

Calculation and Application of the Inflation Factors

Because Medicaid payment rates are based on facility costs incurred during a past reporting period (the Base Year), the Base Year costs must be updated to take into account changes in economic conditions that are expected in the period during which the rates will be in effect. The expected changes in economic conditions are reflected in the Inflation Factors, which are applied to certain categories of Base Year costs. As required by V.D.R.S.R. §5.8(f), this Practice and Procedure Issuance explains how the inflation factors are calculated and applied to the Base Year costs.

CALCULATION OF INFLATION FACTORS

V.D.R.S.R. §5.8 requires the Division to use a number of different indices as the basis for calculating the Inflation Factors, all of which are available quarterly as prepared for the *Health Care Cost Review*, published by DRI/McGraw-Hill, and available on diskette from DRI/McGraw-Hill. Each issue of this publication includes both historic data and forecasts. For each index required by V.D.R.S.R. §5.8, the most recently updated historic and forecast data is used.

The following indices are used, pursuant to V.D.R.S.R. §5.8(a)-(e):

Cost Category	Subcomponent	Index
Nursing Care	Wages and salaries	DRI-NHMB ¹ wages and salaries portion
	Employee Benefits	DRI-NHMB employee benefits portion
Resident Care	Wages and Salaries	DRI-NHMB wages and salaries portion
	Employee Benefits	DRI-NHMB employee benefits portion
	Food	NECPI-U ² food-at-home portion
	Utilities	NECPI-U producer price index - commercial electric power,
	All other Resident Care costs	NECPI-U (all items)

¹ DRI-NHMB is the Nursing Home without Capital Market Basket Index developed by DRI for the Health Care Financing Administration.

² NECPI-U is the New England Region Consumer Price Index - All Urban historical data developed by the U.S. Bureau of Labor Statistics and forecasts by DRI.

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Cost Category	Subcomponent	Index
Indirect	Wages and Salaries	DRI-NHMB wages and salaries portion
	Employee Benefits	DRI-NHMB employee benefits portion
	All other Indirect costs	NECPI-U (all items)
Director of Nursing	Wages and Salaries	DRI-NHMB Wages and Salaries
	Employee Benefits	DRI-NHMB employee benefits portion

The Inflation Factor for each cost category is calculated in two steps:

1. The changes to each index are calculated by comparing the average of the four quarters in the Base Year with the average of all quarters in Rate Year (the State fiscal year during which the rate is in effect). For example, for the 1997 Rate Year, the four quarters covering the Base Year (first to fourth quarters of 1994) are compared to the average for the state fiscal year (the third and fourth quarters of 1996 and the first and second quarters of 1997). The percentage changes between the two periods are used in the calculation of the Inflation Factors.

2. The Inflation Factors are based on the average Base Year costs incurred in each category and its subcomponents by all the Vermont facilities participating in the Medicaid program. The Inflation Factor for each cost category is calculated using the required indices, with the relative weight for each index based on the proportion of its related cost subcomponent to the total category cost.

The Division will publish the data used for each year's inflation factor calculations in its annual *Fact Book* for July.

APPLICATION OF THE INFLATION FACTORS

Only the rates for cost categories (and rate adjustments related to those categories) listed in the table above are revised using the Inflation Factors. The Inflation Factor for each cost category is applied to each individual facility's Base Year costs³ for that category in order to update those costs for the changes in economic conditions between the Base Year and the Rate

³ Base Year costs for cost reporting periods other than those ending on December 31 are adjusted to the calendar year end before the annual Inflation Factors are applied.

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Year. For the Nursing Care cost category, the inflation factor is applied to the Base Year cost per case-mix point.

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s/Veronica Celani
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