May 25, 2016

LEGISLATIVE ANALYST'S OFFICE

LAO 75 YEARS OF SERVICE

State Fees on Hospitals. Federal Medi-Cal Matching Funds. Initiative Statutory and Constitutional Amendment.

Presented to:
Assembly Health Committee
Hon. Jim Wood, Chair
and
Senate Health Committee
Hon. Ed Hernandez, Chair

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LAO Role in Initiative Process

☑ Fiscal Analysis Prior to Signature Collection

- State law requires our office to work with the Department of Finance to prepare a joint impartial fiscal analysis of each initiative before it can be circulated for signatures. State law requires that this analysis provide an estimate of the measure's fiscal impact on state and local governments.
- The fiscal analysis must be submitted to the Attorney General within 50 calendar days from the initiative's submission date. A summary of the estimated fiscal impact is included on petitions that are circulated for signatures.

☑ Analyses After Measure Receives Sufficient Signatures to Qualify for the Ballot

- State law requires our office to provide impartial analyses of all statewide ballot propositions for the statewide voter information guide, including a description of the measure and its fiscal effects.
- We are currently in the process of preparing these materials.

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Summary

☑ Under current state law, the Hospital Quality Assurance Fee (hereafter referred to as "the fee")—charged to most private hospitals with most of the revenue used to pay for services in Medi-Cal—is scheduled to sunset on January 1, 2017. This measure makes the fee permanent and generally makes it harder for the Legislature to make changes to the fee.

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Background

- ***Medi-Cal Provides Health Care Benefits to Low-Income Californians.*** The Medi-Cal Program is California's Medicaid Program and it provides health care benefits to low-income Californians, such as families, children, and seniors, who meet certain eligibility requirements.

- ***Medi-Cal Costs Are Shared Between the State and Federal Governments.*** Currently, Medi-Cal provides health care benefits to over 13 million Californians with a total estimated budget of roughly $95 billion (about $24 billion General Fund) for 2015-16. The cost of the Medi-Cal program is shared between the state and the federal government. For most costs, the state and federal government each pay half of the costs. In some instances, such as for the Patient Protection and Affordable Care Act (ACA) optional expansion population, the federal government pays more of the costs than the state.

- ***Public and Private Hospitals Provide Care to People Enrolled in Medi-Cal.*** There are about 450 private and public general acute care hospitals (hereafter referred to as "hospitals") licensed in California that provide acute health care services such as emergency services, surgery, and outpatient care to Californians, including those enrolled in Medi-Cal. Public hospitals are owned and operated by public entities such as counties or the University of California. Private hospitals are owned and operated by private entities, which can be nonprofit or for-profit.

- ***State Charges a Fee on Certain Hospitals.*** Under state law, the state collects a fee from most private hospitals called the Hospital Quality Assurance Fee. The fee has been collected since 2009, extended three times, and under current law, will sunset on January 1, 2017.

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Background *(Continued)*

- ***Fee Results in State Savings.*** Twenty-four percent of the revenue raised by the fee creates a General Fund offset in Medi-Cal. This revenue is used to pay for children's health care services in Medi-Cal which would otherwise be a General Fund cost. In 2015-16, the fee is estimated to result in a General Fund offset of about $850 million.

- ***Fee Revenue Also Creates a Net Benefit for Hospital Industry.*** Fee revenue is also used to fund the state share of payment increases to public and private hospitals for providing Medi-Cal health care services. These payments leverage federal funds because the state and federal government share the cost of Medi-Cal health care services. Additionally, some of the money raised by the fee is used to provide grants in support of health care expenditures to certain public hospitals. The use of fee revenue to draw down federal funds results in an estimated net benefit to the hospital industry as a whole (after accounting for the amount of fees paid by private hospitals) of $3.5 billion in 2015-16. Of this industry-wide benefit, public hospitals receive an estimated benefit of $235 million in 2015-16.

- ***Any Fee Extension Must Be Approved by the Federal Government.*** Because some of the fee revenue is used to pay for Medi-Cal health care services, the federal government must approve any extension of the fee, whether the fee is extended in its current form or with a somewhat different structure.

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Proposal

☑ ***Makes Fee Permanent Unless Specified Circumstances Occur.*** The measure makes the fee permanent, and the measure amends the circumstances that would automatically trigger an end of the fee. These amended circumstances include where (1) the Legislature does not appropriate fee revenues within 30 days following enactment of the annual budget act, and (2) there are net *costs* to the General Fund from implementing the fee as a result of the courts' decision in a lawsuit related to the fee. Consistent with current state law, the measure includes other circumstances that would automatically end the fee, such as a denial of approval of the fee by the federal government.

☑ ***Measure Makes It Harder for Legislature to Change or End Fee.*** The measure makes changes to the requirements to end the fee and only allows the Legislature to make changes to the fee under certain conditions.

- ***Requires That Two-Thirds of Both Houses in the Legislature Vote to End the Fee.*** Under the measure, the Legislature may only end the fee if two-thirds of both houses in the Legislature vote to end the fee (only a majority vote is currently required).
- ***Only Allows the Legislature to Make Changes to Statute Implementing the Fee Under Certain Conditions.*** The Legislature may make changes to the statute implementing the fee only if certain conditions are met as described below.
  - ***Condition 1: Requires Two-Thirds Vote of Legislature.*** The Legislature can only make changes to the statute implementing the fee if two-thirds of both houses in the Legislature vote to make the changes. (Under current law, some changes would only require a majority vote.)

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- ***Condition 2: Changes Must Be for Certain Reasons to Avoid Requirement to Seek Voter Approval.*** The second condition that must be met for the Legislature to make changes to the statute implementing the fee without triggering a voter approval requirement is the changes must be made either to (1) obtain federal approval or (2) modify the methodology used to determine the level of the fee or the payments made to hospitals. (Under current law a vote of the people is not required to make changes to the fee.)

☑ ***Measure Exempts Fee Proceeds and Interest From Proposition 98 Calculation.*** The measure amends the Constitution to specify that the proceeds of the fee and all interest earned on such proceeds shall not be considered in calculating the Proposition 98 funding level required for schools.

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Fiscal Effects

☑ ***Measure Results in State Savings and Increased Funding for Local Governments.*** The most significant fiscal effect of this measure on state and local governments, assuming the fee structure under the measure is fully implementable, is state General Fund savings of about $1 billion (in the first full year of implementation). However, there is some uncertainty around the required federal approval of the fee extension given uncertainty about the application of new federal Medicaid managed care regulations to the fee structure.

- ***State Savings Resulting From Extending Hospital Fee.*** In the first full year of implementation, the measure could save the state about $1 billion General Fund. (The increase relative to the 2015-16 estimates for the current fee is a result of year-over-year growth that occurs on the natural rather than any particular impact of the measure.)

- ***Increased Funding for State and Local Governments Through Funding to Public Hospitals.*** The measure would also increase funding to state and local governments by providing grants and other payments to public hospitals. In the first full year of implementation, the measure would likely provide about $300 million to public hospitals.

☑ ***Fiscal Effects Could Change Based on Recently Released Federal Rule That May Require Changes to Fee.*** Some parts of the fee may conflict with a recently released federal rule that governs Medicaid managed care. These rules were released in April 2016 and the state is still working to understand whether changes to the fee are necessary to comply with the rule. If changes to the fee are required, the fiscal effects discussed above could change by an uncertain amount. The changes in the fiscal effects could potentially be positive or negative (relative to the fiscal effects when the new federal rule was not in place).