



## ANALYSIS OF PROPOSED ARIZONA MEDICAL FEE SCHEDULE UPDATE ASSUMED TO BE EFFECTIVE OCTOBER 1, 2016

**NCCI estimates that the proposed changes to Arizona's Medical Fee Schedule, assumed to be effective October 1, 2016, would result in an estimated overall increase in workers compensation system costs in Arizona of +0.4% (\$3.0M<sup>1</sup>).**

### Summary of Changes

The current Arizona Medical Fee Schedule (MFS) was adopted by the Industrial Commission of Arizona (ICA) effective October 1, 2015. The proposed MFS, which contains revisions to the maximum allowable reimbursements (MARs) in the current MFS, did not contain an effective date. For this analysis, NCCI has assumed an effective date of October 1, 2016.

### Actuarial Analysis

NCCI's methodology to evaluate the impact of medical fee schedule changes includes three major steps:

1. Calculate the percentage change in maximum reimbursements
  - a. Compare the current and proposed maximum reimbursements by procedure code and determine the percentage change by procedure code
  - b. Calculate the weighted average percentage change in maximum reimbursements for the fee schedule using observed payments by procedure code as weights
2. Estimate the price level change as a result of the revised fee schedule
  - a. NCCI research by Frank Schmid and Nathan Lord (2013), "The Impact of Physician Fee Schedule Changes in Workers Compensation: Evidence From 31 States", suggests that a portion of a change in maximum reimbursements is realized on payments impacted by the change.
    - i. In response to a fee schedule decrease, NCCI research indicates that payments decline by approximately 50% of the fee schedule change.
    - ii. In response to a fee schedule increase, NCCI research indicates that payments increase by approximately 80% of the fee schedule change and the magnitude of the response depends on the relative difference between actual payments and fee schedule maximums (i.e. the price departure).  
The formula used to determine the percent realized for fee schedule increases is  $80\% \times (1.10 + 1.20 \times (\text{price departure}))$ .

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<sup>1</sup> Overall system costs are based on NAIC Annual Statement data. The estimated dollar impact is the percentage impact(s) displayed multiplied by 2014 written premium of \$818M from NAIC Annual Statement data for Arizona. This figure does not include self-insurance, the policyholder retained portion of deductible policies, or adjustments for subsequent changes in premium levels. The use of premium as the basis for the dollar impact assumes that expenses and other premium adjustments will be affected proportionally to the change in benefit costs. The dollar impact on overall system costs inclusive of self-insurance is estimated to be \$4M, where data on self-insurance is approximated using the National Academy of Social Insurance's August 2015 publication "Workers' Compensation: Benefits, Coverages, and Costs, 2013."



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3. Estimate the share of costs that are subject to the fee schedule
  - a. The share is based on a combination of fields, such as procedure code, provider type, and place of service, as reported on the NCCI Medical Data Call, to categorize payments that are subject to the fee schedule.

In this analysis, NCCI relies primarily on two data sources:

- Detailed medical data underlying the calculations in this analysis are based on NCCI's Medical Data Call for Arizona for Service Year 2014.
- The share of benefit costs attributed to medical benefits is based on NCCI's Financial Call data for Arizona from the latest two policy years projected to the assumed effective date of the benefit changes.

Physician Fee Schedule

In Arizona, payments for physician services represent 33.1% of total medical payments. To calculate the percentage change in maximums for physician services, we calculate the percentage change in maximums for each procedure code which is published by the ICA. The overall change in maximums for physician services is a weighted average of the percentage change in MAR (proposed MAR/ current MAR) by procedure code weighted by the observed payments by procedure code as reported on NCCI's Medical Data Call, for Arizona for Service Year 2014. The overall weighted average percentage change in MARs is estimated to be +2.0%.

The estimated impact by category of the proposed medical fee schedule changes is shown in the table below.

<b>Physician Practice Category</b>	<b>Share of Physician Costs</b>	<b>Estimated Impact</b>
Anesthesia	3.3%	0.0%
Surgery	21.2%	+2.3%
Radiology	9.5%	+4.7%
Pathology & Laboratory	0.9%	+2.2%
Medicine	1.7%	+6.4%
Physical Medicine	30.1%	+1.9%
Special Services	0.2%	+3.1%
Evaluation & Management	25.6%	+1.5%
Physician Payments with no specific MAR	7.5%	0.0%
<b>Total Physician Costs</b>	<b>100.0%</b>	<b>+2.0%</b>



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Since the overall average maximum reimbursement for physicians increased, the percent expected to be realized from the fee schedule increase is estimated according to the formula  $80\% \times (1.10 + 1.20 \times (\text{price departure}))$ . The observed price departure for physician payments in Arizona is  $-16\%^2$ . The percent realized is estimated to be  $73\% (= 80\% \times (1.10 + 1.20 \times (-0.16)))$ . The estimated impact on physician payments due to the proposed physician fee schedule change is  $+1.5\% (= +2.0\% \times 0.73)$ .

The above estimated impact of  $+1.5\%$  is then multiplied by the Arizona percentage of medical costs attributed to physician payments ( $33.1\%$ ) to arrive at the estimated impact on medical costs of  $+0.5\%$ . The resulting estimated impact on medical costs is then multiplied by the percentage of Arizona benefit costs attributed to medical benefits ( $76.5\%$ ) to arrive at the estimated impact on Arizona overall workers compensation costs of  $+0.4\%$  ( $\$3.0M$ ).

The estimated impacts from the proposed updates to the Arizona Medical Fee Schedule are summarized in the following table:

	(A)	(B)	(C)	
	Estimated Impact on Type of Service	Share of Medical Costs	Estimated Impact On Medical Costs (A) x (B)	
<b>Physician</b>	+1.5%	33.1%	+0.5%	
(1) Estimated Impact on <b>Arizona</b> Medical Costs			<b>+0.5%</b>	
(2) Medical Costs as a Percentage of Overall Workers Compensation Benefit Costs in <b>Arizona</b>				76.5%
<b>(3) Estimated Impact on Overall Workers Compensation System Costs in Arizona = (1) x (2)</b>				+0.4%

<sup>2</sup> A departure of  $-16.0\%$  implies that the ratio of actual payments to the fee schedule maximums is 0.84