

State and Federal Budget Highlights: Effects on MemorialCare and the Health Care Industry

All financial experts declare that our nation and state are in the worst recession in at least a generation, possibly the worst since the Great Depression. It does not take economic scholars to tell us that we are in hard times. Indeed, every household and every business in America is feeling the pinch. As a result of decreased revenues from personal income, business and capital gains, government reimbursement for providing care to the uninsured and under-insured is at its lowest levels. As a not-for-profit health care system, we depend greatly on the state and federal government's fair (and timely) reimbursements for services to Medi-Cal and Medicare patients. Continuing reductions in these payments are extremely problematic. In FY 08, MemorialCare derived more than 59% of its gross revenue from Medi-Cal and Medicare. This figure includes both Fee-For-Service and Managed Care Medi-Cal/Medicare. Any additional reductions in reimbursements will have a potentially devastating effect on our ability to continue the service our communities have come to expect. Sadly, the state and federal budgets for the next few years do not hold promise for any relief from these lower reimbursements.

State Budget Highlights

Governor Schwarzenegger signed the 2008-09 budget on September 23, 85 days into the state's fiscal year. The budget called for 10% reductions in Medi-Cal reimbursements for all outpatient services through March 1, 2009 (9% of which has been rescinded leaving a 1% reduction), and 10% reductions for all inpatient services provided at non-CMAC contracting hospitals (AMMC, OCMC and SMMC). By mid-fiscal year, the state was already \$14.2 billion in deficit with a projected \$42 billion deficit through June 30, 2010. The Governor brought the legislature back into Extraordinary Session, requiring the legislature to address the shortfall within 45 days. Subsequently, a party-line bill was vetoed and negotiations continued. On February 19, the legislature passed a 17-month spending plan with the minimum votes required. Negotiations were very tense, and all-night sessions were held. Following the Governor's signature on February 20, Barry Arbuckle was quoted in dozens of newspapers nationwide as saying "MemorialCare recognizes the tireless determination and leadership by the Governor and Legislature to finalize California's budget and although this is not a resolution to California's financial crisis, it is a step in the right direction... MemorialCare will continue to offer its expertise to the legislature and administration to jointly identify long-term solutions to California's broken health care system."

While the plan does not include any further cuts in provider reimbursements, it does call for potential cuts in Medi-Cal optional benefits and tighter eligibility requirements. The budget plan includes \$15 billion in programmatic cuts and spending reductions, \$12.8 billion in temporary tax increases and \$11.4 billion in borrowing. The budget redirects \$54.2 million from county and UC hospitals through the Safety Net Care Pool (SNCP) fund to backfill the General Fund. MemorialCare is exempted from the SNCP, however, we can expect increased uninsured and Medi-Cal patients to access care at our facilities due to decreased funding at these public facilities. The tighter eligibility requirements are designed to slow the rate of increase in Medi-Cal enrollment. As more people lose their employer-based health benefits, and experience a more strident enrollment process, more Californians will not have direct access to a medical home. The data is clear; people tend to delay care, and require services at our EDs when they do not have that medical home.

As part of the final budget agreement, the legislature put five initiatives on a May 19 special ballot asking voters to approve the new revenue streams. Passage of measures 1A-1E is critical to keep the budget in balance (the Legislative Analyst's Office report is described below). Early polling shows voters are likely to support these constitutional amendments:

- Prop 1A – Spending Cap. The Budget Stabilization Act otherwise known as the Rainy Day Fund. The measure caps spending by limiting the amount of revenue that can be appropriated for GR purposes. Three percent of the GF, along with unanticipated revenue increases will be placed into a reserve fund to be used in economic downturns. Prop 1A is polling at 57% Yes, 21% NO and 22% Undecided.
- Prop 1B – Supplemental Education Payments. Voters approved Prop 98 in 1990 mandating that approximately 48% of the GF is directed to K-14 education. This constitutional amendment recognizes \$9.3 billion in funding obligations in past years and begins repayments in FY 11-12. Enactment of this measure is conditioned upon passage of Prop 1A. Prop 1B is polling at 53% Yes, 30% No and 17% Undecided.
- Prop 1C – California State Lottery. This proposition securitizes the state lottery and adjusts the annual calculating method. Although Prop. 1C is polling well, it is the only measure polling below 50%; it is at 47% Yes, 39% No and 14% Undecided.
- Prop 1D – Reallocation of Prop 10 (First 5 Commission Funds). This constitutional amendment revises certain provisions of Prop 10, the California Children and Families Act which was approved by the voters in 1998. Designated funds under Prop 10 will be redirected to support state health and human services programs for children 0-5 years of age. Prop 1D is polling at 54% Yes, 24% No and 22% Undecided.
- Prop 1E – Reallocation of Prop. 63 (Mental Health Funds). This measure allows \$227 million of the Mental Health Services Act (MHSA) in FY 09-10 and up to \$234 million in 10-11 to be redirected to support the Early and Periodic Screening and Diagnostic Treatment Program. The EPSDT is a Medicaid requirement and is designed to improve the health of low income children by financing appropriate and necessary pediatric services. Miller Children’s Hospital works very closely with the California Department of Health Care Services to provide EPSDT to eligible MCH patients. Prop 1E is polling at 57% Yes, 23% NO and 20% Undecided.
- Prop 1F – State Officeholder Pay Raises. This amendment would ban increasing the pay of state lawmakers if there is an operating deficit in the state budget. Balancing the state budget is not dependent upon passage of Prop 1F. It is polling at 77% Yes, 13% No and 10% Undecided.

The budget agreement includes a mechanism to restore some of the revenue enhancements (taxes!) and programmatic cuts if the props pass, AND, enough federal funds are realized from the American Recovery and Reinvestment Act (the stimulus package President Obama signed on February 17). State Treasurer Bill Lockyer and the Department of Finance must both agree no later than April 1 that the stimulus funds are adequate to keep the budget in balance. The governor has said that a minimum of a \$10 billion GF offset must be accessed in order to stave off the cuts and taxes. The administration is now reporting that it is doubtful that these minimums will be met. On March 13, the non-partisan Legislative Analyst’s Office released a report entitled The Fiscal Outlook Under the February Budget Package, which may be accessed on www.lao.ca.gov. In this report, the LAO commends the governor and legislature for adopting the February budget which had been hoped to close the \$42 billion gap. However, the Office finds that the state’s economic and revenue outlook continues to deteriorate. The LAO is now predicting an \$8 billion gap in the current budget ending 6/30/10, even if Props 1A-1E passes.

The LAO is offering the following recommendations:

- The LAO is assuming that the K-14 Prop 98 minimums will drop due to the decreased state revenues. The Office recommends that the legislature take advantage of an opportunity to access additional federal funds to offset GR education costs and lower GF spending on education.
- The legislature should use the spring budget process to continue developing programmatic solutions. These changes can come from health and social service programs as well as shifts in prison and parole policies.

- The LAO is 'extremely reluctant' to recommend an additional increases in the tax rates. However, the Office believes that there are opportunities to make targeted changes in tax expenditures.

Much will be determined over the course of the next few weeks and months. The state's ability to balance its budget through June 2010 goes beyond sufficient federal funds from the stimulus package passage of the May propositions. Averting further program cuts and increased taxes is dependent upon a complex combination of increased consumer confidence, a leveling off of the rising unemployment rate, Wall Street rebounding and other factors, all of which are out of our immediate control.

Federal Budget Highlights

President Obama released his Federal Fiscal Year 2010 Budget Blueprint to Congress on February 26. The outline includes "high level" information regarding the \$3.6 trillion plan and projects at \$1.17 trillion deficit, the largest in U.S history. This outline only offers policy direction and specific spending details will be revealed in the coming weeks.

Of significant importance to MemorialCare and our industry, the budget creates a 'reserve fund' to help pay for the President's forthcoming health reform proposal. This fund, \$633 billion over ten years, is intended to be a down payment towards comprehensive health reform. As with many budget and public policy proposals, the "devil is in the details". The plan proposes to reduce Medicare payments to hospitals, yet the terms of these reductions have not been revealed. The President also plans to increase the tax burden of wealthy Americans.

One of the payment levels that may suffer significant reductions is that of Medicare re-admissions. Again, details are lacking, but the discussions that MemorialCare is involved in are regarding the final definition of the word 're-admission' including time lapsed after discharge, and which Medicare Diagnostic Related Groups, DRGs are impacted. MemorialCare agrees with CHA that the decision of a patient's readmission should not be left to an arbitrary government policy; rather it should be made in full partnership with the patient's medical team.

The proposed changes in the tax code may also have an effect on MemorialCare's ability to fully fund our expansive community benefit programs such as breast and prostate cancer screenings, cholesterol checks and neo-natal classes. In addition to allowing the 2001-2003 tax cuts for upper-income Americans lapse in 2010, Obama proposes to cap at 28% the tax rate at which taxpayers can take itemized deductions. If codified, this proposal may have a negative effect on our Foundations' ability to raise much needed funds for our capital and programmatic improvements.

As Congressional debate begins, the Obama administration is touting this plan for its acceleration of HIT adoption, Comparative Effectives (our Best Practices Teams) expansion, investment in additional cancer research and investment to increase the number of doctors, nurses and dentists in areas experiencing health care workforce shortages. The administration also claims that Medicare will be strengthened by encouraging high quality and efficient care.

The MemorialCare Government Relations Team is closely tracking all state and federal budget proposals and will advise senior leadership on impacts to our system. For more information regarding any health care reform and public policy, please contact your MemorialCare Government Relations Representative: CJ Harmatz (Long Beach Memorial), Sandy King (Miller Children's Hospital), Beth Hambelton (Orange Coast Memorial), Susie Caskey (Saddleback Memorial), Jim Thornton (HIT issues), and Peter Mackler (MemorialCare).