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Memorandum

Date: September 13, 2018

To: Paul Parker, Director, Health Care Facilities Planning and Development, Maryland Health Care Commission

From: Katie Wunderlich, Executive Director
Gerard J. Schmith, Principal Deputy Director, Hospital Rate Setting, HSCRC

Subject: Request for Exemption from Certificate of Need Review Conversion of University of Maryland Laurel Regional Hospital to a Freestanding Medical Facility

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Overview

University of Maryland Laurel Regional Hospital ("the Hospital," or "Laurel Regional") has requested an exemption from Certificate of Need review for the conversion of its general acute hospital to a freestanding medical facility ("FMF") that has its rates regulated by the Health Services Cost Review Commission ("HSCRC"). The Maryland Health Care Commission ("MHCC") has requested that the HSCRC evaluate the services, in addition to the emergency services, that it will regulate at the FMF. MHCC has also requested that HSCRC review and comment on the feasibility analyses provided by the Hospital.

Background

Project Description

UM Capital Regional Health hospitals, formerly the Dimensions Health System, which affiliated with the University of Maryland Medical System ("UMMS") on September 1, 2017, are undertaking a comprehensive modernization plan that includes construction of a replacement facility for Prince George's Hospital Center ("PGHC") and replacement of Laurel Regional with a new FMF. The new FMF will consist of emergency and observation services in addition to outpatient surgery, outpatient psychiatric services, wound care, and supporting ancillary services.

In July 2018, the HSCRC staff met to discuss the plan for converting Laurel Regional to a FMF. A two-phased conversion is proposed. In the initial phase, on or about October 1, 2018, inpatient rehabilitation services and inpatient chronic services will be relocated from Laurel Regional to PGHC. UMMS filed a partial rate application on August 2, 2018 requesting that the current approved rates for these services be

moved from Laurel Regional's rate order to PGHC's rate order. On or about January 1, 2019, the remaining inpatient medical-surgical, intensive care, and psychiatric services will also be relocated from Laurel Regional to PGHC. Since both facilities have rates for these services, PGHC will not need a new rate center, but it will need to adjust its rates to blend these and supporting ancillary services into its facility rates, while maintaining compliance with the overall global revenue limits. The application also requested combining the two facilities' global revenue limits to facilitate the transition. The HSCRC approved the rate application on September 12, 2018, subject to ensuring that volume reductions at Laurel Regional, not shifting to PGHC, would have a revenue reduction applied of no less than fifty percent (consistent with previous discussions with UMMS). The HSCRC also furth er noted that the Laurel Regional and PGHC project is unique and should not be considered a precedent for future conversions or consolidations, where additional savings would be expected.

Upon completion of the service relocation, Laurel Regional will become an FMF. At that time, its services will be billed as a part of PGHC, under the PGHC provider number. The existing physical plant will be converted to function as a freestanding medical facility, using the existing emergency department facilities, patient rooms for observation, surgical facilities for outpatient surgery, diagnostic imaging facilities, and space for the provision of outpatient behavioral health services and wound care.

At a site adjacent to the existing Hospital, Phase 2 will involve construction of a new physical plant with 24 emergency department rooms, ten observation rooms, a two-operating room ambulatory surgical facility operating under the FMF license, and the other outpatient services provided in Phase 1. Phase 2 is estimated to cost $53.1 million, with $38.1 million funded through debt and $14.5 million funded through a State grant.

Determination Requirements

COMAR 10.24.19, contains two requirements for acceptance of the filed request by MHCC that require action by HSCRC. The first requirement [COMAR 10.24.19.04C(3)(c)(v)] is that, "The applicants receive a determination from HSCRC, issued pursuant to COMAR 10.37.10.07-2D, regarding each outpatient service to be provided at the proposed FMF for which the applicants seek rate regulation." The second requirement [COMAR 10.24.19.04C(3)(c)(vi)] is that, "The applicants receive approved rates from HSCRC for each rate-regulated outpatient service at the proposed freestanding medical facility." The proposed FMF is seeking rate-regulated status for outpatient services beyond the standard emergency and observation services specifically authorized by statute for freestanding medical facilities. In addition to these two services, the proposed FMF is asking for rate regulation of charges for:

1. Ambulatory surgery services;
2. Associated diagnostic and other clinical ancillary services required to support the emergency, observation, and ambulatory surgery services;
3. Partial hospitalization/intensive outpatient behavioral health program services; and,
4. Wound care program services, including hyperbaric oxygen therapy.

Legislation provided flexibility to the HSCRC to make such a determination in order to optimize the services that would be provided at a FMF. For example, facilities in rural areas may have additional services to provide healthcare access, including access to uninsured individuals that might not otherwise be readily available. Other specific circumstances could be considered in determining efficiency, effectiveness and access when evaluating any additional regulated services to provide at a FMF.

Analysis

HSCRC staff met with UMMS representatives and reviewed MHCC documents regarding the rationale for providing each service, in addition to emergency services, in the regulated setting. The HSCRC already regulates diagnostic services that are performed as part of the emergency services provided. Including wound care can support effective follow-up of emergency care to avoid infections, improve recovery and avoid emergency department visits or inpatient hospitalizations. The wound care program can also support other preventive efforts in the service area. Staff understands that partial hospitalization for outpatient psychiatric patients was requested by community representatives. With the All-Payer and Total Cost of Care Model focus on improving community behavioral health, this service request appears consistent with Model goals. Ambulatory surgery, in general, is available in both regulated and unregulated sites. However, UMMS representatives argued that access, particularly for Medicaid patients and higher risk outpatients, would be improved through this service offering. With the emergency back-up and 24-hour observation provided through the FMF, patients with chronic conditions and higher risk factors can be treated. MedPAC, Medicare's Payment Advisory Commission, recognizes that lower severity of patients, as well as a lower proportion of Medicaid patients, are treated in freestanding ambulatory surgery centers (See March 2018 MedPAC Report to Congress, Chapter 5).

Because the severity level of patients coming to Laurel Regional's new surgery center will be higher, HSCRC staff expects to establish rates at the new Laurel Regional facility that are higher than unregulated freestanding ambulatory surgical facilities, but lower than hospitals. The capital and overhead costs of Laurel Regional's new surgery suites in the FMF should be competitive with freestanding competitors. While the HSCRC plans to apply existing hospital rates to the Laurel facility during the transition to an FMF once the new facility is constructed, UMMS will need to file a rate application to establish the rates in the new facility. Staff expects to establish rates for emergency, observation, wound care, and related ancillary services that are consistent with other hospital and FMF center rates. Staff will evaluate the outpatient psychiatric services relative to other outpatient hospital programs. Lastly, staff will require that the rates for the outpatient surgery service be lower than acute hospital rates.

UMMS has submitted financial projections incorporating outpatient surgery rates lower than hospital rate, but higher than freestanding counterparts. The rates provided by UMMS are estimated using Medicare Ambulatory Surgery Center fee schedules, plus an add-on to estimate FMF rate levels. On top of the estimated FMF rate staff added a severity increase. HSCRC staff used MedPAC estimates of severity level differences between hospital and FMFs to evaluate the potential add-on for severity. Finally, there will be an add-on to rates for the markup for payer differential and uncompensated care, as well as any assessments (e.g., Medicaid deficit assessment or Medicaid averted bad debt assessment) that are applicable to the rates of the FMF. At least six months before occupancy of the new medical center facility, UMMS should file a rate determination with the HSCRC, including documentation regarding market rates. UMMS can derive these market rates from sources such as Truven Market Scan, the MHCC All-Payer claims data base, or other market data. These figures can be increased for the severity adjustment, mark-up and assessments to set the surgery rates. The remaining rates will be established consistent with existing HSCRC processes.

The projections submitted by UMMS show that in the first three years of operation of the new facility can reach positive cash flows, while experiencing an operating loss when including depreciation. Over time, as capital costs are absorbed, operating results should strengthen.

Summary of Staff Findings

HSCRC staff reviewed the scope of additional services and financial projections provided by UMMS for the Laurel Regional FMF. UMMS provided its rationale for additional services, which appears reasonable to HSCRC staff, so long as the surgery services are operated at rates comparable to freestanding ambulatory surgical facilities after adjustment for severity levels, uncompensated care and payer differential and any assessments. It will be the responsibility of UMMS to operate an efficient and effective FMF with lower outpatient surgery rates. UMMS has presented financial projections that show positive cash flow by the end of the third year of operation at the new facility. Until the new physical plant for the FMF is built (estimated to be in 28 months), HSCRC will continue to set rates consistent with current hospital rate levels. When the new facility opens, HSCRC will set new rates for the FMF.

CC: Ben Steffen