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Kentucky Chamber: Medicaid costs growing at twice the rate of state budget

Although Medicaid is an important part of Kentucky's health-care system, state spending on the program is rising at twice the rate of the overall budget. This trend reflects a priority shift away from funding for education – Kentucky's best hope to improve the long-term health and prosperity of its citizens. The Kentucky Chamber of Commerce is addressing Medicaid spending as part of its review of how the state spends its tax dollars. Its conclusions are based on the following points.

Importance of Medicaid

The Chamber understands that Medicaid is a vital program for many of Kentucky's citizens and health care providers and plays an important role in providing health coverage in Kentucky:

- Medicaid provides coverage to more than 745,000 Kentuckians—approximately 17% of our total population, many whom represent vulnerable populations—the disabled, mentally ill, elderly and children.
- At \$31,111 per year, Kentucky's per capita income is 80% of the national average—ranking Kentucky 46th among the states.¹ Given the fact that Medicaid eligibility is based in part on income, there is strong reliance on Medicaid in Kentucky.
- Medicaid provides approximately \$5.4 billion annually to the Commonwealth's health care economy and is important to the revenue stream of many hospitals, nursing homes, pharmacies, physicians and other health care providers.

The following offers the Chamber's perspective and suggestions for addressing rising Medicaid costs.

The Problem

- **Medicaid Costs Soaring:** Kentucky's Medicaid budget is growing more than twice as fast as total state government spending. Although about 77% of total Medicaid funding is provided by the federal government, the remainder comes from the state General Fund. Recent research by the Chamber on state budget trends revealed that Kentucky's total General Fund spending has increased by 33% since 2000, compared to a 67% increase in General Fund appropriations for Medicaid in the same period (from \$1.5 billion in the FY 2000-02 biennium to \$2.5 billion in FY 2008-10).² This rapid increase in Medicaid spending means the program frequently experiencing shortfalls, with a deficit of over \$280 million last year alone.
- **Reasons for Increase:** Medicaid spending has increased for many of the same reasons that the cost of private health insurance premiums has grown: the cost of prescription drugs, enrollment growth, and medical inflation and utilization.³ Kentucky Medicaid enrollment has increased approximately 25% in the past nine years, from around 560,000 recipients in FY 2000 to more than 700,000 today.⁴ The program is currently growing at a rate of 3,000 new recipients per month--three times the rate anticipated in the current budget.⁵ The current

economic downturn is a major culprit in this enrollment growth. Research by the Kaiser Family Foundation reports a 1% increase in Medicaid enrollment for every 1% increase in the national unemployment rate.⁶ Kentucky's unemployment rate currently stands at 11%--the highest in 26 years.

- **Federal Funds to Decrease after 2010:** Under the federal stimulus legislation (the American Recovery and Reinvestment Act of 2009) all states received a temporary increase of 6.5% in their federal Medicaid match. Kentucky's increased to 77%, up from about 70%—representing almost \$1 billion in additional federal funds.⁷ Unless Congress takes additional action to extend this increased matching rate, Kentucky's rate will return to the 70% level in 2011. One state Medicaid administrator referred to this eventuality as “falling off a financial cliff”.⁸
- **Low Health Status Despite Increased Medicaid Spending:** One of the more perplexing aspects of the rapid rise in Medicaid spending is that, although it provides more Kentuckians with health coverage, the state's health status is still among the worst in America. Consider a few findings from a 2007 University of Kentucky assessment of Kentuckians' health:
 - Kentucky has the highest total mortality rate in the United States—987 per 100,000 population vs. 842 nationally—largely due to high cancer and heart disease death rates.
 - Kentucky's cancer death rate per 100,000 population is 237, compared to the U.S. average of 202, ranking Kentucky the worst among the states for cancer burden.
 - Cardiovascular disease is the leading cause of death in Kentucky. Nationally, Kentucky ranks 4th highest for cardiovascular mortality, 5th highest for heart disease mortality, and 12th in the nation for stroke mortality.⁹
- **Priorities Shifting from Education:** In terms of the state budget, Medicaid's share is growing while education's share is getting smaller. Since 1986, Medicaid's share of the General Fund has doubled—from 6.5% in FY 1986-88 to more than 13% in the current fiscal year. Meanwhile, K-12 education's share of General Fund appropriations has declined from a high of 48.2% in FY 1986-88 to 43.8% in the current fiscal year.¹⁰ Postsecondary education's share declined from 16.9% in 1986-88 to 13.7% in the current fiscal year.¹¹ The increased spending on Medicaid isn't entirely responsible for our shifting priorities. Growth in corrections and public employee benefits also outpace overall government spending.
- **Better Education Improves Health:** Why is the Chamber concerned about the redirection of tax money away from education? Because a significant body of research links higher levels of education with better health. People with more education experience better health than those with less education in terms of higher levels of perceived health, physical functioning, and life expectancy, as well as lower levels of disability, morbidity and mortality.¹² We believe improving the education attainment of Kentuckians will improve health, which can lead to lower health costs. The evidence is also clear that increased education attainment increases employment opportunities and income for Kentuckians, which can reduce our reliance on Medicaid and other social programs.¹³

Potential Solutions

The key question concerning Medicaid is how to slow unsustainable spending growth without inflicting harm on Medicaid recipients and providers. We think some of the potential answers lie in expanding current aspects of Kentucky's program and by looking to best practices in other states:

- **Expand Medicaid Managed Care:** Studies strongly suggest that Medicaid managed care programs can save anywhere from 1% to as much as 20% over the traditional fee-for-service Medicaid model.¹⁴ Fortunately, Kentucky is no stranger to the Medicaid managed care.

Starting with the Citicare program in the early 1980s, up to the Passport Health Plan today, Kentucky has been a national leader in using managed care principles in Medicaid.

The Passport Health Plan was created 10 years ago under a federal waiver as a partnership between local providers using a managed care model for 159,000 Medicaid and KCHIP (Kentucky Children's Health Insurance Program) recipients in Jefferson and 15 surrounding counties.

Passport has achieved a number of impressive accomplishments:

1. Average growth in medical costs of 5% annually compared to more than 10% in the region.
2. Saved more than \$200 million in Medicaid costs, with savings amounting to as much as 10% in some years.¹⁵
3. Increased the use of generic drugs from 22% of prescriptions in 2000 to more than 79% in 2009.
4. Payments to providers have consistently equaled or exceeded those of the regular Medicaid program.
5. Passport was rated the 9th-best Medicaid plan in the country in 2008, based on quality and member satisfaction, by *U.S. News and World Report*.
6. Passport was awarded the Excellent level of accreditation by the National Committee for Quality Assurance, the highest level possible.¹⁶

One of the best practices identified by the National Governors Association for controlling Medicaid costs is for states to make their Medicaid programs "resemble a private insurance model".¹⁷ We think Passport fills the bill in this regard as it is more like private insurance than traditional fee-for-service Medicaid. Given this best practice and the demonstrated results, **the Chamber recommends that the General Assembly work to expand managed care similar to the Passport model as soon as possible in the more populous areas of Kentucky and to look for appropriate ways to incorporate managed care in other areas of the state based on regional demographics and the number of health providers.**

- **Incorporate Wellness Into Medicaid:** Another best practice identified by the National Governor's Association Center for Best Practices is for states to incorporate more wellness activities into their Medicaid programs. A number of states use financial incentives for Medicaid recipients who maintain healthy behaviors. In Florida, credits are awarded to recipients who meet specific goals that can be used to purchase services not covered by the program (such as smoking cessation and weight loss programs) and medical supplies (bandages and over the counter drugs).¹⁸

The Chamber fully recognizes the value of wellness activities in reducing health costs having recently developed a Workplace Wellness Tool Kit to help employers set up effective wellness programs for their employees. Recognizing that smoking-related illness costs Kentucky more than \$1.5 billion per year in health costs (over \$500 million per year of this is in Medicaid costs) the Chamber also supported an increase in Kentucky's cigarette tax to discourage smoking.

The Chamber recommends that:

- **an increasingly larger portion of Medicaid expenditures be shifted from treating illness to promoting wellness**
- **higher co-pays be required for recipients who smoke**
- **health care providers be given incentives to order wellness or preventive services for Medicaid patients**
- **Kentucky provide a statewide smoking cessation program for Medicaid recipients (Kentucky is one of only five states without such a program).**

- **Program Administration:** Other potential areas for possible savings in Medicaid include:
 1. Improving the “error rate”, meaning reducing overpayments to providers as well as the number of recipients who are incorrectly determined to be eligible for participation.
 2. Ensuring that child support orders require that noncustodial parents who have access to health insurance provide coverage for their children (as permitted by Kentucky law).
 3. Increasing the use of generic drugs by Medicaid recipients.
 4. Revisiting the use of co-pays for recipients at higher income levels.

- **Questions to Consider:** Finally, we would encourage state officials to consider six key questions when considering changes to Medicaid. The choices represented by these questions are identified in a recent report on state Medicaid reform by Deloitte Consulting and provide a good framework for discussion:¹⁹
 1. What should be the core functions of our Medicaid program?
 2. Are we going to manage the services in our program directly, or will we contract for them?
 3. Where do we want to be on the continuum between “traditional” Medicaid benefits and coverage and free health care for all low-income residents?
 4. Which cost savings and policy levers will we use to reduce, or at a minimum contain, the costs of our program?
 5. Will we go beyond simple program administration and use our Medicaid program to actively control the costs and quality of health care in our state?
 6. To what degree will Medicaid recipients share the state’s burden of cost reduction and quality?

The Bottom Line

Kentucky has been fortunate in that we have been able to balance the state budget without significant cuts in Medicaid eligibility and reimbursement. However, given the current rate of growth in Medicaid spending, the Commonwealth faces a “financial cliff” in 2011, when a billion dollars in additional federal Medicaid funding will expire. The potential solutions are not about being punitive to recipients and providers, but are about using innovative solutions, such as the expansion of the Passport Health Plan, that resemble approaches found in the private sector. If we fail to confront these issues now, Medicaid spending will continue to spiral, and our ability to invest in education will be further reduced. In the long run, education is the one investment that can improve health, increase income and improve the quality of life for all Kentuckians.

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