

March 1, 2018

The Honorable John Kavanagh  
Chairman, Joint Legislative Budget Committee  
1700 West Washington  
Phoenix, Arizona 85007

Dear Senator Kavanagh:

Pursuant to a footnote in the General Appropriation Act, the Arizona Health Care Cost Containment System (AHCCCS) is required to report to the Joint Legislative Budget Committee (JLBC) by March 1 annually “on the preliminary actuarial estimates of the capitation rate changes for the following fiscal year along with the reasons for the estimated changes.”

AHCCCS is Arizona’s single state Medicaid agency; however, the Arizona Medicaid system includes state agency subcontractors including the Department of Economic Security (DES) and the Department of Child Safety (DCS).

The coming year is going to be transformative for Arizona Medicaid. AHCCCS is currently engaged in the largest Request for Proposal (RFP) in state history for contracts beginning October 1, 2018 for the AHCCCS Complete Care (ACC) program. The ACC program will further AHCCCS’ strategic objective of integrating physical and behavioral health services for its members. A holistic approach to healthcare, the RFP is an important step in reducing fragmentation in the Medicaid delivery system by recognizing that wellness does not separate the mind from the body.

One aspect of the RFP is the elimination of a “carved-out” program for children with special health care needs via the Children’s Rehabilitative Services (CRS) program. Rather, children diagnosed with a CRS condition will have choice of any ACC Contractor in their geographic region which will all manage care for these members, including physical health care both related and unrelated to the CRS condition, as well as behavioral health care. As a result, DES and DCS will also be taking the first steps toward integration with regard to their members who qualify for CRS in that those specialized services will ultimately be managed through their programs.

The preliminary estimates contained in this letter address the capitation rates for Contract Year Ending (CYE) 2019 (October 1, 2018 through September 30, 2019, unless otherwise noted) for the following programs:

- AHCCCS Complete Care (ACC) (formerly Acute Care, CRS, and behavioral health services for the majority of Acute Care members managed through Regional Behavioral Health Authorities)
- Regional Behavioral Health Authorities (RBHAs)
- Arizona Long Term Care System (ALTCS)/Elderly and Physical Disability (EPD)

- ALTCS DES/Division of Developmental Disabilities (DDD) (July 1, 2018 through June 30, 2019)
- DCS/Comprehensive Medical and Dental Program (CMDP) (July 1, 2018 through June 30, 2019)

This preliminary review of capitation rates for contract year ending (CYE) 2019 allows for the following:

- Funding utilization increases and unit cost trends
- Provider rate increases for select providers if access to care analysis merits such increases, and other provider rate considerations

This letter is designed to provide policymakers with information to inform funding-related discussions during the legislative session, given that capitation rate calculations will occur during the late-spring and early summer months. For FY 2019, the recommendations in the Executive Budget and of the JLBC staff increase capitation rates by 1.25% (2% for ALTCS) and 3.50% respectively. Please note that Federal law does require that capitation rates be actuarially sound, meaning that all expected expenses must be covered by the rates.

Over the past nine years, AHCCCS capitation rates have grown by 10.5% in total, at an average annual rate of 1.25%. Nationally, the average Medicaid per enrollee cost has increased by 14.7% in total, at an average annual rate of 1.7%, and is projected to grow at an average annual rate of 4.7% through 2025. In comparison, per capita national health expenditures for all payers during this same period increased by 35.1%, at an average annual rate of 3.8%, and are projected to grow at an average annual rate of 4.8% through 2025.

It is clear AHCCCS has employed a variety of levers to keep growth in program spending low and far below national figures. AHCCCS continues to develop initiatives such as integration, value-based purchasing, and care coordination projects designed to reduce the overall growth in the cost of care for its members. Increasing pharmacy rebates have also offered program savings over the last several years; AHCCCS continues its efforts to negotiate rebates to the benefit of the state.

Competitive bidding on AHCCCS' managed care contracts has historically contributed to awarded capitation rates that were lower than would have been paid without bidding. In the two most recent competitive RFP cycles including Acute Care CYE 2014 and ALTCS/ EPD CYE 2018, bid capitation rates were 3.5% and 3% below, respectively, the rates developed by the actuaries (but still within the actuarially-sound rate ranges developed by those actuaries). The ACC RFP for CYE 2019 is not expected to produce a comparable level of savings due to recent limitations imposed by CMS.

Despite these positive trends and cost containment efforts, there are cost pressures that moving forward will need to be recognized in order to assure ongoing access to care for AHCCCS members. Broadly, AHCCCS has concerns about its ability to assure access to care without some recognition of increasing provider costs.

The issues that are outlined below will all be incorporated into the rates for October 1, 2018.

### **Utilization and Unit Cost Trends**

AHCCCS' actuaries have not had an opportunity to update the comprehensive review of historical utilization or unit cost trend data based on the most recent dates of service. System programming to extract recent data is in process and such a review shall commence this spring. The actuaries will ascertain how utilization and unit cost trends should impact capitation rates for CYE 2019 across all programs so that policy decisions can be finalized to develop the capitation rates in accordance with budgetary expectations. Please note that unit cost increases can occur for a variety of reasons, even when provider reimbursement levels are flat or decreasing. Unit cost trends increase when the mix of the services utilized by members shift to more costly services. Pharmacy costs also contribute to increasing trends as AHCCCS cannot influence gross pharmaceutical pricing. AHCCCS' actuaries have observed double-digit growth in the limited use of brand-name drug expenditures.

### **Provider Rates**

#### *Provider Rate Adjustments Due to Access to Care*

The AHCCCS Administration and its contracted Managed Care Organizations (MCOs) are responsible for ensuring an adequate network of providers to secure members' access to needed care. AHCCCS has extensive tools in place to monitor network adequacy among various provider types. As part of this process, AHCCCS conducts yearly reviews of how rate reductions, and conversely rate increases, impact access to care. Past studies have been published on the AHCCCS website, are made available for public comment, and can be found at:

<https://www.azahcccs.gov/PlansProviders/RatesAndBilling/FFS/> and at:  
<https://www.azahcccs.gov/AHCCCS/PublicNotices/#AccesstoCare>.

The provider reimbursement rate review considers, among other things, factors such as the economy and market trends (including employment trends and wage pressures for providers), access and network adequacy, and potential opportunities for efficiencies. AHCCCS will complete this access to care analysis to inform its provider rate decisions for CYE 2019.

In addition to these standard reviews, CMS has implemented heightened scrutiny on rate changes, including establishing additional reporting requirements regarding fee-for-service (FFS) rate changes and the implications of those changes on access to care. These requirements include both a periodic monitoring report as well as a specific analysis each time rates are changed. The analysis is required for access to care for primary care services, specialist services, behavioral health services, obstetrics and home health. Arizona must consider the availability of Medicaid providers, utilization of Medicaid services and the extent to which Medicaid beneficiaries' healthcare needs are fully met and demonstrate that Medicaid beneficiaries have access to healthcare that is similar to that of the general population. In accordance with this mandate regarding access to care reporting beginning in 2016, AHCCCS' first Monitoring Review Plan can be found on the AHCCCS website at: <https://www.azahcccs.gov/AHCCCS/PublicNotices/> under the Access Monitoring Review heading, with the 2017 publication found at: <https://www.azahcccs.gov/AHCCCS/PublicNotices/#AccesstoCare>

Below are specific areas of focus but ultimately the access to care analysis will further inform the need for rate changes.

*Pressures on Home and Community Based Services (HCBS) Rates*

Federal law and regulatory changes over the last several years have created compounding pressure on in-home care providers who are critical partners in AHCCCS' cost-saving HCBS model of care and for whom AHCCCS is the predominant source of revenue. These requirements include:

- the Affordable Care Act's "large employer" health insurance coverage mandate for employers with at least 50 full-time employees (or equivalent full- and part-time workers) and their dependents
- the Department of Labor's (DOL) home care final rule which extends minimum wage and overtime protections to home care workers (for weekly hours exceeding 40)
- the DOL ruling that travel time between multiple clients during a workday is considered hours worked under the Fair Labor Standards Act and must be paid and counted toward the 40-hour work week

In addition to these federally-driven rate impacts, the passage of Proposition 206, as well as Flagstaff's Proposition 414, has compounded previously-reported wage pressure and related challenges in recruiting HCBS providers. AHCCCS and DDD increased ALTCS provider rates effective January 1, 2017, July 1, 2017, and January 1, 2018, to address increased labor costs associated with the Propositions. In addition to these increased labor costs, wage compression is an additional challenge to retaining direct care providers, particularly when considering that HCBS providers already faced challenges in attracting individuals to work in direct care, which is more demanding both from a training and day-to-day work basis than jobs that pay comparable salaries. Effective January 1, 2019, the next increase to the minimum wage is required.

Laws 2017, Chapter 305 directed AHCCCS to conduct an analysis of "the impact of provider cost increases resulting from the enactment of Proposition 206...on the adequacy of the provider network for enrollees in the Arizona Long Term Care System." While the timing of the report did not allow for a comprehensive analysis of the impact of the Proposition, it is clear that providers are beginning to experience fiscal stress in response to the minimum wage increases. Specifically, providers noted challenges in regard to starting paraprofessional wages and increased staff turnover. As such, it will be critical that AHCCCS continue to monitor the impact of the Proposition, including, as suggested in the report, the development of additional reporting mechanisms which provide more definitive insight into the impact of minimum wage increases on this segment of the provider network. The report can be found on AHCCCS' website at the following link: <https://www.azahcccs.gov/shared/Downloads/Reporting/Prop206Report.pdf>

It is imperative that AHCCCS ensure continued availability of direct care services to offer members HCB services that meet the members' needs in the least restrictive and least costly settings.

### *Differentiated Provider Rates*

Value-Based Purchasing (VBP) is a cornerstone of AHCCCS' strategy to bend the upward trajectory of health care costs. AHCCCS continues to implement initiatives to leverage the managed care model toward value based health care systems where members' experience and population health are improved, per-capita health care cost is limited to the rate of general inflation through aligned incentives with managed care organization and provider partners, and there is a commitment to continuous quality improvement and learning. One such initiative which began in CYE 2017, and is modified annually including for CYE 2019, is increased payment rates for select AHCCCS-registered providers which meet established value based performance metrics requirements. For CYE 19, the types of providers which will tentatively be offered differentiated payments include:

- Hospitals
- Nursing facilities
- Integrated Clinics
- Physicians, Physician Assistants, and Registered Nurse Practitioners
- Behavioral health providers

The purpose of the differentiated payment is to distinguish providers which have committed to supporting designated actions that improve patients' care experience, improve members' health, and reduce cost of care growth.

### **Continuation of Mid-Year Funding**

#### *Annualize the Provider Rate Adjustment for Minimum Wage*

As described previously, AHCCCS adjusted provider rates to reflect the minimum wage increase effective January 1, 2018. Capitation rates have been amended for CYE 18 to include the additional funding needed by MCOs to pay these higher wages. When the CYE 18 cap rates were amended for this purpose, funding was only provided for half of the year for DDD, and three-quarters of the year for other AHCCCS programs. Annualizing the CYE 18 adjustment for minimum wage in the CYE 2019 capitation rates will require an estimated \$24.3 million.

#### *Annualize APR-DRG Rebased Rates*

AHCCCS rebased the rates for the inpatient hospital reimbursement methodology, the All Patient Refined Diagnosis Related Groups (APR-DRGs), in accordance with the "access to care" federal Medicaid provision at 42 USC 1396a(a)(30)(A), effective January 1, 2018. Capitation rates have been amended for CYE 18 to include the additional funding needed by MCOs to pay these rebased rates. When the CYE 18 cap rates were amended for this purpose, funding was only provided for half of the year for DDD and CMDP, and three-quarters of the year for other AHCCCS programs. Annualizing the CYE 18 adjustment for the APR-DRG rebase in the CYE 2019 capitation rates will require an estimated \$21 million.

#### *Annualize Newborn Screening Fees*

Law 2017, Chapter 339, increased fees for newborn screening; these increased costs are passed on to AHCCCS' MCOs. When the CYE 18 cap rates were amended for this purpose, funding was only provided for half of the year for DDD, and three-quarters of the year for other

AHCCCS programs. Annualizing the CYE 18 adjustment for the fees in the CYE 2019 capitation rates will require an estimated \$133,000.

*Annualize Medication Assisted Treatment (MAT) Funding*

In order to ensure member access to care for opioid use disorder (OUD) treatment, effective January 1, 2018, AHCCCS amended Acute Care and DDD contracts to require that Primary Care Practitioners (PCPs) be permitted to provide medication management of OUD when within their scope of practice. Annualizing the CYE 18 adjustment for MAT in the CYE 2019 capitation rates will require an estimated \$6.7 million.

**Other Changes**

*Health Insurer Fee*

Under the Affordable Care Act, beginning on January 1, 2014, health insurers including Medicaid health plans are required to pay a health insurer assessment due by September 30 each year. Assessments are based on each insurer's market share of the previous year's revenue as calculated by the US Treasury Department, and increase each year. Certain exceptions apply. AHCCCS intends to update capitation rates annually on a retroactive basis after the Treasury Department notifies each entity of its Health Insurer Fee payable – such notification will occur after the capitation rates for the new contract year are already established. For this reason, AHCCCS will not include these assessment payments in the annual cap rates until later in the calendar year. The Health Insurer Fee for 2018 will be reimbursed by AHCCCS in SFY 2019, and will impact AHCCCS' capitation rates by an estimated 1.45% inclusive of income taxes..

The actuarial analysis for the rate adjustments will continue throughout the spring, and will be based on the most up-to-date encounter data and contractor financial statements available. Mandated or court-ordered program changes that occur prior to July 1, 2018 or October 1, 2018 may result in changes to these estimates.

Please direct any questions regarding this letter to Shelli Silver at [shelli.silver@azahcccs.gov](mailto:shelli.silver@azahcccs.gov) or (602) 417-4647.

Sincerely,



Thomas J. Betlach  
Director

cc: The Honorable David Livingston, Arizona House of Representatives  
Richard Stavneak, Director, Joint Legislative Budget Committee  
Christina Corieri, Senior Policy Advisor, Arizona Governor's Office  
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