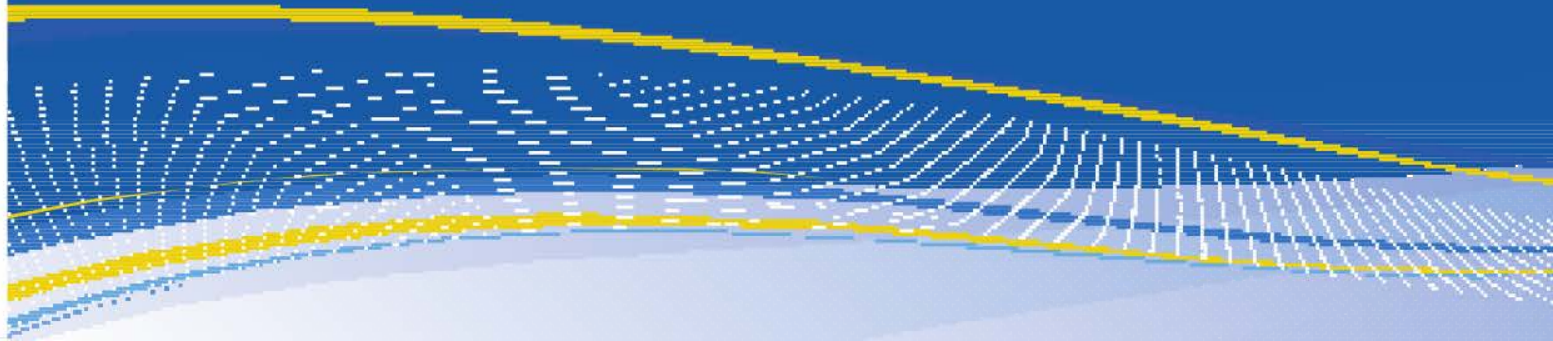


HCBS Waiver Rate Setting Use of Inflation Factors

Division of Long Term Services and Supports
Disabled and Elderly Health Programs Group
Center for Medicaid and CHIP Services



Training Objectives

- Understand the definition and significance of inflation.
- Apply concepts of inflation to the rate setting process, including:
 - Consumer Price Index (CPI) overview.
 - The impact of inflation on rates.
 - Limits to using inflation indices in rate setting.

Inflation Overview

- Inflation is a sustained increase in the general price level of goods and services in an economy over a period of time.
 - In rare periods of economic crisis, the price level of goods and services can also decrease causing a period of deflation.
- As prices rise, a unit of currency (\$1) holds less monetary value in the market than it did previously (it does not buy as many goods/services).
 - Indicates a reduction in purchasing power per unit of money, loss of value in currency.
- Reported as annualized percentage growth of an index of prices.
- Inflation rates may vary from year to year.

Importance of Inflation

Inflation:

- Is an indicator of economic conditions and is the primary basis for cost of living adjustment increases.
- Is most commonly measured by the Consumer Price Index (CPI) <http://www.bls.gov/cpi/>, released by the Bureau of Labor Statistics (BLS).
- Percentage increases in CPI is a rough approximation of percentage increases in an individual's cost of living.
- Demonstrates price changes from year to year.
 - Shows the amount of money required to buy goods and services.
- Is relative to the amount of money in circulation.
 - More money in circulation dilutes purchasing power, resulting in higher prices for services and supports.

Publicly Available Inflation Source: Consumer Price Index (CPI)

What is a Consumer Price Index?

- A measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services.

The Market Basket:

- Is developed from detailed monthly records in which prices of preselected goods and services are tracked and then compared over time.
- Is broken into more than 200 categories arranged into 8 major groups:
 - Food and Beverages, Housing, Apparel, Transportation, Medical Care, Recreation, Education and Communication, and Other Goods and Services (tobacco, personal services such as haircuts, funeral expenses, etc.).
- By monitoring the fluctuation in the cost to purchase this set basket of goods, the government is able to track the cost of living for most individuals.

Publicly Available Inflation Sources: Consumer Price Index (CPI)

Uses:

- Used primarily as an economic indicator, CPI is the most widely used measure of inflation.
- Used as a means to adjust income payments.
 - Over 2 million workers are covered by collective bargaining agreements, which tie wages to the CPI. Payments for Social Security, Military and Federal employees' retirement and payments for food stamp recipients are also tied to CPI.

CPI for All Urban Consumers (CPI-U)

- Most Cost of Living Adjustment (COLA) cited in federal legislation uses CPI-U
 - The most well-known legislation is the indexing of federal income tax brackets.
 - Each year, the IRS adjusts more than 40 tax provisions to prevent people from being pushed into higher tax brackets due to inflation rather than actual increases in real income, and the IRS uses CPI-U to make these adjustments.
 - <http://www.bls.gov/news.release/cpi.t01.htm>
- CPI-U was originally introduced in 1978 to replace the Cost Price Index for Wage Earners and Clerical Workers (CPI-W) because the CPI-U represented a much broader population. While CPI-U did not replace CPI-W altogether, it did replace CPI-W as the most common metric used to calculate COLA.
- The CPI-U represents about 87% of the total U.S. population.
- It is based on the expenditures of almost all residents in urban or metropolitan areas, including professionals, the self-employed, the unemployed, individuals with low income, and retired people, as well as urban wage earners and clerical workers.

Inflation within Rate Development

- Services and supports prices will change from year to year, partially based on inflation.
- Changes in cost may be captured during rate development, ensuring appropriate prices are set for each service. Changes may be the result of:
 - Geographic Factors
 - Inflation factors and cost of living vary by location, broken down by state or more specific locales.
 - Different localities have different prices for the same services.
 - Legislative Factors
 - Legislative action may limit or curtail state funding reserved for inflation-related rate increases.
 - Limits imposed by legislative action may yield rates and wages that no longer support the cost of living, in which case it is critical for the state to rebase rates regularly to maintain an adequate provider pool.

Inflation within Rate Development

- Fee For Service Rates
 - *Use of COLA must be fully justified, including documentation of:*
 - **Why** the COLA metric (e.g., CPI-U, CPI-W) used is **appropriate**.
 - **Example:** The state set a COLA percentage increase by using the percent change in CPI-U for the first half of 2015 for all items in the Northeast BLS region. The state used this because this was the most recent data available at the time of rate setting.
 - **How** it was **calculated**.
 - **Example:** We obtained CPI-U information from the bls.gov website. We inflated the rate paid at the start of the state's fiscal year, using the most recent CPI-U information available for the Northeast BLS region.
 - **What** that metric **reflects** and **how** it **applies** to the particular service or support rate.
 - **Example:** We use inflation by CPI-U as one method of ensuring rates are sufficient to maintain an adequate provider pool. Inflation must go through legislative approval.

Inflation within Appendix J

- Waiver cost projections can account for inflation.
- Per 1915(c) Technical Guide, page 276, “As a general matter it is expected that the basis of the derivation of each factor will be the data that the state has reported via the CMS-372(s) trended forward to reflect inflation adjustments.”
 - Projecting funds for services under HCBS waivers requires reflecting estimated increases in prices of services/supports.
 - If these projections are not included, prices for services and supports will not increase when inflation occurs, potentially causing lower than customary rates.
 - Lower rates may induce shortages in the state’s provider base as many providers may not be willing to accept such rates.

Inflation within Appendix J

How to ensure competitive market rates are paid to providers:

- Build into the rate setting how often rates will be reviewed and adjusted based on CPI or other metrics.
 - Recommendation to the state for adjusting rates by inflation:
 - Allow providers to participate in the process and give feedback.
 - Specify a reference period from which changes in the CPI or other metrics will be measured.
 - Make adjustments to rates for CPI or other metrics at fixed time intervals.
 - Document clearly in Appendix I-2-a how rates are adjusted using CPI or other metrics.
- If rate adjustments are tied to the legislative action, then the state must specify how those rates will be re-based.

How to Increase Rates Using CPI

1. **DEFINE** clearly the base rate that is subject to increase.
2. **IDENTIFY** precisely which CPI index series will be used to increase the base payment. This should include:
 - Population (CPI-U or CPI-W).
 - Area (state, region, county, city, etc.).
 - Series title (all items, subset of services and supports, etc.).
 - Index base period (range of years on which CPI is based).
3. **SPECIFY** a reference period from which changes in the CPI will be measured (usually a single month or an annual average).

How to Increase Rates Using CPI

4. STATE the frequency of adjustment (usually made at fixed time intervals, such as quarterly, semiannually, or, most often, annually).

5. DETERMINE the formula for the adjustment calculation:

- Usually, the change in payments is directly proportional to the percent change in the CPI index between two specified time periods.
 - **Example:** “CPI-U increased an average of 1.7% in 2012-2015, rates will be increased 1.7% in proportion to CPI-U.”
- Consider whether to make an allowance for a "cap" that places an upper limit on the increase in prices, or a "floor" that promises a minimum increase regardless of the percent change in the CPI.
- COLA should be compounded annually. As you are applying a COLA, it should be applied to the year and that new rate becomes the base rate for the next year.

Summary

- Inflation is a sustained increase in the general price level of goods and services in the economy over a period of time.
- CPI-U is one of the most common inflation metrics used to calculate cost of living.
- Projections should account for inflation in the form of Cost of Living Adjustments, which must be detailed to explain how they were derived and which data source was used.
- Accounting for inflation by implementing Cost of Living Adjustments acknowledges §1902(a)30(A) of the Social Security Act (i.e., “payments are consistent with efficiency, economy, and quality of care and are sufficient to enlist enough providers”). It also prevents underpayment, helps ensure quality of care, and helps retain an adequate pool of providers.

Additional Resources

- Additional rate setting resources are available in the below website. Topics include:
 - Rate Methodology in a FFS HCBS Structure
 - HCBS Rate Construction Illustration and Topical Discussion
 - Documentation of Rate Setting Methodology
 - Data Validation
 - Cost Neutrality Demonstration
- <https://www.medicare.gov/medicaid-chip-program-information/by-topics/long-term-services-and-supports/home-and-community-based-services/hcbs-training.html>

Questions

For questions contact:

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