

Healthcare Association of Hawaii



Financial Trends of Hawaii's Hospitals, Nursing Facilities, Home Care and Hospice Providers

November 2007

Prepared by:

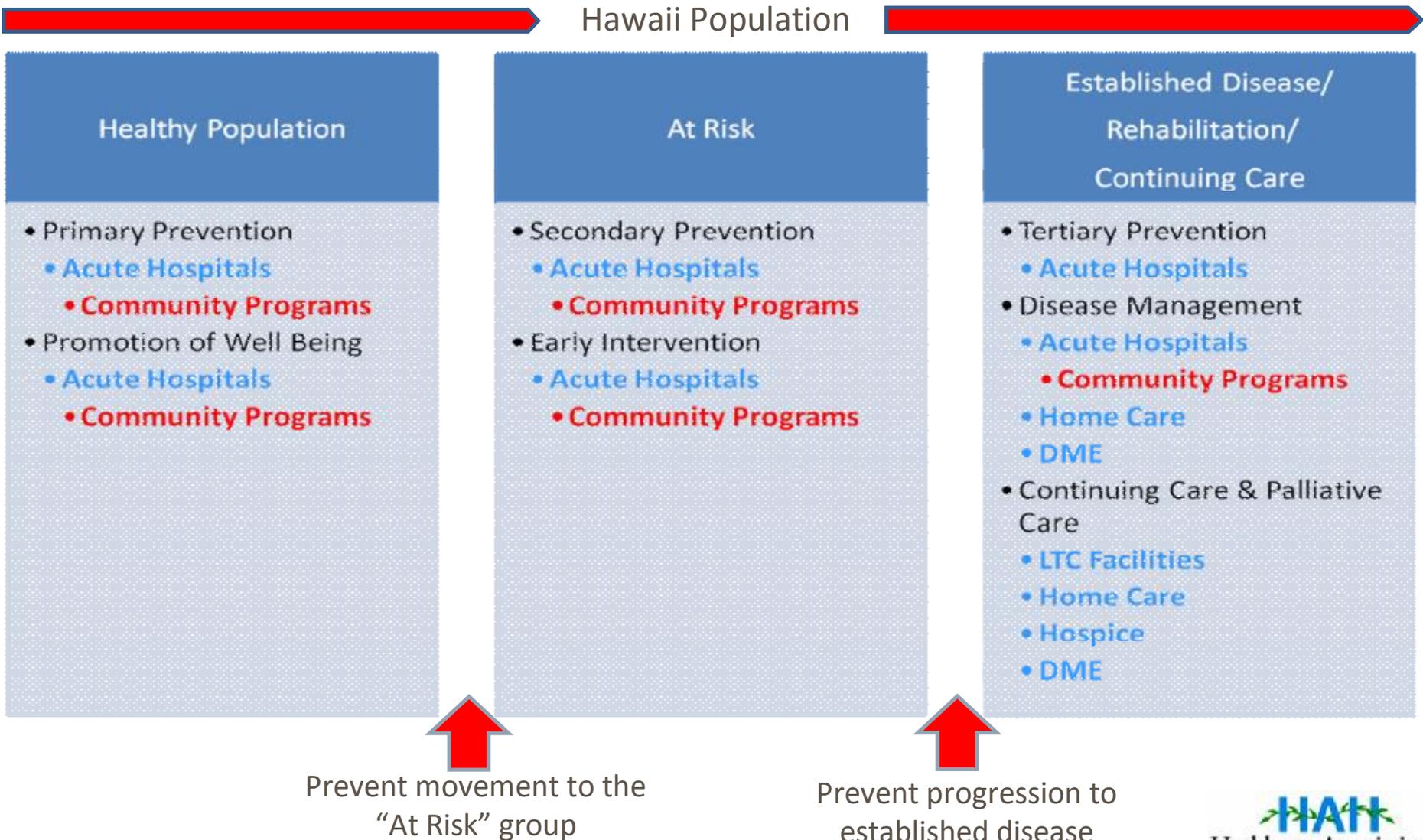
 **ERNST & YOUNG**
Quality In Everything We Do

and

 **HAWAII HEALTH
INFORMATION CORPORATION**
Hawaii's source of healthcare data

Healthcare Continuum

HAH member organizations provide services across the continuum of care to meet Hawaii's health needs.



Healthcare has an Impact on Everyone

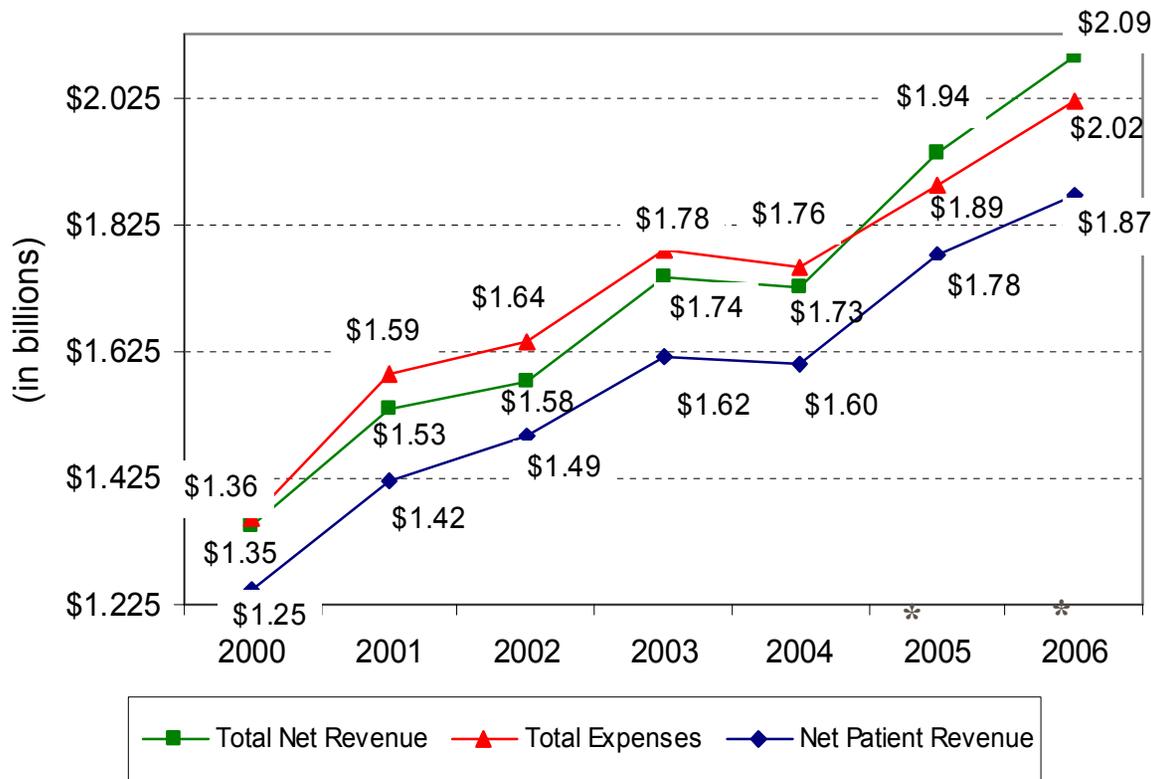
Everyone is impacted as an employee, a supplier or a patient/consumer of services

- Healthcare industry is still in financial crisis
 - Financial losses
 - Payments from government payors continue to be less than costs
 - Rising costs
- If the financial situation continues, the following may be impacted
 - Access to care and services
 - Ability to finance new medical equipment
 - Ability to attract and retain personnel (nurses, therapists, physicians, etc.)
 - Ability to provide care to uninsured
- Healthcare is a significant and necessary part of Hawaii's economy
 - 4th largest private industry
 - Major employer
 - Trickle down effect on all aspects of economy

Hawaii Hospital Financial Data

Since payments received for services by Hawaii's hospitals do not cover expenses, hospitals are forced to rely on other sources of income

Hawaii Hospital Financial Data



* - The increase in the 2005 and 2006 total net revenue was primarily from the larger hospitals and due to non-patient amounts including decreases in pension liability and increases in investment income

- Expenses exceeded net patient revenues for Hawaii's hospitals since 2000
- Although in recent years total revenue has exceeded expenses, the cumulative loss for 7 years is \$80,000,000
- Hospitals need help to cover expenses from other income such as:
 - Operating income from cafeteria and parking which increases cost for workers and visitors
 - Nonoperating revenues including interest income which requires significant investments

Financial Condition Improvement Efforts

Hospitals have implemented cost control and efficiency measures. These necessary measures can have a significant impact on access to care and the condition of the facilities.

- Consolidation of services into fewer locations (i.e. closing of clinics)
- Discontinuation or sale of unprofitable service lines
- Administrative staff reductions and minimal wage increases
- Reduced administrative office space
- Sale of real property and other businesses not directly related to patient care
- Deferred maintenance to facilities
- While acute care facilities have spent more than \$100,000,000 over the past five years on new information system applications and computer upgrades, other information systems that could potentially improve efficiencies have been delayed due to lack of capital
- Implemented energy conservation projects
- Negotiated increased reimbursements with private payors
- Reduced patient length of stay
- Developed new pharmacy formulary

Payments to Hawaii Hospitals

Hawaii's overall payment as a percentage of costs is the lowest in the United States

- Hawaii payments are primarily from Medicare, Medicaid, commercial payors (HMSA, UHA, HMAA, etc.) and others (Workers' Compensation, No-Fault, etc.)
- Medicare and Medicaid do not pay for the full cost of hospital services provided to beneficiaries in most states
 - Over 50% of all inpatients hospitalizations are covered by Medicare or Medicaid/Quest
 - 2006 Medicare losses for hospitals were approximately \$181,200,000
 - 2006 Medicaid/Quest losses for hospitals were approximately \$63,500,000
- In many states, private insurance covers the shortfall from the government payors

**Calendar Year 2006
Percent of Costs Paid by:**

	<u>Medicare</u>	<u>Medicaid/ Quest</u>	<u>Commercial and Other</u>	<u>Overall</u>
Hawaii	79.77 %	80.02 %	111.24 %	92.39 %
Lowest Overall State	66.65 %	32.93 %	101.80 %	92.39 %
Average for US	80.36 %	75.30 %	124.89 %	104.32 %
Highest Overall State	101.03 %	105.46 %	145.94 %	115.62 %

Costs of Trauma Care

Trauma cost exceeded payment by \$29.5 million in FY2005

- Payment for trauma services does not cover the cost of the patient care provided (excess of cost over payment is \$11,500,000 in FY2005)
- Hospital staff is paid to be on call for trauma care (cost was \$6,200,000 in FY2005). There is no payment for this.
- Physicians, are paid to be on call for trauma care even when there are no trauma cases at the time (cost was \$11,800,000 in FY2005). There is no payment for this.
- Specialized trauma equipment and drugs must be purchased and maintained
- Specialized training must be provided to employees
- Cost of having physicians as medical staff is high even if not specifically for trauma

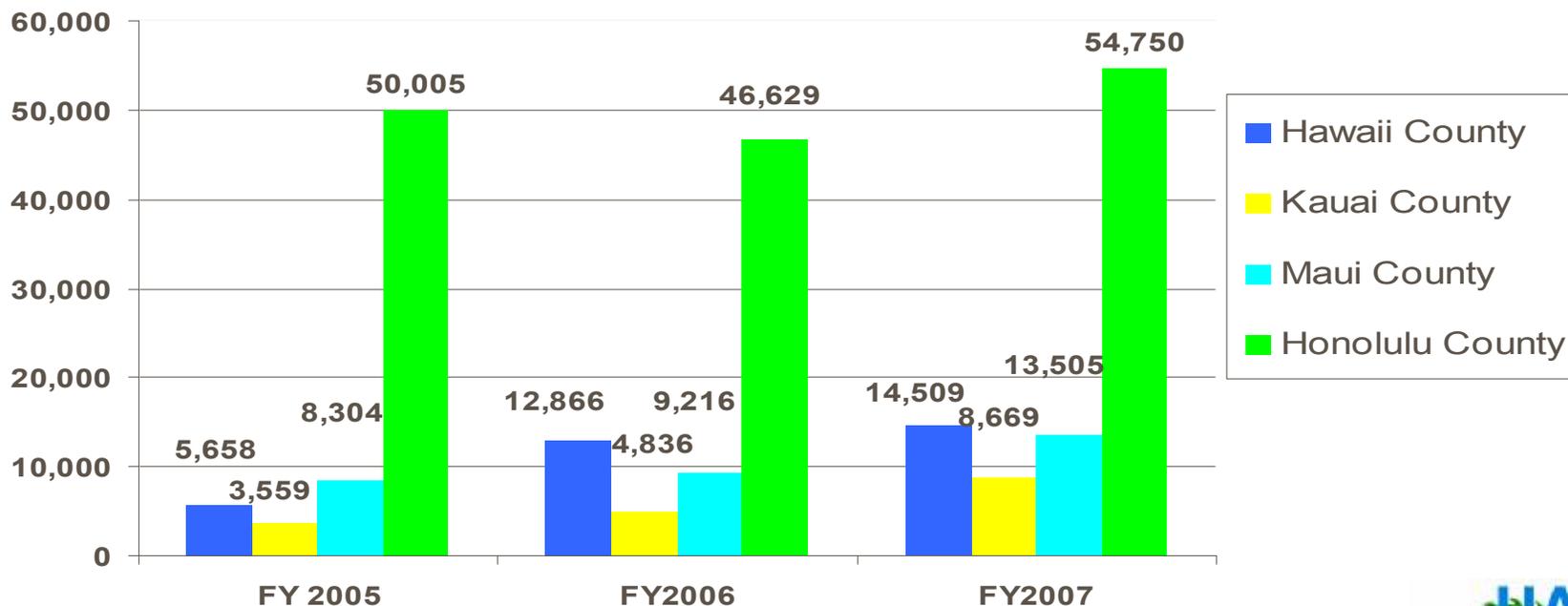
Source: As reported by 21 acute care facilities

Waitlisted Patients

Patients who are deemed medically ready for discharge from acute care services but cannot be discharged and, therefore, must remain in the higher cost hospital setting

- Waitlisted Medicare patient days are not reimbursed separately from the DRG payment for the acute care stay
- Waitlisted Medicaid patient days are reimbursed at approximately 20% to 30% of cost
- Estimated uncompensated costs for waitlisted patients for FY2006 is between \$80,000,000 to \$95,000,000. Additional analysis is being performed by the Waitlist Task Force, which is studying the waitlist issue in Hawaii.

Estimated Waitlisted Days by County



Source: HAH, As Filed Cost Reports, Medicaid Correspondence

Long Term Care Losses

Medicaid payments do not cover the cost to care for residents in nursing facilities

- Medicaid payments to nursing facilities did not cover costs by \$11.09 per day in 2005 for a shortfall of \$11,000,000 for all Medicaid nursing facility days
- Medicaid payments to nursing facilities did not cover costs by \$11.14 per day in 2006 for a shortfall of \$11,000,000 for all Medicaid nursing facility days
- Medicaid is a significant payor of services for the nursing facilities in Hawaii

Source: American Health Care Association, A Report on Shortfalls in Medicaid Funding for Nursing Home Care, June 2006 and September 2007

Long Term Care, Home Care and Hospice

Long Term Care (LTC), Home Care and Hospice face similar issues as the hospitals

<u>Issue</u>	<u>Consequence</u>	<u>Acute</u>	<u>Long Term Care</u>	<u>Home Health</u>	<u>Hospice</u>	
Employee Shortages	<ul style="list-style-type: none"> ■ Reduced capacity ■ Increased costs for temporary personnel 	}	√	√	√	√
Rising Wages	<ul style="list-style-type: none"> ■ Increased costs ■ Increased competition for workers 	}	√	√	√	√
Drug Costs increased an averaged of 7.5% each year from 1994 to 2006	<ul style="list-style-type: none"> ■ Increased costs to providers ■ Patients may be noncompliant with prescribed medication therapy 	}	√	√	√	√
Shortage of LTC Beds and Other Care Options	<ul style="list-style-type: none"> ■ Waitlisted patients in acute care 		√	√		

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<u>Issue</u>	<u>Consequence</u>	<u>Acute</u>	<u>Long Term Care</u>	<u>Home Health</u>	<u>Hospice</u>
Government payments do not cover costs	<ul style="list-style-type: none"> ■ Lose money on every governmental patient 	√	√	√	
Discontinuation of Additional Medicaid Capital Payments for New LTC Facilities	<ul style="list-style-type: none"> ■ Fewer new facilities are built although the population over age 65 is increasing 	√	√		
Medicare Inflation Updates Less than Full Market Basket	<ul style="list-style-type: none"> ■ Expenses increase faster than reimbursement 			√	
Increase in Gasoline Costs	<ul style="list-style-type: none"> ■ 49% increase in the per mile reimbursement since 2000 ■ More expensive to make visits to patients in remote locations 			√	√

Medicaid Impact

Medicaid payment issues have a significant impact on the State as Medicaid patients represent approximately 80% of nursing facility days and 8% of acute care days

- In 2006, Medicaid spent \$769 million in Hawaii on acute care (including outpatient and prescription drugs) and \$332 million on long term care
- There are four major components or programs that could impact providers
 - QUEST Expansion
 - Medicaid DSH
 - State Children's Health Insurance Program (SCHIP)
 - Going Home Plus

QUEST Expansion

- Quest Expansion will move the aged, blind and disabled (ABD) population to the managed care program from a fee for service program
- Providers will negotiate payment for services with the health plans similar to QUEST plans
- The impact on the providers has not been determined as it will depend on the negotiated payment with the health plans
- The expected date of implementation is November 2008

Medicaid Impact

Medicaid DSH

- Prior to the implementation of QUEST, disproportionate share hospital (DSH) payments from Medicaid averaged \$34 million a year
- Hawaii and Tennessee are the only states that do not receive DSH payments as a regular part of the Medicaid payments
- Payments that may be received if DSH is reinstated are unlikely to reach the historical \$34 million level

SCHIP

- Program focuses on providing health benefits to uninsured children
- In 2006, 22,031 children enrolled in SCHIP in Hawaii for total expenditures of \$19.3 million (\$13.7 million Federal and \$5.6 million State)
- In 2006, 19,636 children (18 years and younger) were uninsured
- Federal matching percentage for SCHIP is currently (Federal FY2008) 69.55% thus, 70 cents out of every dollar spent on SCHIP in Hawaii, is paid by the Federal government
- Each child enrolled in SCHIP reduces the uninsured population
- Uninsured tend to use expensive emergency room services and wait longer to obtain care resulting in higher charges that may lead to increases to bad debt and charity care
- SCHIP has not been approved by Congress past Federal FY2007

Source: State Health Facts, Kaiser Family Foundation, CMS and the Federal Register,
November 30, 2006

Community Benefit

Hospitals provide many services that benefit the community

Requirements for Community Benefit

- The IRS has Community Benefit Standards that must be met by hospitals to maintain tax-exempt status
- A survey by the IRS showed an average of \$14 million in uncompensated care costs per hospital in the U.S. with smaller hospitals experiencing approximately \$3 million and larger hospitals experiencing approximately \$27 million

Examples of Community Benefit

- Health Promotion and Wellness Programs
- Disease Management Programs
- Adult Foster Family and Day Care services
- Free inpatient and outpatient services to those who cannot or do not pay (Charity Care and Bad Debt)
- Training and education opportunities for medical residents and interns
- Caring for patients who no longer need acute care but have no other place to go (waitlisted patients)
- Maintaining availability of trauma services 24/7, although they are only needed periodically
- Maintaining emergency services 24/7 in all hospitals

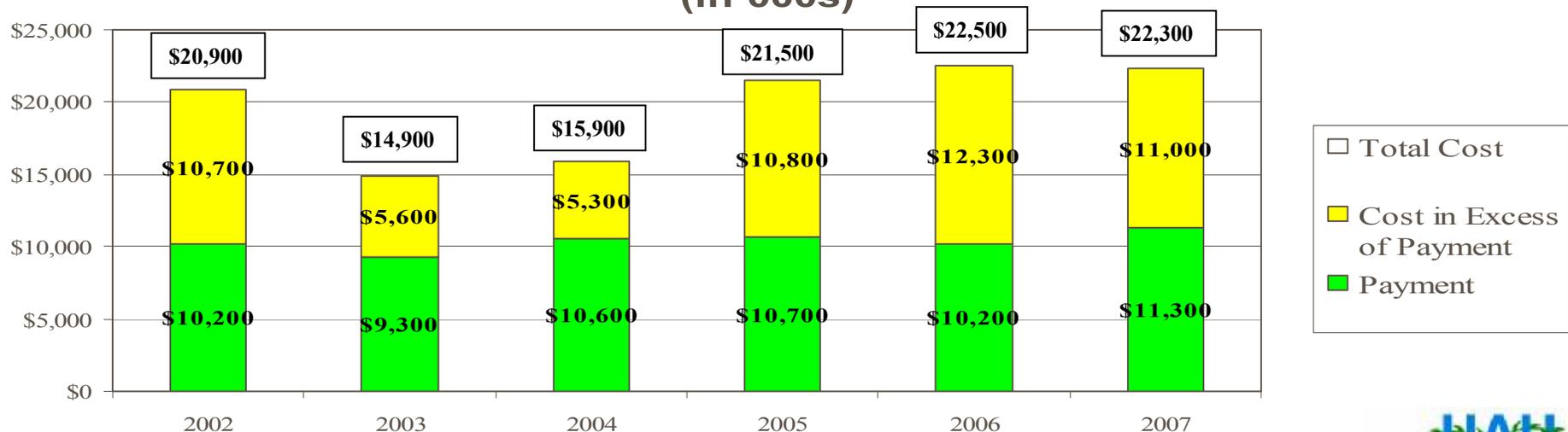
Source: Community Benefit Information from Non-Profit Hospitals: Lessons Learned from the 2006 IRS Compliance Check Questionnaire, AHA, Nov. 2006

Community Programs

Hospitals provide medical and social services with no or partial payment received

- Examples include health promotion, disease management programs, services for the elderly and adolescents, counseling services and outpatient clinics for the underserved and uninsured
- Medicare and Medicaid do not pay for most of these programs
- State and federal funds received through appropriations and grants are minimal
- Six year total program cost is \$118,000,000 with only \$62,300,000 received in payment. Total unfunded (net) cost is \$55,700,000
- Average annual unfunded cost from 2002 to 2007 is \$9,300,000

Community Programs
(in 000s)



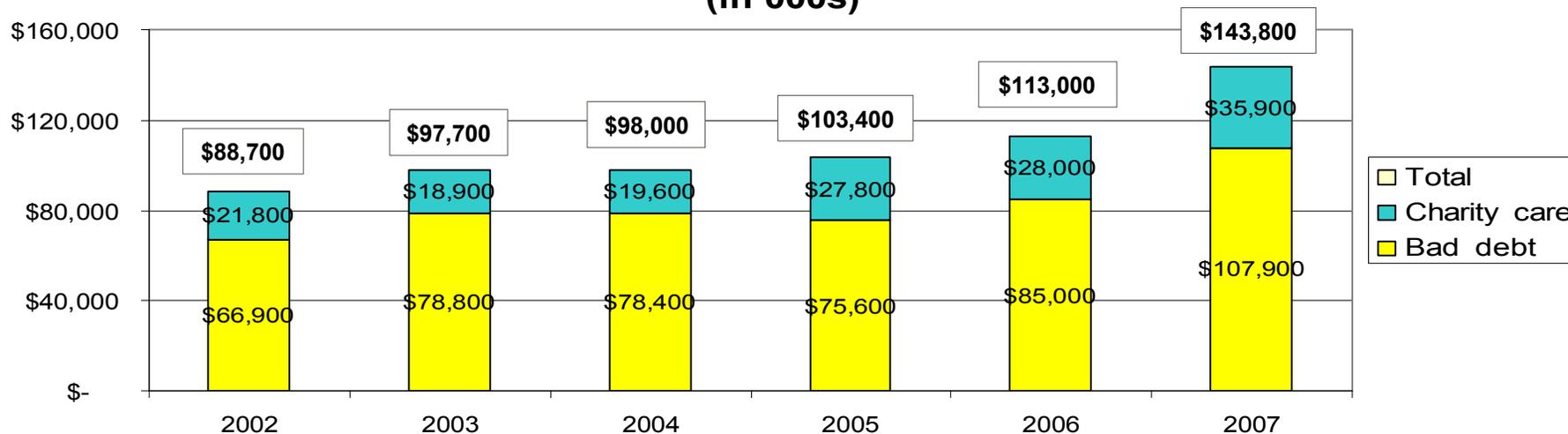
Source: Information provided by *five* hospitals and *one* nursing facility

Charity Care and Bad Debt

Total uncollected payments increased an average of \$11,000,000 annually from 2002 to 2007

- Six year total for Bad Debt and Charity Care is \$644,000,000 with an average yearly Bad Debt and Charity Care amount of \$107,000,000
- Services provided to those without the ability to pay result in bad debt or charity care
 - Bad debt is incurred when the amount due from a patient cannot be collected (services are provided with partial or no payments received)
 - Charity care is incurred when the hospital never expected to collect payment from the patient (services are provided at no charge to patient)
- Despite a decreasing unemployment rate, bad debt and charity care have been increasing since 2001
- Not all that are employed are insured even with employer-based insurance

Charity Care and Bad Debt
(in 000s)



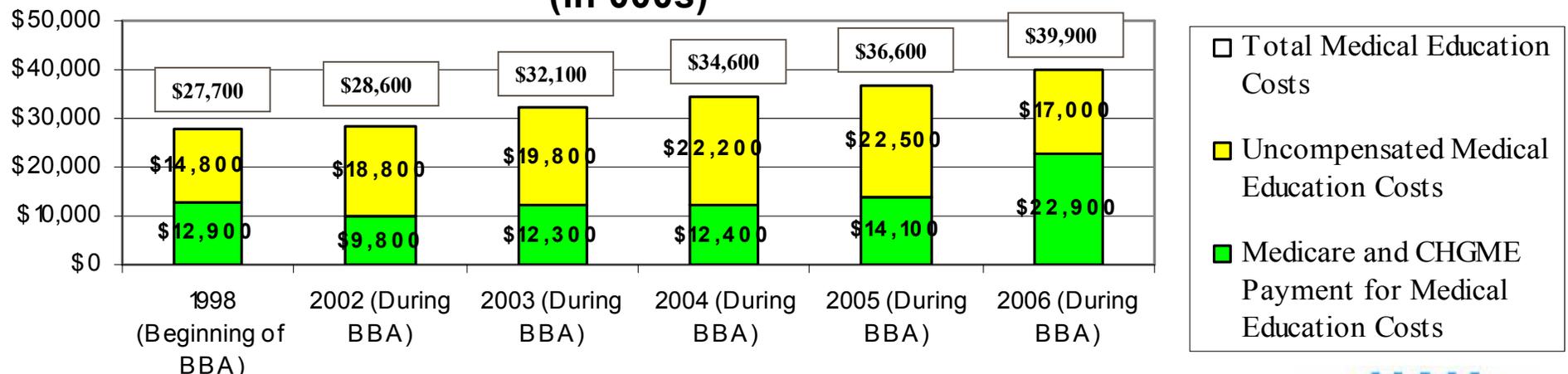
Source: Bad Debt and Charity Care information provided by 28 hospitals and 9 nursing facilities.
Unemployment data from US Dept. of Labor, Bureau of Labor Statistics

Medical Education

The payment received does not cover the cost for training interns and residents

- Seven hospitals have teaching programs (interns and residents) to support the University of Hawaii's School of Medicine and medical research
- This training is essential to the UH School of Medicine and to help alleviate the physician shortage in Hawaii
- Medicare, the major source of payments for intern and resident programs, reduced payments due to the Balanced Budget Act (BBA)
- A federal program was established to provide additional payment to children's hospitals for medical education (CHGME program)
- Hospitals need to shift funds from other uses to provide medical education
- The five year (2002 to 2006) total uncompensated Medical Education Costs are \$100,300,000 and the annual average is \$20,100,000

Medical Education in Hawaii
(in 000s)



Source: Teaching hospitals as-filed cost reports

Community Benefit and Uncompensated Care Costs

The cumulative financial effect of the Community Benefit provided by Hawaii's hospitals and nursing facilities is a significant loss for providers

- Average for Medical Education, Community Programs and Bad Debt and Charity Care over 5 years is \$129,200,000 annually
- Unfunded amounts incurred by the hospitals and nursing facilities for community support increase each year
- New issues are being identified and quantified as they increase in significance such as:
 - Trauma Care
 - Waitlist Patients

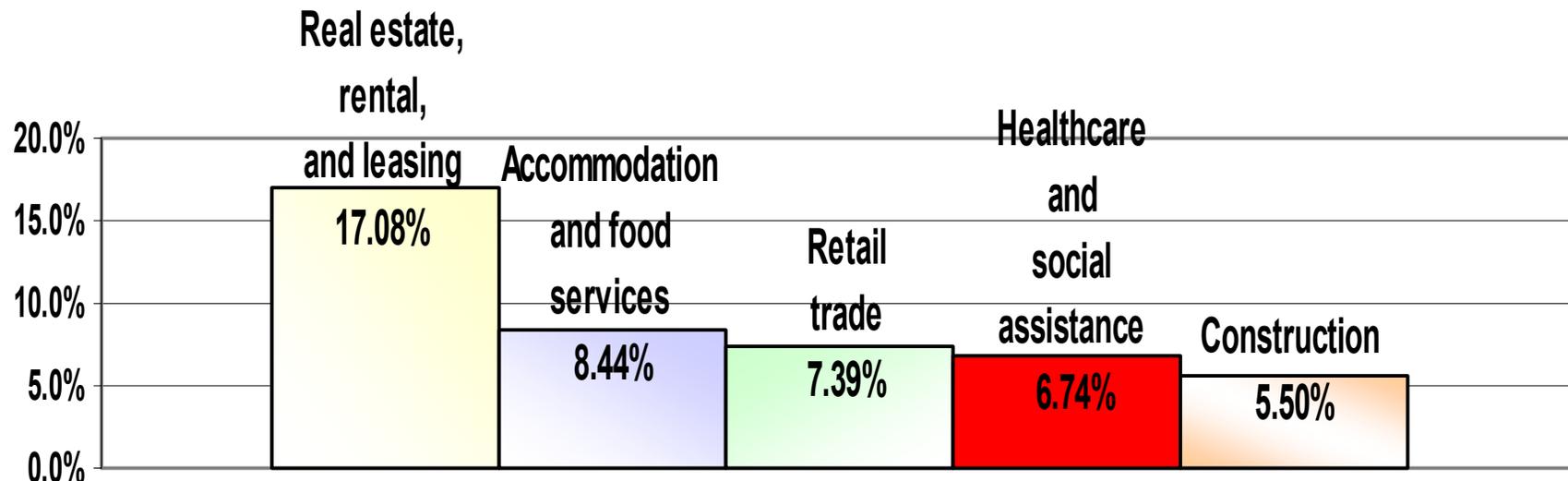
Unfunded Costs	2002	2003	2004	2005	2006	Total
Medical Education	\$ 18,800,000	\$ 19,800,000	\$ 22,200,000	\$ 22,500,000	\$ 17,000,000	\$ 100,300,000
Community Programs	10,700,000	5,600,000	5,300,000	10,800,000	12,300,000	\$ 44,700,000
Bad Debt/Charity Care	\$ 88,700,000	\$ 97,700,000	\$ 98,000,000	\$ 103,400,000	\$ 113,000,000	\$ 500,800,000
Total	\$ 118,200,000	\$ 123,100,000	\$ 125,500,000	\$ 136,700,000	\$ 142,300,000	\$ 645,800,000

Why Care About Healthcare Finance?

Healthcare is Big Business in Hawaii...

Healthcare contributed \$3.9 billion to Gross Domestic Product (GDP) in 2006, or 7% of the GDP, ranking 4th among all private industries

Average Annual Sector Share of Gross Domestic Product 2002-2006



- The healthcare and social assistance percentage of the GDP would be increased if government facilities such as HHSC, Tripler and the VA Hospital were reclassified from government to healthcare and social assistance

Source: 2006 State of Hawaii Data Book, DBEDT, table 13.05, reflecting NAICS industry classifications. Healthcare is Health care and social assistance.

Healthcare in the Top 50 Businesses

HAH Members represent 7 of Hawaii's top 50 businesses in 2007

#8 – Kaiser Foundation Health Plan and Hospitals, Inc.

- Moanalua Medical Center

#11 – Hawaii Pacific Health

- Kapiolani Medical Center at Pali Momi
- Kapiolani Medical Center for Women and Children
- Straub Clinic and Hospital
- Wilcox Memorial Hospital

#14 – The Queen's Health Systems

- The Queen's Medical Center
- Molokai General Hospital

#25 – Hawaii Health Systems Corporation (Cont'd)

- Big Island – Hilo Medical Center, Kona Community Hospital, Kau Hospital, Hale Ho'ola Hamakua, Kohala Hospital
- Maui – Maui Memorial Medical Center, Kula Hospital
- Lanai – Lanai Community Hospital
- Oahu – Leahi Hospital, Maluhia
- Kauai – Kauai Veteran's Memorial Hospital, Samuel Mahelona Memorial Hospital

#29 – Castle Medical Center

#34 – St. Francis Health Care System of Hawaii

- St. Francis, Liliha – Hawaii Medical Center East (*)
- St. Francis, West – Hawaii Medical Center West (*)

#42 - Kuakini Medical Center

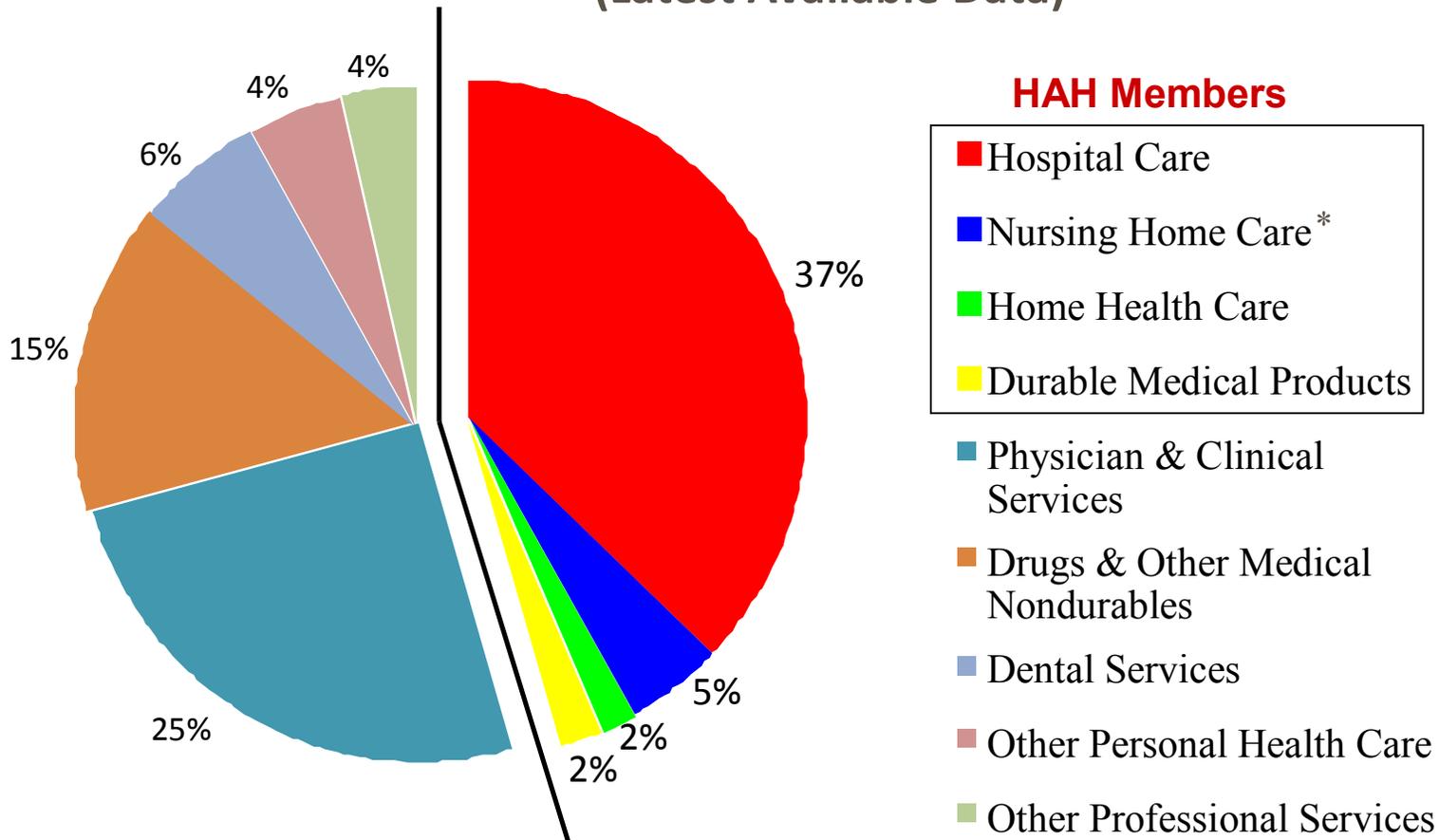
(*) - St. Francis Medical Centers became Hawaii Medical Centers in January 2007 through a change in ownership

Source: Hawaii Business, "The Top 250 Companies", August 2007

Hawaii Personal Health Care Expenditures

46% of Hawaii's Personal Healthcare Expenditures is provided by HAH Members

Calendar Year 2004
(Latest Available Data)



* Not all nursing homes are members of HAH. 62% of the long term care beds belong to HAH members.

Who Pays For Healthcare?

Healthcare insurance premiums continue to increase for both employees and employers

- Average annual increase in healthcare insurance premiums from 2002 to 2005 has been
 - HMSA – 6.9%
 - HMAA – 7.0%
 - UHA – 4.9%
 - Kaiser – 9.0%

Portion of Annual Health Insurance Premiums Paid by Employee and Employer (2005)

	National		Hawaii	
	\$	%	\$	%
Single Coverage				
Employee Portion	\$ 723	18%	\$ 302	9%
Employer Portion	\$3,268	82%	\$3,037	91%
Family Coverage				
Employee Portion	\$2,585	24%	\$2,193	23%
Employer Portion	\$8,143	76%	\$7,199	77%

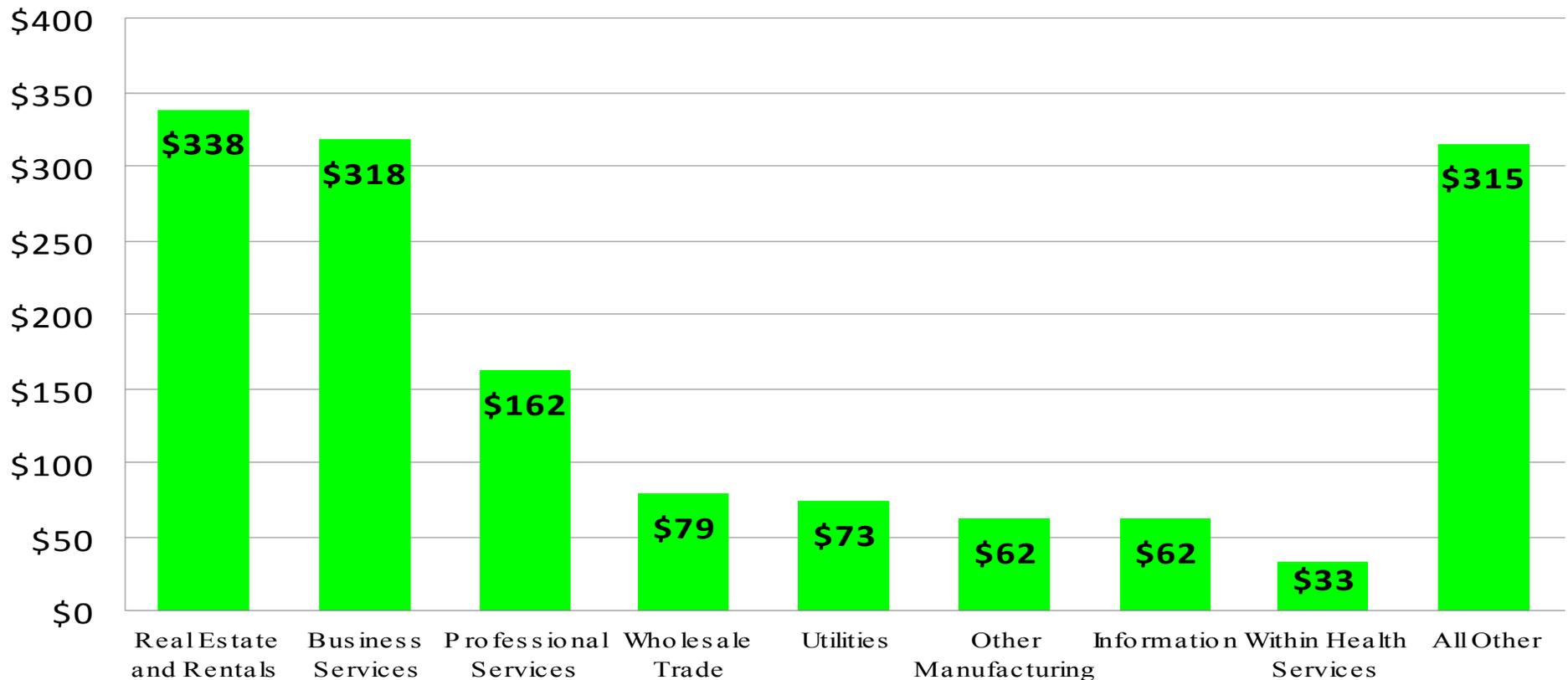
- Hawaii has the lowest total premiums in the nation for single coverage and the fourth lowest for family coverage

Source: Pacific Business News and Star Bulletin, Kaiser Family Foundation, Agency for Healthcare Research and Quality (AHRQ)

Direct Impact - Purchases

The Health sector purchased over \$1.4 billion from Hawaii businesses in 2002 (latest available data)

Purchases from Other Hawaii Businesses 2002 (in millions)



Source: The 2002 State Input-Output Study for Hawaii, DBEDT, June 2006

Direct Impact - Employment

Healthcare generates jobs and employs voters

Average Annual Sector Share of Private Sector Employment, 2002-2006



2006 Wage and Salary Job Count in the **Private** Sector:

Hospitals	13,800
Long Term Care Facilities	6,700
Ambulatory Health Care Services *	<u>22,800</u>
	43,300

* - Includes Home Health and related organizations

Source: 2006 State of Hawaii Data Book, DBEDT. Latest available data.

Healthcare as an Export Industry

A substantial share of the economic impact of Hawaii's healthcare industry is generated by new money coming into the State

- To the extent that Hawaii's healthcare services are funded by out-of-area monies, HAH members are considered to be among Hawaii's exporting firms. Examples are clinical, research, and educational services funded by sources outside the local economy.

Example: Acute Care Hospitals, 2006

Area of Patient Residence	Estimated Payment for Inpatient Care	Estimated Payment for Emergency Room Care	Estimated Total Emergency Room and Inpatient Payments
US non-Hawaii	\$ 42,173,255	\$ 12,501,221	\$ 54,674,476
Outside of US	\$ 6,476,245	\$ 1,750,610	\$ 8,226,856
Total	\$ 48,649,501	\$ 14,251,832	\$ 62,901,332

- The **\$62,901,332** in payments generated by “Other US” and “Outside of US” patients in 2006, generates an additional **\$69,191,465** in economic activity in the region in the form of purchases from other sectors such as rentals, business services, construction, etc.
- Healthcare industry also brings in to Hawaii substantial amount of federal funds from Medicare and Medicaid

Financial Trends of Hawaii's Hospitals, Nursing Facilities, Home Care and Hospice

Providers have been experiencing losses consistently since 2000

- Total costs exceeded payments for Hawaii's hospitals in 2006 by \$150,000,000 (\$150 million)
- Contributing to those losses are costs not covered by government payors and community benefits including medical education, community programs, bad debt and charity care, waitlist patients and trauma care
- Investment income and other revenues have helped to reduce the overall losses for some hospitals
- Hospitals without significant investments and other revenue sources operate at an overall loss
- Cumulative losses since the implementation of the Balance Budget Act of 1999, have depleted reserves the hospitals had saved for future capital projects and serving the community

Closing Remarks

Hawaii's residents expect to have continued access to quality healthcare.

Hawaii's healthcare providers are faced with reduced payments, increasing costs and the need to comply with mandates and other issues such as patient safety; transparency; electronic medical records; and preparations for bioterrorism, natural disasters and more virulent flu epidemics.

If the financial condition of Hawaii's healthcare providers is not improved, Hawaii can expect that the "Perfect Storm" will hit the healthcare industry, the fourth largest private industry in Hawaii, and have a significant impact on Hawaii's economy and residents.