



Economic Impact Analysis Virginia Department of Planning and Budget

12 VAC 5-410 –Regulations for Licensure of Hospitals in Virginia Virginia Department of Health January 3, 2005

The Department of Planning and Budget (DPB) has analyzed the economic impact of this proposed regulation in accordance with Section 2.2-4007.G of the Administrative Process Act and Executive Order Number 21 (02). Section 2.2-4007.G requires that such economic impact analyses include, but need not be limited to, the projected number of businesses or other entities to whom the regulation would apply, the identity of any localities and types of businesses or other entities particularly affected, the projected number of persons and employment positions to be affected, the projected costs to affected businesses or entities to implement or comply with the regulation, and the impact on the use and value of private property. The analysis presented below represents DPB's best estimate of these economic impacts.

Summary of the Proposed Regulation

The proposed change will add a definition for "rural hospital" to current regulations in order to prevent some Virginia hospitals from losing their rural designation for Medicare reimbursement purposes.

Estimated Economic Impact

Critical Access Hospitals (CAHs) receive cost-based Medicare reimbursements, which are higher than the prospective Medicare payments. By federal statute, CAH hospitals must be located in rural areas. Thus, the rural designation has significant revenue implications for CAH hospitals serving Medicare patients. The Federal Office of Management and Budget (OMB) reclassified 19 rural Virginia counties as Metropolitan Statistical Areas, effective October 1, 2004, based on the 2000 census. CAH Hospitals in reclassified counties currently face the possibility of losing their rural status and therefore their CAH designation if the county in which they are located is not classified as rural as of December 31, 2005. However, federal regulations (42 CFR 412.103 (a) (2)) allow these hospitals to maintain their rural designations provided they

are designated as a rural hospital by state law or regulation. Originally, this federal provision applied only to prospective payment hospitals and not to critical access hospitals. In August 2004, Center for Medicare and Medicaid services revised federal regulations (42 CFR 485.610 (b) (3)) to allow the critical access hospitals as well to maintain their rural designations provided they are designated as a rural hospital by state law or regulation. The purpose of this action is to add a definition for rural hospitals so that hospitals in affected counties including critical access hospitals could maintain their rural designation and continue to receive higher cost-based Medicare reimbursements.

According to Virginia Department of Health (VDH), only one critical access hospital is currently facing the possibility of losing its rural designation as a result of the OMB reclassification. Medicare patients make up approximately 66% of the 1,085 total patients served in 2003 at this hospital. Based on 2003 data, this hospital would lose approximately 26% of its Medicare revenues or approximately \$1.7 million if it were to lose its rural designation. This potential loss from Medicare payments represents approximately 12% of its total patient revenues, which is significant.¹ In fact, VDH believes that such a significant revenue loss could lead to the closure of this particular hospital. If a closure were to materialize, not only 711 Medicare patients, but also approximately 374 other patients would lose access to services offered by this hospital. Additionally, approximately 164 employment positions at this hospital would be lost. Thus, the proposed addition of the rural hospital definition is expected to produce economic benefits in terms of avoided loss of access to services and in terms of avoided loss of employment positions. These two main economic benefits could also provide other ancillary benefits such as improved productivity as a result of maintaining access to hospital services or avoided social costs as a result of maintaining employment positions. Furthermore, as Medicare is fully funded by the federal government, any loss of Medicare revenues is a net loss for the Virginia economy and is likely to result in a much larger negative impact through the economic multiplier process.

In addition to the definitive impact on one critical access hospital as discussed, the proposed change might also impact other hospitals receiving federal grants under the Small Rural Hospital Improvement Grant Program (SHIP). VDH notes that the agency responsible for

¹ This estimate is calculated based on the net patient revenue information provided by Virginia Health Information.

administering the CAH program, the Health Resources and Services Administration (HRSA) also is responsible for administering the SHIP program. The SHIP program provides about \$10,000 per SHIP hospital to be used exclusively for patient safety programs, Health Insurance Portability and Accountability Act compliance, and technical capacity development for the submission of electronic claims for prospective payment system payment. Thus, the proposed rural hospital definition could accommodate an additional 20 hospitals and allow them to continue to participate in the SHIP program. However, the possibility that the Center for Medicare and Medicaid might provide a similar option for the additional 20 hospitals is no more than a speculation at this time.

Businesses and Entities Affected

The proposed change is expected to affect only one critical access hospital. However, there is chance that an additional 20 small federal grant hospitals could be affected depending on the future regulatory actions of HRSA.

Localities Particularly Affected

The proposed regulations apply throughout the Commonwealth. However, the only hospital expected to be definitely affected is located in Pearisburg.

Projected Impact on Employment

The proposed change will help one critical access hospital to avoid significant Medicare revenue losses and consequently could avoid its closure. The number of full time equivalent positions in this hospital was 164 in 2003. Even though some of the employees could find jobs elsewhere if the hospital were closed, the net impact on employment would be positive.

Effects on the Use and Value of Private Property

The proposed regulations should not have an impact on the value and use of real property. There should be a positive impact on the asset value of the only hospital known to be affected as its Medicare revenues would be maintained at their current levels. In addition, there could be a positive impact on the asset value of an additional 20 Virginia small federal grant hospitals if HRSA revises its regulations as anticipated.