Harris County Hospital District

FY 2012 Operating & Capital Budget
(February 2011)

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FY2012 Operating & Capital Budget
Executive Summary

Introduction

The past twelve (12) months have been very challenging, as we have seen more patients this year than ever before, while at the same time revenues are less than expected. The current environment is filled with uncertainty related to the development of federal health reform regulations and possible changes, as well as state budget reductions, and the potential financial and operational impact on the District and the health system we operate. While we feel confident in our ability to develop and adjust strategies in response to whatever federal reform and state budget initiatives are eventually implemented, we will continue to carefully monitor and respond to changes as they are introduced.

During this past year, there have been numerous positive events which have occurred within our health system. The following list provides a few of these accomplishments.

- The District achieved the NCQA Medical Home Designation for its community health centers in 2010. A patient-centered medical home is a practice that provides and coordinates care for patients' total health care needs in a timely, personal manner that achieves measurable high-quality outcomes.
- During October and November 2010, the District automated the inpatient physicians and nursing clinical order entry and documentation, completing the transformation of our medical records from paper to electronic medical records (EMR). The integration of certain supporting systems (radiology upgrade, operating room, obstetrics, oncology, etc.) will continue during the next two budget years.
- In pursuit of its goal to become a paperless environment, the District has implemented processes to scan loose documentation into the EMR so that it is available electronically for clinical and business purposes. Document scanning will be reduced concurrent with the integration of the remaining support systems for the Epic EMR, gradually eliminating virtually all paper documents.
- The District completed its strategic planning process, and had the plan approved by the Board of Managers in May of 2010. The document – "Harris County Hospital District, Strategic Plan 2011 to 2015, Positioned for the Future" – was presented to County Commissioners on June 22, 2010. The plan will be updated annually, based on the need to be flexible in an evolving healthcare environment.

- Harris County Hospital District was recognized as a "Platinum Start! Fit-Friendly Company" by the American Heart Association in November 2010, noting that "Through your ongoing efforts to provide a culture of corporate wellness your organization has demonstrated extraordinary, tangible results." The results were evidenced by a lower than average increase in employee health claims costs for FY 2011.
- The District increased access to surgical services by increasing outpatient surgery by 18% while reducing inpatient surgeries by 5%. The shift from inpatient to outpatient reduces inpatient cost, reduces length of stay, and performs surgery in a more cost effective manner.
- The El Franco Lee Community Health Center, which opened in May 2009, saw an increase in patient visits from 33,954 in FY 2010 to a projected 53,735 in FY 2011. Similar growth is expected for FY 2012.
- Construction of the MLK Community Health Center and adjacent Eligibility Center was completed, and the new clinic opened at the end of May 2010. The new MLK Community Health Center (63,366 square feet) replaces the clinic that was formerly located at Quentin Mease Hospital. The new Southeast Eligibility Center (10,154 square feet), which opened in June 2010, replaced the South Loop Eligibility Center which was located at 5959 Long Drive.
- Construction on the Outpatient Specialty Clinic/Diagnostic Center on the Holly Hall campus is underway. The parking garage for the project was completed in September 2010.
- Construction has just been completed on the new LBJ General Hospital Emergency Center (EC). The second phase of the project – renovation of the old EC space to support the new construction – is currently underway. The new facility is expected to increase EC capacity by 20%. Construction on the Outpatient Specialty Clinic/Diagnostic Center on the LBJ campus should begin in April 2011.
- The Hospital District opened its ninth school-based clinic, Goose Creek School-Based Clinic, on April 20 at San Jacinto Elementary School in Baytown. The 3,000 square-foot clinic has six exam rooms. The clinic's pediatric providers care for newborns to teenagers up to age 18.
- Working in conjunction with Community Health Choice, the District's Medicaid HMO, we began a pilot project with two of the FQHC's in Harris County, Denver Harbor and Spring Branch Community Health Centers. In this pilot, these two health centers are able to sign up patients for district subsidized eligibility, provide services at their sites and receive reimbursement for those patients, based on Medicaid rates, from Community Health Choice.
- The Hospital District is fully operational on the new web based eligibility system purchased from Network Sciences, Inc. Mental Health Mental Retardation (MHMR) of Harris County is currently utilizing the system and

the other agencies, Harris County and the City of Houston, should be operational by early 2011. The system allows the participating agencies to share, with patient authorization, basic patient demographic data as we work to coordinate services.

- Patient Satisfaction scores are continuing to improve, especially in the District's emergency rooms. Based on the latest results, the District's overall adult inpatient satisfaction score was 68.5% which is better than the national average of 68.0%. Beginning March 2008, in order to avoid a 2% reduction in the annual Medicare payment update, hospitals had to submit and publicly report patient satisfaction data. The adjusted data is posted on the Hospital Compare Web site (http://www.hospitalcompare.hhs.gov).
- Primary care visits increased by 3.5% from 693,844 in FY 2010 to a projected 718,032 in FY 2011.
- Harris County Hospital District's Ben Taub and Lyndon B. Johnson General Hospitals and Quentin Mease Community Hospital were awarded the prestigious Pathway to Excellence® designation from the American Nurses Credentialing Center.
- The District's Outpatient Orthopedic Rehabilitation Department at Quentin Mease Community Hospital received the Exemplary Site Award for Physical Therapy Clinical Education Experiences from the Texas Consortium for Physical Therapy Clinical Education, recognizing the District for the exceptional clinical mentoring and education it provides to physical therapy students.

The proposed annual Operating & Capital Budgets (Exhibits A and D) for the fiscal year ending February 28, 2012 reflect the District's commitment to provide high quality health care services to Harris County residents in a cost effective manner. This past year, we have seen an increase in the number of Harris County residents coming to the District for their health care services. Driving the increase is the continued high unemployment rate, 8.1% in December 2009 and 8.3% (preliminary) in December 2010 (U.S. Bureau of Labor Statistics, www.bls.gov/bls/unemployment.htm). When people lose their jobs, they generally lose their health insurance. Many turn to the District for help. In FY 2009, the District treated 272,882 unduplicated patients. In FY 2010 that number increased by 9.8% to 299,583 and for FY 2011 it is expected to reach 312,476, a 4.3% increase over FY2010.

On January 27, 2011, the District's Board of Managers approved the District's Operating Budget, Standard Capital Budget, and affirmed the multi-year Strategic Capital Plan (Exhibit E - initially approved January 31, 2008). The multi-year Strategic Capital Plan outlines the District's plan to build new or replacement facilities in areas with a demonstrated need and to expand diagnostic and treatment capability. Exhibit A summarizes the revenues available for the provision of services and the expenses incurred in delivering those services. The District's budget excludes the operating results for Community Health Choice HMO and the Harris County Hospital District Foundation, except that the Foundation's capital campaign is listed as a source of funding for the multi-year capital plan (Exhibit E).

The proposed Budget includes FY 2012 Service Initiatives (Exhibit B) and reflects the ongoing commitment to the District's key strategic priorities, including:

- Meeting community needs through improved access to care
- Providing high quality healthcare
- Improving patient, physician and employee satisfaction
- Hiring and retaining excellent employees
- Maintaining financial strength and stability

The Operating Budget (Exhibit A) reflects total revenues of $1,061,137,000 available for the provision of health services. The Operating Budget includes expenses of $1,061,137,000 funding the cost of salaries, benefits, supplies, services, and facilities used to provide health services to persons who are sick or injured and come to the District for care.

Service Indicators (Exhibit C)

Primary care visits are projected to increase by 5.3%, to a total of 755,956 in FY 2012, from the projected 718,032 in FY 2011. The increases are planned for (1) El Franco Lee and MLK clinics, as they reach full provider staffing, (2) the transfer of pediatric primary care visits from Ben Taub Hospital to the planned clinic in Pasadena, and (3) the opening of two group practice primary care clinics in northwest Harris County, which are projected to open during the second half of the fiscal year, increasing our capacity to care for the residents of Harris County.

Hospital based clinic visits are expected to remain relatively flat for FY 2012, due to ongoing capacity constraints, as well as the anticipation of a positive impact from the Medical Home initiative focus on disease management in the primary care setting.

Emergency room visits are projected to grow a little more than 7%, primarily due to the opening of the new ER facility at LBJ Hospital, as well as the continued high level of unemployment with no health insurance.

Surgery cases are budgeted to increase about 2% in FY 2012 from the prior year, based on continuing throughput improvement.

Total outpatient visits are budgeted to increase by 2.7%, from a projected 1.64 million in FY 2011 to 1.68 million in FY 2012.

Inpatient cases are expected to decline slightly in FY 2012 due to the transition of inpatient pediatrics out of Ben Taub Hospital. After spiking in FY 2011, observation cases are projected to decline in FY 2012 as enhanced case management protocols identify outpatient cases that can be cared for as true outpatients, not requiring the utilization of observation beds.

Budgeted deliveries of 7,643 for FY 2012 are flat compared to FY 2011.

As we continue to work with physicians on inpatient case management, we are planning a 4% reduction in inpatient average length of stay, from the projected 5.85 days for FY 2011 to 5.66 days for FY 2012. Observation days should decline commensurately with the reduction in observation cases discussed above, and improved case management.

Inpatient Case Mix Index (CMI) is projected to increase 1% in FY 2012 from FY 2011, as the electronic health record facilitates better clinical documentation, and the coding improvements achieved in FY 2011 through enhanced training and accountability are effective for the entire FY 2012.

Payor mix is expected to improve, primarily due to better front end tools and processes to identify Medicaid and other third party payors at point of service. We have budgeted a shift of 2% from Charity and Self Pay to Medicaid.

The number of new patients and unduplicated patients are expected to increase commensurately with the overall increase in outpatient volumes.

Revenues (Exhibit A)

Net Patient Revenue is budgeted to increase from the $297 million projected for FY 2011, to $324 million in FY 2012, an increase of 9.0%. The expected growth is due to the improvements in payor mix and inpatient case mix discussed previously, as well as the ongoing improvements in all patient revenue cycle processes at the District. We have better clinical documentation and revenue cycle tools available through EPIC and other supporting software, combined with efforts by revenue cycle management to streamline work flows.

Disproportionate Share and Upper Payment Limit (DSH/UPL) funding is expected to remain flat. Due to statewide cap limitations in FY 2011, the projected DSH/UPL revenue for FY 2011 is $183.4 million. While the extension of the enhanced federal matching does provide the possibility of some increase for FY 2012, it is likely that the statewide cap may again limit the total DSH/UPL funding.

Other Operating Revenue budgeted for FY 2012 reflects an increase of approximately $2.0 million from the projected FY 2011 amount of $25.9 million. The increase is primarily due to the anticipated appropriation by the state legislature of a portion of the remaining accumulated red light funds in the upcoming legislative session.

Ad valorem tax revenues are projected to be comparable to the current year projection of $503 million. As the economic recovery in Harris County continues very slowly, we do not expect any increase in overall property values for the 2011 tax year/HCHD FY 2012.

Tobacco settlement revenue for the District is expected to be around $11 million for FY 2012, roughly the same as FY 2011. Although the overall distribution from the settlement fund is expected to increase, due to improvements in the investment market and the positive impact on the endowment portfolio, approximately 14% ($1.8 million) of the total distribution will be passed through to Harris County, based on the juvenile and jail health costs borne by the County, which are included in the statewide distribution calculation.

Interest income and other nonoperating revenue and expenses are budgeted at $9.3 million in FY 2012, which is $1.4 million higher than the projected $7.9 million for FY 2011, since we do not expect the same negative fair market adjustments to investments in FY 2012 that occurred in FY 2011.

The total Hospital District revenue budget for FY 2012 is $1.061 billion, an increase of almost $34 million from the projected FY 2011 revenues. The expected increase is primarily attributable to the improvement in revenue cycle operations and the resulting positive impact on patient revenue billing and collections.

Working with the Board of Managers, Commissioners Court, as well as with elected officials at the State and Federal levels, the administration and medical staff leadership of the District will actively monitor any changes and communicate their impact to the Board of Managers and Commissioners Court.

Expenses (Exhibit A)

From the perspective of resource utilization, the budgeted increase in outpatient volume is balanced by a commensurate decrease in inpatient utilization. Therefore, overall District expenses will remain stable, as we balance productivity and utilization improvements against inflationary increases, with the exception of the cost of certain strategic initiatives and the intergovernmental transfers (IGT) related to the Harris UPL program. Those variances will be highlighted in the following discussion.

Salaries are budgeted to decrease by 0.9% in FY 2012 from FY 2011 projected expense. An average merit increase program of 1.5% has been included in the budget, to keep the District in line with the healthcare industry. The increase will be offset by planned reductions in overtime and contract labor utilization, meeting all productivity targets, and a decrease in FTE's through work flow redesign. The reduction should be achieved through normal attrition and a soft hiring freeze. Total Full-time Equivalent staff (FTE's) are budgeted to decline by 2.5% from the projected FY 2011 of 7,411 to 7,229 in FY 2012. Nursing and other vacancy rates are expected to remain relatively low.

Employee Benefit costs are expected to increase with the conversion of the environmental services contract to in-house staff, and an expected increase in health claims costs for our self-funded plan. Based on preliminary discussions with our actuaries, pension and post-retirement health benefit costs are assumed to be slightly lower in FY 2012 than in FY 2011, due to positive investment performance in the pension plan, and the approved increase in the monthly retiree contributions for the health plan.

Supply expenses are budgeted to decrease to $159.0 million in FY 2012 from FY 2011 projected expense of $160.7 million. The improvement is based primarily on taking over management of the patient assistance program for pharmaceuticals, which is projected to improve the replacement benefit by $2 million (from $6 million in FY 2011 to $8 million for FY 2012). Other, smaller, improvements are expected from numerous supply chain and utilization management initiatives that offset the expected inflationary increases.

The Medicaid Services IGT is budgeted to increase to $127 million for FY 2012, up from the projected – but not yet finalized – FY 2011 estimate of $112 million. The increase is due to the declining federal matching percentage for the Harris UPL program, as the enhancements provided by the stimulus bill gradually wind down. This represents the majority of the budgeted expense increases for FY 2012.

Purchased services are budgeted to increase 4.2% in FY 2012; including $1.8 million more for contract software and hardware maintenance, covering our expanding information technology platform. Other increases include nursing magnet activities, additional lease and utility costs related to the planned primary care clinics, and other miscellaneous expenses.

Depreciation expense is budgeted to increase by $1.1 million, to a total of $42.6 million in FY 2012, due to ongoing capital purchases and project completions. Interest expense is budgeted at $7.6 million for FY 2012, about $700 thousand less than FY 2011, reflecting a small increase in the capitalized interest offset, as the Holly Hall and LBJ ambulatory care buildings construction gets underway.

Total operating expenses for the Hospital District are budgeted to increase from the $1.046 billion projected for FY 2011, to $1.061 billion for FY 2012, an increase of 1.5%.

The resulting margin is a breakeven budget for FY 2012, compared to the projected loss of $18.3 million for FY 2011. As discussed earlier, management's goal of a breakeven margin will be achieved through ongoing revenue cycle improvement, as well as numerous initiatives and redesign and reengineering efforts currently being evaluated. Included in those initiatives are the following:

Work with medical staff to prioritize, develop and implement evidence based protocols for high volume, high cost admissions and outpatient procedures. Goals include timely services, elimination of medically unnecessary procedures or visits, and timely patient discharge or dismissal.

Creation of project management teams to facilitate evaluation, work flow redesign and implementation of each plan for high impact improvement opportunities. Goals are to substantially reduce rework and to eliminate work flow barriers to timely service.

Ongoing evaluation of fixed positions which are not directly involved in patient care, in conjunction with the work flow redesign, to reassign existing staff, or not replace departing staff, as the improvements are realized.

Standard Capital Expenditures (Exhibit D)

For the FY 2012 Capital Budget, the District conducted an assessment of its facilities, equipment and technology to determine the priorities for replacement, repair and any new acquisitions. The assessment and prioritization process included representatives of the medical staff from both Baylor College of Medicine and The University of Texas Health Science Center. The assessment and prioritization process addressed patient safety, obsolescence, new technology, building safety and code compliance requirements.

Given the projected margin for FY 2011 and the uncertainty for FY 2012, and the resulting cash flow impact, the regular capital budget recommendation is being limited to $29 million in FY 2012, about 70% of the prior year depreciation of $41 million.

Multi-year Capital Plan (Exhibit E)

In addition, the Hospital District expects to commit approximately $60 million of capital funds related to the strategic capital projects during FY 2012, while the total cash outflow for the strategic capital projects is forecast to be $83 million (most of the commitments for the Holly Hall project were made in FY 2011, with much of the cash outflow to occur in FY 2012).

Exhibit E provides a listing of Phase I, II and III projects, as well as the source of financing for those projects. In addition to the 2007 bond funds of $158 million, the District plans to fund the projects from a combination of internally generated funds and the capital campaign being conducted by the Harris County Hospital District Foundation.

Conclusion

Together, the FY 2012 Operating Budget, FY 2012 Capital Budget, and Multi-year Capital Plan represent the District's continuing progress to improve the health status of the residents of Harris County.

Administration recommends the approval of the proposed FY 2012 Operating Budget, FY 2012 Capital Budget, and Multi-year Capital Plan for the Harris County Hospital District.

EXHIBITS

EXHIBIT A

Summary Statement of Operations

(In Thousands)

	FY2012 Budget
Net Patient Revenue	$ 324,000
Net Ad Valorem Tax Revenue	505,000
Other Operating Revenue [UPL, DSH, Trauma]	211,837
Tobacco Settlement Revenue	11,000
Interest Revenue & Other	9,300
Total Net Revenue	**$ 1,061,137**
Total Salaries and Benefits	618,991
Total Drugs and Supplies	158,959
Medicaid Services IGT	127,000
Purchased Services	37,015
Utilities	13,091
Maintenance and Repairs	23,270
Rentals and Leases	8,042
Other Services	24,516
Depreciation, Amortization, Interest	50,252
Total Operating Expenses	**$ 1,061,137**
Net Revenue Over Expenses	**$ 0**

Note: Community Health Choice, HMO budgeted net income for calendar year 2011 is $4,487,516. This amount is not included above.

EXHIBIT B
FY2011 Service Initiatives

- Grow the primary care services at the El Franco Lee Health Center in the Alief community, the Martin Luther King Health Center, and the new pediatric clinic being established in Pasadena.

- Develop more robust chronic disease management programs, as a component of the NCQA Patient-Centered Medical Home Designation for the District's Community Health Program and Ambulatory Care Services.

- Continue to improve throughput in the emergency centers, reducing wait times, reducing left without being seen and reducing time on divert.

- Improve CMS mandated quality measures (CORE indicators) to meet national benchmarks. Implement evidence-based guidelines utilizing protocols to achieve National Healthcare Safety Network (NHSN) standards. Expand healthcare Effectiveness Data and Information Set (HEDIS) to incorporate 2011 indicators.

- Continue to reduce inpatient length of stay and re-admission rates by working with the medical staff leadership, providing scorecards comparing to benchmarks by DRG and best practices.

- Work with medical staff to prioritize, develop and implement evidence based protocols for high volume, high cost admissions and outpatient procedures. Goals include timely services, elimination of medically unnecessary procedures or visits, and timely patient discharge or dismissal.

- Improve processes throughout the District in order to continue providing cost effective/high quality care in a difficult economic climate. Create project management teams to facilitate evaluation, work flow redesign and implementation of each plan for high impact improvement opportunities. Goals are to substantially reduce rework and to eliminate work flow barriers to timely service.

- Ongoing evaluation of fixed positions which are not directly involved in patient care, in conjunction with the work flow redesign, to reassign existing staff, or not replace departing staff, as the improvements are realized.

EXHIBIT C
Service Indicators
(Utilization)

	FY2012 Budget
Adjusted Patient Days	502,957
Adjusted Admissions	88,816
Unduplicated Patients	331,345
<u>Outpatient Service Related Statistics</u>	
Emergency Visits	
Ben Taub	109,273
Lyndon B. Johnson	78,264
Total Emergency Visits	187,537
Clinic Visits	
Ben Taub & Quentin Mease	187,334
Lyndon B. Johnson	104,880
Community Health Programs	755,956
Total Clinic Visits	1,048,170
Total Emergency Room and Clinic Visits	1,235,707
<u>Inpatient Service Related Statistics</u>	
Admissions	
Ben Taub	23,512
Lyndon B. Johnson	12,505
Quentin Mease	582
Total Inpatient Admissions	36,598
Observation Stays	8,292
Patient Days	
Ben Taub	137,006
Lyndon B. Johnson	58,084
Quentin Mease	12,162
Total Inpatient Days	207,252
Average Length of Stay	5.66
Newborn Deliveries	
Ben Taub	4,261
Lyndon B. Johnson	3,382
Total Deliveries	7,643

EXHIBIT D

Capital Budget Summary

(In Thousands)

Category Totals		FY2012 Budget
Facility Projects	$	8,685
Information Technology – Ongoing Projects		8,675
Information Technology – New Projects		2,664
Medical Equipment		3,571
Other (Pyxis Capital Leases, Emergency Capital)		5,001
Community Health Choice (HMO) Capital		375
Total FY2012 Capital Budget	$	28,971

Notes:

- FY2011 Projected Depreciation is $41.5 million
- Community Health Choice strategic capital budget of $5 million for replacement of the managed care system is not included above.

EXHIBIT E
Multi-Year Capital Plan
(In Thousands)

Phase I Capital Projects	Current Cost Projected	Status (Planned Completion)
El Franco Lee Health Clinic	$ 16,821	Completed April 2009
Southwest Eligibility Center	2,800	Completed October 2009
MLK Primary Care Clinic and Eligibility Center	21,500	Completed June 2010
Holly Hall Parking Garage	17,025	Completed September 2010
Holly Hall Ambulatory Care Center	101,378	Construction in progress (August 2012)
LBJ Emergency Center Expansion	49,188	Construction in progress (February 2012)
Total Phase I	**208,713**	
Phase II Capital Projects		
Ben Taub - Old Tower Renovation	46,105	Design development (October 2012)
LBJ Ambulatory Care Center	60,092	Design development (May 2013)
QM - Physical Therapy Rehab Center	2,535	Completed June 2010
Total Phase II	**108,733**	
Phase III Capital Projects		
Ben Taub 2nd Floor - Day Surgery	19,000	A&E funding approved (October 2013)
Ben Taub EC Remodel - Holding Area	41,751	A&E funding approved (October 2013)
Ben Taub and Holly Hall Data Centers	12,395	A&E funding approved (October 2012)
Total Phase III	**73,146**	
Total Estimated Cost of Strategic Projects	**$ 390,592**	($83.761 million projected cash expenditures for strategic projects in FY2011)
Projected Cash Funding of Projects		
Series 2007A Bond Funds	$ 158,003	Bonds issued October 2007
Board Designated for Future Expansion	32,818	As of February 28, 2007
Set Aside from FY2008 Operating Income	87,631	75% of Actual Margin for FY 2008
Set Aside from FY2009 Operating Income	43,095	75% of Actual Margin for FY 2009
Set Aside from FY2010 Operating Income	10,868	75% of Actual Margin for FY 2010
Investment income - Bond & Designated Funds	36,973	As of December 2010
HCHD Foundation	20,000	
TOTAL Funds Available for Projects	**$ 389,388**	

EXHIBIT F

Projected FY2011 Compared to FY2012 Budget Summary
Statement of Operations

(In Thousands)

	FY 2011 Projected	FY 2012 Budget	Variance
Net Patient Revenue	$ 297,229	$ 324,000	$ 26,771
Net Ad Valorem Tax Revenue	502,567	505,000	2,433
Other Operating Revenue	209,274	211,837	2,563
Tobacco Settlement Revenue	11,154	11,000	(154)
Interest Revenue	7,290	9,300	2,010
Total Net Revenue	1,027,514	1,061,137	33,623
Total Salaries and Benefits	621,726	618,991	(2,735)
Total Drugs and Supplies	160,747	158,959	(1,788)
Medicaid Services IGT	111,922	127,000	15,078
Purchased Services	36,227	37,015	787
Utilities	12,596	13,091	495
Maintenance and Repairs	21,316	23,270	1,954
Rentals and Leases	7,938	8,042	105
Other Services	23,548	24,516	968
Depreciation, Amortization, Interest	49,800	50,252	451
Total Operating Expenses	1,045,821	1,061,137	15,316
Net Revenue Over Expenses	$ (18,308)	$ 0	$ 18,308