MR.00
Health Regulatory Commissions
Department of Health and Mental Hygiene

4 *Operating Budget Data*

($ in Thousands)

	FY 01 Actual	FY 02 Working	FY 03 Allowance	Change	% Change Prior Year
Special Fund	$51,522	$48,817	$52,537	$3,720	7.6%
Total Funds	**$51,522**	**$48,817**	**$52,537**	**$3,720**	**7.6%**

- The Governor's budget transfers $2.9 million from the Uncompensated Care Fund administered by the Health Services Cost Review Commission (HSCRC) to the general fund in fiscal 2002.
- The Governor's budget transfers $0.1 million from the HSCRC administration to the general fund in fiscal 2002.
- The Uncompensated Care Fund increases $2.4 million in fiscal 2003.

Personnel Data

	FY 01 Actual	FY 02 Working	FY 03 Allowance	Change
Regular Positions	98.10	101.70	103.70	2.00
Contractual FTEs	3.00	0.00	0.00	0.00
Total Personnel	**101.10**	**101.70**	**103.70**	**2.00**
Vacancy Data: Regular Positions				
Budgeted Turnover: FY 03	6.20	5.98%		
Positions Vacant as of 12/31/01	10.10	9.93%		

- The Maryland Health Care Commission (MHCC) has requested the addition of two health policy analysts to respond to increased workload demands.

Note: Numbers may not sum to total due to rounding.

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Analysis in Brief

Issues

Reducing Excess Fund Balances: As required by fiscal 2002 budget bill language, MHCC and HSCRC have implemented plans to reduce high fund balances.

Report on the Hospital Rate System: HSCRC reported to the budget committees on the impact of the rate setting system on hospitals.

Recommended Actions

		Funds	Positions
1.	Delete two new health policy analyst positions because they do not meet spending affordability guidelines.	$ 77,802	2.0
	Total Reductions	**$ 77,802**	**2.0**

MR.00

Health Regulatory Commissions

Department of Health and Mental Hygiene

Operating Budget Analysis

Program Description

The two regulatory commissions within the Office of the Deputy Secretary for Health Care Financing form the foundation of Maryland's health care regulatory system.

The Health Services Cost Review Commission (HSCRC) was established in 1971 at a time when costs for health care services were rising rapidly and hospital solvency was an important issue. HSCRC is responsible for setting hospital rates. Inherent in this task is the development of incentives for hospitals to provide quality care to everyone, regardless of insurance status. Responsibilities include:

- administration of a Medicaid- and Medicare-waivered all-payor system;
- review and approval of hospital rates;
- guarantee of access for the uninsured through administration of an uncompensated care fund; and
- collection of data on hospital utilization.

Mandated by statute, the Health Care Access and Cost Commission merged with the Health Resources Planning Commission to form the Maryland Health Care Commission (MHCC). This commission is responsible for the following:

- development and implementation the of State Health Plan;
- management of the Certificate of Need process;
- development of cost containment strategies;
- establishment of a basic benefit package for the small group health insurance market;
- establishment of a medical care database;
- development of a nursing home performance evaluation system;
- establishment of electronic clearinghouses for claim submission and exchange of payment information;
- development of a system to compare health maintenance organizations on quality and performance;
- development of a hospital and ambulatory surgical facility performance evaluation system; and
- development of electronic data interchange guidelines for medical confidentiality as part of the Health Insurance Portability and Accountability Act of 1996.

Fiscal 2002 Actions

Cost Containment

Cost containment actions in the Health Regulatory Commissions totaled $769,580 in fiscal 2002. Reductions to the MHCC budget totaled $522,173 in fiscal 2002, due to a $476,068 reduction in salaries and a $46,105 reduction in operating expenses. Reductions to the HSCRC budget totaled $247,407, due to a $236,809 reduction in salaries and a $10,598 reduction in operating expenses. Inability to spend these funds has reduced the commissions' ability to reduce their fund balances as scheduled in fiscal 2002.

Budget Reconciliation

The Governor has proposed transferring monies from a variety of specially-funded programs in order to balance the fiscal 2002 and 2003 budgets. The Budget Reconciliation Act of 2002 would transfer a total of $239 million in special fund balances to the general fund in fiscal 2002. Included in this action is a transfer of $2.9 million from the HSCRC Uncompensated Care Fund and $0.1 million from the HSCRC administration budget.

Uncompensated Care Fund

HSCRC administers the Uncompensated Care Fund, whereby assessments made against each of the acute care hospitals in the State are redistributed to hospitals serving the highest proportions of uninsured patients. Health General Article 19-214 limits the use of funds generated by this mechanism to exclusively finance the delivery of hospital uncompensated care. This program accumulates a fund balance in the period between assessment and redistribution of collections, approximately a two-month period.

HSCRC collected $44.3 million in fiscal 2001 to administer the Uncompensated Care Fund; $41.5 million, in turn, was distributed through the fund. The $2.8 million unexpended in fiscal 2001 was added to the $6.9 million fund balance remaining at the end of fiscal 2000 to bring the total to $9.8 million at the start of fiscal 2002. The action proposed by the Governor would reduce the fund balance by $2.9 million, leaving a $6.8 million remaining fund balance. The Department of Budget and Management (DBM) has estimated that the funds remaining will be sufficient to leave a two-month reserve.

Administration Fund

User fees billed to all hospitals fund the administration of HSCRC. The administration fund began fiscal 2001 with a balance of $1.1 million. After expenditure of $2.7 million and a transfer of $0.3 million to the general fund, the commission carried a balance of $1.3 million to fiscal 2002. The action proposed by the Governor would reduce the fund balance by $0.1 million in fiscal 2002. DBM has estimated this amount to be 20% of fiscal 2002 operating expenses net of contractual services and relocation expenses.

Governor's Proposed Budget

The fiscal 2003 allowance increases by $3.7 million, or 7.6% of the 2002 working appropriation, as detailed in **Exhibit 1**. As the commissions are entirely supported by provider fees, the entire increase is in special funds.

Exhibit 1

Governor's Proposed Budget
Health Regulatory Commissions
($ in Thousands)

How Much It Grows:	Special Fund	Total
2002 Working Appropriation	$48,817	$48,817
2003 Governor's Allowance	52,537	52,537
Amount Change	$3,720	$3,720
Percent Change	7.6%	7.6%

Where It Goes:	
Personnel Expenses	
Change in budgeted turnover	$567
Employee and retiree health insurance	148
Annualize fiscal 2002 general salary increase	115
Employees' retirement system	79
New positions	78
Fiscal 2003 increments	69
Other adjustments	3
Other Changes	
Increase in Uncompensated Care Fund	2,400
Development of a cardiac outcome database	200
Hospital and ambulatory surgical facility report card costs	100
Contractual services for redesign of the rate setting system	(75)
Miscellaneous operating expenses	36
Total	**$3,720**

Note: Numbers may not sum to total due to rounding.

Maryland Health Care Commission

The allowance for MHCC increases $1.1 million, or 15% over the 2002 working appropriation; approval of a pending 2002 budget amendment would reduce the rate of increase to 6%. The increase is primarily the result of increasing personnel costs, including the addition of two new health policy analysts for MHCC. One position will support the development of the cardiac outcome database as part of the State Plan for Cardiac Surgery and Therapeutic Services; the other will support the certification of electronic health networks in accordance with Chapter 270, Acts of 2000. The allowance also provides for increases in the cost of employee benefits and a reduction in turnover expectancy.

In addition to personnel costs, a significant portion of the MHCC budget supports data systems and development. Fiscal 2003 increases support development of a cardiac outcomes database and a report card for hospital and ambulatory surgical facilities. Ongoing costs include maintenance of health care services databases and production of industry report cards.

Health Services Cost Review Commission

The allowance for HSCRC increases $2.6 million, or 6% over the 2002 working appropriation. The increase is almost entirely due to an anticipated $2.4 million growth in uncompensated care collections. The remainder of the increase, $0.2 million, results from general increases in personnel expenses and a reduction in the turnover expectancy. Personnel increases of $0.3 million are offset by a $0.1 million reduction in legal and contractual services.

Performance Analysis: Managing for Results

The commissions' Managing for Results plans, as shown in **Exhibit 2**, reflect the commissions' impact on the regulatory environment in health care. For example, MHCC's measures reflect the heightened interest in mandated health benefits as well as the decline of certificate of need activities. HSCRC's measures highlight the commission's success in keeping the growth in Maryland hospital rates below the national trend.

Exhibit 2

Program Measurement Data
Health Regulatory Commissions
Fiscal 1999 through 2003

	Actual 1999	Actual 2000	Est. 2001	Actual 2001	Est. 2002	Est. 2003	Ann. Chg. 99-01	Ann. Chg. 01-03
MHCC								
Mandated health benefit estimates	n/a	9	15	8	10	10	n/a	11.8%
Small employers offering health insurance	50%	50%	N/A	50%	51%	51%	0.0%	1.0%
Electronic health networks certified	6	8	10	8	12	14	15.5%	32.3%
Certificate of Need applications	60	53	52	15	13	15	-50.0%	0.0%
Determination of coverage letters	237	138	172	102	168	170	-34.4%	29.1%
HSCRC								
Growth in Maryland hospital rates	3.6%	1.5%	2.5%	3.0%	3.5%	3.8%	-8.7%	12.5%
Growth in national hospital rates	2.8%	3.2%	2.5%	3.7%	3.8%	4.0%	15.0%	4.0%

Source: Department of Health and Mental Hygiene

Issues

1. Reducing Excess Fund Balances

Each of the health regulatory commissions has operated with high fund balances, indicating that fees exceeded costs, as shown in **Exhibit 3**.

Exhibit 3

Excess Fund Balances
Health Regulatory Commissions
Fiscal 2002 and 2003 Projections
($ in Millions)

	MHCC	HSCRC
Fiscal 2001 Fund Balance	$1.9	$1.3
Fiscal 2002 Revenue Collection	7.3	3.2
Fiscal 2002 Expenses	(8.1)	(3.8)
Fiscal 2002 Balance	1.1	0.7
Fiscal 2003 Revenue Collections	8.6	3.2
Fiscal 2003 Expenses	(8.6)	(3.4)
Fiscal 2003 Fund Balance	**$1.1**	**$0.5**

Note: Fiscal 2002 expenses include proposed budget amendments of $620,000 for MHCC and $532,000 for HSCRC. HSCRC fiscal 2002 expenses also include a proposed transfer of $100,000 as part of the Budget Reconciliation Act of 2002. HSCRC revenue and expenses are exclusive of the Uncompensated Care Fund.

Source: Department of Health and Mental Hygiene

Each of the commissions has recently collected fees in excess of direct costs. As required by fiscal 2002 budget bill language, MHCC and HSCRC have implemented plans to reduce high fund balances.

Maryland Health Care Commission

MHCC has made progress in reducing its fund balance. At the end of fiscal 2000, the commission posted a balance of nearly $4 million. By the end of fiscal 2002, MHCC projects that the fund balance will fall to $1.1 million. This reduction has been achieved by lowering fees and drawing on the fund balance to support budget growth. Fees for third-party payors, health occupation boards, nursing homes, and hospitals were reduced in fiscal 2001, with continued reductions in fiscal 2002 for licensees assessed

biennially. MHCC's projected fiscal 2002 ending balance includes a proposed $0.6 million budget amendment. The proposed amendment, which provides for costs related to relocation and continuing study of patient safety and the small group market, reduces the fund balance to $1.1 million by the end of fiscal 2002. Original projections of a $0.6 million ending balance in fiscal 2003 will not be met due to the restriction of $0.5 million in fiscal 2002 due to cost containment.

Health Services Cost Review Commission

HSCRC ended fiscal 2000 with a fund balance of $1.1 million. By the end of fiscal 2001, the fund balance had increased to $1.3 million. HSCRC had originally projected that they would again end the year with a $1.3 million fund balance in fiscal 2002. This estimate has been revised with the introduction of a special fund budget amendment to allow the HSCRC to draw on the fund balance to increase expenditures in fiscal 2002. The $0.5 million budget amendment would provide for office relocation expenses and the cost of expert witnesses related to the rate review process. The amendment, in addition to the proposed transfer of $0.1 million to the general fund as part of the 2002 Budget Reconciliation Act, would lower the fiscal 2002 ending balance to $0.7 million. Projected expenditures of $3.4 million in fiscal 2003 will further lower the ending balance to $0.5 million in fiscal 2003.

2. Report on the Hospital Rate System

The 2001 *Joint Chairmen's Report* required HSCRC to report on the following: the impact of the commission's rate redesign process on hospitals; the consequences of federal actions related to hospital funding; the effect of cost inflation on hospitals; the adequacy of hospital rates to allow efficient hospitals to operate effectively; and the impact of the commission rate actions on the State budget, the Medicare waiver, and private payors. Report highlights will follow.

Maryland's Medicare waiver from federal hospital payment rules requires HSCRC to maintain the rate of growth in Medicare payments at or below the rate of growth nationally in Medicare payments. Since 1981 Maryland has met the waiver test, as Maryland rates have increased 176% at the same time rates have increased 199% nationally. High growth in Maryland rates from 1993 to 1998, however, endangered Maryland's waiver and the ability to regulate hospital rates. In response, HSCRC made structural changes to the rate setting system, including regulating charges per case rather than per unit of care and developing a formula to calculate systemwide inflation adjustments. The newly designed rate system, implemented in fiscal 2002, aims to provide attainable per-case targets and take account of systemwide increases in costs for individual products and services. As this action has been implemented only recently, impact data are not yet available.

Changes in federal regulations as a result of the federal Balanced Budget Act of 1997 reduced inpatient payments to hospitals under Medicare's prospective payment system. Rates increased significantly through 1998 and 1999 until the passage of the federal Balanced Budget Refinement Act of 1999 and the federal Benefits Improvement and Protection Act of 2000. At the same time, Maryland hospitals were able to make record gains in efficiency, outperforming inflation by 6.5%. In other words, Maryland hospitals were able to control costs in order to offset inflation in the costs of goods and services, rather than raising additional

revenue. HSCRC made increasing internal efficiencies (0.5%) a part of its rate system as part of continued attempts to constrain the rate of growth in hospital costs.

After experiencing record profits in the years 1994 to 1997 hospital net profits have returned to normal levels. Hospital margins have fallen from a record high of 6.0% of total revenue in 1997 to 2.8% of total revenue in 2000. The current average margin, while lower than recent years, remains higher than the average margin since the inception of the Maryland rate setting system. Operating margins would have been higher in recent years had continuing losses in activity not regulated by HSCRC, such as physician practices, drugs and supplies, ambulatory surgery facilities, and freestanding clinics, been reversed. Reported losses in unregulated activity have increased from $5 million in 1994 to $110 million in 2000. HSCRC estimates that operating margins would have averaged in excess of 5%, rather than 2.8%, had hospitals not incurred losses in unregulated activity in fiscal 2000.

Because several hospitals were under financial constraints through fiscal 2000, the commission negotiated rates with these hospitals in excess of the 2.5% update negotiated for fiscal 2001. A preliminary rate increase of 2.3% in fiscal 2002 was upwardly revised in consideration of the rate of increase in fiscal 2001 and an increase in costs due to inflation. The commission also added a $54 million supplemental increase to rates, resulting in an average rate increase of 3.97% in fiscal 2002.

At a rate of increase of 3.97%, general fund expenditures under Medicaid and the State Employee Health Benefit Program are expected to increase $23.4 million, according to HSCRC. Estimates assume that Medicaid accounts for 15% of total patient revenue, 50% of which is reimbursed by the federal government, and that the State Employee Health Benefit Program remains at 1.65% of total patient revenue. Federal expenditures are expected to increase $104 million under the Medicare program. Expenditures for commercial third-party payors are expected to increase $74.2 million as a result of the rate increase. **HSCRC should discuss the report's findings.**

Recommended Actions

		Amount Reduction		Position Reduction
1.	Delete two new health policy analyst positions because they do not meet spending affordability guidelines.	$ 77,802	SF	2.0
	Total Special Fund Reductions	**$ 77,802**		**2.0**

Appendix 1

Current and Prior Year Budgets

Current and Prior Year Budgets

Health Regulatory Commissions

($ in Thousands)

	General Fund	Special Fund	Federal Fund	Reimb. Fund	Total
Fiscal 2001					
Legislative Appropriation	$0	$48,092	$0	$0	$48,092
Deficiency Appropriation	0	0	0	0	0
Budget Amendments	0	4,809	0	0	4,809
Reversions and Cancellations	0	(1,378)	0	0	(1,378)
Actual Expenditures	**$0**	**$51,522**	**$0**	**$0**	**$51,522**
Fiscal 2002					
Legislative Appropriation	$0	$49,587	$0	$0	$49,587
Budget Amendments	0	(770)	0	0	(770)
Working Appropriation	**$0**	**$48,817**	**$0**	**$0**	**$48,817**

Note: Numbers may not sum to total due to rounding.

Fiscal 2001

Special fund amendments resulted in the following changes to the 2001 working appropriation:

- The MHCC appropriation increased $667,886 to provide funding for a report on nursing homes, to conduct a study on the uninsured, and for a mental and behavioral health contract.

- The HSCRC appropriation increased $4,141,099 due to higher than anticipated collections of user fees. The majority, $4.0 million, were fees generated by the Uncompensated Care Fund. The remainder, $0.2 million, was used for expert witnesses, consultant services, and office renovations and furniture.

Object/Fund Difference Report
DHMH - Health Regulatory Commissions

Object/Fund	FY01 Actual	FY02 Working Appropriation	FY03 Allowance	FY02 - FY03 Amount Change	Percent Change
Positions					
01 Regular	98.10	101.70	103.70	2.00	2.0%
02 Contractual	3.00	0	0	0	0.0%
Total Positions	**101.10**	**101.70**	**103.70**	**2.00**	**2.0%**
Objects					
01 Salaries and Wages	$ 6,251,663	$ 6,247,194	$ 7,305,728	$ 1,058,534	16.9%
02 Technical & Spec Fees	80,291	35,780	38,775	2,995	8.4%
03 Communication	98,971	115,027	98,454	(16,573)	(14.4%)
04 Travel	115,850	96,463	114,811	18,348	19.0%
07 Motor Vehicles	888	2,021	(545)	(2,566)	(127.0%)
08 Contractual Services	44,388,854	41,726,488	44,355,364	2,628,876	6.3%
09 Supplies & Materials	55,070	69,065	67,334	(1,731)	(2.5%)
10 Equip - Replacement	51,849	37,046	42,273	5,227	14.1%
11 Equip - Additional	14,180	24,519	20,500	(4,019)	(16.4%)
13 Fixed Charges	464,533	463,784	494,302	30,518	6.6%
Total Objects	**$ 51,522,149**	**$ 48,817,387**	**$ 52,536,996**	**$ 3,719,609**	**7.6%**
Funds					
03 Special Fund	$ 51,522,149	$ 48,817,387	$ 52,536,996	$ 3,719,609	7.6%
Total Funds	**$ 51,522,149**	**$ 48,817,387**	**$ 52,536,996**	**$ 3,719,609**	**7.6%**

Note: Full-time and contractual positions and salaries are reflected for operating budget programs only.

Fiscal Summary
DHMH - Health Regulatory Commissions

Unit/Program	FY01 Actual	FY02 Legislative Appropriation	FY02 Working Appropriation	FY01 - FY02 % Change	FY03 Allowance	FY02 - FY03 % Change
01 Maryland Health Care Commission	$ 7,339,619	$ 7,976,670	$ 7,454,497	1.6%	$ 8,575,353	15.0%
02 Health Services Cost Review Commission	44,182,530	41,610,297	41,362,890	(6.4%)	43,961,643	6.3%
Total Expenditures	**$ 51,522,149**	**$ 49,586,967**	**$ 48,817,387**	**(5.2%)**	**$ 52,536,996**	**7.6%**
Special Fund	$ 51,522,149	$ 49,586,967	$ 48,817,387	(5.2%)	$ 52,536,996	7.6%
Total Appropriations	**$ 51,522,149**	**$ 49,586,967**	**$ 48,817,387**	**(5.2%)**	**$ 52,536,996**	**7.6%**