MESSAGE FROM THE DIRECTOR OF HEALTH ON FY 04-05 BUDGET

Introduction

As I have previously reported to the Health Commission, the City is currently facing a very significant revenue shortfall. The local economy has not significantly improved. The County, the State, and the Federal government are all facing substantial revenue shortfalls. Unlike the State and the Federal government, the County is strictly forbidden by the State Constitution from borrowing money for operating expenses. Therefore, one way or another, the City will have to balance its budget.

The Mayor's budget staff is forecasting a shortfall of $260 million. This includes an estimated loss from the State Budget of $100M. This estimate assumes approval of a $15 billion state bond on the ballot for this March. Should that bond measure fail, the State loss will likely be much greater.

Following is a listing of issues that comprise the $260 million shortfall.

Starting General Fund Balance & Reserves	($ 38M)
General revenue growth	$ 55M
Loss of one-time sources	($ 65M)
Fixed labor cost increases	($ 25M)
Benefit cost increases	($ 57M)
Debt, welfare, and other fixed costs	($ 30M)
Estimated loss from State Budget	($100M)
Total Projected Shortfall	($260M)

The above shortfall assumes that city employees continue to pay the 7.5% of their retirement contribution. If this were not the case the deficit would be greater.

The Health Department's General Fund subsidy represents 20% of the city's discretionary General Fund budget. Twenty percent of the projected shortfall is $52M.

Although the County will undoubtedly be looking at new fees, its important to remember that tax increases would need approval from the voters; the next election on which a County revenue measure could be placed would be November 2004. The last revenue increase placed on the ballot (a doubling of the real estate transfer tax for properties sold for more than one million dollars) lost. Therefore, it is unlikely that the City will be able to budget significantly higher revenues for the coming year.

In recognition of these difficult times the Mayor's Budget Office has given us the following instructions.

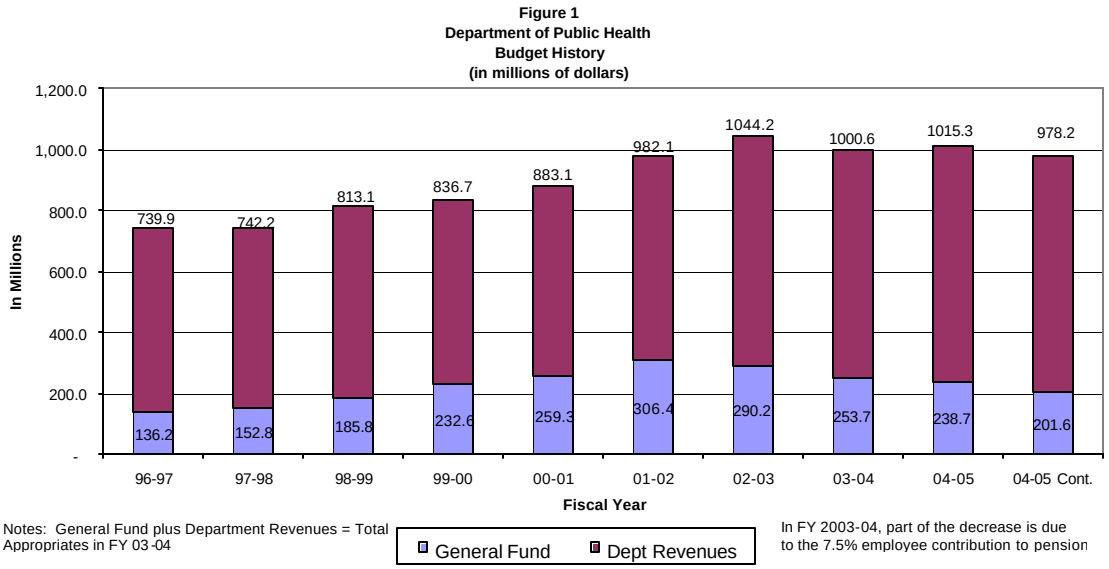
- Departments are to absorb any structural, inflationary, and regulatory cost increases.

- Departmental budgets should assume the absorption of a target equal to a 5.5% reduction in the General Fund contribution equal to the projected citywide benefit cost increase of $55M. For us, that is a General Fund reduction of $13.06M.

- Only ongoing savings may be proposed to meet this initial target. All position eliminations resulting in lay-offs, or reductions to funding for community organizations must be scheduled for September 1st, 2004. This is a change from prior years when reductions went into effect in July. This change allows the Board of Supervisors to fully consider the service impact, but also magnifies the size of the needed cuts since the reductions will only produce 5/6th of the annual savings.

- In addition, departments are instructed to submit a prioritized State contingency plan equal to 15% of the budget year General Fund support or $37.1 million.

Constructing a budget under these circumstance will be extremely difficult. Also making reductions is harder this year than last year because our General Fund has been steadily decreasing since its peak in FY 2001-2002. This can be seen in Figure 1.



Note that these amounts are not adjusted for health care inflation. Only 25% of our budget comes from the General Fund. To maintain our service array despite decreasing General Fund during the past 3 years we have been increasing our revenues, decreasing our administrative expenses, and making sensible program consolidations/restructuring. Cutting services that produce revenue does not help us to balance our budget. Cuts must therefore be concentrated in narrow areas.

For Fiscal Year 03-04, the reductions in the General Fund were achieved through the following methods:

Cost increases before MOU concessions	($22,563,000)
Increased revenues	28,526,000
Administrative Eliminations	8,446,000
Service Eliminations	4,785,000
Unionized Staff Paying Own Retirement (7.5% giveback)	17,306,000
Reduction to General Fund	$36,500,000

Having made this substantial reduction in our General Fund last year, in addition to the decreases in the two previous years, it is difficult for us to generate similar increases in revenue, or generate decreases due to administrative eliminations and programmatic restructuring.

Before we can even begin to address the request to decrease our General Fund, we must take into account the unavoidable costs of doing business resulting from structural, inflationary, and regulatory issues. These are discussed below and shown in greater detail on the attached spreadsheets.

Inflationary Increases/Unavoidable Increases in doing business

In building this year's budget we have also been challenged by significant inflationary increases in the cost of providing health care. Inflationary increases occur due to unavoidable price increases on products or services that we currently rely on. National reports show that health care inflation is running at a rate greater than 10% per year.

Wherever possible we have tried to deal with inflationary costs by decreasing our level of utilization. But in several areas, that is impossible. The largest inflationary increases are for the nurse's step adjustments in the MOU approved by the Health Commission and Board of Supervisors.

We project additional unavoidable inflationary increases at $10.3M, as shown below.

Pharmaceutical Utilization at SFGH, Community Programs, LHH, & Jail Health	$ 1,385,370
Nurses step increases	$7,176,577
UC contract – Supply and labor costs required by MOU	$1,400,000
Rent Increases – Direct Access to Housing	$321,708
Total Inflationary increases	$10,283,655

Structural Problems

We also recognize that our current budget has significant structural problems of $13.6M. A structural problem exists when the dollars allocated are insufficient to support the level of compensation to employees or services to clients currently being provided. For example, the Health Commission is aware that we are not fully appropriated for our expenses in providing jail health. Since the level of service we provide is determined by the census at the jail and our MOU's with our labor partners, this money will be spent by the Department regardless of whether it is appropriated. The result of failure to appropriate the dollars is that it puts our budget in deficit, giving the impression that we are overspending our allocation when in fact our allocation is too low to fund the necessary programs.

Worker's compensation expenses SFGH, PC, Jail Health	$ 1,724,468
Premium & holiday pay – SFGH	$ 1,608,975
Backfill mandatory paid time off for Nurse training	$1,067,000
Jail Staffing at Required Levels, including fringe benefits	$ 2,280,258
Laguna Honda Staffing at required levels	$1,500,000
Laundry contract for 03-04 outsourcing of LHH Laundry	($104,358)
Radiology, Pharmacy and Nurse Registry contracts – SFGH	$891,000
Siemens Invision increases to processing SFGH & PC billings	$240,000
RN Uniform Allowance	$221,300
Environmental Services staffing to industry benchmarks –SFGH	$219,957
Underfunding of Pharmacy Service Contract (PCN)	$651,000
Underfunding for materials and supplies – SFGH	$2,804,000
Increased security costs for Ward 93 – SFGH	$110,720
Increased Utilization of NAPA beds	$403,286
Total Increases due to Structural problems	$13,617,606

New regulatory requirements

Our institutions SFGH, LHH, and Jail Health work in a tight regulatory environment where our staffing is determined by a combination of licensing requirements (DHS), accreditation requirements (JCAHO), legal mandates (OSHA & DOJ), voter approved mandates and our collective bargaining agreements with our labor partners.

For example, our base budget includes an increase of 10.5 FTEs at a cost of $966,250 to comply with a new law, AB394, which requires increased staffing in the emergency department and in the Psychiatry Inpatient Department. (This annualizes the baseline budget that funded the period from 1-1-04 to 6-30-04.)

Our base budget also includes $1,973,249 to comply with Proposition C, which expands the Controller's funding to expand their role to support City Departments with management audit and consulting services.

We have included $100,000 to comply with SB151, which mandates new standards for printing prescriptions.

Nursing Ratio Title 22 Staffing	$966,250
Proposition C funding to City Controller	$1,973,249
SB151 Compliance – Pharmacy	$100,000
Total Increases due to regulatory environment	$3,039,499
Total Increases due to Structural, Inflationary and Regulatory requirements	$26,940,760

Revenue Neutral Programs

One fortuitous aspect of our ability to generate revenue is that in a few cases we are able to create new services, which are funded entirely through revenues linked to the services. In this budget we propose five such initiatives.

	Expend	Revenue	General Fund
Expand PC Medi-Cal eligibility staff	$ 70,131	$132,193	($62,062)
Expand interventional drug studies	$ 49,091	$ 60,000	($10,909)
DHS CALWORKS backfill	$150,000	$150,000	0
Cover increased Expenses in the Adult Immunization Clinic with Revenues	$197,817	$214,020	($16,203)
Annualization of EPSDT Pilot Project	$119,016	$119,016	0
Replace Mayor's local Law Enforcement Block Grant	$89,980	$89,980	0
Women's Health Center Business Expansion Plan	$332,083	$332,083	0
Mobile Ophthalmology Service (Eye Van)	$127,000	$159,822	$32,322
Total Revenue Neutral Programs	$1,135,618	$1,257,114	($121,496)

Increased Revenues

By increasing revenues we are able to decrease the size of the General Fund reductions that we must make. This is consistent with our Strategic Planning initiative to adopt a financial strategy that enhances revenue and reduces expenditures to ensure that the overall public health system operates cost-effectively.

I am proud that the Department is increasing revenues in the following areas:

SFGH	$ 8,535,963
Central Admin (Initiative to charge for parking at all DPH sites)	$ 622,468
Public Health	$ 1,248,300
LHH	$ 641,293
Mental Health	$ 4,165,000
Environmental Health	$ 1,133,169
Substance Abuse	$ 458,889
Total increased revenues	$16,835,082

Next Steps

It is our practice to present the Department's budget to the Health Commission at its first and second scheduled meetings in February. This year, however, given the serious nature of the program reductions that will be required to balance the budget and the impact of such reductions on public health, the Mayor has asked for additional time to review our baseline budget. We therefore do not have a balanced budget to present to you at this time. We will return to the Health Commission with a full budget presentation as soon as we are able to schedule a meeting.