Virginia Regulatory Town Hall

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Final Regulation
Agency Background Document

Agency name	DEPT. OF MEDICAL ASSISTANCE SERVICES
Virginia Administrative Code (VAC) citation	12VAC30, Chapter 70
Regulation title	Methods and Standards for Establishing Payment Rates—Inpatient Hospital Services
Action title	Inpatient Operating, DSH, and IME Payments for Type One Hospitals
Document preparation date	6/10/2004; **NEED GOV APPROVAL BY: 6/22/2004**

This information is required for executive review (www.townhall.state.va.us/dpbpages/apaintro.htm#execreview) and the Virginia Registrar of Regulations (legis.state.va.us/codecomm/register/regindex.htm), pursuant to the Virginia Administrative Process Act (www.townhall.state.va.us/dpbpages/dpb_apa.htm), Executive Orders 21 (2002) and 58 (1999) (www.governor.state.va.us/Press_Policy/Executive_Orders/EOHome.html), and the *Virginia Register Form, Style, and Procedure Manual* (http://legis.state.va.us/codecomm/register/download/styl8_95.rtf).

Brief summary

In a short paragraph, please summarize all substantive changes that are being proposed in this regulatory action.

This final regulation provides for two parallel actions: (i) to reduce fee-for-service (FFS) operating rates for state teaching hospitals (referred to as "Type One hospitals") to a level commensurate with all other hospitals (referred to as "Type Two hospitals"); and, (ii) to increase payments to Type One hospitals through other means (modifying Indirect Medical Education and Disproportionate Share Hospital payments) to compensate for reductions in operating payments as well as revenue losses due to a federal regulatory change that now precludes previously used pass-through payments based on Medicaid managed care rates. These suggested changes will not result in new revenues to the Type One hospitals but will maintain the overall previous revenue levels. These suggested methodology changes will permit the continuation of managed care payments commensurate with fee-for-service (FFS) payments. The goal of this action is to maintain reimbursements for Type One hospitals at their current levels and thus maintain Medicaid managed care clients' access to the medical services these hospitals provide.

Statement of final agency action

Please provide a statement of the final action taken by the agency including (1) the date the action was taken, (2) the name of the agency taking the action, and (3) the title of the regulation.

I hereby approve the foregoing Regulatory Review Summary with the attached amended State Plan pages, Methods and Standards for Establishing Payment Rates—Inpatient Hospital Services: Inpatient Operating, DSH, and IME Payments for Type One Hospitals and adopt the action stated therein. I certify that this final regulatory action has completed all the requirements of the Code of Virginia § 2.2-4012, of the Administrative Process Act.

6/10/2004

Date

/s/ P. W. Finnerty

Patrick W. Finnerty, Director

Dept. of Medical Assistance Services

Legal basis

Please identify the state and/or federal source of legal authority to promulgate this proposed regulation, including (1) the most relevant law and/or regulation, including Code of Virginia citation and General Assembly bill and chapter numbers, if applicable, and (2) promulgating entity, i.e., the agency, board, or person. Describe the legal authority and the extent to which the authority is mandatory or discretionary.

The *Code of Virginia* (1950) as amended, § 32.1-325, grants to the Board of Medical Assistance Services the authority to administer and amend the Plan for Medical Assistance. The *Code of Virginia* (1950) as amended, § 32.1-324, authorizes the Director of DMAS to administer and amend the Plan for Medical Assistance according to the Board's requirements.

The Medicaid authority as established by § 1902 (a) of the *Social Security Act* [42 U.S.C. 1396a] provides governing authority for payments for services.

Purpose

Please explain the need for the new or amended regulation by (1) detailing the specific reasons why this regulatory action is essential to protect the health, safety, or welfare of citizens, and (2) discussing the goals of the proposal and the problems the proposal is intended to solve.

This regulatory action has the potential for a significant impact on the health, safety or welfare of Virginia citizens. The intent of this final regulation is to provide for changes to the reimbursement methodologies for operating reimbursement, disproportionate share hospital (DSH) payments, and indirect medical education (IME) payments to Type One hospitals. In the absence of these changes, the reduction in reimbursement to Type One hospitals will create a significant disincentive for the Type One hospitals to continue participation in the Medallion II program. If the Type One hospitals choose to not participate in the Medicaid managed care program, the viability of the managed care program in the areas of the Commonwealth served by these hospitals will be threatened. As such, access to a proper level of care will be impeded, therefore threatening the public health.

Substance

Please identify and explain the new substantive provisions, the substantive changes to existing sections, or both where appropriate. A more detailed discussion is required under the "All changes made in this regulatory action" section.

The section of the State Plan for Medical Assistance that is affected by this action is Methods and Standards for Establishing Payment Rates -- Inpatient Hospital Services (Attachment 4.19-A (12 VAC 30-70-291, 70-301, and 70-331)).

Due to a change in federal regulations (42 CFR § 438.6) regarding the actuarial soundness of capitation rates, DMAS is now prohibited from making supplemental payments to Type One hospitals for services these providers render in the DMAS managed care program (Medallion II). This prohibition, effective as of August 13th, 2003, creates a significant disincentive for the Type One hospitals to continue participation in the Medallion II program. If the Type One hospitals choose to not participate in the Medicaid managed care program, the viability of the managed care program in the areas of the Commonwealth served by these hospitals will be threatened. This has the potential to reduce access to medical services for the Medicaid population. This final regulation changes the reimbursement methodologies for operating reimbursement, disproportionate share hospital (DSH) payments, and indirect medical education (IME) payments to Type One hospitals. These changes will not result in new revenues to the Type One hospitals but will maintain previous payment levels to Type One hospitals for the reasons set forth above. These methodology changes will permit the continuation of managed care payments commensurate with fee-for-service payments.

In 1991, DMAS determined it would be appropriate to place the state teaching hospitals in their own peer group (named Type One hospitals) for purposes of Disproportionate Share adjustment payments, known as DSH payments. DSH payments are made to those hospitals that render proportionately higher amounts of care to low-income patients relative to other hospitals. Over the years, Medicaid DSH payments to Type One hospitals have figured significantly in these hospitals' revenues. In addition, Type One hospitals' operating rates are subject to an adjustment factor of one, while Type Two hospitals adjustment factors have historically been less than one. This has contributed to higher payment rates for Type One hospitals relative to Type Two hospitals.

These higher rates are significant in the determination of the capitated rates DMAS pays to participating managed care organizations (MCOs) in the Medallion II program. In calculating capitation rates, DMAS considers all providers' rates. Because Type One hospitals are paid significantly higher rates (due to the adjustment factor), DMAS does not include the Type One hospital rates in the calculations of the Medallion II rates. Instead, Type One hospital fee-for-service data is assigned a "community rate" for capitation rate setting purposes, and this rate is less than those facilities' actual fee-for-service cost experience. To promote participation by the Type One hospitals in Medallion II, DMAS had made supplemental payments to the Type One hospitals based on the difference in payment under fee-for-service versus payment under Medallion II with the lower community rate. In light of the recently initiated federal managed care requirements, regarding the capitation rates' actuarial soundness, DMAS is no longer able to continue this approach. Thus the need arose to adjust payment to Type One hospitals through an alternative methodology in order to avoid the loss of these providers from the Medallion II program.

To address this situation, this final regulation sets forth two parallel actions: (i) to reduce FFS operating rates for Type One hospitals to a level commensurate with Type Two hospitals; and, (ii) to increase payments to the Type One hospitals through other means to compensate them for revenue losses due to this operation rate reduction and the federal regulatory change.

Equalizing Type One and Type Two Operating Payments

Because the Medicaid program recognizes that higher costs are incurred at the Type One hospitals, the adjustment factor calculated for Type Two hospitals is not sufficient to reduce Type One costs to the Type Two costs for rate setting purposes. Therefore, DMAS is implementing a methodology change that will calculate an adjustment factor that causes the Type One hospital statewide operating rate per case to equal the statewide operating rate per case as calculated for the Type Two hospitals. This serves to bring fee-for-service reimbursement at Type One hospitals in line with reimbursement levels utilized in calculating the managed care capitation rates under Medallion II.

An undesirable consequence of the reduction in operating payments to Type One hospitals is also a reduction in DSH payments. DSH payments are directly related to the fee-for-service operating payments, so any reduction in operating payments will serve to reduce the DSH payments as well. Consequently, DMAS is incorporating a "DSH factor" into the calculation of

Type One hospital DSH payments that will cause an increase in DSH to offset the reduction caused by lower operating payments. Essentially, the DSH factor will produce DSH payment amounts for Type One hospitals under the new methodology that are equivalent to Type One DSH payment levels under the previous methodology incorporating an adjustment factor of 1.0.

Increasing Type One Hospital Payments Through Other Means

In order to maintain total Medicaid payments to Type One hospitals at current levels, the reduction in operating payments on the fee-for-service side must be offset with additional payments elsewhere. DMAS is offseting the operating payment reductions through enhancement of the indirect medical education (IME) payment levels for the Type One hospitals. The basic goal is to provide IME payments equaling payments calculated under the current IME methodology, plus an additional amount equaling the reduction on the fee-for-service operating side under the new adjustment factor. DMAS has determined that a multiplier applied to the current IME percentage is the most efficient way to accomplish this goal. Because IME is calculated for Medicaid managed care business as well, this multiplier will result in additional IME payment to cover what DMAS previously paid Type One hospitals as supplemental payments described above.

The net effect of these changes will be the maintenance of overall payment levels to Type One hospitals. Because this is simply a shifting of payments currently in the fee-for-service operating side and the Medallion II program to the IME program, with DSH payments held harmless, there is no additional financial impact on the Commonwealth nor is there added pressure to upper payment limits imposed on the program.

Issues

Please identify the issues associated with the proposed regulatory action, including:
1) the primary advantages and disadvantages to the public, such as individual private citizens or businesses, of implementing the new or amended provisions;
2) the primary advantages and disadvantages to the agency or the Commonwealth; and
3) other pertinent matters of interest to the regulated community, government officials, and the public.

If the regulatory action poses no disadvantages to the public or the Commonwealth, please so indicate.

The net effect of these changes will be the maintenance of payment levels that would be achieved had the current methodology, with the additional payments for Medallion II claims to Type One hospitals, continued unchanged. Because this is simply a shifting of payments currently in the fee-for-service operating side and the Medallion II program to the IME program, with DSH held harmless, there is no additional financial impact on the Commonwealth nor is there added pressure to upper payment limits imposed on the program.

Changes made since the proposed stage

Please describe all changes made to the text of the proposed regulation since the publication of the proposed stage. For the Registrar's office, please put an asterisk next to any substantive changes.

No changes were made between the proposed regulation and the final regulation.

Public comment

Please summarize all comment received during the public comment period following the publication of the proposed stage, and provide the agency response. If no public comment was received, please so indicate.

DMAS' proposed regulations were published in the April 5, 2004 (Vol. 20, Issue15), *Virginia Register* for their public comment period from April 5, 2004 through June 4, 2004. There were no public comments.

All changes made in this regulatory action

Please detail all changes that are being proposed and the consequences of the proposed changes. Detail new provisions and/or all changes to existing sections.

Current section number	Proposed new section number, if applicable	Current requirement	Proposed change and rationale
12VAC30-70-291		Sets forth formula for calculating the IME percentage for Type One hospitals.	Inserts a clause stating that the IME Factor in the formula is to be assigned a value for each Type One hospital to insure that the total payments (operating payments plus fee-for-service IME) remain the same as calculated under the previous methodology.
12VAC30-70-301		Sets forth the formula for calculating the DSH payment for Type One hospitals.	Inserts a clause stating that the formula values are to be adjusted to insure that current DSH payments to Type One hospitals remain the same as under the previous methodology.
12VAC30-70-331		Sets forth the formula for calculating the statewide operating rate per case.	Inserts a clause stating that the adjustment factor for Type One hospitals shall be a calculated percentage that causes the Type One Hospital statewide operating rate per case to equal the Type Two Hospital statewide operating rate per case.

Family impact

Please assess the impact of the proposed regulatory action on the institution of the family and family stability.

These changes do not strengthen or erode the authority or rights of parents in the education, nurturing, and supervision of their children; or encourage or discourage economic self-sufficiency, self-pride, and the assumption of responsibility for oneself, one's spouse, and one's children and/or elderly parents. They do not strengthen or erode the marital commitment, but may decrease disposable family income depending upon which provider the recipient chooses for the item or service prescribed.