



Date: November 22, 2013

To: Chief Executive Officer
Chief Financial Officer
Managed Care Officer

From: Craig Becker

Subject: Implementation of TennCare Year 2 Rate Variation Recommendations

Attached please find background information related to the second year (Year 2) of THA board activities to address the extensive variation in reimbursement from TennCare MCOs that exists among hospitals. The board has been working with the Bureau of TennCare for three years to develop a proposal for reducing the variation in TennCare reimbursement to hospitals for the same or similar services. The state and THA engaged Aon Hewitt to provide actuarial support for the analyses and to ultimately develop a plan, approved by both the Bureau and the THA board, for reducing the variation. Aon was authorized to make minor modifications to the board recommended ranges to ensure the implementation would be budget neutral to TennCare.

The range of reimbursements recommended by the THA board are based on each hospital's individual Medicare rates excluding operating indirect medical education payments (IME) and pass through amounts. The analyses included hospital specific factors (DSH, wage index, etc.) for each hospital applicable to 2010 Medicare payments. Medicare amounts were determined using the Medicare inpatient and outpatient grouper and pricer tables in effect for the date of each claim.

The updated rate variation analysis, based on claims data from the MCOs covering the period September 2010 to August 2011 and paid through November 2011, provided the percentage of Medicare reimbursed by the MCOs for each hospital for routine and high-cost routine inpatient services, specialized inpatient services, and outpatient services. To calculate the percentage of Medicare reimbursed by TennCare MCOs, Aon compared the actual reimbursement from the MCO to the amount Medicare would have reimbursed based on the above definition.

As indicated in the accompanying background document, the recommendation has no impact on reimbursement for specialized services, defined as neonatal, cardiac surgery and other, including burns, multiple significant traumas, transplants and HIV related services. However, the board recommended that the ranges for future negotiations be set at the ranges that existed in the period September 2010 to August 2011 and paid through November 2011.

Based on the rate variation analysis, your hospital's routine inpatient and/or outpatient payments fell outside of the final budget neutral ranges agreed upon by the THA board and TennCare. As a result, TennCare, working through the MCOs, will be implementing rate adjustments for your facility. When these adjustments are complete, your facility's projected total reimbursement from TennCare MCOs should be adjusted according to the **attached chart**.

For a small number of hospitals the initial Medicare percentage(s) will vary from the figures provided in your Year 1 rate variation letter. This variance is due to updates to the rate variation model as discussed in the rate variation webinar of November 14 and does not adversely impact your rate adjustment.

For hospitals receiving positive adjustments, these adjustments will move your facility's total reimbursement from all MCOs as a percent of Medicare toward the rate variation model's budget neutral floors of **53.8%** of Medicare for Year 2 inpatient and **93.2%** of Medicare for Year 2 outpatient. For hospitals receiving negative adjustments, these adjustments will move your facility's total reimbursement from all MCOs as a percent of Medicare toward the rate variation model's budget neutral ceilings of **80%** of Medicare for Year 2 inpatient and **104%** of Medicare for Year 2 outpatient. Significant changes in utilization would impact the projected total reimbursement in the model. The model's projected impact assumes consistent utilization of inpatient and outpatient services.

Concurrently with your receiving this information, the MCOs also are being provided information on adjustments that they must make to increase a hospital's rates to the floor or decrease them to the ceiling. Because the ceilings and floors are based on total amounts reimbursed to your hospital from TennCare but payment rates can vary by MCO, the adjustments communicated to individual MCOs will likely be different from the average percentage movement toward the Medicare "floor" or "ceiling" for your facility. On the MCO side, that adjustment is proportionally spread across the MCOs where the current reimbursement amounts are above the ceiling or below the floor. The rate variation model prescribes the percentage changes in rates for each MCO that will result in the appropriate overall reimbursement percentage increase or decrease toward the floor or ceiling. The Bureau of TennCare will require the MCOs to verify that the changes being proposed in the contracts are consistent with the rate variation model.

In accordance with the agreement between TennCare and the THA board, contract changes should be implemented by the MCOs in an across-the-board rate change and should not be service specific. All Year Two rate changes should have an effective date of July 1, 2013.

The target for the completion of all contract amendments is the end of the First Quarter of 2014. No amendments will go into effect until amendments for all hospitals impacted rate variation are finalized.

The Bureau of TennCare will review all rate changes made by MCOs to ensure that the changes accurately reflect the required adjustments.

Any disagreements between the hospital and MCO about the rate changes should be sent to TennCare for resolution. Additional actuarial work may be required to settle disputes and this work would be funded jointly by THA and TennCare. All contract negotiations should be complete before the changes are implemented.

If you have questions or need additional information, please contact Mary Layne Van Cleave, mlvc@tha.com or David McClure, dmcclure@tha.com.

Attachment