with 26 U.S.C. 409A and 409A(a), and, if applicable, 26 U.S.C. 457.

(ii) Ledger accounts/account statements for each plan participant noting current year deferrals, distributions and loans, including any deferral election forms completed by employees, any change requests, and the approval of such requests.

(iii) Documentation that demonstrates the amount(s) and date(s) of actual contributions or payments made to the Qualified or Non-Qualified Deferred Compensation Plan during the current cost reporting period.

(iv) Schedule SB of Form 5500 (tri-agency form (Department of Labor (DOL), Internal Revenue Service (IRS), and PBGC) that plans file with the DOL's "EFAST" electronic filing system) for a QDBP for the current cost

reporting period, or any applicable prior periods.

(v) In the case of a system-wide (multiple employer) plan, the home office shall identify the contributions attributed to each participating provider of services. If the costs included in the cost report for a period differ from the contributions made during the reporting period (that is, as a result of carry forward contributions), the provider of services must also have data available to track and reconcile the difference.

(2) *Additional documentation.* The following additional documentation must be made available, upon request by the contractor or CMS, to substantiate the allowability of the payments/contributions by a provider of services to a Qualified or Non-Qualified Deferred Compensation Plan:

(i) The plan document, the trust document and all amendments related to the current cost reporting period.

(ii) If applicable, any Form 5330, Return of Excise Taxes Related to Employee Benefit Plans, for the cost reporting period.

(iii)(A) Supporting documents for all plan assets and liabilities, such as broker's statements, bank statements, insurance contracts, loan documents, deeds, etc.

(B) Verification of how assets are valued.

(iv)(A) Trustee or administrator reports.

(B) Ledgers.

(C) Journals.

(D) Trustee, administrator, and investment committee minutes.

(E) Certified audit report and other financial reports for the trust.

(F) Any other financial reports, including receipt and disbursement statements, a detailed income statement, and a detailed balance sheet.

(v) For each covered QDBP, documentation of the certified premium information and payments to the PBGC.

(f) *Administrative and other costs associated with Deferred Compensation Plans.* The provider of services shall file a cost report required under §§ 413.20 and 413.24(f) that is consistent with the policies set forth in this section.

(1) *Trustee and custodial fees.* Reasonable trustee or custodial fees, including PBGC premiums, paid by the provider

of services are allowed as an administrative cost except where the plan provides that such fees are paid out of the corpus or earnings of the fund.

(2) *Vested benefits.* The forfeiture of an employee's benefits for cause (as defined in the plan) is recognized as an allowable cost provided that such forfeited amounts are used to reduce the provider of services contributions or payments to the plan during the cost reporting period in which the forfeiture occurs.

(3) *Benefits to be paid.* If an employee terminates participation in the Deferred Compensation Plan before their rights are vested, the applicable non-vested contributions/payments cannot be applied to increase the benefits of the surviving participants. Instead the non-vested contributions or payments should be used to reduce the provider of services contributions or payments to the Deferred Compensation Plan, in the cost reporting period in which the employee terminated participation in the Deferred Compensation Plan. Otherwise, the contributions/payments made by the provider of services must be applied to reduce the subsequent contributions or payments to the Deferred Compensation Plan in the next cost reporting period. If subsequent provider of services contributions/payments to the Deferred Compensation Plan are not made, then the provider of services costs are reduced by the contractor to the extent of such non-vested funds.

(4) *DOL, IRS, or PBGC penalties.* If the provider of services is assessed an excise tax or other remedy by the DOL, IRS, or PBGC for failure to follow DOL, IRS, or PBGC requirements under ERISA or any other penalty fee or penalty interest applicable to its Deferred Compensation Plan, the cost is unallowable in accordance with section 1861(v)(8) of the Act.

(5) *Loans made from a Deferred Compensation Plan.* A provider of services cannot make a loan to itself from a Deferred Compensation Plan where ERISA or IRS rules prohibit such a transaction, except where specifically excepted.

(6) *Termination/discontinuation of a Deferred Compensation Plan.* If the provider of services declines to vest its

outstanding required contributions or payments (that is, matching or non-elective) to a Deferred Compensation Plan as a result of a termination in full or in part or a discontinuation of contributions or payments to a Deferred Compensation Plan, then the provider of services total outstanding required contributions or payments to the Deferred Compensation Plan during the cost reporting period wherein such termination is initiated cannot be included in the provider of services allowable cost for the cost reporting period in which the termination is initiated, nor any future period.

(7) *Required offset against interest expense.* Investment income earned on a Deferred Compensation Plan after its termination but prior to liquidation of the plan's assets and distribution to the provider of services must be offset against the provider of services allowable interest expense under § 413.153.

(8) *Treatment of residual assets following termination of a Funded Plan.* (i) Residual assets arising from the termination of a funded Deferred Compensation Plan must be recouped in the year of the plan termination only against the cost center(s) in which the provider of services reported its plan contributions or payments, usually the administrative and general cost center.

(ii) Residual assets exceeding the amount in the administrative and general (or other) cost center are not further offset in the current or subsequent years.

(iii) The Medicare share of the reversion is based on the Medicare utilization rate in the year the reversion occurs (or the year the actuarial surplus is determined), and not Medicare's utilization in the years the contributions to the plan were made.

(g) *Treatment of costs associated with the PBGC.* Costs associated with the requirements set forth in ERISA and by the PBGC and incurred by a provider of services who sponsors a QDBP are allowable or unallowable under the program as provided for in this paragraph (g).

(1) *Costs paid out of the plan trust.* PBGC premiums and costs paid out of the corpus or earnings of the trust are included in the contributions allowed under paragraph (d)(1)(iii)(A) of this

section, and are not allowable as separate costs.

(2) *Premium payments for single- and multi-employer plans.* The amount of PBGC premiums paid for basic benefits (flat rate or variable, excluding amounts paid out of the corpus or earnings of the trust) by a provider of services who sponsors a QDBP are allowable under the program.

(3) *Liability for missing participants or beneficiaries.* The total amount paid to the PBGC by a provider of services who sponsors a QDBP (excluding amounts paid out of the corpus or earnings of the trust) of the benefit transfer amount (as described in 29 CFR 4050.103(d)) for all missing participants or beneficiaries of the QDBP, is allowable under the program.

(4) *Plan termination due to distress.* For a defined benefit plan that terminated with insufficient assets to pay all of the plan benefits, which resulted in the PBGC making payment of vested benefits up to limits defined by law in accordance with 29 CFR part 4022, such amounts contributed to the QDBP by the provider of services who sponsors the QDBP are allowable. Benefits paid to the participants and beneficiaries of the QDBP by the PBGC are unallowable.

(5) *Restored plan payments.* If the PBGC issues or has issued a plan restoration order as described in 29 CFR part 4047, the amounts that the provider of services repays to the PBGC for guaranteed benefits and related expenses under the plan while the plan was in terminated status, and any administrative costs assessed by the PBGC, excluding penalties, are allowable.

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§413.100 Special treatment of certain accrued costs.

(a) *Principle.* As described in §413.24(b)(2), under the accrual basis of accounting, revenue is reported in the period in which it is earned and expenses are reported in the period in which they are incurred. In the case of accrued costs described in this section, for Medicare payment purposes the costs are allowable in the year in which the costs are accrued and claimed for Medicare payment only

under the conditions set forth in paragraph (c) of this section.

(b) *Definitions*—(1) *All-inclusive paid days off benefit.* An all-inclusive paid days off benefit replaces other vacation and sick pay plans. It is a formal plan under which, based on actual hours worked, all employees accrue vested leave or payment in lieu of vested leave for any combination of types of leave, such as illness, medical appointments, holidays, and vacations.

(2) *Self-insurance.* Self-insurance is a means by which a provider independently or as part of a group undertakes the risk of protecting itself against anticipated liabilities by providing funds in an amount equal to anticipated liabilities, rather than by purchasing insurance coverage.

(c) *Recognition of accrued costs*—(1) *General.* Although Medicare recognizes, in the year of accrual, the accrual of costs for which a provider has not actually expended funds during the current cost reporting period, for purposes of payment Medicare does not recognize the accrual of costs unless the related liabilities are liquidated timely.

(2) *Requirements for liquidation of liabilities.* For accrued costs to be recognized for Medicare payment in the year of the accrual, the requirements set forth below must be met with respect to the liquidation of related liabilities. If liquidation does not meet these requirements, the cost is disallowed, generally in the year of accrual, except as specified in paragraph (c)(2)(ii) of this section.

(i) *A short-term liability.* (A) Except as provided in paragraph (c)(2)(i)(B) of this section, a short-term liability, including the current portion of a long-term liability (for example, mortgage interest payments due to be paid in the current year), must be liquidated within 1 year after the end of the cost reporting period in which the liability is incurred.

(B) If, within the 1-year time limit, the provider furnishes to the contractor sufficient written justification (based upon documented evidence) for nonpayment of the liability, the contractor may grant an extension for good cause. The extension may not exceed 3 years beyond the end of the cost