Economic Impact Analysis
Virginia Department of Planning and Budget

12 VAC 30-70; 80; 90 –Methods and Standards for Establishing Payment Rates: Inpatient Hospital Services, Other Types of Providers, and Long Term Care
Department of Medical Assistance Services
January 26, 2007

Summary of the Proposed Regulation

Pursuant to Item 302 KK of the 2006 Appropriation Act, the proposed regulations will increase reimbursements for pediatric physician services by five percent effective July 1, 2006. Also, pursuant to Item 302 PP of the same act, the adjustment factor for private inpatient hospitals will be increased from 76 percent to 78 percent effective July 1, 2006. Item 302 DD of the act furthermore mandates changes to the methodology for determining nursing facility ceilings and eliminates limits on certain nursing facility management salaries and fees effective July 1, 2006. Finally, the Department of Medical Assistance Services (DMAS), at its discretion, proposes to add IV (intravenous) therapy to the list of covered ancillary nursing home services.

Result of Analysis

The benefits likely exceed the costs for most of the proposed changes.

Estimated Economic Impact

Pursuant to Item 302 KK of the 2006 Appropriation Act, one of the proposed changes will increase reimbursements for pediatric physician services by five percent effective July 1, 2006. The main economic effect of the proposed regulations is to increase reimbursements to pediatric physicians by about $7 million annually. Approximately, $3.3 million of this amount will be financed by the Commonwealth and the remaining $3.6 million will be an increase in federal matching funds.

Increased funding to pediatric physician services is expected to strengthen their incentives to continue to participate in Virginia's Medicaid program and maintain Medicaid recipients' access to pediatric medical care.

Also, the flow into the Commonwealth of approximately $3.6 million in federal funds represents a net injection into Virginia's economy and is expected to have an expansionary effect on the overall economic activity.

It appears that physician services category is one of few categories that do not receive periodic rate increases to cope with changes in general inflation, medical inflation, service mix, and other factors that may be relevant. Without periodic rate updates, the rates are adjusted irregularly and the magnitude of the adjustments often appear to be arbitrary. The current methodology may cause discrepancies in the price of physician services relative to all other Medicaid services and adversely affect provider incentives to participate in the program. In theory, the physician rates should be commensurate with the value of services provided. This is generally accomplished by establishing rates in a base year and revising the rate according to the factors affecting the value of the services. In this particular case, significant economic disincentives that may be present as a result of current irregular and arbitrary adjustments to the rates may be avoided by establishing a new reimbursement methodology that takes into account, on a regular basis, changes in the general inflation, medical inflation, service mix, and other relevant factors.

Pursuant to Item 302 PP of the 2006 Appropriation Act, another proposed change will increase the adjustment factor used in private inpatient hospital reimbursement methodology from 0.76 to 0.78 effective July 1, 2006. An adjustment factor of 0.78 translates to a 22% discount taken by the Medicaid program relative to the statewide average cost of inpatient hospital care reimbursements made under the fee-for-service delivery method.

The main economic effect of this change is to increase inpatient hospital reimbursements to private hospitals by about $15 million in fiscal year (FY) 2007, $16.8 million in FY 2008 and thereafter. Approximately, one half of these amounts will be financed by the Commonwealth and the remaining half will be an increase in federal matching funds.

Increased funding to private inpatient hospitals is expected to strengthen their incentives to continue to participate in Virginia's Medicaid program and maintain Medicaid recipients' access to inpatient medical care.

Also, the flow into the Commonwealth of approximately $7.5 million federal funds in FY 2007 and $8.4 million federal funds in FY 2008 and forward represents a net injection into

Virginia's economy and is expected to have an expansionary effect on the overall economic activity.

Pursuant to Item 302 DD of the 2006 Appropriation Act, the proposed regulations remove limits on nursing facility management salaries and fees of individuals who are not related to the facility and increase indirect care ceilings from 103.9 percent to 106.13 percent of the day-weighed median costs effective July 1, 2006. These changes are budget neutral. The budget neutrality is accomplished by eliminating a scheduled $3 per day increase in both direct and indirect care ceilings that was to be effective July 1, 2006.

One rationale for removing certain administrative salary limits and fees is that they represent "limits within limits" and not considered necessary for cost containment as the direct and indirect care ceilings provide an overall reimbursement limit. Because the elimination of limits is offset by the elimination of a $3 increase in ceilings, no fiscal impact is expected at this time. However, this change may lead to an increase in salaries and fees paid to outside managers and increase the unreimbursed direct and indirect costs of nursing homes which could provide a basis for future rate adjustment requests and create additional fiscal effects over the long-run. On the other hand, the facilities will be able to attract and maintain outside managerial resources that they currently cannot with limited flexibility on outside management salaries and fees.

Pursuant to Item 302 DD of the 2006 Appropriation Act, the proposed regulations also increase the direct care cost ceiling from 112 percent to 117 percent of the day weighted median costs and indirect care cost ceiling from 103.9 percent (or 106.13 percent with the change discussed above) to 107 percent of the day weighted median costs. The estimated fiscal impact of this change is a $7.8 million increase in FY 2007 and $8 million increase in FY 2008 and forward provided to nursing home facilities. Approximately, one half of these amounts will be financed by the Commonwealth and the remaining half will be an increase in federal matching funds.

Prior to this change 63 percent of the facilities were under the direct care ceiling and 55 percent were under the indirect care ceiling. With this change, the percentage of facilities under the direct care ceiling will increase from 63 percent to 67 percent or by 12 facilities and the percentage of facilities under the indirect care ceiling will decrease from and 55 percent to 47 percent or by 22 facilities. This means that an additional 12 facilities will now be reimbursed for a portion of their direct care costs that would not have been reimbursed otherwise. Also, 22 facilities will no longer be reimbursed for a portion of their indirect care costs. Although increasing indirect care ceiling should have reduced the number of facilities whose indirect care costs are covered, having 22 facilities with the opposite impact is the result of eliminating limits on outside management salaries and fees. As previously discussed, removing limits on outside management salaries and fees appears to increase the amount of unreimbursed indirect costs as expected.

Increased net funding to nursing homes is expected to strengthen their incentives to continue to participate in Virginia’s Medicaid program and maintain Medicaid recipients’ access to nursing facility care.

Also, the flow into the Commonwealth of approximately $3.9 million federal funds in FY 2007 and $4 million federal funds in FY 2008 and forward represents a net injection into Virginia’s economy and is expected to have an expansionary effect on the overall economic activity.

Finally, DMAS proposes to add IV therapy to the list of covered ancillary services. This change is not mandated by a legislative action, but intended to correct an inadvertent exclusion of coverage for this service that occurred in 2003. The estimated fiscal effect of this change is about $14,000 per year in total funds. Approximately, one half of these amounts will be financed by the Commonwealth and the remaining half will be an increase in federal matching funds. This funding for IV therapy is expected to remove any disincentives to provide this service that may have existed before and improve Medicaid recipients’ access to IV therapy services.

The remaining changes related to nursing facility reimbursements are mere clarifications and are not expected to have any significant economic effects other than avoiding some potential communication costs that may have resulted from unclear language.

Businesses and Entities Affected

The proposed regulations will increase Medicaid reimbursements for pediatric physician services, private inpatient hospital services, and nursing home services. Currently, there are approximately 96 hospitals 6,900 physicians, and 260 nursing facilities.

Localities Particularly Affected

The proposed regulations apply throughout the Commonwealth.

Projected Impact on Employment

The proposed reimbursement increases will likely have an expansionary effect on the state economy. To the extent increased funding, particularly the federal portion of the increases, is directed toward purchase of goods and services within the state, there could be a positive effect on demand for labor.

Effects on the Use and Value of Private Property

The proposed regulations are likely to improve revenues and the future profit streams of affected providers. An increase in profits would, in turn, increase their asset values.

Small Businesses: Costs and Other Effects

The proposed regulations are not anticipated to have an adverse impact on small businesses.

Small Businesses: Alternative Method that Minimizes Adverse Impact

The proposed regulations are not anticipated to have an adverse impact on small businesses.

Legal Mandate

The Department of Planning and Budget (DPB) has analyzed the economic impact of this proposed regulation in accordance with Section 2.2-4007.H of the Administrative Process Act and Executive Order Number 36 (06). Section 2.2-4007.H requires that such economic impact analyses include, but need not be limited to, the projected number of businesses or other entities to whom the regulation would apply, the identity of any localities and types of businesses or other entities particularly affected, the projected number of persons and employment positions to be affected, the projected costs to affected businesses or entities to implement or comply with the regulation, and the impact on the use and value of private property. Further, if the proposed regulation has adverse effect on small businesses, Section 2.2-4007.H requires that such economic impact analyses include (i) an identification and estimate of the number of small businesses subject to the regulation; (ii) the projected reporting, recordkeeping, and other administrative costs required for small businesses to comply with the regulation, including the type of professional skills necessary for preparing required reports and other documents; (iii) a statement of the probable effect of the regulation on affected small businesses; and (iv) a description of any less intrusive or less costly alternative methods of achieving the purpose of the regulation. The analysis presented above represents DPB's best estimate of these economic impacts.