



JOHN CHIANG
California State Controller

February 27, 2012

Tim Matsumoto, Acting Chief
Fee-for-Service Rates Development Division
California Department of Health Care Services
PO Box 997417, MS 4600
Sacramento, CA 95899-7417

Re: Hearing Aid Reimbursement Policy

Dear Mr. Matsumoto:

The State Controller's Office (SCO) has completed a review of the significant difference between what a provider paid for hearing aids (acquisition cost) and the amount of reimbursement the provider received under Medi-Cal's reimbursement policies existent at that time. We found that significant savings of up to \$27.3 million over a three-year period (see Schedule 1, page 3) could be achieved by modifying the reimbursement policies.

We made several attempts to arrange a meeting with DHCS staff (Policy/Benefit Unit) to present the results of our review and seek input before issuing a final report. However in September 2011, before we were able to meet, DHCS issued Operating Instruction Letter (OIL) No. 406-11. OIL No. 406-11 revises the definition of "wholesale cost" for purposes of hearing aid reimbursement. On January 27, 2012, the SCO provided the DHCS with a draft of our report and on February 23, 2012, DHCS submitted the following comment on that draft report:

The Department of Health Care Services (DHCS) has received the Medi-Cal Hearing Aid Reimbursement Analysis developed by the State Controller's Office. As your letter indicates, DHCS has proposed a significant change in our reimbursement policy for hearing aids; however, we have received provider input and legislative inquiries expressing concerns about this proposal and the potential negative impact on access for our beneficiaries, particularly the impact on children. As such, we are conducting further analyses before determining the appropriate action. DHCS will similarly incorporate the findings and recommendations of the State Controller's Office in our analysis. We will inform you of the final decision on proceeding with this proposed reimbursement change or modification thereof. DHCS intends to review the analysis carefully to determine the feasibility of implementing changes to the Medi-Cal Hearing Aid reimbursement policy to take advantage of the findings and recommendations made by the State Controller's Office.

The SCO agrees with the revised definition and believes that OIL No. 406-11 is a constructive step toward reducing costs to the State while maintaining a high level of services to participants. DHCS's policy change also is supported by the results of our aforementioned review. While the new policy is not as extensive as our recommendations, we believe that annual savings (which we calculated using Medi-Cal's pre-OIL No. 406-11 reimbursement policies) similar to those suggested in our review can be achieved by implementing policy changes.

We also found that additional savings could be achieved by considering the following:

- In developing a new reimbursement methodology, consider whether the mark-up fees are needed at the current level to ensure adequate treatment.
- Provide assurance that the State is obtaining the most favorable prices by implementing the provisions of Welfare and Institutions code section 14105.3(e). As noted in our review, the contract(s) required under this section also can be used to ensure the quality of hearing aid products provided to Medi-Cal beneficiaries.

The SCO is providing the results of our review to assist in any ongoing policy discussions related to hearing aid reimbursements. We request that you inform the SCO of any actions taken by the DHCS with regard to our review. If we can be of further assistance regarding this issue, please contact Lisa Hughes, Chief, Community-Related Audits Bureau, by telephone at (916) 322-8489 or by e-mail at lhughes@sco.ca.gov.

Sincerely,

Original signed by

JEFFREY V BROWNFIELD
Chief, Division of Audits

JVB/wm

RE: S11-MPA-906

Attachment

cc: Toby Douglas, Director
California Department of Health Care Services
Mari Cantwell, Deputy Director
Health Care Financing
California Department of Health Care Services
V. David Banda, Chief
Systems for Care Division
California Department of Health Care Services
Stephen Halley, Acting Chief
Benefits & Waiver Analysis Division
California Department of Health Care Services

Hearing Aid Reimbursement Analysis

Introduction

The State Controller's Office (SCO), through an interagency agreement with the California Department of Health Care Services (DHCS), performs reviews of Medi-Cal providers at the request of DHCS. Providers that can be reviewed under this contract include audiologists and hearing aid dispensers.

In March 2011, the SCO issued a report on an audiologist that identified \$507,871 in questioned costs because the provider was unable to provide documents to support the purchase of hearing aids. During that review, the SCO auditors found a significant difference between what the provider paid for hearing aids (acquisition cost) and the amount of reimbursement the provider received under Medi-Cal's reimbursement policies. For instance, in one case, the provider had purchased a pair of binaural hearing aids for \$120 but, under Medi-Cal's reimbursement policy in effect at the time, the provider received \$1,465. While this was the most extreme example, we noted 31 similar instances of reimbursement for this particular provider.

To determine whether similar results were occurring in other providers, we undertook a non-reimbursable review of 60 claims for five additional providers. Based on the results of this review, we believe that the Medi-Cal program could save up to \$27.4 million over a three-year period by adopting an alternate reimbursement methodology.

Background

Hearing aids have been a covered benefit of the Medi-Cal program since 1972. In general, for both the monaural and binaural hearing aids, the current reimbursement is based on the one-unit wholesale cost, including sales tax, plus a specified mark-up fee, up to a set maximum. Per DHCS Operating Instruction Letter (OIL) No. 136-05, the one-unit wholesale cost is defined as the manufacturer's catalog list price to wholesalers or direct purchasers, not including discounts, rebates, or other reductions in price. The mark-up fee is intended to cover professional services for fitting of the hearing aid(s), the actual equipment purchases, and up to six patient follow-up visits.

Actual reimbursement is the lesser of the following:

- Monaural hearing aid
 - 1) \$883.80—Maximum for all allowable costs, or
 - 2) One-unit wholesale cost, including sales tax, plus a mark-up of \$256.37
- Binaural hearing aid
 - 1) \$1,480.32, or
 - 2) One-unit wholesale cost, including sales tax, plus a mark-up of \$326.08

In many instances, the wholesale cost before sales tax plus the mark-up exceeds the maximum and, as a result, the providers may not include sales tax information on the claim. In addition, effective March 2009, the maximum payments to Allied Health Providers were subject to a 1% payment reduction due to the budget deficit. For purposes of our analysis, we have used the reduced figures of \$875 and \$1,465, rounded to the nearest whole dollar. In addition, because the sales tax information is not always available, we have not included it in the data we collected and provided in this report.

Scope of Work

During our review, we performed the following tasks:

- Interviewed each of the five audiologists/hearing aid dispensers selected and audited a total of 60 claims. The claims were for dates of service in 2009. We obtained invoices and manufacturer catalogs they used to prepare the 60 claims for reimbursement.
- Compared the wholesale cost data for each claim to actual acquisition cost for the hearing aid(s). We also performed three individual analyses to determine potential savings to the State by making revisions to the current Medi-Cal reimbursement policy for hearing aid(s).
- Verified with DHCS Fiscal Intermediary (FI) the current reimbursement methodology employed. Verified reimbursed amounts from the 60 claims submitted to the FI.
- Researched data from other states to determine their Medicaid reimbursement methods for hearing aids.
- Reviewed the hearing aid reimbursement methods for California Children's Services (CCS). We also reviewed the current Medi-Cal policy for reimbursing the costs of Durable Medical Equipment (DME) products. In some states, hearing aids are considered DME.

Outcome of Analysis

Significant Discounts/Rebates to the Provider are Being Reimbursed as Costs by Medi-Cal

We found that discounts/rebates were offered to providers, resulting in a significant difference between the actual acquisition cost for the provider and the one-unit wholesale costs reported to DHCS and used for reimbursement. For example, for one claim that was reviewed, the one-unit wholesale cost for binaural hearing aids was \$1,358 each, but the actual acquisition cost to the provider was only \$456, a discount of \$902. DHCS reimbursed this provider's claim based on a claim of \$1,461 (sales tax not included). As the reported one-unit wholesale cost of \$1,358 plus the mark-up added up to \$1,514, it appears that the State saved \$53. However, because the provider only paid \$456, the \$902 discount was retained by the provider as part of the Medi-Cal reimbursement policy. Schedule 1 illustrates this claim and the results of reviews of the other 59 claims.

Different Levels of Actual Acquisition Costs are Reimbursed at the Same Reimbursement Level

In addition to the significant discounts/rebates, we found that in some cases, while the actual acquisition cost for a Medi-Cal provider can vary, the current reimbursement formula, which uses the same one-unit wholesale costs, will make little difference in the amount reimbursed by Medi-Cal. For example, as indicated in Schedule 2, we noted that the provider reimbursement amount of \$1,465 (not including sales tax) was used in 14 cases in which the actual acquisition cost to the providers ranged from \$436 to \$590 for binaural hearing aids.

Welfare and Institutions (W&I) Code section 14105.3(e) was added by Assembly Bill 203. This bill was chaptered on August 24, 2007, and required DHCS to enter into exclusive or nonexclusive contracts, on a bid or negotiated basis, for purchasing hearing aid appliances. The deadline for having this contract(s) in place was June 30, 2008. However, we understand that such a contract(s) has not yet been put in place, nearly three years after the legislature anticipated it would be completed. If these contracts were in place, the variation in actual acquisition costs that are described above would be unlikely to occur.

Quality of Care in Question

Our review of the 60 claims did not identify the same significant difference between actual cost of acquisition and the Medi-Cal reimbursement that we found in the provider that was initially referred to us by DHCS (this provider paid only \$120 for a hearing aid, but was reimbursed \$1,464), the results shown in Schedule 1 indicates that the range of costs for the 60 claims reviewed was between \$218 and \$590, depending on whether the hearing aid acquired was binaural or monaural. It is not clear that the standard of care expected from the Medi-Cal program can be met with the less expensive versions of hearing aids. Currently providers have the option to purchase hearing aids from a variety of vendors and there are no guidelines/ instructions relating to approved vendors/products from which to select.

If the contract required under W&I Code section 14105.3(e) were in place, DHCS would be in a better position to ensure that the products purchased would be consistent with the level of care expected of the Medi-Cal program.

Lack of Follow-Up Visits Documented

As noted previously, a mark-up fee is added to the claimed cost of the hearing aid to cover professional services for fitting of the hearing aid(s), the actual equipment purchases, and up to six follow-up visits. However, in interviews with four of the five providers, we found the following:

- Three of the four providers stated that patients made few follow-up visits. The remaining provider refused to estimate the number of follow-up visits that take place per patient.

- Two providers stated that not all follow-up visits were documented, and one provider stated that no follow-up visits were documented. The remaining provider stated that it kept and maintained sufficient notes regarding follow-up visits, but a review of 15 patient records pertaining to this provider disclosed that follow-up visits were documented in only four cases. The average number of visits documented in these four cases was 2.5 visits per patient. For the remaining 11 cases, the records disclosed no follow-up visits documented.

Alternatives to the Current Reimbursement Process for Hearing Aids

- Durable Medical Equipment (DME): In general, most DME products are reimbursed using a formula of actual acquisition cost plus a percentage mark-up established by DHCS. The mark-up has been established at no more than 100%. Prior to implementing this new formula, DME products also were reimbursed at wholesale costs. It is our understanding that hearing aids may be included under DME when a state Medicaid program defines hearing aids as DME.
- California Children's Services (CCS) Program: The reimbursement formula is actual acquisition cost plus 60% mark-up which is supposed to cover the same types of services as the Medi-Cal markup for hearing aids (including dispensing costs and costs for up to six follow-up visits).
- State of New York: This state uses actual acquisition costs as the start-up base for reimbursements for hearing aids. Acquisition cost is defined as the actual amount the supplying provider pays for the hearing aid(s). In addition to payment for the acquisition costs, a dispensing fee typically is associated with the reimbursement. According to a 2010 fee schedule we obtained, New York's dispensing fee is \$200 for binaural hearing aids and \$135 for monaural hearing aids. The administrative fee, which includes reimbursement for all fittings, is a component of the dispensing fee.

Potential Savings

To determine potential savings, we performed three individual analyses on the 60 claims we reviewed using the following methodologies:

- Using the current Medi-Cal methodology, but substituting the actual acquisition cost (rather than the one-unit wholesale cost) to the existing hearing aid reimbursement formula;
- Using the DME reimbursement methodology (actual acquisition cost plus a 100% mark-up); and
- Using the current reimbursement policy of the CCS program (actual acquisition cost plus a 60% mark-up).

The potential savings—calculated using the hearing aid reimbursement policy in effective prior to the issuance of OIL No. 406-11—to the Medi-Cal program would be:

	Alternative Pricing Method 1	Alternative Pricing Method 2	Alternative Pricing Method 3
	Hearing Aid Formula	DME Formula	CCS Formula
Savings in dollars	\$25,546,549	\$18,699,513	\$27,408,246
Savings in percentage	41.04%	30.04%	44.03%

The percentages were extrapolated to \$62,243,177, the total payments made by the Medi-Cal program for hearing aids for calendar years 2008 through 2010. For further details on the calculations, see Schedule 1.

The level of savings may be affected because of implementation of Assembly Bill 97 (W&I Code section 14131.05) which requires hearing aid benefits per beneficiary to be capped at \$1,510 for each state fiscal year. The bill requires DHCS to implement this provision by October 1, 2011, or 60 days after federal approval. If the \$1,510 is to replace the current maximums of \$883.80 and \$1,480.32, the level of reimbursements should go up if no change is made to the current reimbursement methodology.

Conclusion

We recommend that DHCS Medi-Cal program revise the current reimbursement policy for hearing aids as reflected in the current OIL No. 136.05, by adopting one of the alternative methodologies described above to ensure that the Medi-Cal program can benefit from any discounts and rebates given to hearing aid providers. In addition, we recommend that DHCS consider the following:

- In developing a new reimbursement methodology, consider whether the mark-up fees are needed at the current level to ensure adequate treatment.
- Provide assurance that the State is obtaining the most favorable prices by implementing the provisions of W&I Code Section 14105.3(e). As noted above, the contract(s) also can be used to ensure the quality of hearing aid products provided to Medi-Cal recipients.

**Schedule 1—
Hearing Aid Issues
Alternative Pricing Methods
(Excluding All Sales Taxes)**

Count	[A] Reimburse- ment**	[B] Acquisition Cost	[C] Alternative Pricing Method 1 (col. [B] + \$326.08)*	[D] Alternative Pricing Method 2 (col. [B] × 2)	[E] Alternative Pricing Method 3 (col. [B] × 1.6)
1	\$ 1,465.09	\$ 436.00	\$ 762.08	\$ 872.00	\$ 697.60
2	851.18	189.00	445.37	378.00	302.40
3	1,465.09	436.00	762.08	872.00	697.60
4	1,459.91	578.00	904.08	1,156.00	924.80
5	1,465.11	436.00	762.08	872.00	697.60
6	1,465.16	436.00	762.08	872.00	697.60
7	1,465.16	436.00	762.08	872.00	697.60
8	1,460.98	456.00	782.08	912.00	729.60
9	1,465.11	436.00	762.08	872.00	697.60
10	1,326.69	678.00	1,004.08	1,356.00	1,084.80
11	846.64	218.00	474.37	436.00	348.80
12	866.62	228.00	484.37	456.00	364.80
13	1,464.74	798.00	1,124.08	1,596.00	1,276.80
14	1,439.60	436.00	762.08	872.00	697.60
15	1,333.18	436.00	762.08	872.00	697.60
16	1,251.04	436.00	762.08	872.00	697.60
17	1,313.39	436.00	762.08	872.00	697.60
18	1,313.41	436.00	762.08	872.00	697.60
19	1,313.39	456.00	782.08	912.00	729.60
20	1,251.08	436.00	762.08	872.00	697.60
21	1,251.04	436.00	762.08	872.00	697.60
22	1,251.02	436.00	762.08	872.00	697.60
23	1,313.39	456.00	782.08	912.00	729.60
24	1,313.41	436.00	762.08	872.00	697.60
25	1,313.41	436.00	762.08	872.00	697.60
26	1,251.06	456.00	782.08	912.00	729.60
27	1,313.41	436.00	762.08	872.00	697.60
28	1,416.76	500.00	826.08	1,000.00	800.00
29	1,419.26	500.00	826.08	1,000.00	800.00
30	1,291.03	500.00	826.08	1,000.00	800.00
31	1,424.26	500.00	826.08	1,000.00	800.00
32	1,416.76	500.00	826.08	1,000.00	800.00
33	943.74	500.00	756.37	1,000.00	800.00
34	1,419.26	500.00	826.08	1,000.00	800.00

Schedule 1 (continued)

Count	[A] Reimburse- ment**	[B] Acquisition Cost	[C] Alternative Pricing Method 1 (col. [B] + \$326.08)*	[D] Alternative Pricing Method 2 (col. [B] × 2)	[E] Alternative Pricing Method 3 (col. [B] × 1.6)
35	1,419.26	500.00	826.08	1,000.00	800.00
36	1,419.26	500.00	826.08	1,000.00	800.00
37	1,419.26	500.00	826.08	1,000.00	800.00
38	1,291.03	500.00	826.08	1,000.00	800.00
39	1,424.26	500.00	826.08	1,000.00	800.00
40	1,419.26	500.00	826.08	1,000.00	800.00
41	1,424.26	500.00	826.08	1,000.00	800.00
42	1,450.97	550.00	876.08	1,100.00	880.00
43	1,538.45	460.00	786.08	920.00	736.00
44	1,327.42	590.00	916.08	1,180.00	944.00
45	1,450.91	550.00	876.08	1,100.00	880.00
46	1,327.75	550.00	876.08	1,100.00	880.00
47	1,465.05	460.00	786.08	920.00	736.00
48	1,464.97	590.00	916.08	1,180.00	944.00
49	1,465.10	460.00	786.08	920.00	736.00
50	1,464.97	590.00	916.08	1,180.00	944.00
51	874.69	295.00	551.37	590.00	472.00
52	1,397.45	550.00	876.08	1,100.00	880.00
53	1,469.07	460.00	786.08	920.00	736.00
54	1,465.07	460.00	786.08	920.00	736.00
55	1,465.01	550.00	876.08	1,100.00	880.00
56	1,464.97	590.00	916.08	1,180.00	944.00
57	768.03	218.00	474.37	436.00	348.80
58	768.03	218.00	474.37	436.00	348.80
59	1,328.69	436.00	762.08	872.00	697.60
60	874.75	225.00	481.37	450.00	360.00
	<u>\$ 79,268.32</u>	<u>\$ 27,727.00</u>	<u>\$ 46,734.12</u>	<u>\$ 55,454.00</u>	<u>\$ 44,363.20</u>

NOTE: The potential savings were calculated using the hearing aid reimbursement policy in effective prior to the issuance of OIL No. 406-11.

* The mark-up allowed by Medi-Cal is \$326.08 (binaural) or \$256.37 (monaural) for fittings and up to six patient follow-up visits. We are adding it to the acquisition costs for comparative purposes.

** If a provider submits documentation, its total reimbursement will include the sales tax actually paid. For comparative purposes, and to project savings, sales tax was excluded. Therefore, column [A] does not include any sales tax that was reimbursed. In addition, effective March 2009, payments to Allied Health Providers were reduced by 1% due to the State budget deficit. That reduction is included in the amounts in column [A], where applicable.

Schedule 1 (continued)

Calculated and Projected Savings

Alternative Pricing Method 1:

Savings in dollars	\$46,734	
Saving percentage	41.04%	(1.00 – (col. [B] ÷ col. [A])
Total projected savings*	\$25,546,549	(\$62,243,178 × 41.04%) ³

Alternative Pricing Method 2:

Savings in dollars	\$55,454	
Saving percentage	30.04%	(1.00 – (col. [C] ÷ col. [A])
Total projected savings*	\$18,699,513	(\$62,243,178 × 30.04%)

Alternative Pricing Method 3:

Savings in dollars	\$44,363	
Saving percentage	44.03%	(1.00 – (col. [D] ÷ col. [A])
Total projected savings*	\$27,408,246	(\$62,243,178 × 41.04%)

NOTE: Variances are due to rounding. The potential savings were calculated using the hearing aid reimbursement policy in effective prior to the issuance of OIL No. 406-11.

* Projected savings was calculated using total amount spent on hearing aid procedures from January 2008 through December 2010 (\$62,243,178).

**Schedule 2—
Hearing Aid Issues
One-Unit Wholesale Cost
Compared With Actual Cost**

Count	Reimbursement Minus Sales Tax (Invoice)	One-Unit Wholesale Cost (List Price)	Acquisition Cost	Difference Between One-Unit Wholesale Cost and Acquisition Cost
1	\$1,465	\$1,218	\$436	\$782
2	\$1,465	\$1,178	\$436	\$742
3	\$1,465	\$1,178	\$436	\$742
4	\$1,465	\$1,178	\$436	\$742
5	\$1,465	\$1,178	\$436	\$742
6	\$1,465	\$1,178	\$436	\$742
7	\$1,465	\$1,238	\$460	\$778
8	\$1,469	\$1,238	\$460	\$778
9	\$1,465	\$1,238	\$460	\$778
10	\$1,465	\$1,220	\$460	\$760
11	\$1,465	\$1,530	\$590	\$940
12	\$1,465	\$1,488	\$590	\$898
13	\$1,465	\$1,488	\$590	\$898
14	\$1,465	\$1,254	\$550	\$704

NOTE: The potential savings were calculated using the hearing aid reimbursement policy in effective prior to the issuance of OIL No. 406-11.