

HB

19

Position Paper
S.S. for House Bill 19 am

An Act repealing the certificate of need program, amending or repealing provisions relating to state aid for health facilities, Medicaid and general relief medical assistance; and providing for an effective date.

Sponsor Substitute for House Bill 19 am proposes amendments to state law which primarily affect three areas of the Department of Health and Social Services' responsibility: 1) the certificate of need program, 2) coordination of the certificate of need program with the Alaska Medical Facility Authority, and 3) prospective reimbursement under the Medicaid and General Relief Medical Assistance Programs.

I. Certificate of Need

The bill effectively repeals the certificate of need program. The Administration supports this portion of SSHB 19 am.

II. Coordination of the Certificate of Need Program with the Alaska Medical Facility Authority

The bill repeals and reenacts AS 18.26.220. The apparent reason for the proposed changes in this portion of state law is to remove the references to the certificate of need program.

The Department of Health and Social Services supports this change in state law in order to maintain consistency with the proposed repeal of the certificate of need program as set out in SSHB 19 am.

III. Prospective Reimbursement - Medicaid and General Relief Medical Assistance Programs

A. General Overview

Hospital and Nursing home rates in Alaska have traditionally been established retrospectively, that is, costs are estimated at the beginning of a fiscal year and an "interim payment" determined. At the end of the fiscal year, the total interim payments made is compared to the allowable costs of the facility. The difference is either collected from or paid to the facility. This process is referred to as "cost settlement".

Prospective payment, on the other hand, provides for establishment of the payment rate prior to the fiscal year as a result of discussions between each facility and the State, each facility must then operate and provide care at this predetermined rate for the fiscal period.

While the retrospective method assures providers that all of their allowable costs will be reimbursed, a fundamental weakness of these retro-

spective systems is the lack of incentives to control staffing levels, equipment purchases, wage increases, and service expansion.

In view of reduced federal revenues and a new state spending limit, Alaska needs improved cost containment and predictability from its medical reimbursement system. The system must not only consider price, but also eligible groups and service coverages before the budget year commences. It also must consider the differences in "rural" and "urban" health delivery problems.

B. Problems with Retrospective Cost-Based Reimbursement Systems

- Tendency toward ineffective cost containment -- The key problem with a retrospective system is the lack of incentives to control expenditures so that unnecessary costs are avoided.
- Dependence upon auditing and monitoring procedures -- A retrospective system must have a tight, effective auditing system to monitor costs in order to curb abuses of the system.
- Tendency of the system to become inflexible -- Decisions are often made by accountants based on "generally acceptable accounting principles" rather than on the merits of each individual facility's situation.
- State is uncertain of total program costs until the fiscal period is well over -- Final cost figures may not be known to the State until 6 months after a fiscal year ends.
- Cost Shifting occurs where unallowable costs under Medicaid are borne by other payors (insurance and private payors).

C. Advantages of a Prospective Payment System

- Based on the principle that predetermined rates will result in lower costs. A 1982 study by THE URBAN INSTITUTE concluded that prospective systems lower the rate of increase in hospital spending by several percentage points a year, after an initial start-up period.
- Predictability of costs to the State. Prices are agreed upon by the facilities and the State before the fiscal period starts.
- Predictability of revenues to the facilities. The industry can negotiate wages, purchases and other business decisions with a set service price in mind.
- The technique encourages development of more sophisticated budgeting and cost monitoring capabilities. These are desirable management tools and will permit the State to see how a facilities' budget is built and discuss their assumptions in each of the major cost categories.

D. Disadvantages of a Prospective Payment System

Administrative costs are generally greater than those of a retrospective system. However, administrative costs vary greatly according to the design of the system, and as such, this factor is not of significant concern when compared to the total dollars being monitored in the health area.

Arbitrary cost limiters ("FREEZES", "LIDS") may be introduced into the prospective system to balance costs versus revenues. This eventually places hospitals and nursing homes in a "no win" situation since the rates do not fairly reflect efficiently run facilities' costs.

If rates are not applied industry wide, cost shifting can still occur if Medicaid rates are set unrealistically low by the State based on arbitrary limiters.

E. Operation of a Prospective Payment System

There are a wide variety of prospective payment systems operated in the acute care and long term care sectors around the nation.

A common element of a prospective rate payment setting mechanism is an allowable rate of increase in per diem cost for the following year. This percentage is normally calculated through application of economic indicator such as U.S. Department of Labor wholesale and consumer price indexes. The percentage is then routinely applied to actual cost from the previous period to arrive at the prospective rate. Determination of allowable rates of increase can be undertaken either on an individual facilities or groups of facilities.

Another element of a prospective payment system is more precisely defined cost categories combined with a uniform method of reporting costs to the State. A common cost breakdown would be labor vs. non-labor with further categorization inside these areas. The following example uses "natural" expense categories in reporting facility costs.

- Labor expenses
 - physician's fees
 - management
 - clerical
 - technical (e.g., LPNs', therapists)
 - registered nurses
 - household services (e.g., dietary, housekeeping workers)

- Non-labor expenses
 - food
 - utilities
 - drugs and supplies
 - maintenance of personnel
 - other

While some level of categorization is necessary to assure accuracy of prediction, the model outlined above may require an excessive level of accounting time and expertise for some of Alaska's smaller facilities.

The compromise approach shown below may suffice:

- Salaries and fringe benefits
- Non-labor expenses
 - administrative and general
 - household and maintenance
 - dietary
 - professional care

F. State Reimbursement Trends

To date, approximately thirty-four states have instituted a prospective system of reimbursement for nursing home services under Medicaid, and sixteen states have instituted a prospective system of reimbursement for hospital services under Medicaid. These prospective systems have taken many forms, each state's structure is a little different. However, they share the same philosophical purposes: "to encourage economy and efficiency, and to establish a uniform system of accounting, budgeting, and reporting in determining a health facility's future reimbursement".

G. Why Alaska Should Consider Prospective Payment Now

1. Total overall spending is growing at 20% each year in Medicaid/GR Medical.

In any period, total spending is always a function of: 1) the number of recipients, 2) the volume of services used, and 3) the unit price of service. With an automatic cost-of-living increase that expands Alaska's eligible population, coupled with no unit price control or volume limits, Alaska currently has no ability to effectively control growth in medical costs.

According to a recent study by THE URBAN INSTITUTE, Medicaid payments rose at an annual rate of 15.5 percent from FY73 to FY79 nationally. Alaska had the highest annual rate of increase at 41.8 percent during this same period. Since FY79, costs have increased in excess of 20 percent annually in Alaska.

These three factors (recipients, volume, and unit price) need to be considered collectively in any fiscal year. Currently, critical decisions concerning eligible populations, service coverages and unit price are handled independent of each other and do not produce a final cost figure until the fiscal year is past. If total spending is to be contained at a level below 20%, these factors must be considered collectively before each fiscal year starts.

2. Federal funding for Medicaid is reduced in FY84 and later years. The State is facing an unknown dollar cutback in federal funding for FY84. Unless additional State funding replaces these lost federal revenues, critical decisions must be made to bring program spending in line with available resources.
3. Prospective Systems reduce costs in the long term. The Urban Institute recently concluded that "a consensus is now developing that

POSITION PAPER/Department of Health & Social Services

prospective rate setting is effective in lowering the rate of increase in hospital spending by several percentage points a year, at least in mature rate setting programs after an initial start-up period".

H. Why Doesn't the Department of Health and Social Services Simply Adopt Prospective Payment by Regulation?

The Legislature must specifically endorse adoption of a prospective system in Alaska. The Alaska Attorney General has ruled in a 1982 opinion that present Alaska Statutes prevent adoption of a prospective payment system by regulation. The Legislature must change Alaska Statutes to clearly authorize the Department to adopt a prospective system.

I. What Options Exist?

1. Do Nothing. This strategy would leave reimbursement in the present retrospective environment and require the Department to pass reductions in federal revenues on to hospitals and nursing homes through reduced rates. Most recent calculations place hospital and nursing home revenue reductions at 8% and 24% respectively for FY84. This strategy would not require any additional funds beyond the FY84 Governor's request for Medical Assistance but would severely impact Alaska facilities.
2. Remain on retrospective system and replace lost federal revenues with State funds, if State law permits. This strategy will require replacement funds and may require a statute change as well. There is some doubt whether the present statutes would permit the Department to pay rates in excess of the federal limits.
3. Same as option #2 but reduce persons eligible and medical services available. Under existing Alaska law, the Department is empowered to eliminate certain medical services and certain eligibility groups if funds were deemed inadequate for FY84. If it were determined that the Department could pay in excess of new federal limits with all State funds, or legislation were passed to permit this, the Department could make reductions in services and eligible groups to stay within its FY84 request.
4. Adopt Prospective System and replace lost federal revenues with State funds. This strategy will cost roughly the same as Option #2 but FY84 costs could be predicted with greater certainty. Assuming no changes were made in medical services covered or persons eligible, this option would save the State from 1 to 3% annually compared to Option #2 after the initial start-up period.
5. Adopt Prospective System but reduce persons eligible and medical services available. Herein lies the true value of a prospective system. Once the prospective rules are established and the rates (unit price) for services agreed upon for the fiscal year, eligible groups and medical services are then balanced against unit price to operate within the available appropriation. If no changes were made in persons covered or services offered, the price for this option would be the same as Option #4. If major reduction in eligibles or

services were made, the costs for this option could be reduced proportionately.

- 6. Seek Relief from Congress. This is always an option but not one with as much potential in light of Alaska's present financial image. Nonetheless, there is provision within the new federal changes for special negotiation with the Secretary of Health and Human Services regarding "rural" hospitals. Alaska could pursue this option in conjunction with one of the strategies described in Option 1 through 5 above.

J. Summary

Alaska must balance eligible populations, medical services covered and unit price against available funds to define an affordable FY84 medical program. While a prospective system will not in and of itself make this totally possible, it could provide a business environment in which critical decisions will be made before the fiscal year starts.

Department's Position

The Department of Health and Social Services supports this legislation as proposed.

5/25/83
Date

Robert London Smith
Robert London Smith, Ph.D.
Commissioner
Department of Health and
Social Services

May 27, 1983
Date

John Pugh
John Pugh, Deputy Commissioner
for Social Services
Department of Health and
Social Services

May 19, 1983
Date

Daniel J. Middleton
Daniel J. Middleton, Director
Division of Planning, Policy, and
Program Evaluation

May 19, 1983
Date

Rod Betit
Rod Betit, Director
Division of Public Assistance

STATE OF ALASKA
FISCAL NOTE

Revision Date _____, 1983

I. REQUEST
 Bill/Resolution No.: SSHB 19 am
 Title: Prospective Rate Setting
 Sponsor: _____
 Requestor: _____

II. FISCAL DETAIL
 Agency Affected: Health and Social Services
 Program Category Affected: Medical Assistant
 BRU, Program of Subprogram(s) Affected: _____
 Medicaid/General Relief Medical _____

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 83	FY 84	FY 85	FY 86	FY 87	FY 88
OPERATING						
100 PERSONAL SERVICES		84.7	90.6	97.0	103.8	111.0
200 TRAVEL		27.0	28.9	30.9	33.1	35.4
300 CONTRACTUAL		70.0	20.0	20.0	20.0	20.0
400 COMMODITIES		2.0	2.1	2.3	2.4	2.6
500 EQUIPMENT		6.0	1.0	1.0	1.0	1.0
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS, ETC						
TOTAL OPERATING		189.7	142.6	151.2	160.3	170.0
CAPITAL						
REVENUE						

FUNDING: (Thousands of Dollars)

GENERAL FUND		99.1	74.5	79.0	83.7	88.8
FEDERAL FUNDS		90.6	67.1	72.2	76.6	81.2
OTHER (Specify Source)						

POSITIONS:

FULL-TIME		2	2	2	2	2
PART-TIME						
TEMPORARY						

III. SOURCE OF FUNDS TO OFFSET FISCAL IMPACT OF BILL:

IV. ANALYSIS: Attach a separate page for any Analysis

Prepared By: *James S. Harris* Phone: 465-3355
 Division: Public Assistance Date: 5/24/83
 Approved by Commissioner: *Robert L. Smith* Date: 5/25/83
 Department: W&SS

Distribution:

- Original to Legislative Finance
- Copy to Office of Management and Budget (for legislature introduced bills)
- Copy to Department (for Governor introduced bills)
- Copy to Sponsor
- Copy to Requestor (if different from Sponsor)

FISCAL NOTE REVIEW

100	Personal Services				
	1) Executive Director	R24	\$4,251 X 12 =	\$51,012	
	2) Clerk Typist III	R 8	1,487 X 12 =	17,844	
		Benefits .23%		<u>68,856</u>	
				15,837	
				<u>84,693</u>	
200	Travel and Per Diem				
	1) 5 Commission Members X 12 meeting X \$450			\$27,000	
300	Contractual (Data Processing Assistance)			\$70,000	
400	Commodities			\$ 2,000	
500	Equipment			\$ 6,000	
	1) Desks, Chairs and Files				
	Word Processor				
					<u>\$189,693</u>

Three existing Auditor III positions from the Division of Public Assistance will be transferred for Commission use as well as travel funds, etc.

FY'85 and succeeding fiscal years based on 7 percent increase.

ALASKA STATE LEGISLATURE

... 13th Legislature **FIRST** Session

SPONSOR SUBSTITUTE
HOUSE **BILL** NO. **19**....

By .. **FRITZ, HAYES, ZHAROFF, CATO, LINDAUER, SZYMANSKI, McBRIDE, BUSSELL**

"An Act repealing the certificate of need program; and providing for an effective date."

NEW TITLE

"An Act repealing the certificate of need program, amending or repealing provisions relating to state aid for health facilities, Medicaid and general relief medical assistance; and providing for an effective date."

certificate of need program

Introduced in the House **1/24**, 19... **33**

HISTORY IN THE HOUSE

19	83	Read first time and referred to Committee on
Jan	24	HESS and Finance
		Reported back with recommendation that
		<i>they & dogan - 3-20-83 to finance</i>
		<i>finance - 3-21-83 2 dogan - 2-2-83</i>
		Read second time and
		<i>CS 55 (2 in 7 at) done adopted</i>
		Read third time and
		<i>Reconsideration held onto 7/9 Reconsideration held onto 7/9</i>
		<i>Reconsideration held onto 7/9 Reconsideration held onto 7/9</i>
		<i>Reconsideration held onto 7/9 Reconsideration held onto 7/9</i>
		PASS Effective Date
		Yeas 27 Yeas 28
		Nays 11 Nays 10
		Absent 0 Absent 0
		Excused 2 Excused 2
		Reconsideration
		PASS Effective Date
		Yeas 32 Yeas
		Nays 6 Nays
		Absent 1 Absent
		Excused 1 Excused
		Reported correctly engrossed
		Signed by Speaker
		Sent to Senate
		<i>David C. Cook</i>
		CHIEF CLERK OF THE HOUSE

HISTORY IN THE SENATE

19	83	Read first time and referred to Committee on
		HESS FIN
		Reported back with recommendation that
		Read second time and
		Read third time and
		PASS Effective Date
		Yeas Yeas
		Nays Nays
		Absent Absent
		Excused Excused
		Reconsideration
		PASS Effective Date
		Yeas Yeas
		Nays Nays
		Absent Absent
		Excused Excused
		Reported correctly engrossed
		Signed by President
		Returned to House
		SECRETARY OF THE SENATE

HISTORY IN THE HOUSE

19	83	Received from Senate
		Concurred in Senate amendment thus adopting:
		VOTE
		Failed to concur in Senate amendment; asked Senate to recede
		VOTE
		Senate receded from amendment
		VOTE
		Senate failed to recede from amendment
		VOTE
		CC appointed by House
		CC appointed by Senate
		CC adopted by House
		VOTE
		CC adopted by Senate
		VOTE
		To enrolling
		Reported correctly enrolled
		Sent to Governor
	 by Governor
		Filed with Lt. Governor
		Chapter No.

STATE OF ALASKA
PRELIMINARY STATEMENT OF FISCAL IMPACT

Bill No: 55 House Bill 19 Date on Bill: 1/24/83
 Title: An Act repealing the certificate of need program; and providing for an effective date
 Sponsor: Representatives Fritz, Hayes, Zharoff, Cato, Lindauer, Szymanski
 Requestor: _____

1. Estimated fiscal impacts on:

a. Expenditures:

	FY 83	FY 84	FY 85	FY 86
Capital	0	0	0	0
Operating	0	0	0	0
Total	0	0	0	0

b. Revenues:

Revenue	FY 83	FY 84	FY 85	FY 86
	0	0	0	0

2. Source of funds to offset fiscal impact of bill:

3. Assumptions:

4. Disclaimer:

This statement has not been reviewed by the OMB in the Office of the Governor. It does not represent the policy of the Sheffield Administration or the final estimate of fiscal impact.

Prepared By: Dave W. Williams ^{DW} M. H. Samuel Phone: 465-3038
 Division: State Health Planning and Development Date: 2-14-83

Approved by Commissioner: Robert Gordon Smith, Ph.D. Date: 2/22/83
 Department: Health and Social Services Date: _____

6. Distribution:

- Original to Legislative Finance
- Copy to OMB
- Copy to Sponsor

THE LEGISLATURE OF THE STATE OF ALASKA
THIRTEENTH LEGISLATURE

FISCAL NOTE

I. REQUEST

Bill/Resolution No. CSSSHB 19 (Finance) Page 1 of 2
 Title Relating to C.O.N. and state aid for health facility
 Requested by House Finance Date 4/13/83

II. FISCAL DETAIL

Agency Affected Dept. Health & Social Services
 Program Category Affected Health Facility Development
 BRU, Program, Or Subprogram(s) Affected Health Planning & Development

(Note: If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

	FY 83	FY 84	FY 85	FY 86	FY 87	FY 88
100 PERSONAL SERVICES	84,693	90,621	96,965	103,753	111,015	
200 TRAVEL	27,000	28,890	30,912	33,076	35,391	
300 CONTRACTUAL	70,000	20,000	20,000	20,000	20,000	
400 COMMODITIES	2,000	2,140	2,290	2,450	2,621	
500 EQUIPMENT	6,000	1,000	1,000	1,000	1,000	
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS, ETC						
TOTAL	189,693	142,651	151,167	160,279	170,027	

FUNDING (Thousands of Dollars)

GENERAL FUND	99,115	74,535	78,985	83,745	88,839
FEDERAL FUNDS	90,578	68,116	72,182	76,534	81,188
OTHER (Specify Source)					

POSITIONS

FULL TIME	2	2	2	2	2
PART TIME					
TEMPORARY					

III. ANALYSIS (See Fiscal Note Preparation Instruction, Section III)

See Attachment A

IV. DATE 4/13/83 PREPARED BY Al Adams, Chair *APA*
 AGENCY House Finance Committee
 Original: Legislative Finance PHONE 465-3706
 cc: Budget & Management
 Prime Sponsor (First Legislator Named)
 33-001 (Rev. 12/82)

100 Personal Services			
1) Executive Director	P24	\$4,251 X 12 =	51,012
2) Clerk Typist III	R8	1,487 X 12 =	<u>17,844</u>
			68,856
		Benefits .23%	<u>15,837</u>
			\$84,693
200 Travel and Per Diem			
5 Commission Members X 12 meetings			
X average cost of \$450		=	27,000
300 Contractual (Data Processing Assistance)			70,000
400 Commodities			2,000
500 Equipment			
1) Desks, Chairs and Files			6,000
Word Processor			
			<u>\$189,693</u>

Three existing Auditor III positions from the Division of Public Assistance will be transferred for Commission use as well as travel funds, etc.

Note that 47.7% of this budget will be supported with federal funds.