



Janice K. Brewer, Governor
Anthony D. Rodgers, Director

Our first care is your health care
ARIZONA HEALTH CARE COST CONTAINMENT SYSTEM

801 East Jefferson, Phoenix, AZ 85034
PO Box 25520, Phoenix, AZ 85002
Phone: 602 417 4000
www.azahcccs.gov

September 1, 2009

The Honorable Janice K. Brewer
Governor
State of Arizona
Capitol Tower
1700 West Washington
Phoenix, Arizona 85007

SUBJECT: Fiscal Year 2011 Budget Request

Dear Governor Brewer:

I am submitting the Fiscal Year (FY) 2011 Budget Request for the Arizona Health Care Cost Containment System (AHCCCS). This request represents an increase of \$564.0 million in General Fund (GF) and a decrease of \$29.3 million in Other Appropriated Funds for a total appropriated funds increase of \$534.7 million. Of the \$564.0 million increase in General Fund, \$206.9 million is attributed to reduced savings from the American Recovery and Reinvestment Act (ARRA) increased Federal Matching Assistance Percentage (FMAP) in FY 2011. The remaining increase of \$357.0 million consists of (unless otherwise indicated the following amounts are Pre-ARRA):

- 1) \$200.9 million increase attributed to member growth,
- 2) \$220.8 million increase attributed to medical inflation and utilization,
- 3) \$89.5 million decrease attributed to the projected increase in regular FMAP for FY 2011,
- 4) \$2.1 million increase attributed to requested administrative issues,
- 5) \$10.0 million increase attributed to other policy and technical changes, and
- 6) \$12.7 million increase requested to backfill potential tobacco funding shortfalls.

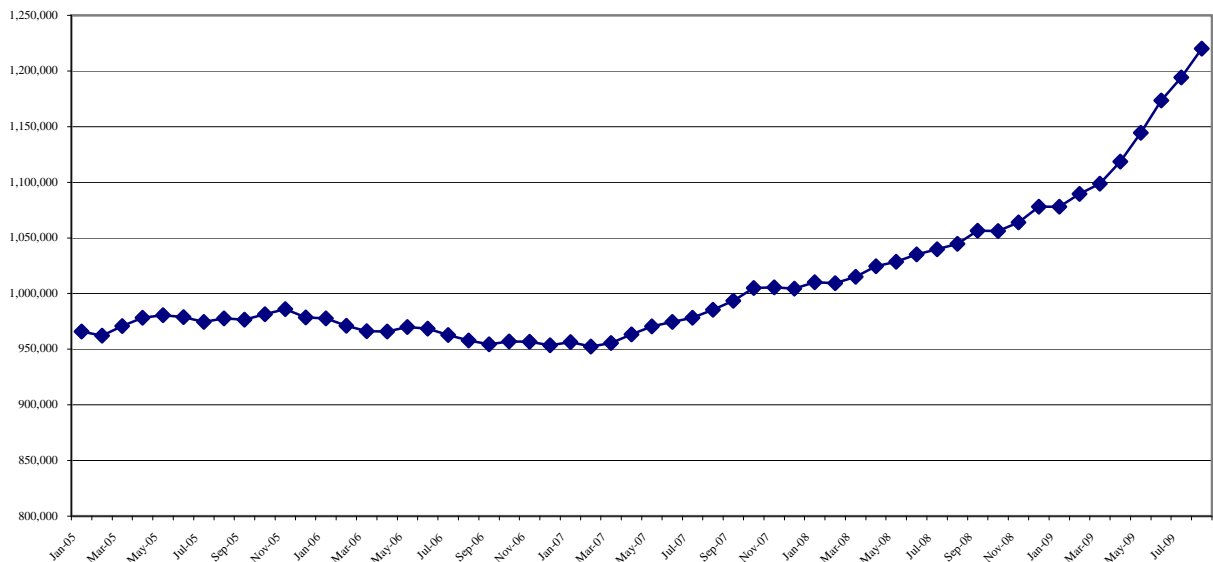
Overall, the AHCCCS Fiscal Year 2011 Total Fund Request, including only AHCCCS appropriations is \$8.392 billion, a \$1.325 billion increase over the FY 2010 Total Fund appropriation of \$7.067 billion.

The Agency has identified thirty-three (33) decision packages for your consideration. Eleven (11) of the decision packages are caseload or rate driven Title XIX requirements. Of the remaining decision packages, six (6) are administrative increases due to caseload growth, funding formulas, federal mandates, or contractual obligations; six (6) are Federal Matching rate or technical fund source issues, six (6) are decremental issues; and four (4) involve changes to non-appropriated funds only.

In FY 2009, the AHCCCS program experienced the most significant enrollment growth since the Proposition 204 expansion in calendar years 2001-2003. Since February 2007, AHCCCS enrollment has increased in 25 out of 30 months (see the graph on the following page) with the most significant growth coming in the last seven months. The August 2009 enrollment of

1,220,124 (this number does not include Federal Emergency Services members, Healthcare Group enrollment, or certain Medicare Cost Sharing populations) represents an all time record high. The statewide economic recession is resulting in higher unemployment and more Arizonans are requiring assistance with their health care needs. Most recent economic forecasts believe that the national recession may be coming to an end, however, most agree that Arizona's recovery will lag behind the rest of the nation due to the real estate market issues and other challenges. The growth rates built into the population forecasts in this budget submittal reflect the assumption that populations will continue to be impacted by the state's economic issues with some reduction in growth starting in April 2010.

AHCCCS Enrollment
January 2005 to August 2009
Excluding Federal Emergency Services



The following are some key items I would like to bring to your attention:

Pending Legislation on Budget Assumptions:

- Laws 2009, Chapter 12, Section 6 included a lump sum deferral associated with the rollover of a portion of the June 2010 acute care capitation payments. Pending budget reconciliation bill language will require AHCCCS to suspend one hundred percent of the June 2010 capitation payments for one month for acute care health care plans that have at least one hundred thousand members enrolled in May 2010 and fifty percent of the June 2010 capitation payments for one month for acute care health care plans that have less than one hundred thousand members enrolled in May 2010. The same pending legislation notwithstanding A.R.S §§ 35-342 and 44-1201 and sets interest on this rollover at a rate of five-tenths of one percent per year. For the purposes of FY 2011 budget development, it was assumed that another rollover will be passed next year that will move the majority of the June 2011 payments into FY 2012. Therefore, the Acute Base, Proposition 204, and KidsCare capitation budgets include only 12 payments in FY 2011 (June 2010 to May 2011). If another rollover is not passed, AHCCCS would require an additional \$409.7 million Total Fund (\$133.0 million General Fund) in FY 2011.

- Pending budget reconciliation bill language is expected to result in maintaining Contract Year (CY) 2010 hospital rates at current levels. The capitation rates used in this budget submittal assume that this language will be passed by October 1, 2009, the start of the new CY.
- Pending budget reconciliation bill language is expected to repeal the HIFA Parent program effective September 30, 2009. Even without this language, AHCCCS is moving forward to end this program since the budget contains no funding for this program after September 30, 2009.
- Additional items included in the pending budget reconciliation bill that AHCCCS requires in order to fully implement the FY 2010 budget include: FY 2010 Acute County contributions, FY 2010 Hospitalization and Medical Care County contributions, FY 2010 Disproportionate Share Hospital distributions, and the elimination of dentures as a covered service.

Member Month Growth:

- The Acute 1931 (TANF) and SOBRA populations grew an astounding 18.0% in FY 2009 (June over June member month growth). These populations represent approximately 72% of the AHCCCS Title XIX capitated membership. Over the last eight months, capitated enrollment for this population has grown by almost 104,000 members. The annual forecasted June over June member month growth for these populations is 12.5% in FY 2010 and 5.0% in FY 2011. The annual growth for FY 2010 is based on a sensitivity analysis comparing member month growth with the unemployment rate from the trough of the business cycle in January 2007 through April 2009. Based on this analysis and a projected 10% unemployment rate for Arizona before the end of 2009, approximately 8,000 members are added to this population per month through March 2010, with a 5% annualized growth rate applied thereafter. The growth in FY 2011 is closer to the historical average growth for these populations and reflects a gradual economic recovery in FY 2011.
- The Social Security Income (SSI) populations grew slowly but steadily at 2.6% in FY 2009 and are expected to grow 2.7% in FY 2010 and 2.4% in FY 2011 based on linear regressions. As the Arizona population continues to age, this population should continue to experience slow and steady growth.
- The Proposition 204 Title XIX Waiver Group (TWG) was the fastest growing population in FY 2009, growing by 27.5% from June 2008 to June 2009. This population consists primarily of childless adults. The significant growth over the past year is generally attributed to job losses, primarily in the construction industry due to the housing market decline. Laws 2008, Chapter 288, Section 3 adjusted the frequency of eligibility re-determinations for the TWG population from 12 months to 6 months. However, as a result of ARRA provisions, this change was reversed effective June 1, 2009. Using the same sensitivity analysis as the TANF/SOBRA population, this population is grown in FY 2010 by 2,500 members per month through March 2010, then 5% annualized

thereafter. Additionally, the change back to 12 month redeterminations is expected to add 10,062 member months per month until October 2009 and then 3,341 member months per month from October through December 2009. The resulting June over June projected growth rates are 40.2% for FY 2010 and 5.0% for FY 2011.

- The Children's Health Insurance Program enrollment has steadily declined in FY 2009. Over the last twelve months, enrollment has dropped by 15,528 members. Much of this drop is attributed to the recession, reducing family incomes resulting in children moving into Title XIX. Also, as part of the FY 2009 budget reductions, AHCCCS doubled the premiums for children between 150% and 200% FPL effective May 1, 2009. For the FY 2011 budget, member months were held flat at the July 2009 level until April 2010 when growth resumes at a 5% annualized rate.
- The ALTCS population grew 5.6% in FY 2009, marking the highest level of growth in recent years. With an increasing elderly population in Arizona and the increasing age demographics, AHCCCS is forecasting ALTCS to continue to grow at a rate of 5.1% for FY 2010 and 5.2% in FY 2011.

Provider Reimbursement

- As described earlier in the legislation section, the capitation rates used for CY 2010 assume that BRB language will pass that continues the hospital rate freeze and allows for up to 5% rate reductions for other services. Also for CY 2010, AHCCCS is reducing the risk contingency for health plans from 2% to 1%, reducing health plan administration by 5.88%, and requiring health plans not already at the lowest reinsurance deductible level to drop one level. The result of these actions and assumptions is an overall weighted rate decrease of 2.4% for Acute rates and a slight decrease of .4% for ALTCS rates versus the current rates. Note that this reflects the latest capitation rate estimates and that the CY 2010 rates are still being finalized, and are still subject to approval by the Centers for Medicare and Medicaid Services (CMS).
- This marks the second year in a row that hospital rates will be frozen and the FY 2009 budget reductions already included FFS rate reductions for certain providers and Capitation reductions effective May 1, 2009. Due to the reductions and freezes in reimbursement rates to health plans, hospitals, and other providers made during the past year and in recognition that the program must increase capitation rates to reflect changes in medical utilization, the FY 2011 budget includes rate increases of 5.0% across the board for both prior and prospective payments for CY 2011.

American Recovery and Reinvestment Act of 2009 (ARRA)

- ARRA provides states with a temporary increase in the state's FMAP from October 1, 2008 to December 31, 2010. The purpose of ARRA is to provide fiscal relief to states in a period of economic downturn; to protect and maintain state Medicaid programs by helping to limit cuts to provider payment rates, benefits, or services; and to prevent constrictions of income eligibility requirements. As a result, the ARRA increased FMAP comes with a series of conditions that states must meet to remain eligible. These

conditions include restrictions on changing eligibility standards, prompt payment requirements for certain providers, limitations on use of the additional funding, and equity savings retention requirements related to political subdivisions. A more comprehensive description of the entire ARRA impact is provided in the budget request under the ARRA tab.

- The ARRA increased FMAP savings span over three fiscal years. In accordance with the Governor’s Office of Strategic Planning and Budgeting guidance, the ARRA General Fund offset adjustments included in Laws 2009, Chapter 12, Section 49 were loaded into the FY 2010 expenditure plan and the additional General Fund required to backfill the ARRA savings in FY 2011 (FY 2010 includes 4 quarters of savings while FY 2011 only includes 2 quarters) is included as a decision package.
- A summary of the ARRA savings impact is shown in the table below.

ARIZONA HEALTH CARE COST CONTAINMENT SYSTEM					
ARRA INCREASED FMAP SAVINGS					
(DOLLARS IN THOUSANDS)					
	<u>FY09 Actual</u>	<u>FY10 Approp</u>	<u>FY10 Rebase</u>	<u>FY11 Request</u>	<u>FY11 Inc/(Dec).</u>
AHCCCS Appropriation					
General Fund Savings	320,238.7	581,861.7	563,425.6	374,916.8	(206,944.9)
County Fund Savings	51,358.0	72,422.0	89,234.9	39,954.7	(32,467.3)
Subtotal AHCCCS Appropriation	<u>371,596.7</u>	<u>654,283.7</u>	<u>652,660.5</u>	<u>414,871.5</u>	<u>(239,412.2)</u>
ADHS - Title XIX BHS & CRS	83,167.3	133,171.6	130,678.8	73,422.4	(59,749.2)
ADES - Title XIX LTC DD	57,812.9	100,644.6	99,728.3	52,169.0	(48,475.6)
Other State and Local Funding	-	-	4,119.9	1,038.6	1,038.6
Medicaid Total	<u>512,576.9</u>	<u>888,099.9</u>	<u>887,187.5</u>	<u>541,501.5</u>	<u>(346,598.4)</u>

Note: The FY09 Actuals above are from the AFIS 13th month reports and will not tie to the final CMS-64 claim for the June 30, 2009 quarter due to final reconciliations, the April-June quarter retro increase to the third unemployment tier, and prompt payment retro activity for the other state and local funding groups (which includes Local Education Authorities for School Based Services, ADOC for Title XIX eligible inmates, and select Arizona counties for Title XIX eligible inmates). The April-June retro increase and prompt pay retro activity equate to nearly \$22 million in additional funding (for all programs) and are included in the FY10 projection above.

- For FY 2010, AHCCCS is assuming a 75.93% increased ARRA FMAP rate for all four quarters. For FY 2011, AHCCCS is assuming a 75.93% increased ARRA FMAP for the July-September quarter and a 76.97% increased ARRA FMAP for the October-December quarter due to the estimated increase in regular FMAP effective October 1, 2010. The projections above assume that county contributions for the Acute Capitation and ALTCS programs are appropriately refunded based on methodologies negotiated with CMS. The currently pending FY 2010 budget bills do not yet include language to refund the

counties their portion of the FY 2010 savings, therefore, this language is required in future sessions along with the FY 2011 refund language.

- Additionally, ARRA includes billions of dollars to aid in the development of a robust information technology (IT) infrastructure for healthcare and to assist providers and other entities in adopting and using health IT. AHCCCS, using funding from Medicaid Transformation grants, has been a state leader for the expanded use of Electronic Health Records (EHR) as part of the Medicaid Health Information Exchange (HIE). This budget includes a request for \$53 million in non-appropriated federal grant pass-through expenditure authority for Arizona providers that may be eligible for Medicaid Incentive payment funding.

Other Issues

- AHCCCS is very cognizant of the State's budget shortfall in FY 2010 and the potential for an additional shortfall in FY 2011. Therefore, it was prudent in the submission of administrative decision packages for FY 2011. AHCCCS is submitting a trio of issues related to critical Information Technology and Program Integrity efforts. The IT issues deal primarily with increased network security to further secure Protected Health Information from malicious activity. Additionally, the Office of Program Integrity (OPI) is seeking additional investigative staff to process fraud and abuse cases. Pending budget legislation includes language requiring the Agency to continue to consider best available technologies in detecting fraud. To that end, the Agency issued a Request For Information on what fraud investigative tools may be available that are not currently in use by AHCCCS that may potentially increase the effectiveness of the AHCCCS program integrity efforts. AHCCCS is currently reviewing the RFI responses and may issue one or more RFP. Current staffing levels are not sufficient to deal with the current caseload, let alone any increase in the number of cases due to new technology.
- Healthcare Group continues to comply with the provisions enacted by Laws 2008, Chapter 288. This budget indicates a declining HCG enrollment through the end of calendar 2010, then a stable population with minor increases for the rest of SFY 2011. As of May 31, 2009, HCG continues to carry \$13.6 million in reconciliation liability from prior years. Therefore, for FY 2011, HCG requests a \$5,000,000 General Fund subsidy in order to accelerate the pay down of this liability.
- Funding from tobacco sources represents over 19% of the post-ARRA AHCCCS state match for Acute care programs in FY 2010. In FY 2009, revenue collections for the three tobacco tax funded accounts (Proposition 204 Protection, Medically Needy, and Emergency Health Services) were \$25.9 million or 14.5% less than originally appropriated and \$10.5 million or 6.4% less than the adjusted appropriations of Laws 2009, First Special Session, Chapter 1. The Children's Health Insurance Program Reauthorization Act of 2009 (CHIPRA) (PL-111-3) increased the federal tax on tobacco products by approximately \$0.61 per unit. This tax increase, along with the success of smoking cessation programs, makes it very likely that revenues will fall short of the allocations in FY 2010 and FY 2011. This budget requests \$12,712,400 in additional

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General Fund to backfill the estimated shortfall in FY 2011. The shortfall in FY 2010 is an even greater \$28.1 million as the forecast assumes approximately 18 months of continuing decreases in revenues before collections return to a more normal level in FY 2011.

AHCCCS will re-evaluate this budget submittal prior to November 2009 and may refine the request based on additional expenditure data and caseload trends.

Sincerely,

A handwritten signature in cursive script that reads "Anthony D. Rodgers". The signature is written in black ink and is positioned above the printed name and title.

Anthony D. Rodgers

Director