regulations have been in effect. Further, our measure avoids the problems with the Mayo and McFarland measure discussed above.

We enter the effect of CON regulation into our cost function both linearly and multiplied by the number of patient days of care provided. It seems reasonable to assume that any effect of CON will be greater in larger hospitals. This formulation allows for such an effect.

Other variables in our model are generally defined similarly to those used by Mayo and McFarland, though they differ in minor ways. Our wage variable is the average wage of nurses in a particular institution, rather than the average wage of all employees.[15] By reducing the types of employees included in the wage measure, we should reduce the amount of variation resulting because different hospitals use types of employees in different proportions. Our beds variable is the average number of beds set up and staffed, rather than the number of licensed beds. Our variables differentiating types of hospitals follow Sherman [18] and differ from those used by Mayo and McFarland. These variables -- PROFIT, NONFED, TEACH1, TEACH2, and TEACH3 -- are defined, along with the other variables in our model in Table 1.

Our results are reported in Table 2 for the cost equation and in Table 3 for the beds equation. Looking first at the cost equation, CON regulation is found to have a significant effect on hospital variable costs. Variable costs are increased by more than $175,000 plus about

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[15] Our wage variable is calculated as total nursing wages paid by the hospital divided by the sum of full time equivalent registered nurses (RNs) plus full time equivalent licensed practical nurses (LPNs). Full time equivalents are equal to the sum of full time nurses plus one-half of part time nurses.