Vermont Community Hospitals

Actual 2016 operating results – Budget-to-Actual **4/12/2017**

Enforcement issues

The GMCB enforcement policy establishes the rationale and the approach for reviewing hospital budget-to-actual performance once that information is filed. For Actual 2016, eight hospitals exceeded their overall net patient revenue (NPR) budget by more than the 0.5% enforcement trigger established by the Board. Our review examines the following for consideration as part of our enforcement review.

Two hospitals exceeding the NPR target were deemed as needing no further review as discussed at the March 30, 2017 Board meeting. Six hospitals had NPRs below budget; staff is examining the financial health of those hospitals and reviewing any major budget changes such as discontinuing a program or restructuring services that may have occurred.

Questions to consider

a) Why did a hospital exceed our variance? Is this a reasonable explanation? When did the hospital become aware that it was off target?

b) Which issues should be considered controllable by the hospital?

c) What were the effects of the hospital exceeding the variance?

d) What are the actions the Board can or should consider for enforcement? When should these actions occur?

e) How does the Board and staff accomplish this operationally?

Key schedules provided by staff

The hospitals' filings contain as much information as is filed with the annual Budget submissions. After presentation to the Board, staff summarized the findings as follows:

1) A system profile of the budget-to-actual variance and how each hospital variance compares to the 0.5% trigger;
2) Summaries that describe budget-to-actual performance and current year YTD performance;
3) An individual hospital profit and loss summary that shows 2016 budget, actuals, and changes for physician acquisitions;
4) An individual hospital variance summary that shows both NPR and expense variance in more detail, and
5) An individual hospital "decision dashboard" that focuses on how the variance impacts major key performance indicators (KPIs).

Understanding why the hospital exceeded its budgeted NPR

Each of the hospitals testifified about the major reasons for its NPR and expense variances. The following characterizes how the variances could be considered under review:

- Lower bad debt and/or free care
  - Many hospitals saw improvement in their NPR because actual results were lower than budget. This is a favorable development for both the hospital and the health care system in general. This essentially means that more patients are paying their hospital bills and/or that more patients have greater coverage for their hospital care, reducing the need for hospital write-offs that are ultimately passed on to other payers in the system.

    Staff opinion: This can be considered a favorable development. Unless a hospital's prior submissions indicate a consistent failure to reasonably budget for these items, the hospital shouldn't be "penalized" for being able to collect a larger portion of hospital billing from its patients. If a hospital budget-to-actual is substantial, however, then the next budget filing should reflect much lower levels of bad debt and free care. If the Board believes that a rate cut is warranted because of the budgeting variance for bad debt and free care, staff recommends not making an adjustment for the full amount of the variance attribuatable to this issue.

- Better reimbursement than expected

  - Determining whether payer reimbursement assumptions are reasonable involves understanding methods from three major payers. Preparation of the hospital budget occurs 4-6 months before the actual budget year begins.

  - Precision here is also difficult as payer mix, contracts, payer rule changes, and mix of utilization services can all affect reimbursements. Sometimes, a payer may make a major change after the year begins, in which case the hospitals are required to update the Board for a potential change in rates (such as Medicare status change). We have used this rationale in prior periods to change a budget and/or rates.

    Staff opinion: This is an area that could be subject to adjustment. The materiality of the difference, the reason for the difference, and prior history would be factors for determining a need for action.

- Utilization higher or different than budget

  - More utilization, more patients, or an improved "mix" of services to patients can result in higher NPRs. This can be explained as increased capacity (more physicians), more insurance access, increased market share both in and out of service area, and in–migration from other states.

Staff opinion: This is an area where adjustment is warranted as well, but a very difficult area to manage. Regulatory approaches have not yet consistently been able to manage utilization in a way that is appropriate, preserves patient choice, and keeps hospitals within their approved budgets. Indeed, some of the policies that the Board supports— expanded primary care and pediatrics come to mind — may be key drivers of the increased utilization. The Board needs to invest more time and resources to require budget adjustments before they occur. This will require better and more timely reporting.

Although increased utilization will typically result in increased costs, it should also produce a greater surplus, which can be used to lower future increases or current prices. The options below try to capture this:

- Pharmaceutical overages. This is more unique in that it seems to be more uncontrollable in terms of price and ever-changing physician care plans. This area could be isolated, or held harmless, (much like it is in the all payer model) until we have a better handle on circumstances. North Country experienced an issue with pharmaceutical overages and is currently working to move the program out of the hospital. Southwestern Vermont Medical Center (SVMC) is currently experiencing significant pharmaceutical overages in its budget. It is unclear whether SVMC's problem is similar to the problem at North Country.

Staff opinion: This should not be an area for adjustment at this time, though we could require a report outlining options for those hospitals experiencing these overages and how that may affect patient care. It is uncertain how much this might be contributing to surplus.

- Disproportionate share (revenue) and Provider tax

  - These account estimates are provided by DVHA to the hospitals as they are finalizing their budgest. Sometimes, a change will occur, resulting in a wrong estimate by the hospital, which can be favorable or unfavorable, and not in their control.

Staff opinion: Budgets should not be adjusted for these variances in most instances, unless there were unforeseen factors and a history of noncompliance. The results of a favorable change can also be captured as part of the next budget filing.

Decision -making approach

The Board has a consistent policy for reviewing and discussing possible budget adjustments. What has proven more difficult is documenting and articulating the rationale for each decision**.**

Staff opinion: A formula to adjust budgets based on a standard mathematical formula would not be appropriate. Objective data must be weighed with value judgements that each board member has regarding the testimony and information they have received from each individual hospital.

It is very difficult to make a consensus opinion with so many variables in play. Any board member may find one substantial factor that outweighs all other considerations. I have prepared options for each budget as a starting point for discussion.

Criteria for examining each budget could include:

1) Which NPR variances can be deemed as uncontrollable or favorable;
2) Did expenses exceed NPR variance;
3) How did the variance impact operating surplus;
4) What items of the NPR variance caused the operating surplus change;
5) What has been the hospital's history with regard to items 1 thru 3;
6) What is the hospital's financial condition; and
7) Are there extenuating circumstances to be considered?

Determine what you value – prioritize KPIs or other considerations. For example, does a hospital's community circumstances override the problem of not staying within budget? Does chronic poor performance override community circumstances? Does the amount of the excess require more aggressive action?

An Order should be prepared identifying the findings and describing the rationale for the Board's decision. The Board needs to prepare a Budget Order and include its findings and rationale for the decision. Future budget expectations could also be written. The preparation and timing required for these expectations should be carefully discussed as part of the Board's ongoing policies and subsequent decisions. The document could serve as a foundation for contemplating the next budget review for that hospital.

Possible enforcement actions to consider

The formal Board policy describes the action steps the Board may take.

"If the GMCB determines that a hospital's performance has differed substantially from its budget, the GMCB may take actions including but not limited to (see GMCB Rule 3.000, § 3.401(c)):

a) Reduce or increase in a hospital's rates;

b) Reduce or increase net revenue and/or expenditure levels in current year budget;

c) Use finding as a consideration to adjust the hospital's budget in a subsequent year or years; and

d) Establish full budget review of actual operations for that budget year."

Staff opinion: Understanding the Board may consider all the options above, the following outlines suggested approaches for this year:

A. Adjustment to current year prices
   - If the Board wishes to lower rates/prices, it could be done with an effective date of 5/1/ 2017 being the earliest date. How much to lower the rate could be a function of the NPR overage and/or the resulting surplus. Staff has estimated the effect of a 1% price reduction on the 2017 budget for each hospital.

B. Adjustment to future prices expected in the upcoming budget process
    - The Board could require a reduction in the future rate/price for a hospital that has exceeded the budget. While it does not address the immediate budget, it does provide for a hospital to plan and begin to "right size" for the next budget.

C. An adjustment that combines the concepts of A and B.

D. No change and/or more reporting requirements
    - The Board could require more immediate and distinct reporting for:
        - Better information on utilization for market share shifts,
        - Better information for payer changes, i.e., what is really happening in Medicare – type of patient increase, types of services, age profile, etc.

Vermont Community Hospitals

Actual 2016 operating results – Budget-to-Actual **4/12/2017**

Northeastern Vermont Regional Hospital

Findings

These are the items you could weigh in evaluating the action to be taken.

1) Exceeded NPR by 5.1%, $3.5 million
   Expenses 4.6%, $3.1 million
   Surplus - $440,000 higher; increase in margin from 1.5% to 2%
2) Medicare increase was $1.8 million of $3.5 million increase.
3) Variance due to utilization. Testimony indicates it is in-migration. This was noted at the summer FY 2017 budget hearings.
4) Bad debt free care – actually higher than expected (unfavorable)
5) Higher expenses due to hiring of part time ER physicians (locums)
6) 3 year NPR growth higher than VT Median
   3 year expense growth rate higher than VT Median
7) Days cash on hand of 123 which is less than median
8) Age of plant of 13.1 which is higher than median
9) Rate increase of 5.2% FY 2016 Budget, 3.8% FY 2017 Budget
10) Budget-to-actual history (see graphs at end of document).
11) Current year to date FY 2017 performance is over budget 4.8%.

Option A

Because operating surplus is higher require the hospital to submit a 2018 rate increase that is no higher than 2.8%. This 1% rate is lower than the approved rate for FY 2017. A 1% reduction for NVRH is valued at about $341,627 (FY17). (This is about 75% of the increased surplus).

Option B

Reduce rate effective May 1 by 1%. This would have a 5 months effect this year of about $143,000. It could result in higher rate need in FY 2018 since prices would start at a lower base. This would need to be reviewed as part of the 2018 filing.

Option C

If you were to combine A & B, you can reduce the rate by 0.5% and inform the hospital that rates must be lower in FY 2018 than approved in 2017. This would allow more of the surplus to be considered for setting rates in 2018.

Option D

No action taken as increase was from in-migration and the Board had been informed of this during the 2017 hearing. NVRH also has had good budget-to-actual performance in the last few years.

The Board could also order that the hospital file a more complete explanation of the utilization variance. Recapture of Vermont residents should be demonstrated by the hospital as well as projections as to when this will stabilize.

Vermont Community Hospitals

Actual 2016 operating results – Budget-to-Actual **4/12/2017**

Northwestern Medical Center

Findings

These are the items you could weigh in evaluating the action to be taken.

1) Exceeded NPR by 1.9%, $1.9 million
   Expenses 2.4%, $2.4 million
   Surplus - $1.6 million higher; increase in margin from 2.1% to 3.4%
2) Medicare increase was $2.6 million of $1.8 million increase (off-set by lower than budgeted Medicaid)
3) Variance mostly due to changes in bad debt and free care, which were lower than expected by $2.3 million (favorable)
4) Higher expenses due to utilization and depreciation
5) 3 year NPR growth equal to VT Median
   3 year expense growth rate higher than VT Median
6) Days cash on hand of 351 is higher than VT median (the median is 135) and higher than US NFP median (212)
7) Age of plant of 10.6 is lower than VT median
8) Rate decrease of 8.0% FY 2016 Budget, 0.0% FY 2017 Budget
9) Budget-to-actual history (see graphs at end of document).
10) Current year to date FY 2017 performance is under budget 0.9%.

Option A

Because operating surplus is higher, require the hospital to submit a rate of -2.0% for 2018. (This is about 75% of the increased surplus). Last year NMC had no rate increase. A 1% reduction for NMC is valued at about $604,000 (FY17).

Option B

Reduce rate effective May 1 by 2%. This would have a 5 months effect this year of about $507,000. It could result in higher rate need in FY 2018 since prices would start at a lower base. This would need to be reviewed as part of 2018 filing.

Option C

If you were to combine A & B, you could reduce the rate by 1% and inform the hospital that rates must be lower in FY 2018 than approved in 2017. This would allow more of the surplus to be considered for setting rates in 2018.

Option D

No action taken since hospital is under budget in 2017 and projecting a $2.4 million lower surplus than budget, offsetting the 2016 surplus increase.

The Board could order that if 2017 does not result in an operating loss, they would expect to see that rate/prices would be lower in 2018.

Vermont Community Hospitals

Actual 2016 operating results – Budget-to-Actual **4/12/2017**

Rutland Regional Medical Center

Findings

These are the items you could weigh in evaluating the action to be taken.

1) Exceeded NPR by 4.3%, $10.2 million
   Expenses 1.8%, $4.1 million
   Surplus - $4.9 million higher; increase in margin from 2.4% to 4.2%
2) Medicare increase was $20.5 million of $10.2 million increase (off-set by lower than budgeted Medicaid and Commercial)
3) Variance mostly due to changes in utilization and bad debt/free care.
4) Bad debt free care – lower than expected by $3.9 million (favorable)
5) Higher expenses due to utilization and disproportionate share payments.
6) 3 year NPR growth higher than VT Median
   3 year expense growth rate lower than VT Median
7) Days cash on hand of 205 is higher than VT median (the median is 135).
8) Age of plant of 11.8 is close to the VT median
9) Rate increase of 3.7% in 2016, rate decrease in May 2016 of 3.7%, rate decrease of 5.1% FY 2017 Budget.
10) Budget- to- actual history (see graphs at end of document).
11) Current year to date FY 2017 performance is over budget 0.4%.

Comments

The hospital has experienced significant growth in 2015 and 2016 and has responded by reducing its rates three times since May of 2016. (Some growth that occurred in 2015 also occurred in 2016.) For 2016, the hospital explained the utilization growth was from out-of-service area and the other NPR variance was related to lower bad debt and free care. RRMC does have a higher cost structure than its peers (SVMC, CVMC), which is related in part to the psychiatric bed unit it operates. The hospital also experienced a significant reduction in per unit costs in 2016 compared to budget.

Option A

Because the operating surplus is higher, require the hospital to submit a rate decrease of 3% for 2018. The reduction last year was 5.1%. A 1% reduction for RRMC is valued at about $1,411,000 (FY17).

Option B

Reduce rate effective May 1 by 3%. This would have a 5 months effect this year, about $1.8 million. It could result in higher rate need in FY 2018 since prices would start at a lower base. This would need to be reviewed as part of the 2018 filing.

Option C

If the Board combines A & B, it could reduce the rate by 1.5% and inform the hospital it is expected to further reduce rates in FY 2018. This would allow more of the surplus to be considered for setting prices/rates in 2018.

Option D

No action taken since RRMC submitted a proposal to reduce prices/rates effective May 1st. The decrease is based upon its return dollars for reductions in bad debt and free care.

Vermont Community Hospitals

Actual 2016 operating results – Budget-to-Actual **4/12/2017**

Southwestern Vermont Medical Center

Findings

These are the items you could weigh in evaluating the action to be taken.

1) Exceeded NPR by 5.5%, $7.9 million
   Expenses 5.4%, $7.7 million
   Surplus - $916,000 higher; increase in margin from 3.0% to 3.4%
2) Medicare increase was $5.8 million of $7.8 million increase.
3) Variance mostly due to changes in pharmacy, utilization and bad debt/free care.
4) Bad debt free care – lower than expected by $1 million (favorable)
5) Higher expenses due to pharmacy, utilization and bad debt/free care.
6) 3 year NPR growth lower than VT Median
   3 year expense growth rate lower than VT Median
7) Days cash on hand is approximately 160 days, including cash that's at the parent organization. (VT median of 135).
8) Age of plant of 17.1, close to the VT median
9) Rate increase of 3.8% FY 2016 Budget, and 3.4% FY 2017 Budget.
10) Budget-to-actual history (see graphs at end of document).
11) Current year to date FY 2017 performance is under budget 3.3%.

Option A

Because the operating surplus is higher, require the hospital to submite a 2018 rate increase that is no higher than 2.75%. This is about .65% lower than the approved rate for FY 2017. A 1% reduction for SVMC is valued at about $800,000 (FY17).

Option B

Reduce rate effective May 1 by 0.65%. This would have a 5 months effect this year of about $336,000. It could result in higher rate need in FY 2018 since prices would start at a lower base. This would need to be reviewed as part of 2018 filing.

Option C

If the Board were to combine A & B, it could reduce the rate by 0.5% and inform the hospital it is expected to further reduce rates in FY 2018. This would allow more of the surplus to be considered for setting prices/rates in 2018.

Option D

No action taken since SVMC'S history for NPR, expenditure growth, and rates are favorable.

The Board could order that the hospital file a more complete explanation of the options around managing the costs and revenue increase in their pharmaceutical program and provide a better profile of the patients served as well as how the program is funded by payer.

Vermont Community Hospitals

Actual 2016 operating results – Budget-to-Actual **4/12/2017**

Central Vermont Medical Center

Findings

These are the items you could weigh in evaluating the action to be taken.

1) Exceeded NPR by 9.2%, $16.1 million
   Expenses 11.2%, $20.4 million, including the physician transfers
   Surplus - $3.4 million lower than budget; decrease in margin from 2.9% to 1%
2) NPR increase; Medicare was $6.3 million and Commercial was $7.7 million of total
3) Variances of utilization $6.4 million, $3.7 physicians, $2.1 million pharmaceuticals and $3.3 million in improved reimbursement accounted for most of the increase
4) Bad debt free care – lower than expected $1.1 million (favorable)
5) Higher expenses due to higher volumes, physician acquisitions, the need for travelers, and increased costs of pharmacy and medical supplies
6) 3 year NPR growth higher than Vt. Median
   3 year expense growth rate higher than Vt. Median
7) Days cash on hand of 99 is at the 25th percentile
8) Age of plant of 9.7 lower than the 25th percentile
9) Rate increase of 4.7% in 2016 and Commercial Rate increase 2.45% in 2017
10) Budget-to-actual history (see graphs at end of document).
11) Current year to date FY 2017 performance is under budget 0.3%.

Comments

The hospital had significant growth in both 2015 and 2016. Some growth that occurred in 2015 also occurred in 2016. For 2016, the hospital had variances in all categories for NPR. Expenses were even higher as the hospital lost $3.4 million from its budgeted surplus level, despite $4.3 million of improved reimbursement and lower bad debt and free care. Many metrics are unfavorable, as the three-year look for NPR and expenses are among the highest in the state due to the growth the last two years. The good news is that 2017 YTD budget is on target and the age of plant is favorable.

Option A& B

I did not consider these options since the hospital growth problem is related to its inability to manage costs. The 2016 cost per adjusted admission is already higher than what is budgeted for 2017. This is due in part to their expanding quickly and needing to recruit premium labor (i.e., travelers, locums).

Option C

The hospital needs to get costs under control. The Board could order it to file an action plan that begins cost reductions now to address 2018 budget. The Board could direct this to CVMC or to the UVMMC network, but the plan needs to be transparent. It is unclear whether the expansion of physician and capacity is done, and this should be addressed as well. The rate increase was 2.45% in 2017. The Board could require CVMC to file a budget with no rate increase in 2018 – the hospital earns an estimated $800,000 for every 1% increase.

Option D

Not considered because the Board should take some type of action.

Vermont Community Hospitals

Actual 2016 operating results – Budget-to-Actual **4/12/2017**

The University of Vermont Medical Center

Findings

These are the items you could weigh in evaluating the action to be taken.

1) Exceeded NPR by 2.2%, $25.4 million, including $4.4 million in physician transfers. Expenses decreased by .3%, $3.4 million, including the physician transfers
   Surplus - $26.5 million higher than budget; increase from budget to actual 3.8% to 5.9%
2) Medicare increase was $19.7 million of $25.4 million increase.
3) Variances due to utilization of $22 million, DSH $2 million, bad debt/free care $7.8 million, and better payer reimbursement $3.1 million, which cumulatively account for most of the increase. An accounting change of $9.5 million for its health plan explains why this offsets some of these increases.
4) Bad debt free care – lower than expected $7.8 million (favorable)
5) Lower expenses due to the accounting change and reductions in other expenses.
6) 3 year NPR growth lower than Vt. Median
   3 year expense growth rate lower than Vt. Median
7) Days cash on hand of 214 is higher than the 75th percentile
8) Age of plant of 11.9 is at the Vt. Median
9) Commercial Rate increase of 6% in 2016 and 2.45% in 2017
10) Budget-to-actual history (see graphs at end of document).
11) Current year to date FY 2017 performance is over budget 0.4%.

Comments

The hospital had significant growth in both 2015 and 2016. Some growth that occurred in 2015 also occurred in 2016, as explained by the hospital. The hospital experienced a higher operating surplus both years. For 2016, the hospital managed costs, as its 2016 cost per adjusted admission is actually lower than budget and lower than its 2015 actual level. Bad debt and free care improvements also contributed to a more favorable surplus. Many metrics are favorable, as the three-year look for NPR and expenses are less than the 50th percentile. The amount of the surplus does suggest some rate relief could be provided. The approach last year included rate relief and an investment in local community activities.

Option A

Because the operating surplus is higher, require the hospital to submit a budget with no more than a 0% rate increase for 2018. This is 2.45% lower than the approved rate for FY 2017. A 1% reduction for UVMMC is valued at about $5.7 million.

Option B

Reduce rate effective May 1 by 2.45%. This would have a 5 months effect this year of about $5.9 million. It could result in higher rate need in FY 2018 since prices would start at a lower base. This would need to be reviewed as part of 2018 filing.

Option C

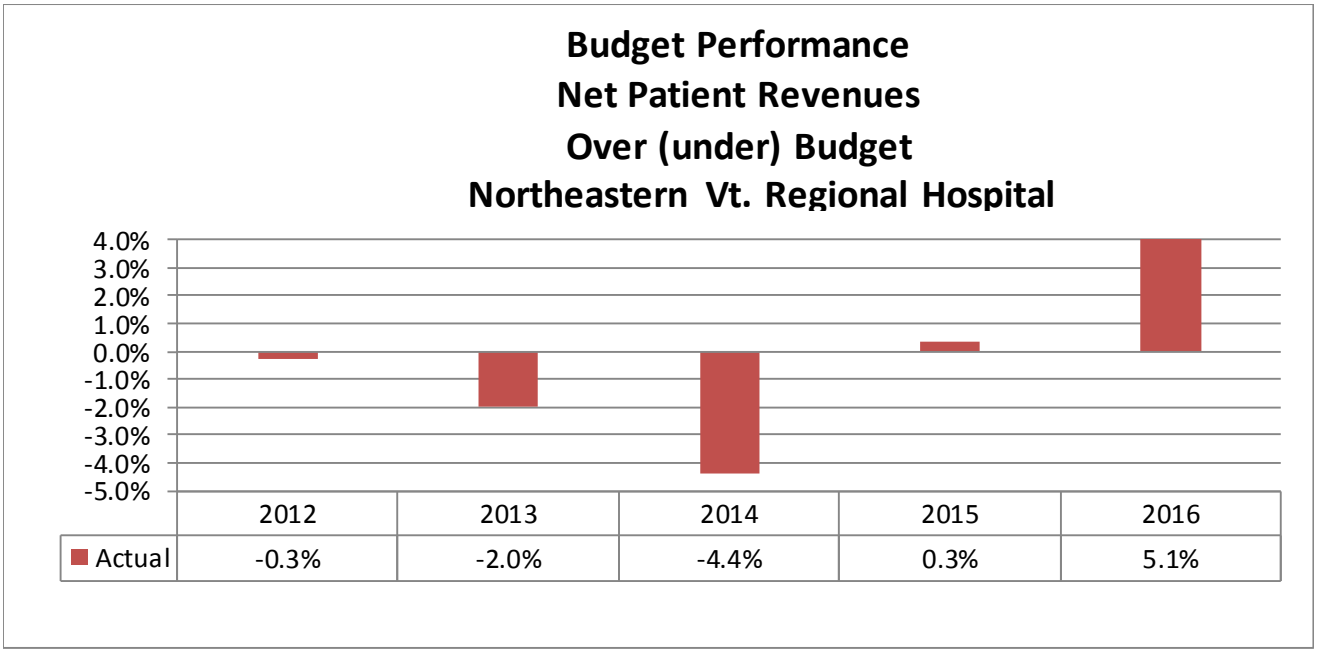
If the Board combines A & B, it could reduce the rate by 1.25% and inform the hospital that it must further reduce its rate in FY 2018. This would allow more of the surplus to be considered for setting prices/rates in 2018.

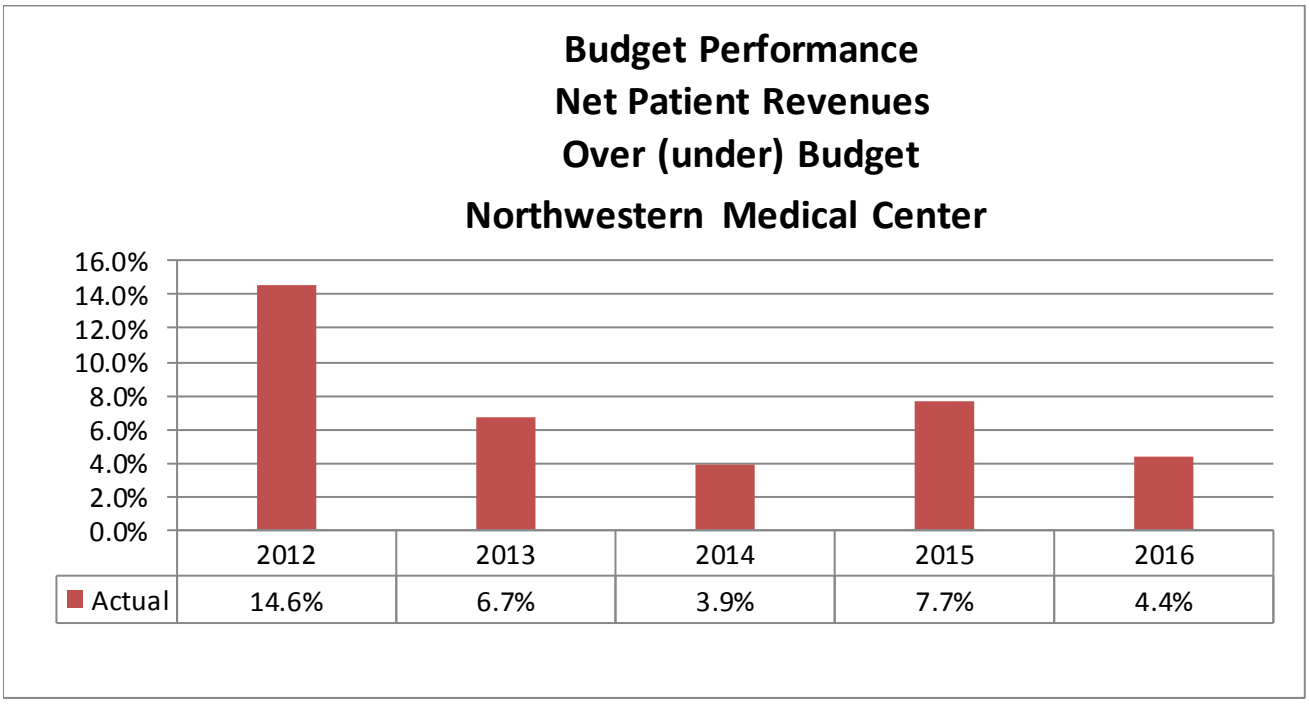
Option D

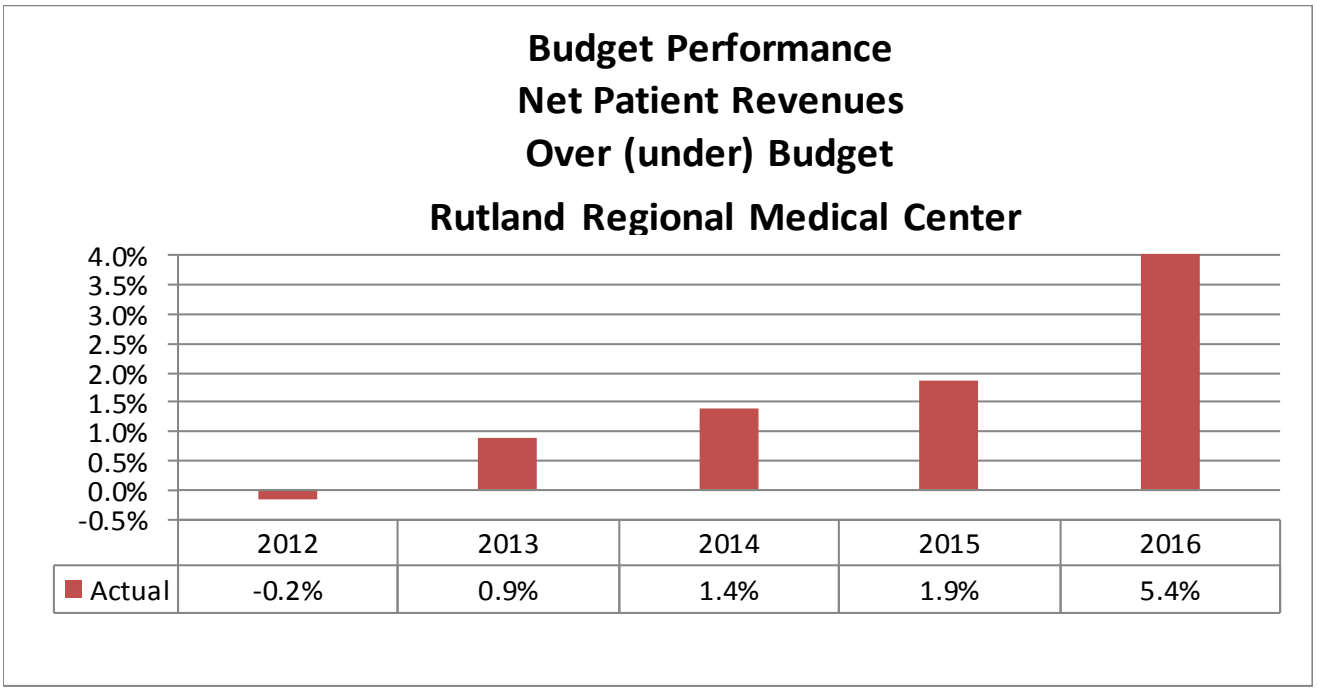
Not considered because the Board should take some kind of action.

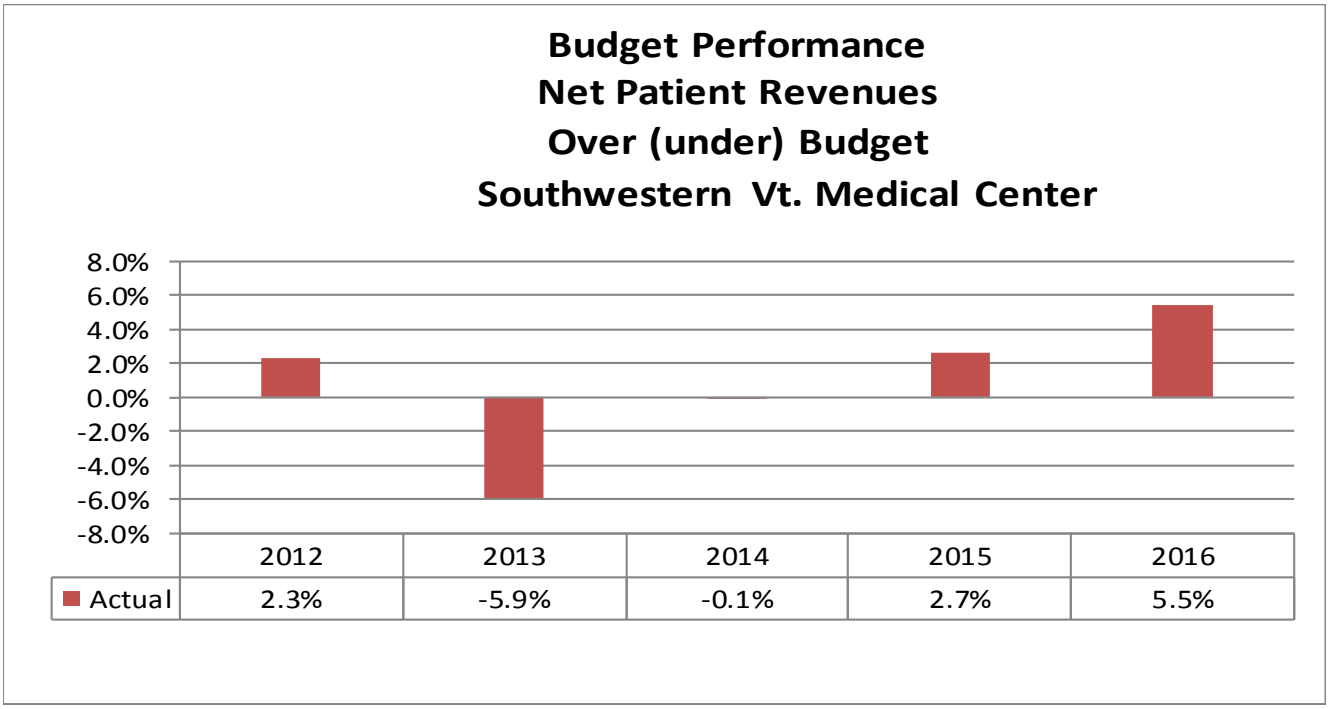
Vermont Community Hospitals

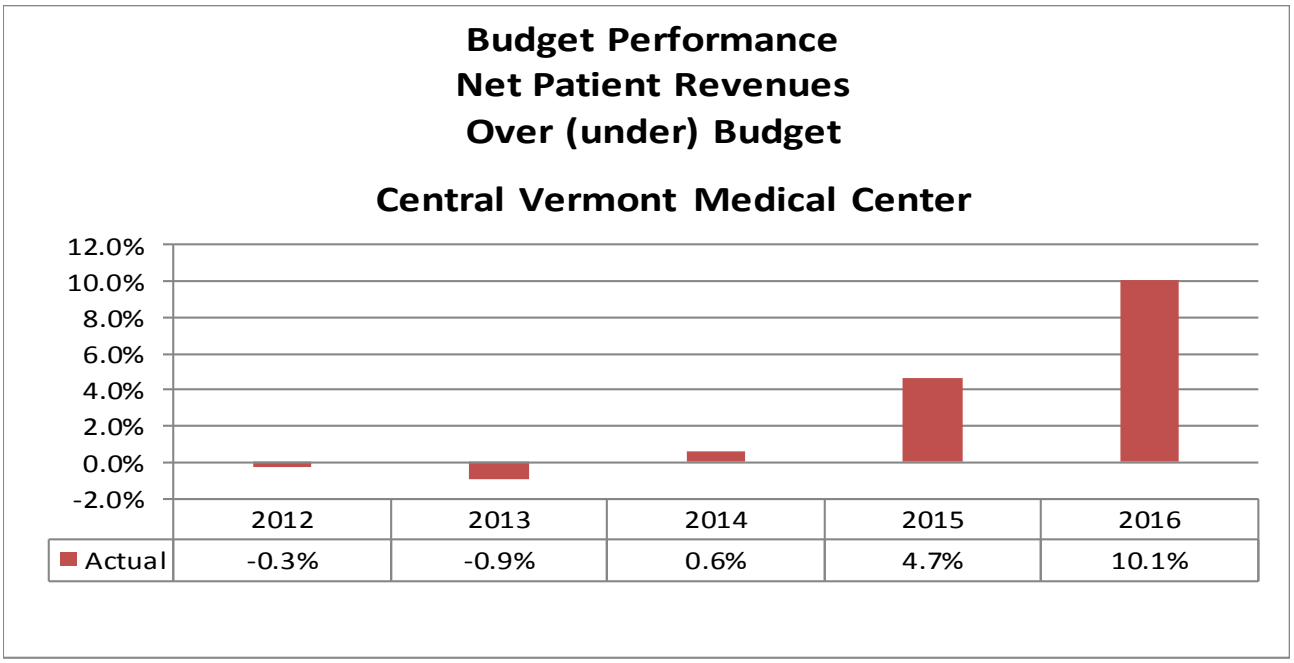
Actual 2016 operating results – Budget-to-Actual **4/12/2017**



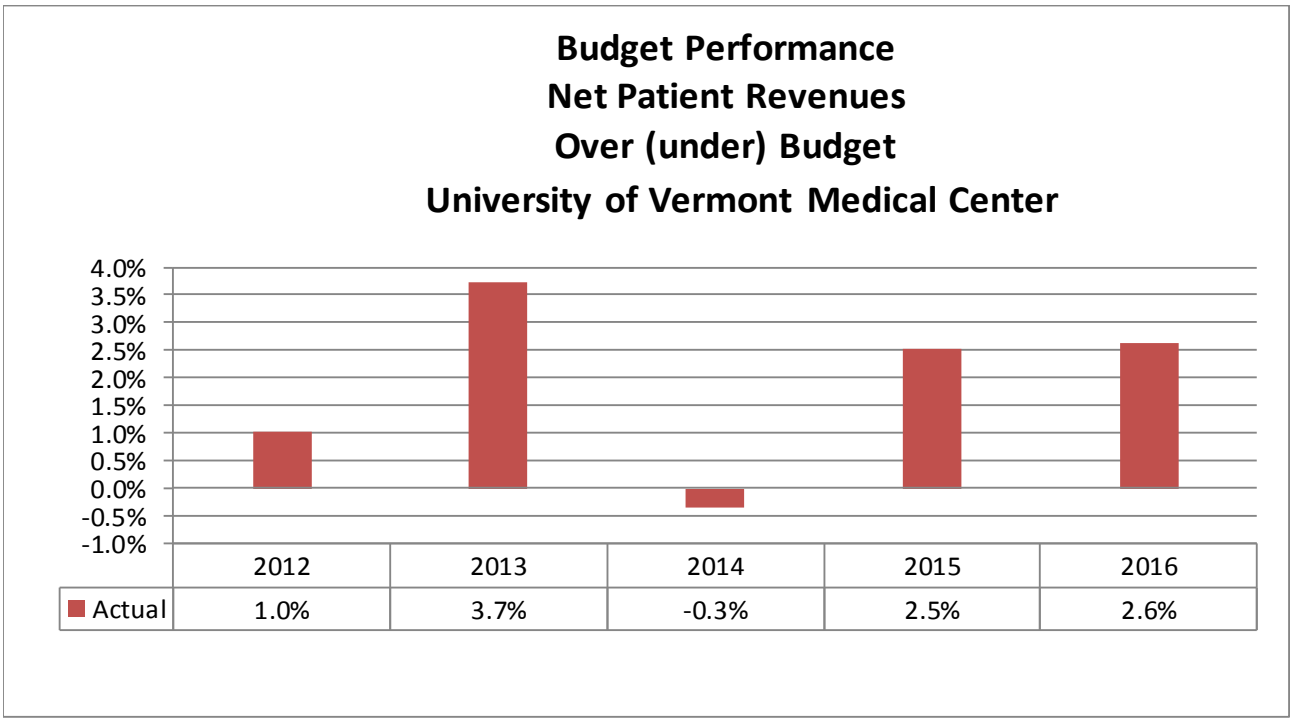



Budget Performance
Net Patient Revenues
Over (under) Budget
Rutland Regional Medical Center
4.0%
3.5%
3.0%
2.5%
2.0%
1.5%
1.0%
0.5%
0.0%
-0.5%
2012
2013
2014
2015
2016
Actual
-0.2%
0.9%
1.4%
1.9%
5.4%


Budget Performance
Net Patient Revenues
Over (under) Budget
Southwestern Vt. Medical Center
8.0%
6.0%
4.0%
2.0%
0.0%
-2.0%
-4.0%
-6.0%
-8.0%
2012
2013
2014
2015
2016
Actual
2.3%
-5.9%
-0.1%
2.7%
5.5%


Budget Performance
Net Patient Revenues
Over (under) Budget
Central Vermont Medical Center
12.0%
10.0%
8.0%
6.0%
4.0%
2.0%
0.0%
-2.0%
2012
2013
2014
2015
2016
Actual
-0.3%
-0.9%
0.6%
4.7%
10.1%

1212


Budget Performance
Net Patient Revenues
Over (under) Budget
University of Vermont Medical Center
4.0%
3.5%
3.0%
2.5%
2.0%
1.5%
1.0%
0.5%
0.0%
-0.5%
-1.0%
2012
2013
2014
2015
2016
Actual
1.0%
3.7%
-0.3%
2.5%
2.6%

Vermont Community Hospitals

Actual 2016 operating results – Budget-to-Actual **4/12/2017**

FY 2017 Budgets -- Results Through February

Net Patient Care Revenue	"Expected" BUD 17 YTD	ACT 17 YTD	Variance YTD Over (under) Budget	Last Year At This Time
SYSTEM	**$ 999,799,129**	**$ 994,540,416**	-0.5%	1.1%
Brattleboro	**$ 31,610,138**	**$ 30,836,418**	-2.4%	-2.8%
Central Vermont	**$ 79,360,281**	**$ 79,133,419**	-0.3%	6.8%
Copley	**$ 27,101,353**	**$ 28,207,608**	4.1%	1.9%
Gifford	**$ 23,896,238**	**$ 22,920,730**	-4.1%	-2.6%
Grace Cottage	**$ 7,945,290**	**$ 7,163,563**	-9.8%	-11.5%
Mount Ascutney	**$ 19,751,917**	**$ 19,182,545**	-2.9%	-3.4%
North Country	**$ 33,588,052**	**$ 32,098,733**	-4.4%	-2.2%
Northeastern	**$ 29,513,012**	**$ 30,934,755**	4.8%	1.7%
Northwestern	**$ 42,170,757**	**$ 41,797,998**	-0.9%	3.1%
Porter	**$ 31,480,365**	**$ 31,581,705**	0.3%	-2.6%
Rutland Regional	**$ 100,700,637**	**$ 101,152,660**	0.4%	6.5%
Southwestern	**$ 63,032,058**	**$ 60,959,445**	-3.3%	5.5%
Springfield	**$ 24,469,133**	**$ 21,609,545**	-11.7%	1.7%
University of Vermont MC	**$ 485,179,898**	**$ 486,961,292**	0.4%	-0.4%