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Other

Financial Impact of a Competitive Payment System on New Jersey Hospitals **ID# 022882**

Harvard University School of Public Health (Boston, MA)
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EXECUTIVE SUMMARY

This grant from The Robert Wood Johnson Foundation (RWJF) funded the Harvard University School of Public Health to study the effects of deregulation on New Jersey hospitals. In 1992 New Jersey eliminated its statewide system for setting hospital reimbursement rates in favor of letting the marketplace determine prices for hospital services; it also altered its system of reimbursements to hospitals for uncompensated care. Investigators from the Harvard University School of Public Health used objective financial data to compare the financial health of New Jersey hospitals in the three years before and the three years after passage of the deregulation legislation. Overall, the study found that elimination of statewide rate setting and the implementation of a market-based pricing system were financial windfalls for hospitals. Hospitals did not reduce markups to payors meant to cover the financial burden of uncompensated care, despite new funding that was meant to cover uncompensated care (uncollectible charges and charity care), and they reported operating profits that were 50% higher following deregulation than in the period before. The introduction of market forces appears to have had only limited ability to contain costs. Rural hospitals were more likely than others to improve their financial position, while inner-city and urban hospitals were more likely to do worse or to improve less. Hospital investment income almost doubled in the period following deregulation, while the volume of inpatient stays declined, largely because of the increased penetration of managed care. One-third of urban and suburban hospitals have joined one of four newly established, multihospital systems, but inner-city hospitals have been left out of these systems — perhaps because of their relatively poor market and financial positions. A paper summarizing these findings has been completed. The principal investigator hopes to collaborate on a paper with other researchers in the field who have studied similar deregulation efforts in Washington State and elsewhere.

BACKGROUND

In November 1992, New Jersey's legislature enacted a sweeping overhaul of its health care system, deregulating the industry and eliminating the state's hospital rate setting. The new laws did away with a payment system for hospitals based on diagnosis-related groups (DRGs) — an elaborate rate-setting mechanism that arrived at hospital fees by determining the average cost of