Q&A: How to Use NASHP's Model Law and Template to Increase Hospital and Health Care System Financial Transparency

What is hospital financial transparency?
Hospital financial transparency describes when hospitals/health systems disclose data so the public and state regulators can understand its assets – including income from a variety of sources, such as payment for services rendered, grants, capital, and other investments – as well as its expenses and liabilities. To date, most state hospital transparency requirements have been designed to provide information about medical service pricing to consumers rather than a hospital/health system's assets, which could better inform state health system cost-containment policies. To address and stem rising health care costs, states need specific information from hospitals and providers.

Why should states require hospital/health system financial reporting?
Year after year, hospitals account for the largest expenditure of US health care dollars, followed by physician and clinical services, of which over half are owned by a hospital or a hospital-affiliated health system. While hospitals/health systems are critically important to their communities, access to quality hospital care must be balanced with affordability. A growing number of state leaders are seeking to implement various cost-containment strategies, from payment reforms to total cost-of-care caps that aim to reduce the rapidly rising health care cost trajectory affecting everyone – employers, including states, and consumers. Understanding the relative financial position of a state's hospitals can help policymakers analyze the vitality of the health care system and better target cost containment efforts.

How to determine if a hospital/health system is financially sound or in trouble?
By evaluating the financial health of hospitals/health systems in their states, policymakers will be better positioned to answer questions about hospitals' ability to continue to meet debt obligations, pay their employees and vendors, and continue to provide quality care to patients. Unfortunately, developing this analysis isn't always simple or straight forward. To gain insight into how hospitals are doing financially, policymakers need access to financial information provided in a standardized manner that is consistent across hospitals and over time. This allows for benchmarking across systems and hospitals at similar points in time and following changes in financial health over time. The National Academy for State Health Policy's (NASHP) model law, An Act to Ensure Financial Transparency in Hospitals and Health Care Systems, and its accompanying financial reporting template can be used to collect the comprehensive data needed to help meet that challenge. Over time, financial information can be used to monitor the vitality of hospitals/health systems and evaluate the impact that policy changes or economic shifts have on them. And, it can help with planning the future of the health care system across a state.

What does the model act and accompanying reporting template do?
In most states, legislative authority would be necessary to require the collection of meaningful, comprehensive data from hospitals/health systems to evaluate their overall financial health. The model act specifies what data that should be collected, notes which hospital documents should be used to obtain the reporting information, and underscores that a state agency or office must be responsible for analyzing the data. Although not specifically written into the model act, NASHP has developed a

reporting template that will help states implement the law because it is designed to collect the information needed to perform a financial health evaluation.

As a result of increased consolidation, most hospitals/health systems are now a part of bigger systems, therefore, to fully understand a hospital's finances, data must be collected from parent system. Individual hospitals, or a consolidated health system, or component entities within a health system such as affiliated physician practices or a health plan are ordinarily included in the financial statements of the "reporting entity." Collecting data at the system level does two things. First, it assigns responsibility to the entity that has the greatest capacity for completing and submitting the template without undue burden. Second, the reporting entity or system is responsible for all of the individual hospitals and affiliated providers that are part and parcel of the system as a whole. It is that entity that has the ability to transfer funds between affiliates to ensure viability. If the system is healthy, individual affiliates should also be healthy.

Alternatively, policymakers may wish to have access to the most granular data possible, which would require collecting data at the individual hospital level as well as at the level of the system. The data collection template can be modified easily to use at the individual hospital level. Similarly, the language included in the model act can be modified to reference the requirement that data be collected at the individual hospital level, the system level or at both levels.

The reporting template also requests data that will help policymakers measure and compare financial performance on key measures of financial health, such as:

- Liquidity – the ability to meet short term obligations, including payroll;
- Profitability – the ability to cover operating expenses and generate enough profit to cover capital and debt service needs;
- Solvency – the ability to repay long term debt; and
- Capital adequacy – the ability to invest in a competitive level of capital assets, such as digital imaging capability (X-ray, magnetic resonance imaging (MRI), or mammography equipment).

Why can't hospitals simply provide audited financial statements?

Unfortunately, not all of the data related to a health care system or an individual hospital's finances are readily available to the public through an audited financial statement. It can be a challenge to access current audited financial statements, even for nonprofit hospitals/hospital systems when they are available, and the structure of those statements can be difficult analyze. Also, individual audited statements may not be comparable across all hospitals/health systems, reducing their utility to state policymakers who are charged with protecting/ensuring access to quality, affordable care throughout the state. Even with expected variations in profitability for hospitals/health systems across a state, there is value in tracking financial health of these facilities using standardized metrics that utilize the same format for all hospitals/health systems in the state. For example, if a state implements a cost-containment strategy that adversely affects a particular hospital, the data will help identify the impact and policymakers can change the strategy.

The reporting templates must be completed by the providers themselves, who must also provide an attestation that the data submitted to the state is true and accurate. Hospitals may claim that sharing financial statements is burdensome, intrusive, or threatens its competitive positioning. But hospitals prepare financial statements as a matter of course, so reporting of its data – even when required on a

standardized template – should not be so burdensome as to override the public interest in monitoring the financial health of these extraordinarily important resources.

Which state agency/office should be the identified lead for receiving and analyzing the data?
Data submissions will need to be directed to a responsible public agency. In states that have an all-payer-claims database, the agency housing that function would be a good candidate, as it is likely to already have the resources required to analyze and report on the data. States with health authorities that oversee system spending can opt to "house" the financial data repository as they are likely already collecting similar information. An alternative is the unit within the state's Medicaid agency that is responsible for auditing hospitals' Medicare Cost Reports, which will have resident expertise to assess financial data. State health planning offices are also worth considering, as the information collected via financial reporting will inform their work. The resources required would not be expected to require an additional appropriation or addition of staff.

Some states may lack the expertise to work with the data collected. In those cases, the state may wish to consider partnering with its public university system which will likely have the ability to support policymakers in their analysis of the financial data collected.

The model act includes a requirement that the state agency collecting the data report out to the Legislature each year on the financial status of the state's hospitals. The proposed language directs data to be reported out on an aggregate rather than on an individual hospital basis. That language is purposeful as the release of specific data can open the door to litigation by hospitals charging the legislation could lead to collusion. By collecting data at a granular level, however, decisionmakers will have access to data to support the development of sound policies, while releasing the data only in an aggregated form protects the integrity of the transparency initiative.

What can state officials immediately learn from data submitted by hospitals/health systems?
The financial template is designed to automatically calculate a number of standard key financial ratios that are important for a high-level understanding of a system's financial condition, including profitability, liquidity, and solvency. These data points will help answer the following questions:

- What is the hospital/health system's snapshot of all financial activities for a given period of time?
- What has the hospital/health system earned and lost in providing patient care services during that period?
- Can the hospital/health system pay its current financial obligations with its existing liquid assets, such as on-hand cash versus funds it has in investments?
- What is the hospital/health system's "days of cash on-hand," which indicates how many days the entity can continue to pay its operating expenses using its liquid assets like cash?
- How many days can a hospital/health system continue to pay its operating expenses given cash on-hand and other liquid resources, taking into account its board of directors-designated and undesignated investments?
- What is the average number of days patient accounts are in a collection period? The longer it takes to get patient care payments "in the door," the less cash is available to meet operation costs.
- What are total net assets compared to total assets, which reflects the ability to take on more debt? A lower value indicates that the reporting hospital/health system has a substantial

amount of financed debt that it has used to underwrite the acquisition of assets and is highly leveraged.

- Is the hospital/health system able to cover its debt with the yearly cash flow from its operations? The higher this ratio, the better able the entity is to handle its debt load.
- How old are the physical buildings and assets of hospital/health system? Generally, the older the average age, there will be a greater need in the short-term for the hospital/health system to invest in capital resources, including X-ray, MRI, etc.
- What is the portion of total patient service revenues that were charged out as charity care?
- What is the proportion of the hospital/health system's bad debt or the patient service charges that are not expected to be collected?

Are there resources available to understand and assess hospital financing?

This model law and accompanying resources includes a helpful publication – *A Community Leader's Guide to Hospital Finance* – that provides a high-level overview of important aspects of hospital finance. This guide was recently updated and is useful to policymakers who want to understand the health system landscapes in their states so they are better positioned to understand the viability of their states' health care infrastructures. It will also help them assess options to address the rising costs of care and to responsibly appropriate scarce state resources.

August 2020