Hospital Global Budget Working Group

April 7, 2023

Agenda

- Recap of the Consensus from the Last Meeting
- Continued Discussion of How to Calculate and Update Budgets Annually
- Discussion of Whether (and if so, How) to Adjust Budgets to Account for Volume Changes
- Public Comment
- Next Steps

Recap of the Consensus from the Last Meeting

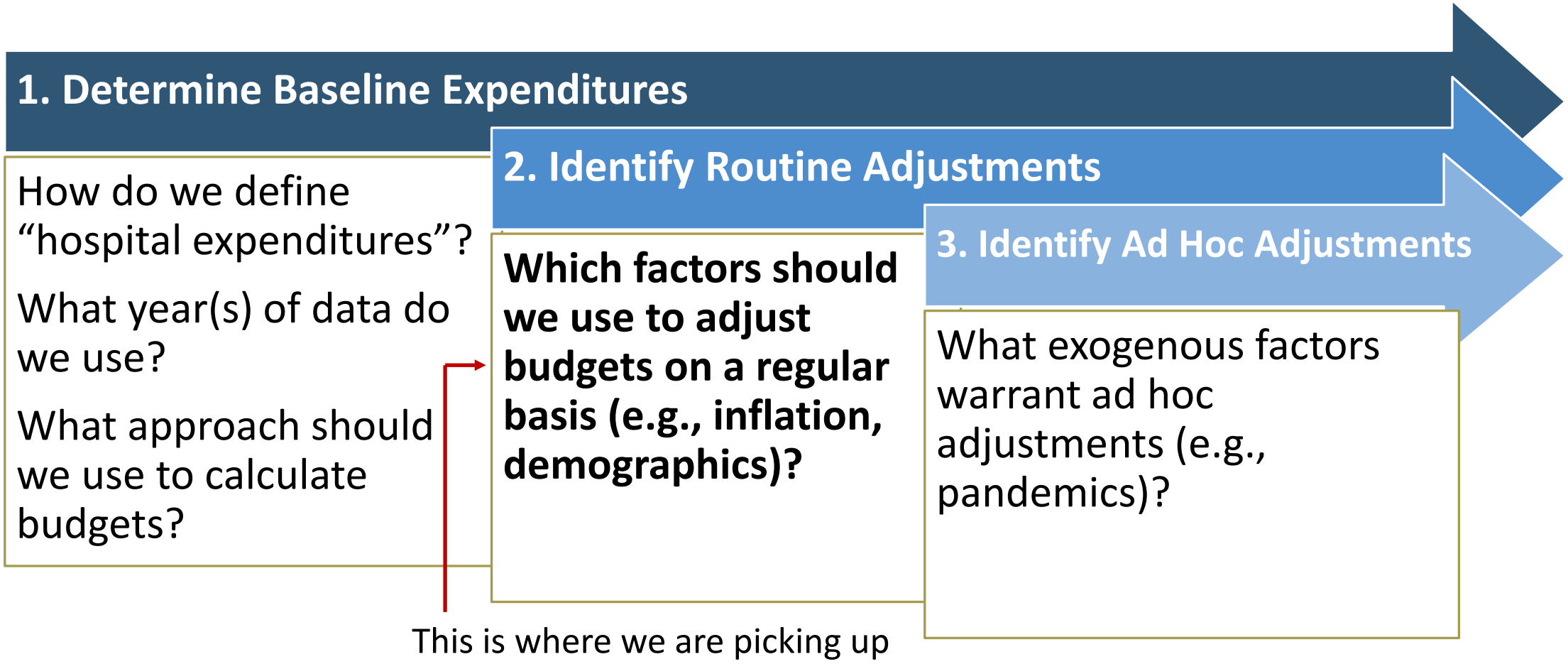
Consensus from the March 6th Meeting

1. Use insurer paid amounts as the basis for developing budgets, but also inform the budgets by an analysis of hospital finances during the base years, considering hospital costs and hospital operating margins.
2. Use 2017-2019 data to model the impact of moving to a hospital global budget. Use more recent data from 2023 onwards when setting budgets for 2026 and evaluate the need for adjustments to account for COVID's impact at that time.
3. Use a "bottom-up approach" to develop market-specific budgets for each participating payer-hospital dyad.
4. Develop one routine budget adjustment (frequency to be defined) to account for changes in age, sex and case mix.

Continued Discussion of How to Calculate and Update Budgets Annually

Reminder of the Steps to Calculate Global Budgets

There are three overarching steps to calculating global budgets.



2. Which Routine Adjustments Should We Make?

Demographics	Inflation	Volume Adjustments*
Case Mix	Uncompensated Care	Other?

Please note that we will discuss the following topics in future meetings:

- How to define each of these adjustments in greater detail
- How to incorporate these adjustments into the budget calculation

*We will defer consideration of volume adjustments until after we discuss flexible global budget arrangements.

Continue Discussion of Adjusting for Inflation

During the last meeting, the Working Group generally agreed with the concept of adjusting budgets to account for inflation.

We will defer recommendation of the specific inflation measure to use to a technical workgroup, but will discuss the "type" of inflation measure that should be considered.

There are two lenses by which to view what an appropriate inflationary adjustment should be:

- Hospital costs
- Consumer affordability

What Type of "Inflation" Should be Considered in Trending Forward Budgets?

	Inflation Description	Examples of Possible Measures
Hospital Cost Lens	Reflects increase in medical expenditures	Producer Price Index (PPI)
	Reflects increase in input prices experienced by hospitals	Specific components of the PPI (e.g., for pharmacy)
Affordability Lens	Reflects increase in overall price growth across the economy as a whole	Core Consumer Price Index
	Reflects wage growth	Median household income

Continue Discussion of Adjusting for Workforce

The Working Group also began to discuss whether budgets should be adjusted to account for hospital workforce cost pressures.

Workforce adjustments has been raised in several contexts (e.g., infrastructure investment, inflation, payment rates, hospital operating budget deficits).

- We should be mindful to not adjust for the same factor in a way that would be duplicative.
- In addition, it is vital that we consider how each adjustment will impact affordability from the consumer and payer standpoint.

We propose that any adjustments to account for hospital workforce cost pressures be included as part of a *one-time* infrastructure investment.

Adjustments for Uncompensated Care

Decisions around payment rates and how to close the gap in hospital operating budgets directly impact hospitals' costs associated with uncompensated care.

Similar to workforce, we need to be mindful to not adjust for uncompensated care in a way that is duplicative and negatively impacts consumer affordability.

We propose that there be no further adjustments to uncompensated care as other adjustments already address this issue.

Are There Other Routine Adjustments We Should Consider?

Are there any additional optional budget adjustments you think we should consider?

As a reminder, a hospital global budget focuses on payments for hospital services. As a result, there will be other payment streams that will remain independent from the hospital global budget, such as:

- Graduate/indirect medical education
- Disproportionate share hospital (DSH) payments

Should Routine Adjustments be Made Prospectively?

Routine adjustments are typically known ahead of the performance period and therefore made prospectively.

- Prospective adjustments ensures changes in performance during the year are reflected in a future year's budget.
- They also provide greater certainty around what a hospital's budget will be in advance of the performance period.

Does this approach seem reasonable to you, or do you recommend adjusting budgets retrospectively?

Should Routine Adjustments be Made Annually or Less Frequently?

ANNUAL ADJUSTMENTS

- Ensures hospital budgets reflect the most recent performance
- Results in one methodology to calculate budgets every year

LESS FREQUENT ADJUSTMENTS

- May be more reasonable to implement less frequently (e.g., every other year) if budget adjustments are small

3. Which Ad Hoc Adjustments Should We Make?

In addition to routine adjustments, there may be grounds to adjust budgets on an ad hoc basis due to planned future changes and/or exogenous factors.

Examples may include:

- New service offerings/ closures
- Pandemics*
- Significant macroeconomic changes
- Social risk/equity

In the following slides, consider which ad hoc adjustments you recommend. Please note that we will discuss how to operationally define these adjustments in future meetings.

*We will defer consideration of pandemics until after we discuss flexible global budget arrangements.

Should We Adjust for New Service Offerings/ Closures?

New Service Offerings/Closures

Accounts for approved expansions or planned reductions in hospital service offerings

- Ensures that budgets are modified to support planned service offerings
- Encourages hospitals to modify service offerings to meet community needs
- Builds upon existing Certificate of Need (CON) process

- May be challenging to predict how changes in service offerings will impact the budget
- Requires coordinating with the CON review process and timeline

Should We Adjust for Significant Macroeconomic Changes?

Significant Macroeconomic Changes

Accounts for economic changes that could impact hospital finances (e.g., recessions, expansions)

- Acknowledges that economic factors outside of a hospital's control can impact finances

- Challenging to identify
  - what changes are significant enough to warrant budget adjustments, and
  - the methodology for making such adjustments

Should We Adjust for Social Risk/Equity?

Social Risk/ Equity

Accounts for the social risk of the population served and aims to correct existing inequities in payments

- Supports hospitals that serve historically marginalized communities that may need additional resources
- Encourages hospitals to improve access and facilitate appropriate utilization

- Limited existing research on how to implement social risk adjustment
- No certainty that added funds would further population health equity

Are There Other Ad Hoc Budget Adjustments We Should Consider?

Are there any additional ad hoc budget adjustments we should consider?

Discussion of Whether (and if so, How) to Adjust Budgets to Account for Volume Changes

Overview of Three Different Approaches to Hospital Payment

FFS MODEL

Hospital is paid 100 cents on the dollar for each new service, even though the the cost to produce the service is <$1

Predominant payment model for hospitals in the U.S.

FLEXIBLE GLOBAL BUDGET

Hospital receives additional revenue for variable costs associated with increases in utilization during the year and retains payment to cover fixed costs when utilization declines

Maryland from 1976-1990; Rochester 1980-1987; International global budgets since 2010 (e.g., Germany)

FIXED GLOBAL BUDGET

Hospitals receives a guaranteed amount of revenue per year that does not change whether volumes increase or decrease

Maryland All-Payer and TCOC Models; International approaches in early 2000s (e.g., Canada, Germany, France)

Comparison of Payment Approaches: Example of Hospital with 50/50 Variable vs Fixed Costs

- Under FFS payment, the profit margin increases with increases in volume
- Under Fixed Global Budgets (GBs), decreases in volume lead to higher profits
- Under Flexible GBs, volume increases or decreases do not impact profit margins

Volume Change over Baseline	**Fee for Service** Paid 100c on the $ VC = 50c on the $	**100% Fixed GBs** Revenue Guarantee 0 Pmt for new Volume	**Flexible GBs** Example 50% FC & 50% VC Volume Adj.	**Modified Flex GB** Stronger Incentive 60% FC & 40% VC.
+5.00%	5.63%	0.92%	3.33%	2.86%
+3.00%	4.74%	1.88%	3.33%	3.05%
+2.00%	4.28%	2.37%	3.33%	3.14%
+1.00%	3.81%	2.76%	3.33%	3.24%
0.00% (baseline)	3.33%	3.33%	3.33%	3.33%
-1.00%	2.85%	3.82%	3.33%	3.43%
-2.00%	2.35%	3.92%	3.33%	3.53%
-3.00%	1.84%	4.78%	3.33%	3.63%
-5.00%	0.79%	5.75%	3.33%	3.83%

Profit Margin

There is some Flexibility in how the Flexible Global Budget is structured (e.g., incentives to manage care can be modified based on experience over time).

Considerations for Fixed Global Budgets

ADVANTAGES

- Guarantees a set level of revenue each year regardless of patient volume or a hospital's cost experience
- Provides a set budget that allows hospitals to allocate resources prior to the start of the year
- Provides the flexibility for hospitals to redesign care delivery to meet the needs of the community and improve population health
- Simpler to administer

DISADVANTAGES

- Incentivizes restrictions in services and shifting care to other providers or settings not covered by the budget
  - May impede technology adoption
- Can only be adjusted for market shifts and not overall utilization changes
- Limits ability to redirect patient volume to low-cost/high quality hospitals
- Does not allow ACOs to realize savings from better care management activities (hospital captures the savings)
- Results in higher levels of financial risk for smaller hospitals

Considerations for Flexible Global Budgets

ADVANTAGES

- Covers hospital fixed costs regardless of volume fluctuations
- Eliminates incentive for hospitals to increase utilization to generate savings/profit, as hospitals only receive additional payments for variable costs
- Reduces incentive for hospitals to stint or shift care outside the hospital/budget
- Provides additional revenues to accommodate new technologies/drugs
- Accommodates payer-induced shifts of care from high-cost to low-cost hospitals
- Provides better protection for all parties in the case of sudden, unexpected shifts in volume

DISADVANTAGES

- Does not provide revenue certainty before the start of the year, as the budget will fluctuate based on utilization (variable costs)
- Challenging to precisely identify the proportion hospital fixed vs. variable costs
- Reduces pressure for hospitals to manage utilization/efficiency; may incentivize hospitals to focus on growing profitable service lines
  - Note: Variable Cost factors used can be adjusted to apply incrementally stronger incentives to manage care

Discussion

Should we adopt a fixed or flexible global budget approach?

Future Discussion Topics

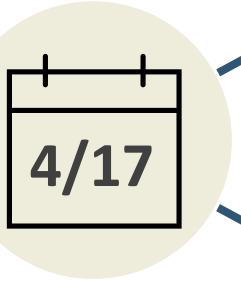
If the Working Group recommends pursuing a flexible global budget approach, we will need to consider the following questions:

1. How can we determine what portion of hospital expenses are fixed versus variable?
   - Should there be asymmetric adjustments made for volume increases versus volume decreases?
2. How should we measure volume for inpatient and outpatient services?
3. How often should we make budget adjustments to account for volume changes?
4. How should we make adjustments for volume fluctuations in non-hospital services that are billed under the hospital TIN?

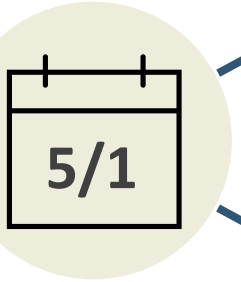
Public Comment

Next Steps

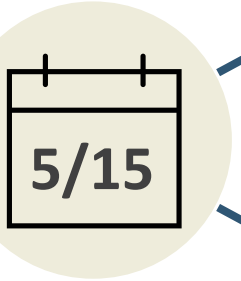
Working Group Meeting Plan and Schedule



- Discuss how to adjust budgets to account for changes in utilization during the performance period (cont'd)



- Discuss how to adjust budgets to account for changes in utilization during the performance period (cont'd)



- Decide whether the hospital global budget model should include supplemental arrangements to improve population health, access and quality