Addressing the Financial Challenges Facing Kansas Hospitals

A July 2024 report from the Center for Healthcare Quality and Payment Reform (CHQPR) titled, *Rural Hospitals at Risk of Closing*[1] highlights a critical issue: over 30% of all rural hospitals in the U.S.—more than 700 facilities—are facing severe financial distress, placing them at high risk of closure. Alarmingly, more than half of these hospitals (approximately 360) are at immediate risk of shutting down due to the gravity of their financial challenges. Kansas has the highest percentage of rural hospitals at immediate risk, with 32% of its rural facilities on the brink of closure. According to CHQPR, the primary driver of this crisis is that private insurance plans are paying these hospitals less than the actual cost of delivering services to patients.

Phase I: Assessing Kansas Hospitals' Financial Health

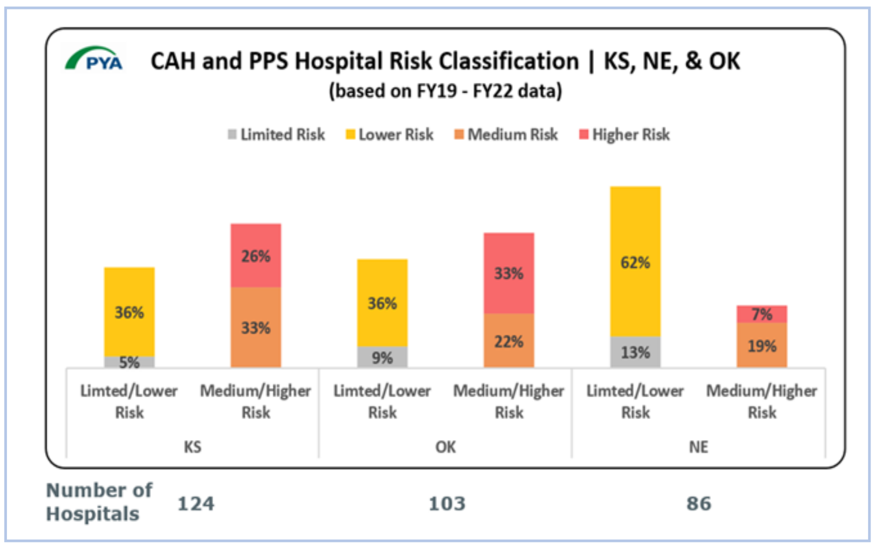
Objective

In 2024, PYA conducted an in-depth study to evaluate the financial health of Kansas hospitals, including 46 Prospective Payment System (PPS) hospitals and 78 Critical Access Hospitals (CAHs). The initial phase focused on patient services revenue and the overall financial position of these facilities, using Medicare Cost Reports from 2019 to 2022 as the primary data source. Each hospital was assigned a risk score ranging from limited risk to higher risk. PYA also assessed the financial strength of key health insurers in the market to understand how insurance company margins and financial strength aligned with hospital providers during this time period.

Key Findings

- *Loss on Patient Services* – In FY 2022, the median operating margin for Kansas hospitals was **negative 12.7%** (PPS hospitals at -7%, CAHs at -19%), with most hospitals losing money on patient services. PYA also evaluated hospitals in neighboring states, that showed Kansas had the lowest median operating compared to Nebraska and Oklahoma.
- *Low Financial Reserves* – The hospitals at greatest financial risk are burdened with more debt than net assets (equity). In FY 2022, more than one-third of Kansas hospitals were in this position.
- *Peer Comparison (KS/NE/OK)* – Kansas had a higher percentage (59%) of hospitals classified as medium to high risk than Nebraska and Oklahoma. Nebraska has the highest percentage (75%) of Limited/Lower Risk hospitals. Kansas had more than twice the percentage of Medium/Higher risk hospitals than Nebraska. (see ***Figure 1***).

Figure 1 – CAH and PPS Hospital Risk Classification (KS, NE, and OK hospitals)



[1] Report available at https://chqpr.org/downloads/Rural_Hospitals_at_Risk_of_Closing.pdf

Key Findings – Insurance Companies

Based on available public information, we determined that:

- Blue Cross Blue Shield holds a dominant market share in the 3 states evaluated (Kansas – 85%, Nebraska – 82%, Oklahoma – 73%)
- Blue Cross Blue Shield of Kansas reported the most favorable financial position of the six insurers in our analysis with an equity financing ratio of 56% on an asset base of over $2.1B which was the highest asset base of the regional insurers analyzed.
- Blue Cross Blue Shield of Nebraska reported an equity financing ratio of 42% on a smaller asset base of just under $1B.
- HCSC (including Blue Cross Blue Shield of Oklahoma) reported the lowest equity financing ratio of 10%.

Phase II: Hospital Assessment – Deep Dive Analysis

Objective

In the study's second phase, PYA completed a deep dive analysis to determine the level of incremental funding required for the sample hospitals to sustainably provide care (generate a positive operating margin). PYA selected three hospital (1 PPS and 2 CAHs) with more than 20% of reimbursement derived from commercial payers that were classified as medium or higher risk. The evaluation used billing and collections data by payer provided by each hospital, audited financial statements, and Medicare Cost Reports[2].

Key Findings

PYA identified key factors impacting operating margins, including service offerings, reimbursement rates, and other considerations. Additionally, PYA estimated the financial impact of commercial payers and Medicare/Medicare Advantage programs reimbursing below the estimated cost of providing services (see ***Figure***

Figure 2 – Key Services and Variable Impacting Operating Margin (Comparing reimbursement to estimated cost)

Key services and variables impacting operating margin (in millions)

		PPS 1	CAH 1	CAH 2
Services	Professional Services, Clinic, and Other Operations	-16.1	-1.3	-0.3
	Home Health/Hospice Operations	0.0	-0.1	-0.7
	Geriatric Psychiatry	0.0	0.6	0.0
Payer reimbursement	Estimated Medicaid Loss	-2.0	-1.4	-0.2
	Medicare reimbursement compared to cost	-9.8	0.0	0.0
	Estimated Medicare Advantage compared to Medicare reimbursement	-2.2	-0.5	-0.7
	Commercial payers other than Blue Cross compared to Medicare reimbursement	8.9	0.1	0.1
	Blue Cross compared to Medicare reimbursement	9.7	-0.9	0.5
Other	340B contract pharmacy	0.0	0.3	0.8
	Other Revenue	0.0	0.3	0.0
	Unreimbursed and uncompensated care	-4.6	-1.0	-0.8
	Other	0.0	0.5	-0.2
	Government appropriations (per cost report)	0.0	0.5	0.0
	Operating Margin $	**($16.1)**	**($2.8)**	**($1.5)**
	Operating Margin %	**-7.3%**	**-14.5%**	**-5.8%**

2). Historically, reimbursement from commercial payers has offset losses from services provided to Medicaid and other underfunded/uninsured patients. With over half of Kansas hospitals operating at a loss, the question arises: where will the additional funds come from to keep these hospitals running? PYA evaluated the impact of increased commercial reimbursements in the following section to understand what types of reimbursement increases would be required to balance the budget for these sample hospitals for fiscal 2022 (the year of data analyzed).

[2] PYA based its analysis on information provided by the evaluated hospitals and did not independently verify the accuracy of this information.

Modeling Commercial Reimbursement Rates

<u>Objective</u>

PYA modeled the necessary reimbursement increases from commercial payers to help hospitals achieve a sustainable operating margin. The analysis used hospital billing and collections data to propose reimbursement rates as a percentage of Medicare reimbursement, aiming for an operating margin between 1.5% and 3.0%. These operating margin levels are intended to cover operational costs, allow for necessary capital improvements, and enable hospitals to continue fulfilling their mission within the community. *The rates as expressed below are rates that would actually be realized or received by the hospitals, not just contracted rates which may likely be reduced due to claim denials, downcoding of services, or unpaid patient obligations*.

The proposed rates that generated a small positive operating margin for the sample hospitals included the following:

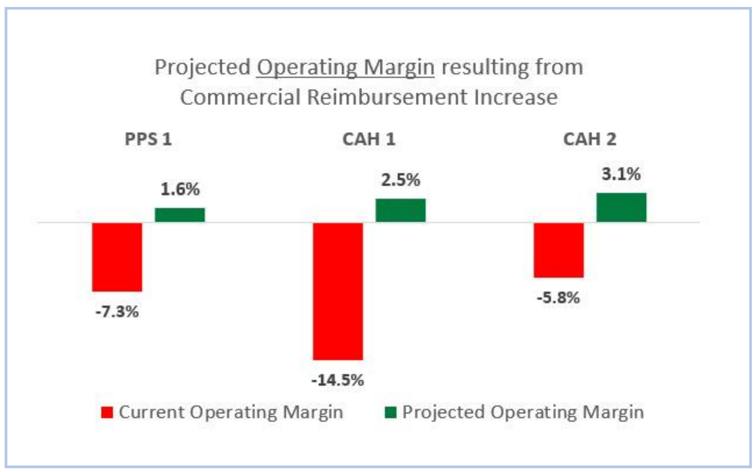
- 220% of Medicare for PPS hospital services
- 130% for CAH services
- 200% for professional services across both PPS and CAH hospitals

These proposed rates ranged from rate increases of 20% to 60% across the three hospitals.

<u>Key Findings</u>

These proposed increases successfully shifted all three from financial losses to positive operating margins (see ***Figure 3***).

Figure 3 – Projected Operating Margin Resulting from Modeled Commercial Reimbursement Increase



Securing the Future of Kansas Hospitals

PYA's analysis underscores the severe financial challenges facing rural hospitals, particularly in Kansas. With over 30% of rural hospitals nationwide at risk of closure, and more than half of Kansas's hospitals threatened, urgent action is needed. Without additional funding, these hospitals will continue to operate at a loss, threatening their ability to provide essential healthcare services, maintain infrastructure, and support necessary staffing levels. By aligning funding more closely with the actual costs of care, whether through commercial reimbursement or other sources, these hospitals can move from financial distress to sustainability, ensuring they continue to serve their communities.