LEGISLATIVE BUDGET AND FINANCE COMMITTEE

MEDICAL ASSISTANCE PAYMENTS TO HOSPITALS

Report Highlights

House Resolution 586 required the LB&FC to evaluate how state Medicaid (MA) payments to acute, psychiatric, and rehabilitation hospitals affect their financial performance. The Lewin Group, a national research and healthcare consulting firm, conducted the study.

- Hospitals need total margins of 4-6% to modernize their facilities and equipment and meet changing healthcare needs. PA hospital margins have deteriorated markedly since 1997, with total margins dropping to 2.4% in 1999 and operating margins averaging only .03%. Nationwide, total hospital margins in 1999 were 4.65% and operating margins were 1.07%.

- The bottom quartile of PA hospitals (the lowest 25% ranked on margins) had total margins below negative 1.4%. 60% of these hospitals have had low or negative margins for the past 3 years and would appear to be in severe financial distress.

- The low margins in PA are not due to cost inefficiency. Costs in PA acute care hospitals are 6 to 7 percent below their expected costs, second most cost efficient in the nation.

- As shown below, a major reason for the increasingly poor financial performance of PA hospitals is the decreasing payment-to-cost ratio of commercial insurers. PA Medicaid's low payment-to-cost ratio is another factor. Both are far below national averages (115% for commercial insurers and 96% for Medicaid).

Pennsylvania

- According to a special survey conducted in January 2001, MA covered 82% of inpatient costs but only 54% of hospital outpatient cost. MA fee-for-service (FFS) and managed care have comparable overall payment-to-cost ratios.

MA Payment-to-Cost Ratios

	FFS	MCO	Total
Inpatient	86%	78%	82%
Outpatient	50%	59%	54%
Total	76%	73%	74%

Source: The Lewin Group analysis of Jan. 2001 survey

- Pennsylvania's MA inpatient rates have been increasing at about the rate of inflation. MA fees for outpatient medical services, however, are virtually unchanged since 1992, which partially explains the low outpatient payment-to-cost ratio.

- In 1999, MA would have had to pay an additional $400 million to hospitals to cover the full cost of care for its patients in acute-care hospitals.

- The General Assembly has appropriated funds to aid hospitals that serve higher numbers of individuals who no longer qualify for MA services. The average operating margin for the 61 hospitals receiving Community Access/Charity Care funds was 1.6 percent compared to 1.1 in the absence of such payments.

- The Lewin Group concluded MA hospital payments should be increased, especially for outpatient care. In return, hospitals should increase their support of community services directed at MA eligibles.