



Auditor of Public Accounts  
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**Auditor Edelen releases special report on the financial strength of rural hospitals**  
*Study finds one-third in poor financial health, raises concerns about maintaining adequate access to health care in rural Kentucky*

**FRANKFORT, Ky. (March 30, 2015)** – Auditor Adam Edelen has released a special report on the financial strength of rural hospitals, finding that a majority of Kentucky’s rural hospitals fared below the national average in assessed financial strength and one-third were in poor financial health.

The report raises concerns about maintaining adequate access to health care in rural Kentucky and makes recommendations intended to help rural hospitals as the health care landscape undergoes a rapid and challenging transformation.

“The importance of rural hospitals cannot be overstated,” Auditor Edelen said. “They provide healthcare to 45 percent of Kentuckians and serve a disproportionate share of low-income and elderly citizens. In many rural communities in particular, hospitals are the first or second largest employer and typically pay higher-than-average wages than other employers.”

Auditor Edelen emphasized that the report is not a rebuke of Medicaid managed care, Kentucky kynect or Medicaid expansion, which has resulted in a net gain of jobs and expanded access to nearly 400,000 Kentuckians.

“What this report is about is making sure that in rural Kentucky, the newly insured and those who already had coverage have adequate access to health care,” Auditor Edelen said. “This study is intended to provide policymakers with a baseline for monitoring the financial health of our rural hospitals and recommendations to help these hospitals adapt their models for delivering health care in the 21<sup>st</sup> century.”

The primary focus of the report was on utilizing a proprietary formula called the Financial Strength Index<sup>®</sup>, or FSI<sup>®</sup>, to assess the financial strength of 44 rural hospitals that agreed to participate in this study. The FSI<sup>®</sup> considers the percentage of revenue kept as profit, number of

days of cash on hand, debt financing and depreciation. The Auditor's office also surveyed rural hospital administrators, held 11 public hearings across Kentucky, met with representatives of all five Medicaid Managed Care Organizations (MCOs) and analyzed ad hoc reports about provider types.

Auditors found that 68 percent of Kentucky's rural hospitals scored below the national average on the FSI<sup>®</sup> and one-third scored low enough to be considered in poor financial health. The hospitals that scored below the national average had 838,000 patients last year, with the majority on Medicaid or Medicare.

The Auditor's office did not conduct a comprehensive review of the financial situation facing all 44 hospitals evaluated in the FSI<sup>®</sup>, but some themes emerged during the study. For example, rural hospitals that are geographically well-positioned, such as Pikeville Medical Center, scored high. On the flip side, geographically-isolated hospitals in Clinton and Wayne counties scored low.

"Those hospitals are vital to their communities due to their distances to larger, regional hospitals," Auditor Edelen said.

At least two rural hospitals – St Claire Regional Medical Center in Morehead and Highlands Regional Medical Center in Prestonsburg – have joined a coalition to provide efficiencies, improve patient access and adapt to changes under the Affordable Care Act.

Responding hospitals indicate on average 72 percent of patients received Medicaid or Medicare, meaning a significant number of low-income and elderly patients are affected if rural hospitals cannot stay afloat. The financial situation facing these hospitals could become more difficult as the percentage of private pay patients declines, the Disproportionate Share Hospital (DSH) payments go away and the federal government makes cuts to Medicare fee-for-service payments.

"While expansion has decreased the amount of uncompensated care that hospitals were previously burdened with, there are new challenges lurking on the horizon," Auditor Edelen said. "We need to get in a position where we are monitoring the impact so we don't get caught off guard by a rural hospital and major employer in a community going under."

Auditors also assessed the impact that Medicaid managed care is having on rural hospitals, finding that the administrative burdens on these facilities have increased since its implementation. Administration costs have increased an average of \$157,000 in total for all respondents combined and half report administrative hours have increased and they have had to hire new administrative personnel and increase overtime.

"Five different MCOs have five different sets of rules and five different sets of paperwork," Auditor Edelen said. "For a hospital with a couple hundred employees or less, that's a serious administrative burden. We've reached a point where some rural hospitals are faced with laying off front-line workers responsible for providing patient care to hire people to fill out forms. That's not acceptable."

Weaknesses in the contracts between the Cabinet and MCOs also appear to be contributing to the declining financial health of many providers. MCO representatives themselves used words like “soft” and “loose” to describe the penalties for contractual noncompliance. Auditors found several areas for improvement, such as strengthening penalties, improving the ability of the Cabinet for Health and Family Service (CHFS) to monitor quality and programmatic requirements and improving transparency. Auditors also recommended establishing restrictions on triage fee caps, which appear to be causing a significant financial burden for some hospitals.

Auditors found the number of providers across the Commonwealth – particularly in rural Kentucky – dropped significantly between 2013 and 2014.

“The drop confirms our fears that many of our providers are struggling to make the transition to a new health care delivery model,” Auditor Edelen said. “It’s important that policymakers get engaged and help ensure that access to care in rural Kentucky remains intact.”

Auditor Edelen recommends that CHFS begins using a tool to regularly monitor the fiscal strength of rural hospitals, particularly Critical Access Hospitals and those that are in poor and fair financial health.

He also recommends that the Governor convene a task force to examine, among other objectives, new models for rural health delivery to ensure quality of care and continued access. The group should evaluate solutions such as affiliations, coalitions and other opportunities for innovation and whether the current regulatory structure gives hospitals the flexibility to retool their business models.

In addition, Auditor Edelen recommends CHFS improve relations with providers and strengthen penalties in MCO contracts.

“We are at a critical juncture in the journey to improving the health of Kentuckians,” Auditor Edelen said. “We’ve made significant strides toward getting more people insured, but we have to make sure those individuals, many of whom are poor and elderly, have places to access care.”

The full report can be found on the [Auditor’s website](#).

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