

439th MEETING OF THE
HEALTH SERVICES COST REVIEW COMMISSION

October 10, 2007

Chairman Young called the meeting to order at 9:30 a.m. Commissioners Joseph R. Antos, Ph.D., Raymond J. Brusca, J.D., Trudy R. Hall, M.D., James Lowthers, William H. Munn, and Kevin J. Sexton were also present.

REPORT OF THE EXECUTIVE SESSION OF OCTOBER 10, 2007

Oscar Ibarra, Chief-Program Administration & Information Management, summarized the minutes of the October 10, 2007 Executive Session.

ITEM I
REVIEW OF THE MINUTES OF THE EXECUTIVE AND PUBLIC SESSIONS OF
SEPTEMBER 12, 2007

The Commission voted unanimously to approve the minutes of the September 12, 2007 Public Meeting and the minutes of the Executive Session.

COMFORT ORDERS

The Commission voted unanimously to ratify the Comfort Orders for: Mercy Medical Center, Upper Chesapeake Medical Center, and LifeBridge Health System approved in Executive Session.

ITEM II
EXECUTIVE DIRECTOR'S REPORT

Robert Murray, Executive Director, outlined the status of the high priority projects currently being undertaken by staff. They include: 1) working with the General Assembly on the issue of Health Insurance reform; 2) the Quality-based reimbursement initiative; and 3) working on the implementation of the Outpatient Constraint System. Mr. Murray stated that staff expects to present a progress report on the Outpatient Constraint System at the Commission's November Public Meeting.

Mr. Murray also introduced Ms. Claudine Williams as new Health Policy Analyst II. Ms. Williams will work primarily on the management of the Nurse Support Program and the discharge data set.

ITEM III
DOCKET STATUS CASES CLOSED

1945A – MedStar Health

1956A – University of Maryland Medical Center

1958A – University of Maryland Medical Center

1951A – Johns Hopkins Health
System

ITEM IV
DOCKET STATUS CASES OPEN

**St. Agnes Health Care, Maryland General Hospital, Washington County Hospital, and
Western Maryland Health System - 1959A**

On August 21, 2007, St. Agnes Health Care, Maryland General Hospital, Washington County Hospital, and Western Maryland Health System (the Hospitals) filed an application requesting approval for the continued participation of Maryland Physicians Care, the risk bearing entity, in the Medicaid Health Choice Program. The Hospitals requested that the renewal be for one year beginning January 1, 2008.

Based on the favorable experience of last year, staff recommended that the Hospitals' request be approved for one year beginning January 1, 2008. Staff also recommended that Maryland Physicians Care report to staff on or before the Commission's July 2008 public meeting on its preliminary CY 2008 financial performance and projections for CY 2009. In addition, staff recommended that the approval be contingent on the execution of the standard Memorandum of Understanding.

The Commission voted unanimously to approve staff's recommendation.

MedStar Health – 1960A

On August 30, 2007, MedStar Health filed an application on behalf of Franklin Square Hospital, Good Samaritan Hospital, Harbor Hospital Center, and Union Memorial Hospital (the Hospitals) seeking approval for the continued participation of Helix Family Choice, the risk bearing entity, in the Medicaid Health Choice Program. The Hospitals requested that the renewal be for one year beginning January 1, 2008.

Based on favorable experience of last year, staff recommended that the Hospitals' request be approved for one year beginning January 1, 2008. Staff also recommended that Helix Family Choice report to staff on or before the Commission's July 2008 public meeting on its preliminary CY 2008 financial performance and projections for CY 2009. In addition, staff recommended that the approval be contingent on the execution of the standard Memorandum of Understanding.

The Commission voted unanimously to approve staff's recommendation.

Johns Hopkins Health System – 1961A

ON September 6, 2007, Johns Hopkins Health System filed an application on behalf of Johns Hopkins Hospital, Johns Hopkins Bayview Medical Center, and Howard County General Hospital (the Hospitals) seeking approval for the continued participation of Priority Partners, Inc., the risk bearing entity, in the Medicaid Health Choice Program. The Hospitals requested that the renewal be for one year beginning January 1, 2008.

Based on favorable experience of last year, staff recommended that the Hospitals' request be approved for one year beginning January 1, 2008, Staff also recommended that Priority Partners, Inc. report to staff on or before the Commission's July 2008 public meeting on its preliminary CY 2008 financial performance and projections for CY 2009. In addition, staff recommended that the approval be contingent on the execution of the standard Memorandum of Understanding.

The Commission voted unanimously to approve staff's recommendation.

Johns Hopkins Health System – 1962A

On September 14, 2007, Johns Hopkins Health System (the System) filed an application on behalf of Johns Hopkins Bayview Medical Center requesting approval for continued participation in a capitation arrangement among the Johns Hopkins Health System, the Maryland Department of Health and Mental Hygiene, and the Centers for Medicare and Medicaid Services. Johns Hopkins Bayview Medical Center, doing business as Hopkins Elder Plus serves as a provider in PACE, Program of All-Inclusive Care for the Elderly. Under this program, Hopkins Elder Plus provides services for a Medicare and Medicaid dually eligible population of frail elderly. The request is to extend the approval for a period of one year beginning July 1, 2007.

Based on favorable performance for the last year, staff recommended that the System's request be approved for one year beginning July 1, 2007. In addition, staff recommended that the approval be contingent on the execution of the standard Memorandum of Understanding.

The Commission voted unanimously to approve staff's recommendation.

ITEM V

FINAL RECOMMENDATION OF THE CORRECTIVE ACTION TASK FORCE

Chairman Young expressed his satisfaction with the work of the Corrective Action Task Force (CATF). The Chairman stated that although the CATF has been extremely successful, there is additional work to be done.

Mr. Murray stated that because of the value of the Medicare Waiver, we must always be aware of Maryland's relative margin on the Waiver test. Mr. Murray noted that the erosion of the

cushion over the period 2004-2006 was expected; however, the magnitude of the erosion was unexpected. According to Mr. Murray if the current policy were to be continued, the waiver cushion would dip below 7% by June 2009. Therefore, consistent with the language of the three year agreement, the Commission took corrective action by convening the CATF.

Mr. Murray noted that the longer term options discussed in the CATF include: 1) Medicare utilization; 2) reexamination of current cost allocation formulas; 3) re-evaluation of the Uncompensated Care Pooling methodology; and 4) a concerted effort to try to eliminate the Medicaid Day Limits.

Mr. Murray noted that a significant portion of staff's written recommendation is devoted to the volume adjustment. Mr. Murray asserted that volume adjustments are economic justified for volume adjustments since there clearly are fixed and variable costs. According to Mr. Murray, volume adjustments have been an integral part of the rate setting system since its inception. Mr. Murray stated that the system moved to 100% variable costs at a time of declining volumes; however, since that time, there has been significant volume growth both in admissions and visits, as well as in units of service. Mr. Murray cited a report by the Maryland Health Care Commission, which points to volume as the major cost driver in Maryland hospital cost increases in the last several years.

Deliberations in the CATF produced three short term options for 2008 and 2009. There are three methods of application within each of the options: 1) a technical, revenue neutral method; 2) a direct reduction to the inpatient Charge per Case; and 3) a volume adjustment in terms of magnitude and also the method by which the adjustments are made

Mr. Murray summarized the short term options as presented in staff's recommendation. The first option was that of the Maryland Hospital Association (MHA). MHA proposed: a) an immediate offset of 1% to the 2008 rate update, which represents an overall revenue give-up in 2008 in excess of 0.5% of total system revenue; b) that we move forward with the Financial Conditions Study; c) that the CATF reconvene later this year to consider longer term changes in the context of a three year time horizon; and d) that case mix change be limited to the previously agreed upon magnitude of 1.25%.

Option two is a hybrid of both the payer option and the MHA option. Option two proposes: a) the MHA option for the direct offset to the rate update for 2008; and b) the imposition of the volume adjustment in 2009.

Option three, the Payer proposal, is based on the philosophy that because of rate realignment, any offset to inpatient rates should have a commensurate offset to outpatient rates. The payers also propose that a direct adjustment of 1.14% be made immediately to both inpatient and outpatient rate updates. This adjustment would result in an overall revenue reduction of 0.86% in 2008 relative to the update approved in April 2007. In addition, the payer's strongly support the need for a volume adjustment.

Mr. Murray noted that there was consensus within the CATF in support of substantial improvements on the Waiver Test and immediate corrective action. However, since we are

already three months into FY 2008, the CATF was mindful that any adjustments to the rate system need to be reasonably implemented and absorbed by the hospital industry. There was also consensus that there must be continued improvement over time.

Mr. Murray summarized the consensus CATF recommendations: 1) that in the winter of FY 2008, the Commission and staff assemble a separate work group to conduct a Financial Conditions Study; 2) that the Commission and staff, with assistance of CATF members, investigate the longer-term initiatives identified during the CATF deliberations and described in the written recommendation document; 3) that since there was no consensus on a target level for the State's position on the Medicare Waiver Test, the CATF be reconvened after the Financial Conditions Study has been completed to review the results and to deliberate over additional short term and longer term initiatives with the goal of achieving sustained improvement over time; and 4) that the members of the CATF and the Commission strongly advocate for the elimination of the Medicaid Day Limits beginning in FY 2009.

Mr. Murray then summarized the recommendations that did not receive a consensus: 1) that the Commission review the range of options identified by the CATF, and described in the written recommendation, and select the option or combination of options that it believes will: a) improve the System's position on the Medicare Waiver Test; and b) achieve the best overall policy outcome for the hospitals, payers, and citizens of Maryland, balancing the multiple goals of ensuring the financial viability of the Maryland hospital system while, at the same time, promoting the delivery of efficient and affordable hospital care; and 2) that the Commission consider and act on the more technical final staff case mix recommendation.

John O'Brien, Deputy Director-Research & Methodology, presented staff's final recommendations on the handling of Case Mix for FY 2007 and 2008. They were: 1) that the 2007 case mix growth be allocated by following steps to provide for the first 1.02% of case mix growth by governed case mix, the next 0.20% for full Root DRG growth, and the remaining 0.08% to restore any available severity growth for a final case mix growth of 1.30%; 2) that there be no special adjustments that give preference to root DRG growth over any other case mix growth, as measured by the APR-DRG grouper for FY 2008; 3) that if measured case mix growth in FY 2008 exceeds targeted levels, the target will be met either by a simple proportional adjustment or a some other methodology that does not give preference to root DRG change; 4) that in FY 2008, an ungoverned care mix adjustment be made for hospitals that experienced case mix declines in FY 2006 followed by increases in case mix in FY 2007, equal to the amount of their FY 2006 case mix decline; 5) that unallocated case mix growth of 0.4% from FY 2006 be restored to hospitals in FY 2008, proportionally by revenue, based on the amount that the hospital's measured growth exceeded approved case mix in FY 2006; and 6) that the prior year case mix adjustments, recommendations 4 and 5, be addressed in FY 2008 rates so that the total allowance for case mix change in FY 2008 be limited to 1.0%, inclusive of all pass through and measured case mix change.

Robert Chrencik, Executive Vice President and CFO of the University of Maryland Medical System, Brian Gagnolati, President and CEO of Suburban Hospital, Thomas Mullen, President and CEO of Mercy Medical Center, and Paul Sokolowski, Senior Vice President-Finance of MHA presented MHA's recommendations for Waiver Test improvement for 2008. The hospital

representatives expressed support for Option #1. According to the representatives, Option #1 results in a 0.46% improvement in the Waiver cushion by the end of FY 2008, and the elimination of Medicaid Day Limits would add another 0.80% to the cushion. They expressed the hospital industry's unanimous opposition to the imposition of volumes adjustments. The representatives urged the Commission to delay making a decision on volume adjustments until after the Financial Conditions Study is completed, since it would not be implemented until FY 2009 if approved. However, they supported the re-convening of the CATF with the goal of crafting a three-year agreement for 2009-2011 that would include: 1) Medicare Waiver Targets; 2) revised National Revenue Targets; 3) revised rate methodologies; 4) updated Productivity Improvement Goals; and 5) revised Financial Condition Targets. They suggested that the CATF also discuss volume adjustments, uncompensated care and access reform, and hospitals' influence on admissions in conjunction with the three-year agreement. They also reiterated the industry's strong support in working to eliminate Medicaid Day Limits.

Commissioner Hall asked when the results of the Financial Conditions Study would be available if the study were to begin immediately.

Mr. Murray stated that it would be at least a two month process.

Commissioner Hall asked how much assurance we have that Medicaid Day Limits will end.

Mr. Murray responded that to his knowledge equivalent savings from Medicaid Day Limits were not currently in the Department of Health and Mental Hygiene's budget.

Vice Chairman Sexton asked Mr. Murray where we stand on beginning to try to craft a new three-year agreement.

Mr. Murray stated his belief that in the current uncertain situation, it is more practical to take a year to year look at policy issues while looking ahead as much as possible to where we want the System to be in the next three years. Mr. Murray expressed doubt as to whether there was sufficient time between February, when the Financial Conditions Study results would be available, and April 2008 to come to an agreement over a three year rate arrangement covering the years 2009 through 2011.

The Chairman agreed that we just do not know enough to structure a three-year agreement. Too many things can happen; e.g., changes in the economy, changes in the Medicare update or in the Waiver test, all of which can result in the agreement being changed.

Vice Chairman Sexton stated that in the past we have set targets.

The Chairman asked whether Mr. Sexton suggested that we should forecast a range of where we might want to be.

Mr. Sexton stated that we should develop a narrative to indicate where, under various circumstances, we want the rate system to be.

The Chairman stated that this should be an agenda item for the re-convened CATF.

Commissioner Brusca asked whether the Financial Conditions Study would address the variable cost issue.

Mr. Murray indicated that it would estimate what the impact would be on the hospital industry if the volume adjustment were approved by the Commission for 2009.

Commissioner Munn asked whether the decision on the volume adjustment had to be made now for 2009. He expressed his concern over the issue of hospitals that are growing fast versus hospitals whose growth is flat.

Mr. Murray stated that one of the benefits of the volume adjustment is that it is more equitable than 100% variability with volume changes because hospitals whose volumes are growing, and are better able to sustain the volume adjustment, are provided their variable costs, while hospitals whose volumes are declining are provided their fixed costs. Mr. Murray observed that hospitals have historically managed to volume adjustments in the System and should be able to do so in the future.

The Chairman asked whether the Commission had to make a decision today on the volume adjustment.

Mr. Murray stated that from staff's point of view, the more we discuss these issues, the more they tend to be put off. According to Mr. Murray, staff and most of the members of the CATF were strongly in support of implementing a volume adjustment in 2009.

Hal Cohen, Ph.D., representing CareFirst and Kaiser Permanente, Barry Rosen, Esquire, representing United Health care, and Ms. Tricia Roddy, representing Medicaid, presented the payers' recommendations to improve the waiver test cushion. The payer representatives stressed the importance of the Commission's to immediately approving the implementation of the volume adjustment because it worked for many years in Maryland; it produces fairer increases to hospitals and it provides better incentives than the current methodology. According to the representatives, volume is driving much of the unaffordability of the System. They expressed approval for staff's recommendation on the handling of case mix and also suggested that the outpatient update in options #1 and #2 be limited to 3.4% because of supply and drug pass throughs. The representatives indicated that the Financial Conditions Study should concentrate on profits and costs and not national revenue standards. They supported a 10% Waiver cushion as the right goal. And, in conclusion, the representatives expressed their support for: 1) MHA's inpatient proposal for 2008; 2) staff's variable costs adjustment proposal for the second year; and 3) the reduction of the outpatient update for 2008 to 3.4%.

A motion was made by Commissioner Lowthers and seconded, that Option #2 presented in staff's recommendation be approved. including the recommendation on case mix.

The Commission voted unanimously to approve Commissioner Lowthers' motion.

Commissioner Hall offered an addendum to the approved motion that once the Financial Conditions Study information is available, the Commission should review the projected impact of the volume adjustment on individual hospitals in 2009.

Mr. Murray assured Commissioner Hall that the projected impact will be presented to the Commission.

ITEM VI
HEARING AND MEETING SCHEDULE

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| November 16, 2007 | Time to be determined, 4160 Patterson Avenue, HSCRC Conference Room |
| December 5, 2007 | Time to be determined, 4160 Patterson Avenue, HSCRC Conference Room |

There being no further business, the meeting was adjourned at 10:45 a.m.