

M00R
Health Regulatory Commissions
Department of Health and Mental Hygiene

Operating Budget Data

(\$ in Thousands)

	<u>FY 02</u> <u>Actual</u>	<u>FY 03</u> <u>Working</u>	<u>FY 04</u> <u>Allowance</u>	<u>Change</u>	<u>% Change</u> <u>Prior Year</u>
Special Funds	\$57,857	\$64,366	\$65,700	\$1,335	2.1%
Contingent & Back of Bill Reductions	0	-7	-37	-30	433.6%
Adjusted Special Funds	\$57,857	\$64,359	\$65,663	\$1,305	2.0%
Adjusted Grand Total	\$57,857	\$64,359	\$65,663	\$1,305	2.0%

- The growth in the Health Regulatory Commissions' budget is due to an increase in the Health Services Cost Review Commission's uncompensated care fund. Uncompensated care collections are anticipated to increase \$2 million in fiscal 2004 to a total of \$54 million.
- Expenses related to the commissions' fall 2002 relocation included in the fiscal 2003 working appropriation do not appear in the fiscal 2004 allowance, accounting for a \$0.4 million decrease between fiscal 2003 and 2004.

Personnel Data

	<u>FY 02</u> <u>Actual</u>	<u>FY 03</u> <u>Working</u>	<u>FY 04</u> <u>Allowance</u>	<u>Change</u>
Regular Positions	101.70	97.70	95.70	-2.00
Contractual FTEs	0.32	0.00	6.00	6.00
Total Personnel	102.02	97.70	101.70	4.00

Vacancy Data: Regular Positions

Budgeted Turnover: FY 04	3.82	3.99%
Positions Vacant as of 12/31/02	6.10	6.24%

- The allowance eliminates one full-time equivalent position each from the Maryland Health Care Commission's and the Health Services Review Commission's budget. The addition of six contractual personnel, at a cost of \$238,215, returns the number of total personnel to pre-workforce reduction levels.
- Salary adjustments and reclassifications, the majority related to implementation of the commissions' independent salary setting authority, comprise \$270,581 of the fiscal 2004 personnel allowance.

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

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Analysis in Brief

Major Trends

Certificate of Need Reviews Increase: New regulations modifying licensing procedures caused a surge in determination of coverage reviews in fiscal 2002. Reviews are expected to remain high due to aging physical plants and increasing nursing home occupancy rates.

Growth in Maryland Hospital Rates Remains Below National Average: The federal law that allows the Health Services Cost Review Commission to set hospital rates requires the rate of growth in the federal government’s Medicare payments per case in Maryland to remain below the average rate of growth in these payments nationwide. Maryland has retained its Medicare waiver by maintaining a growth rate below the national average.

Issues

Fund Balances Exceed Targeted Levels: State law requires fees assessed by the Health Regulatory Commissions to be used exclusively to cover the actual documented costs of fulfilling the statutory and regulatory duties of the commissions; a fund balance indicates that the amount of user fees collected exceeds the cost of commission operations. Each of the commissions projects fiscal 2004 ending balances in excess of 10% of annual costs.

Department of Legislative Services’ Audit Raises Legal Concerns: The Department of Legislative Services’ Office of Legislative Audits reported that the Maryland Health Care Commission user fees assessments were not determined in a manner consistent with State law. The Attorney General’s Office has since concluded that the calculation and assessment of user fees did meet legal requirements.

Recommended Actions

	<u>Funds</u>
1. Delete funding for the addition of six contractual positions.	\$ 238,215
2. Reduce funding for position reclassifications.	170,581
Total Reductions	\$ 408,796

M00R
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Operating Budget Analysis

Program Description

The Maryland Health Care Commission (MHCC) and the Health Services Cost Review Commission (HSCRC), the foundation of Maryland's health care regulatory system, are independent commissions that function within the Department of Health and Mental Hygiene.

MHCC, formed by the merger in 1999 of the Health Care Access and Cost Commission and the Health Resources Planning Commission, has the purpose of improving access to affordable health care, reporting information relevant to availability, cost, and quality of health care statewide, and developing sets of benefits to be offered as part of the standard benefit plan and the nongroup market. The commission's goals include:

- improving the quality of care in the health care industry;
- improving access and affordability of health insurance;
- reducing the cost of health care; and
- guiding the future development of services and facilities regulated under the certificate of need program.

HSCRC was established in 1971 to contain hospital costs, maintain fairness in hospital payment, and provide financial access to hospital care. The commission maintains responsibility for ensuring that the cost of health care is reasonable relative to the cost of service and that rates are set without discrimination. The commission's goals include:

- maintaining affordable hospital care for all Maryland citizens;
- expanding the current system for financing hospital care for those without health insurance; and
- eliminating preferential charging activity through monitoring of hospital pricing and contracting activity.

Performance Analysis: Managing for Results

MHCC operates the certificate of need program, whereby the commission regulates the placement of new health care facilities and services. The certificate of need process was designed to maximize cost effectiveness, quality, and access to health care by eliminating redundancy and inefficiency in the

M00R – DHMH – Health Regulatory Commissions

provision of health care services. Certificates of need are required for all acute general hospitals, specified acute care services, and special hospitals intending to develop or improve capacity, services, or facilities. Managing for Results data in **Exhibit 1** reflect the number of certificate of need determinations and subsequent actions since 2001. New regulations modifying licensure procedures caused a surge in determination of coverage reviews in fiscal 2002. Reviews are expected to remain high due to aging physical plants and increasing nursing home occupancy rates.

Exhibit 1

Managing for Results Data
Fiscal 1999 through 2004
(\$ in Thousands)

	<u>FY 1999</u> <u>Actual</u>	<u>FY 2000</u> <u>Actual</u>	<u>FY 2001</u> <u>Actual</u>	<u>FY 2002</u> <u>Actual</u>	<u>FY 2003</u> <u>Est.</u>	<u>FY 2004</u> <u>Est.</u>
<i>Maryland Health Care Commission:</i>						
Certificate of need actions	n/a	n/a	28	17	18	20
Determinations and precensure reviews	n/a	n/a	118	177	140	150
<i>Health Services Cost Review Commission:</i>						
Maryland average cost per hospital admission (annual percentage change)	1.9%	1.5%	3.0%	4.5%	5.0%	4.0%
National average cost per hospital admission (annual percentage change)	2.5%	2.0%	3.3%	4.9%	5.5%	4.5%
Uncompensated Care Fund	\$33,695	\$37,118	\$41,484	\$47,298	\$52,000	\$54,000
Annual percentage change	n/a	10.2%	11.8%	14.0%	9.9%	3.8%

Source: Department of Health and Mental Hygiene

HSCRC sets rates hospitals may charge for the purchase of care. The commission's ability to standardize rates for all payors, including federal Medicare and Medicaid programs, was established in 1980 by federal legislation, contingent on the commission's ability to constrain the rate of growth of hospital admissions costs. The law requires the rate of growth in the federal government's Medicare payments per case in Maryland to remain below the average rate of growth in these payments nationwide. Maryland has retained its Medicare waiver by maintaining a growth rate below the national average, reflected in Exhibit 1.

In addition to regulating hospital rates, HSCRC also maintains the State's uncompensated care fund. The commission makes an assessment on all acute care hospitals in the State in accordance with State law and redistributes all funds collected to those hospitals that treat a higher proportion of the State's uninsured population. The uncompensated care program, designed to ensure that hospitals treat patients

M00R – DHMH – Health Regulatory Commissions

regardless of their ability to pay, distributes funds among nine of the State’s hospitals. Growth in the fund in recent years, illustrated in Exhibit 1, reflects growth in net patient revenue statewide and across the nation.

Fiscal 2003 Actions

Fiscal 2003 cost containment reflects the reversion of appropriations to support free transit ridership for State employees, contingent upon enactment of a provision in the Budget Reconciliation and Financing Act of 2003. The proposed measure would reduce the commissions’ fiscal 2003 appropriation by \$6,930. The commissions also remain subject to the hiring freeze, although five of seven requested exemptions to the hiring freeze have been approved by the Department of Budget and Management.

Governor’s Proposed Budget

The fiscal 2004 allowance increases funding \$1.3 million above the adjusted fiscal 2003 working appropriation, an increase of 2%. The increase is attributable to an anticipated increase in collections of the uncompensated care fund, reflected in **Exhibit 2**, offset by reductions in administration at each of the commissions. Components of the change in the allowance are presented in **Exhibit 3**.

Exhibit 2

Distribution of Funding by Commission
Fiscal 2001 through 2004
(\$ in Thousands)

	<u>FY 01</u> <u>Actual</u>	<u>FY 02</u> <u>Actual</u>	<u>FY 03 Working</u> <u>Approp.</u>	<u>FY 04</u> <u>Allowance</u>	<u>FY 03-04</u> <u>Change</u>
<i>Maryland Health Care Commission:</i>	\$7,340	\$7,559	\$8,835	\$8,551	-3.2%
<i>Health Services Cost Review Commission:</i>					
Administration	\$2,699	\$2,999	\$3,524	\$3,112	-11.7%
Uncompensated Care Fund	41,484	47,298	52,000	54,000	3.8%
Subtotal	\$44,183	\$50,297	\$55,524	\$57,112	2.9%
Total	\$51,522	\$57,857	\$64,359	\$65,663	2.0%

Source: Maryland Operating Budget Fiscal 2004

Exhibit 3

**Governor’s Proposed Budget
Health Regulatory Commissions
(\$ in Thousands)**

	FY 02	FY 03	FY 04		% Change
	Actual	Working	Allowance	Change	Prior Year
Special Funds	\$57,857	\$64,366	\$65,700	\$1,335	2.1%
Contingent & Back of Bill Reductions	0	-7	-37	-30	433.6%
Adjusted Special Funds	\$57,857	\$64,359	\$65,663	\$1,305	2.0%
Adjusted Grand Total	\$57,857	\$64,359	\$65,663	\$1,305	2.0%

Where It Goes:

Personnel Expenses

Reclassifications related to independent salary review.....	\$225
Employee and retiree health insurance.....	149
Turnover adjustments	42
Elimination of deferred compensation match	-33
Abolished positions	-86
Other salary adjustments.....	-122

Other Changes

Increase in uncompensated care fund.....	2,000
Addition of six contractual positions	237
Elimination of office equipment purchases.....	-100
Reduction in rent due to office relocation	-143
Reduction in use of consultant services	-212
Reduction in production costs of annual report cards.....	-281
Moving expenses related to fall 2002 office relocation.....	-310
Other adjustments	-61

Total

\$1,305

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

Personnel Expenses

Two positions were eliminated in the commissions' fiscal 2004 allowance to produce cost savings of \$86,001. The vacant positions, an MHCC data systems analyst and an HSCRC fiscal accounts clerk, were abolished as part of the Governor's exercise to reduce the size of the State workforce. The reduction in full-time equivalent personnel is offset by the addition of six contractual personnel in the allowance at a cost of \$236,990. The addition of the four contract positions in MHCC and two contract positions in HSCRC returns the number of personnel to fiscal 2002 pre-workforce reduction levels.

Adjustments to employee compensation account for \$320,559 of the fiscal 2004 allowance. The majority of the funds, \$225,000, support reclassification of existing positions pursuant to the commissions' independent salary setting authority. Chapter 702, Acts of 1999 classified commission staff hired after September 30, 1999, as members of the executive service, management service, or special appointments in the State Personnel Management System. It further allowed the commissions, in consultation with the Secretary of DHMH, to determine the appropriate job classifications and grades. In October 2002 the department developed a position evaluation methodology to guide position reclassification. MHCC began the process of reclassifying five positions in January 2003, with the expectation that salaries of all 72 employees will be reclassified in fiscal 2004 at an average cost of \$3,125. HSCRC has delayed implementation of salary adjustments given the State's fiscal condition.

Operating Expenses

Nonpersonnel expenses increase \$1.2 million in the fiscal 2004 allowance. The increase is driven by an anticipated \$2 million increase in the HSCRC's uncompensated care fund, an assessment on all acute care hospitals in the State redistributed to those hospitals that treat a higher proportion of the State's uninsured population. Collections are anticipated to increase from \$52 million in fiscal 2003 to \$54 million in fiscal 2004. This increase is offset by reductions in miscellaneous operating expenses. Specifically:

- Costs related to the commissions' fall 2002 move will not be incurred in fiscal 2004, including \$0.3 million for relocation costs and \$0.1 million in office furnishings. Office rent is expected to decrease \$0.1 million from fiscal 2003 to 2004.
- The HSCRC budget for consulting services decreases \$0.2 million, with the intention of requesting additional funds by budget amendment, as needed, to reduce the fund balance.
- MHCC report card production costs are anticipated to decrease \$0.3 million in fiscal 2004 due to reductions in data collection and production costs.

Impact of Cost Containment

M00R – DHMH – Health Regulatory Commissions

The fiscal 2004 allowance reflects the elimination of the appropriation for matching employee deferred compensation contributions up to \$600, contingent upon enactment of a provision in the Budget Reconciliation and Financing Act of 2003. The measure reduces the fiscal 2004 allowance by \$36,979.

Issues

1. Fund Balances Exceed Targeted Levels

State law requires fees assessed by the Health Regulatory Commissions to be used exclusively to cover the actual documented costs of fulfilling the statutory and regulatory duties of the commissions; a fund balance indicates that the amount of user fees collected exceeds the cost of commission operations. Sunset reviews have suggested that the commissions carry a maximum fund balance of 10% of annual appropriations in case of unforeseen expenses. As the commissions are exclusively financed through annual assessments on health care facilities and practitioners, a small balance provides a contingency in case of unexpected midyear costs. Detailed in **Exhibit 4**, each of the commissions projects fiscal 2004 ending balances in excess of 10% of annual costs.

Exhibit 4

Health Regulatory Commissions' Estimated Fund Balances Fiscal 2001 through 2004 (\$ in Millions)

	<u>MHCC</u>	<u>HSCRC</u>
Fiscal 2001 Fund Balance	\$1.78	1.05
Fiscal 2002 Revenue Collection	7.67	3.30
Fiscal 2002 Expenses	-7.56	-3.19
Fiscal 2002 Fund Balance	1.89	1.16
Balance relative to fiscal 2002 appropriation	25%	35%
Fiscal 2003 Revenue Collection	8.41	3.13
Fiscal 2003 Expenses	-8.84	-3.53
Fiscal 2003 Fund Balance	1.46	0.77
Balance relative to fiscal 2003 appropriation	16%	22%
Fiscal 2004 Revenue Collection	8.58	2.81
Fiscal 2004 Expenses	-8.58	-3.12
Fiscal 2004 Fund Balance	\$1.46	\$0.45
Balance relative to fiscal 2004 appropriation	17%	14%

Note: Fiscal 2002 revenues exceed expenses due to cost containment.

Source: Department of Health and Mental Hygiene

M00R – DHMH – Health Regulatory Commissions

Fiscal 2002 cost containment measures limited the commissions' ability to reduce their fund balances. User fees are assessed annually based on the amount of legislative appropriation. Cost containment was imposed subsequent to the commissions' collection of user fees, limiting fiscal 2002 expenditures but not fiscal 2002 collections. As a result, both the MHCC and the HSCRC fiscal 2002 ending balance exceeded projections.

The commissions have been reducing their surpluses by increasing their appropriation midyear by budget amendment, allowing the commissions to spend additional funds without increasing assessments. In fiscal 2002, MHCC increased its appropriation \$0.6 million by budget amendment for costs related to office relocation and additional studies; HSCRC increased its appropriation \$0.5 million by budget amendment for office relocation and consulting costs. These actions partially offset the effect of cost containment on commission surpluses, but still resulted in a net increase in the fund balances. Largely unaffected by cost containment in fiscal 2003, the commissions should be able to reduce their fund balances below fiscal 2002 levels. HSCRC will collect only 90% of the amount of its fiscal 2004 appropriation from its users, allowing for further reductions in the upcoming fiscal year.

2. Department of Legislative Services' Audit Raises Legal Concerns

The Department of Legislative Services' Office of Legislative Audits conducted an evaluation of the Health Regulatory Commissions' fiscal activity beginning August 5, 1999, and ending March 7, 2002. The audit disclosed that the user fees assessed by MHCC to fund its operations were not determined in a manner consistent with State law; however, the commission felt there was insufficient time to implement the law before fiscal 2002 fees were assessed. As a consequence, the auditors reported that user fee assessments were not properly allocated among health care facilities.

Chapter 565, Acts of 2001 requires the commission, in assessing user fees to each regulated industry, to use a methodology that considers the amount of the commission's workload attributable to each industry. Prior to July 1, 2001, the percentage of the commission's total user fees assessed to each industry was specified in State law. The legislation introduced a revised user fee assessment calculation and increased the cap on annual user fee assessments. In anticipation of the revision to the law, the commission adopted a revised user fee methodology in December 2000 but felt that there was insufficient time to implement the changes before fiscal 2002 fees were assessed. As a result, fiscal 2002 user fees did not reflect the revised methodology specified by law and were not assessed to all required health care practitioners. The difference between the required and the actual fiscal 2002 assessment is detailed in **Exhibit 5**.

The commission disagreed with the auditors' findings, citing provisions unanticipated at the time the revised user methodology was developed. In addition to revising the distribution of user fees, the law extended fees to a greater number of health care practitioners as well as exempted from commission assessments the health care practitioners with below-average hourly wages. These provisions, according to the commission, obligated the commission to a process of outreach to educate health care practitioners newly subject to MHCC user fee assessments; furthermore, the determination of health care practitioners exempt from assessment required extensive research and calculation. Due to time constraints, the impact

M00R – DHMH – Health Regulatory Commissions

on the industry, and the outreach process, the commission believed it would not have been feasible to implement the changes to user fee assessments included in the law until fiscal 2003.

Exhibit 5

**Distribution of Maryland Health Care Commission User Fees
Fiscal 2002**

<u>Industry</u>	<u>User Fees Assessed</u>	<u>User Fees Required</u>	<u>Difference</u>
Hospitals	\$2,934,601	\$2,323,226	\$611,375
Nursing homes	407,584	1,059,717	-652,133
Health occupation boards	1,548,817	1,711,851	-163,034
Health insurers	3,260,668	3,056,876	203,792
Total	\$8,151,670	\$8,151,670	\$0

Source: Department of Legislative Services

In response to the recommendation of the Department of Legislative Services' Office of Legislative Audits, MHCC consulted with the Office of the Attorney General to determine if future user fee assessments should be adjusted to reflect the changes to the law cited by the auditors. The Attorney General has concluded that the commission assessed fiscal 2002 user fees according to law and has concluded that there is no need to recalculate previous year assessments. The user fee methodology authorized by statute has been used to calculate assessments as of fiscal 2003.

The Department of Legislative Services recommends that MHCC comment on this issue.

Recommended Actions

	<u>Amount Reduction</u>
1. Delete funding for the addition of six contractual positions. The addition of the four positions in the Maryland Health Care Commission and two positions in the Health Services Cost Review Commission would return the number of commission personnel to fiscal 2002 pre-workforce reduction levels. This action maintains efforts to reduce the size and cost of the State workforce.	\$ 238,215 SF
2. Reduce funding for position reclassifications. The Maryland Health Care Commission has requested funds to reclassify all 72 positions at a higher grade or class; the Health Services Cost Review Commission has requested funds to adjust salaries as needed. Although the commissions have broad authority to set salaries, these adjustments are incongruous with the current limitations on the State personnel system. A pool of \$100,000 remains to permit the agencies to deal with critical recruitment and retention issues.	170,581 SF
Total Special Fund Reductions	\$ 408,796

Current and Prior Year Budgets

Current and Prior Year Budgets Health Regulatory Commissions (\$ in Thousands)

	<u>General Fund</u>	<u>Special Fund</u>	<u>Federal Fund</u>	<u>Reimb. Fund</u>	<u>Total</u>
Fiscal 2002					
Legislative Appropriation	\$0	\$49,587	\$0	\$0	\$49,587
Deficiency Appropriation	0	0	0	0	0
Budget Amendments	0	12,859	0	0	12,859
Reversions and Cancellations	0	-4,590	0	0	-4,590
Actual Expenditures	\$0	\$57,856	\$0	\$0	\$57,856
Fiscal 2003					
Legislative Appropriation	\$0	\$52,341	\$0	\$0	\$52,341
Budget Amendments	0	12,018	0	0	12,018
Working Appropriation	\$0	\$64,359	\$0	\$0	\$64,359

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

M00R – DHMH – Health Regulatory Commissions

Fiscal 2002

Special fund amendments resulted in the following changes to the fiscal 2002 working appropriation:

- The MHCC appropriation increased \$0.6 million for costs associated with office relocation and studies of preventable adverse medical reactions and the small group health insurance market.
- The HSCRC appropriation increased \$11.7 million due to higher than anticipated collections of the Uncompensated Care Fund. Additional appropriations totaling \$0.5 million supported office relocation, retention of expert witnesses, and consulting and data processing costs.

Fiscal 2002 special funds were cancelled primarily due to the lag between collection of uncompensated care and processing of hospital payments. This caused the HSCRC to cancel \$3.3 million in fiscal 2002, which remained in the fund for use at the beginning of fiscal 2003. \$0.6 million was cancelled by MHCC due to anticipated delays in office relocation. Cost containment by both commissions in contractual services and hiring freeze savings reduced the appropriation by an additional \$0.8 million.

The HSCRC special fund appropriation increased \$12 million in fiscal 2003. The majority of the increase, \$11.2 million, was due to higher than anticipated collections of the Uncompensated Care Fund. The remainder supported office relocation and consulting costs.

M00R - DHMH Health Regulatory Commissions

Appendix 2

Object/Fund Difference Report
DHMH - Health Regulatory Commissions

Object/Fund	FY 02	FY 03	FY 04	FY 03 - FY 04	Percent Change
	Actual	Working Appropriation	Allowance	Amount Change	
Positions					
01 Regular	101.70	97.70	95.70	-2.00	-2.0%
02 Contractual	0.32	0	6.00	6.00	N/A
Total Positions	102.02	97.70	101.70	4.00	4.1%
Objects					
01 Salaries and Wages	\$ 6,688,329	\$ 7,141,524	\$ 7,303,225	\$ 161,701	2.3%
02 Technical & Spec Fees	31,557	38,775	275,765	236,990	611.2%
03 Communication	162,470	98,454	94,732	-3,722)	-3.8%
04 Travel	87,823	114,811	119,008	4,197	3.7%
07 Motor Vehicles	(8,579)	(545)	0	545	-100.0%
08 Contractual Services	50,307,718	56,280,364	57,443,668	1,163,304	2.1%
09 Supplies & Materials	70,176	67,334	73,631	6,297	9.4%
10 Equip - Replacement	58,110	110,000	12,432	-97,568	-88.7%
11 Equip - Additional	4,133	20,500	25,000	4,500	22.0%
13 Fixed Charges	455,107	494,302	352,671	-141,631	-28.7%
Total Objects	\$ 57,856,844	\$ 64,365,519	\$ 65,700,132	\$ 1,334,613	2.1%
Funds					
03 Special Fund	\$ 57,856,844	\$ 64,365,519	\$ 65,700,132	\$ 1,334,613	2.1%
Total Funds	\$ 57,856,844	\$ 64,365,519	\$ 65,700,132	\$ 1,334,613	2.1%

- Note:
1. Full-time and contractual positions and salaries are reflected for operating budget programs only.
 2. Fiscal 2003 appropriations and fiscal 2004 allowance do not include cost containment and contingent reductions.

M00R - DHMH Health Regulatory Commissions

Fiscal Summary						
DHMH Health Regulatory Commissions						
<u>Unit/Program</u>	<u>FY 02 Actual</u>	<u>FY 03 Legislative Appropriation</u>	<u>FY 03 Working Appropriation</u>	<u>FY 02 – FY 03 % Change</u>	<u>FY 04 Allowance</u>	<u>FY 03 – FY 04 % Change</u>
01 Maryland Health Care Commission	\$ 7,559,359	\$ 8,409,727	\$ 8,839,727	16.9%	\$ 8,575,709	- 3.0%
02 Health Services Cost Review Commission	50,297,485	43,930,792	55,525,792	10.4%	57,124,423	2.9%
Total Expenditures	\$ 57,856,844	\$ 52,340,519	\$ 64,365,519	11.2%	\$ 65,700,132	2.1%
Special Fund	\$ 57,856,844	\$ 52,340,519	\$ 64,365,519	11.2%	\$ 65,700,132	2.1%
Total Appropriations	\$ 57,856,844	\$ 52,340,519	\$ 64,365,519	11.2%	\$ 65,700,132	2.1%

Note: Fiscal 2003 appropriations and fiscal 2004 allowance do not include cost containment and contingent reductions.