Sweeping Changes to Knox-Keene Licensing Requirements Coming

Insights

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On Friday, January 25, 2019, the Department of Managed Health Care (DMHC) published its latest draft of a proposed regulation that will dramatically expand the scope of arrangements subject to licensure under the Knox-Keene Act. The regulation breaks with the DMHC's longstanding policies and threatens to disrupt common provider payment arrangements in California, including hospital risk pools, bundled payment arrangements, and accountable care organizations (ACOs), and to stifle innovation in the area of value-based payments.

Under the proposed regulation, a Knox-Keene license would be required for an entity to accept "global risk," which is defined as the acceptance of a "prepaid or periodic charge" in exchange for assuming "both professional and institutional risk." (28 C.C.R., proposed § 1300.49, subds. (a) & (b)(1).) The statute has long defined health care service plans in reference to providing or arranging for health care services in exchange for a "prepaid or periodic charge." However, the regulation provides a new definition of that term that encompasses payments made "at the start or end of a predetermined period… that may be fixed either in amount or percentage of savings or losses in which the entity shares." (28 C.C.R., proposed § 1300.49, subd. (a)(4).) Providers that engage in shared risk arrangements, which involve fee-for-service payments with shared savings payable after a set period of time, even those involving upside risk *only*, may be subject to licensure under the new rule.

- *What would the new regulation do?* The proposed regulation would require an entity to obtain a Knox-Keene license in order to engage in a range of payment arrangements that involve the assumption of upside and/or downside risk for professional and institutional services. As an alternative, the proposed regulation would allow an entity to seek an exemption from the licensure requirement from the DMHC.
- *Who would be affected?* The new regulation would affect health systems, medical groups, independent practice associations (IPAs), skilled nursing facilities (SNFs), and any other entity that engages in risk-sharing arrangements.
- *When will the new regulation take effect?* The proposed regulation still faces review by the Office of Administrative Law (OAL), which has thirty working days to review the proposed regulation. If the OAL approves the rule by February 28, the rule will take effect April 1. If the OAL rejects the rule or does not act on it by February 28, then the rule's effective date could be pushed to July 1 or later.
- *What arrangements are affected?* The proposed regulation would apply to arrangements entered into, amended or renewed on or after its effective

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- *How can my organization obtain an exemption?* The regulation requires the Director of the DMHC to grant an exemption if it determines that doing so is in the "public interest" and "not detrimental to the protection of subscribers, enrollees or persons regulated under the Knox-Keene Act." The regulation describes the criteria the Director should consider in determining whether to grant an exemption – including the level of risk assumed by the entity, the entity's market share, and the potential negative impact to the region if the entity fails to maintain financial solvency – but it does not establish any bright-line rules to identify which entities may be eligible for an exemption.

The Rulemaking Process

The DMHC has already engaged in several rounds of notice and comment. After publishing three initial drafts and providing the public with three opportunities to comment, the DMHC provided the OAL with what it described a "final" version of the regulation. The OAL rejected that draft, citing DMHC's failure to follow required procedures in providing an economic impact statement and its failure to provide sufficient clarity in describing the exemption process. The DMHC responded to those concerns in a fourth draft and gave the public another opportunity to comment. The version published last Friday responds to comments provided in response to the fourth draft, though the DMHC largely declined to make changes in respond to those comments.

Next Steps

It appears likely that the OAL will approve the proposed regulation by February 28, clearing the way for the rule to take effect April 1. HLB encourages its California clients to review their payment agreements, particularly those that involve the acceptance of upside or downside risk for the provision of health care services. It may be prudent to extend the expiration date of existing arrangements prior to the regulation's effective date in order to put off the impact of the new regulation, develop alternative financial arrangements, or begin the process of seeking an exemption from the licensure requirement from the DMHC.

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