

LEGAL UPDATES

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A New Era in Healthcare Cost Regulation in California

Key takeaways

A newly created agency will begin collecting healthcare cost data to set statewide growth targets for healthcare costs by 2025.

Healthcare transactions will be subject to new regulatory scrutiny for their impacts on cost and effect on healthcare market competition, starting in January 2024.

Standards will be developed to promote alternative payment models by the end of 2024.

Enforceable cost targets for payers and providers will be established by 2028.

Background of the Act

On June 30, 2022, Governor Gavin Newsom approved SB 184, the California Healthcare Quality and Affordability Act, a far-reaching law that will have a significant impact on the delivery and payment for healthcare services in California. While the law contains several provisions affecting the Medi-Cal program, expansion of public health and mental health programs, and negotiation of contracts for the purchase of generic drugs, the most important feature of the Act is the creation of a state body that will develop and enforce cost targets for healthcare payers and providers within the next five years. In adopting the Act, California joins the States of Connecticut, Delaware, Massachusetts, Nevada, New Jersey, Oregon, Rhode Island and Washington in establishing an agency to set statewide healthcare cost targets and collect data intended to better understand drivers of healthcare cost.

The new California agency, named the Office of Health Care Affordability (OHCA), is being organized under the Department of Health Care Access and Information (HCAI), which was formerly known as the Office of Statewide Health Planning and Development. While historically HCAI had as its primary mission the licensing and oversight of construction of healthcare facilities in California, as part of the 2021-22 budget process the Department was given a much broader portfolio, including responsibility for enhanced data collection related to the healthcare workforce, healthcare workforce education and training programs, rural healthcare delivery programs and geriatric care in underserved communities.

Structure and mission of OHCA

The creation of OHCA represents a dramatic intervention by the State into the healthcare economy to address problems of affordability. The law provides that OHCA will have a three part mission: (a) collection and analysis of data on total health care expenditures in California (THCE) on a per capita basis, (b) development of cost target methodologies and cost targets on both statewide and sector specific (geography and by type of entity) bases, and (c) progressive enforcement of cost targets on healthcare entities, ranging from technical assistance and required performance improvement plans to escalating financial penalties for failure to meet targets. As part of its responsibilities, OHCA will also have authority to examine the impact of mergers and acquisitions on healthcare costs. In this respect it will focus on transparency rather than enforcement and will not displace existing oversight of transactions by the Attorney General and the Department of Managed Health Care.

Within OHCA there will be two operative bodies—a Health Care Affordability Board, consisting of eight members selected by the Governor, the Senate, the Assembly, the Director of Health Services and CalPERS, and an Advisory Committee composed of representatives of providers and health plans, organized labor, consumer groups and other stakeholders. Appointments of the Board members was scheduled for December 2022 but have not yet been announced.

Implementation of the Act

The leadership of OHCA has announced the following schedule of its activities in the implementation of the Act:

January to June 2023—commencement of meetings of the Board, appointment of the Committee members and the development of a regulatory framework for the collection of THCE data from payers in California.

July to December 2023—commencement of meetings of the Committee, development of a statewide cost growth target methodology and completion of the regulatory framework for collection of THCE data.

January to June 2024—Development of preliminary cost growth targets for 2025 and collection of data on health care transactions.

June 2024—Board approval of 2025 cost growth targets.

July to December 2024—Adoption of standards for alternative payment models (to promote a shift from fee for service to payments based on cost and quality) and workforce stability. Collection of 2022 and 2023 THCE data from payers.

January to June 2025—Completion of a baseline report on THCE based on 2022 and 2023 data collected from payers. Set the 2026 cost growth targets.

July to December 2025—Presentation of the baseline report on THCE in a public hearing. Collection of 2024 THCE data.

January to June 2026—Set the 2027 cost growth targets.

July to December 2026—Collection of 2025 THCE data from payers.

January to June 2027—Complete an initial Annual Report on cost expenditures and targets based on 2024 and 2025 THCE data.

July to December 2027—Presentation of the initial Annual Report at a public meeting and define healthcare sectors (by October 1, 2027) which will be subject to cost growth targets.

January to June 2028—Complete an Annual Report based on 2026 THCE data and establish sector-specific healthcare cost growth targets.

Observations

OHCA expects to operate in a highly transparent manner. Meetings of the Board and the Committee will be subject to California's Open Meeting Act, with agendas and minutes posted on its website. Public comments will be solicited on baseline and annual reports concerning THCE as well as proposed cost growth targets.

The initial cost growth targets will be established in advance of the collection of data, based on resources such as reports from the California Health Care Foundation, the Milbank Memorial Fund program on Sustainable Health Care Costs, the Peterson-Milbank Program for Sustainable Health Care Costs and reports from the Commonwealth Fund. As THCE data is collected and OHCA refines

its methodology, the targets will be adjusted from time to time, with the prospect of multi-year targets being set.

THCE reporting will be required from managed care payers, health insurance providers, Medi-Cal managed care plans and “fully integrated delivery systems” as defined in the Act (which presently is limited to Kaiser Permanente). The initial deadline for submission of data from the years 2022 and 2023 will be September 1, 2024. In addition, OHCA will coordinate with Health Care Payments Data Program, which is California’s All-Payer Claims Database, which is expected to be substantially complete in June 2023 and will collect claims encounter data from the commercial market, Medi-Cal and Medicare. As has been the experience in other states THCE data will capture information that is otherwise not reflected in the All-Payer Claims Database, thus the need for dual reporting by payers.

With some exceptions all payers, providers and fully integrated delivery systems will be subject to cost targets. The Board has authority to exempt certain entities from the targets based on factors such as annual revenue, patient volume and high-cost outlier status in a geographic region or service line. Physician organizations with fewer than 25 physicians will be exempt unless the practice is a high-cost outlier.

Enforcement of cost targets against entities will begin in 2028, with initial enforcement measures limited to technical assistance, development of performance improvement plans and public hearings. Imposition of financial penalties for failure to meet cost targets will follow, with the adoption of sector specific cost targets.

OHCA will measure and publicly report on performance relative to quality and equity indicators, progress toward adoption of alternative payment models and investment in primary care and behavioral health.

During 2023 OHCA will develop regulations concerning a cost and market impact review (CMIR) program, which will define certain transactions to be subject to review by OHCA for potential impacts on competition or affordability of health care. Starting in January 2024, healthcare entities involved in a transaction involving a material change of ownership or governance, such as mergers, acquisitions, and corporate affiliations (to be defined in the regulations) will be required to provide OHCA with 90-day advance notice of the transaction. OHCA will have 60 days to determine whether

to require a CMIR review or grant a waiver. If OHCA undertakes a CMIR review it will issue a preliminary report available to the public and the affected parties and invite comments. OHCA will then issue a final report and will work with other state agencies (such as the Attorney General and Department of Managed Healthcare) to address any issues identified in the report and supplement oversight responsibilities of those agencies. A transaction that is subject to CMIR review may not be closed until 60 days after a final report is issued by OHCA.

What this means to you

Payers should monitor announcements from OHCA as it develops its requirements for TCHE data submission.

Providers and payers should stay abreast of the development of regulations concerning transactions that will be subject to Cost and Market Impact Review.

Interested parties may wish to seek representation on the Advisory Committee.

Contact us

This legal alert was authored by Andrew Demetriou. If you have any questions regarding these developments, please contact Andrew Demetriou, Curt Chase, Thomas Shorter or your Husch Blackwell attorney.