SPECIAL REPORT

BOSTON MUNICIPAL RESEARCH BUREAU
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The New Boston Public Health Network Should Be Approved

The Boston Public Health Act of 1995, the home rule petition submitted by the Mayor that permits the creation of a new health care system for the City of Boston should be approved by the City Council. This home rule petition represents a critical step forward in the effort to ensure the mission of Boston City Hospital (BCH) at a time of significant change and contraction in the health care market. The petition is the first step in the establishment of a new health care system involving the creation of a Public Health Commission, a new private medical center and the affiliation of eight neighborhood health centers. The petition creates the Public Health Commission as successor to the Department of Health and Hospitals (DH&H) and authorizes the City to negotiate a merger agreement with Boston University Medical Center Hospital (BUMCH). This negotiation will result in the creation of a private, nonprofit corporation, the *Boston Medical Center*, which will maintain a public mission established through a merger of BCH and Boston Specialty and Rehabilitation Hospital (BSRH) with BUMCH. The merger agreement will have to be presented to the Mayor and City Council for approval once it is negotiated. Eight Boston neighborhood health centers have agreed to affiliate with the Commission and the *Medical Center* to create the new health care network for Boston.

The totality of this plan, combining the elements that retain the public involvement and mission, the capacity to be more cost effective and competitive and the ability to provide the critical mass of patient volume, may be the only way this new entity can be competitive and survive in this changing environment. Also of importance is that the final plan will improve the City's financial position by placing a limit that is fixed in term and amount regarding Boston's fiscal obligation to the new medical center. Maintaining a competitive edge is the key to health care survival in the 1990s and the plan before the City Council is the City's best option for its long term interests.

The growth and clout of managed care and the expected reductions in federal health care funding point to increasing funding pressures on public hospitals. In 1994, BCH relied on Medicaid, Medicare and the Free Care Pool for 86.1% of its total net revenues. These are the revenues that are most vulnerable to cuts by Congress and the President as they agree to reduce the federal deficit. Establishing a new health care system in Boston that will be competitive and still maintain the mission to serve the poor and indigent will not come without difficulty and hardship. Nevertheless, these steps are necessary to ensure that both the hospitals and the mission will survive in this competitive health care environment. Approval of this petition now will allow the merger negotiations to be completed so that a final detailed agreement can be presented for a subsequent vote by the Council. Amendments to the petition should be limited to maintain its flexibility. This issue must be thought of in economic, not political terms.

The Boston Public Health Act of 1995

This petition has two objectives: (1) to establish a change in the governance structure of the DH&H through the creation of the Public Health Commission and (2) to authorize the City to enter into negotiations with BUMCH or any other hospital for the purpose of merging or consolidating its operations with those of BCH and the BSRH. Once a detailed agreement is negotiated, it must be presented to the Council for final approval. The new health system will be accountable to the Mayor and City Council through the annual appropriation process and other procedures in the law.

The home rule petition provides for the creation of a new quasi-independent agency of the City called the Boston Public Health Commission. The Commission will be the successor to DH&H and the Trustees of Health and Hospitals on July 1, 1996. The Commission will be governed by a Board of Trustees of seven members, six of whom are appointed by the Mayor. The seventh member is the CEO of the consolidated *Medical Center* or the City's Collector-Treasurer if no merger takes

place. Civil Service laws will not apply to new Commission employees but pension, benefit and collective bargaining rights remain the same. The Commission is responsible for:

- Retaining title to DH&H property and assuming the City's debt service obligations to DH&H.
- Contracting with the consolidated *Medical Center* to operate BCH and BSRH. The lease will pay for the BCH debt service.
- Contracting with the *Medical Center* for medical services for its programs.
- Administering the Emergency Medical Services (EMS).

The petition authorizes the City to negotiate a merger agreement with BUMCH to create a private, nonprofit corporation modeled after the neighborhood health centers. This new corporation, called the *Boston Medical Center*, will be a private employer driven by a public mission. The merger partner for BCH must accept the mission statement of BCH. The new *Medical Center* will operate BCH and BSRH under contract and BUMCH. It will provide public health medical services under contract with the Boston Public Health Commission. A Board of Trustees of 30 members appointed by the Mayor, BUMCH and neighborhood health centers will govern the *Medical Center*.

A Public Health Advisory Board will be established to provide citizen input and review of the Commission's performance and budget. Similar to the MWRA Advisory Board, this Board will encourage coordination among the Commission, public health providers and funding sources in addressing the City's public health needs. The *Medical Center's* programs relating to public health will also be reviewed by this Board.

Boston's Health Care Costs

DH&H is the second largest city department. In fiscal 1995, the City budgeted for a gap between DH&H's revenues and expenditures of $33.7 million. A review of the final operating results of the DH&H for fiscal 1994 shows city assistance of $30.7 million based on total net revenues of $205.5 million and patient service expenses of $236.2 million. Broken down by service, the bulk of the City's support was allocated to public health programs ($22.9 million), followed by BSRH ($8.6 million), Long Island Shelter ($2.3 million) and EMS ($1.4 million). The operating results of DH&H for the last four years are shown in the table to the right. In addition to the operational costs, the City is responsible for debt service costs of $54.5 million in DH&H general obligation bonds outstanding. The new BCH facility was financed through the issuance of $169.3 million of revenue bonds in November 1990, which were secured by a mortgage on BCH by HUD through the Federal Housing Administration. These bonds are being paid through the Hospital's operating revenues and not through the City's annual debt service account. The debt service for the new BCH will be $16.7 million in fiscal 1996.

DEPARTMENT OF HEALTH & HOSPITALS
OPERATING RESULTS, FY91-94
FIGURES IN 000'S

	1991	1992	1993	1994
BCH	$103	($1,657)	($3,956)	$4,479
BSRH	1,820	(7,132)	(5,721)	(8,649)
Long Island	3,603	(3,201)	(1,807)	(2,350)
Ambulance	(8,276)	(3,255)	(1,616)	(1,360)
Public Health	(22,262)	(23,784)	(19,820)	(22,872)
Total DH&H	($25,012)	($39,029)	($32,920)	($30,752)

BOSTON CITY HOSPITAL
ESTIMATED NET REVENUE BY PAYOR, FY91-94

	FIGURES IN 000'S				PERCENT DISTRIBUTION			
	1991	1992	1993	1994	1991	1992	1993	1994
Medicaid	$81,168	$57,678	$54,213	$40,357	59%	44%	39%	25%
Medicare	20,234	15,577	11,217	25,537	15%	12%	8%	16%
Blue Cross	4,351	4,437	3,028	3,842	3%	3%	2%	2%
HMO's	4,311	5,069	5,939	7,257	3%	4%	4%	5%
Com/Indust Acc	9,391	8,802	8,993	10,191	7%	7%	6%	6%
Free Care Pool	16,538	38,136	53,137	72,058	12%	29%	38%	45%
Misc.	2,578	2,325	2,883	914	2%	2%	2%	1%
Total	$138,571	$132,024	$139,410	$160,156	100%	100%	100%	100%

The operating revenues for BCH come primarily from government-subsidized programs such as Medicaid, Medicare and the Free Care Pool. As shown on the opposite page, these three sources constitute 86.1% of total net revenues. The revenue share for BCH from HMOs is increasing while the share for Blue Cross, the traditional indemnity plan, is decreasing.

Why The Home Rule Petition Should Be Approved

Successfully addressing the BCH financial issue is critical to Boston because the extent to which its resources will be required to operate BCH will have a direct impact on the City's financial health and will play a key role in its future. The driving force behind the need for change in BCH's governance structure is the rapidly changing health care environment. The growth and clout of managed care, even with Medicaid and Medicare programs, the move toward a capitated payment system, the shift to non-institutional health care alternatives, declines in patient volume and expected cuts in federal Medicaid and Medicare funds all point to greater pressure on the City's own resources unless steps are taken now to ensure a more efficient and competitive health service operation. The City is not in a position to support ever increasing appropriations to BCH. The home rule petition before the City Council should be approved for three main reasons:

1. Changes In Health Care Market - Market forces are dictating the need for the governance change and the merger if the hospitals are to be viable in the future. The significant contraction in the health care market is resulting in the competition moving quickly to establish alliances or consolidations with other medical institutions and networks of physicians. This situation is evident in Boston where Massachusetts General Hospital, together with Brigham and Women's Hospital has formed Partners HealthCare System, Inc., the New England Deaconess Hospital has entered into merger discussions with the New England Medical Center and St. Margaret's has consolidated with St. Elizabeth's Hospital. The changing market forces in this managed care environment means that BCH and BUMCH cannot survive as "stand alone" hospitals and that the long-term best interests of the City and the patients and employees of both institutions depend on the success of the creation of a Public Health Commission, a private, nonprofit medical center and the affiliation of the health centers this year. The market forces driving these changes are highlighted below.

- The Massachusetts health care market is undergoing major structural changes with hospital utilization expected to decrease by 25-50% over the next few years. The health care delivery system is shifting to non-institutional alternatives and more primary and preventive care.

- Managed care membership and market clout are growing and will place increasing pressure on hospitals to reduce charges for services. On average, managed care program payments for services are 36% less than other payers at BCH. This rate disparity will place pressure for changes at BCH as government-subsidized programs such as Medicaid and Medicare increasingly are being converted to managed care plans and HMOs as a method of cost control. Under the direction of the state's Department of Medical Assistance (DMA), Medicaid has shifted from a reactive fee-for-service payor to a pruchaser of managed care services. DMA directly negotiates Medicaid rates with hospitals and pays per discharge to reward efficiency. DMA has enrolled over 400,000 recipients in its Medicaid managed care program. Two major physician groups at BCH have contracted to participate in this program. Performance expectations are now tied to reimbursements.

- The new Insurance Reimbursement Program in the State's recently approved health reform waiver will mean that more uninsured will be covered under employer plans. Over time that change threatens to reduce the Uncompensated Care Pool which has been a significant source of funding for BCH.

- The Boston Teaching Hospitals, which drive the Boston health care market, are expected to reduce their bed capacity by as much as 40-60% and their operating costs by 20-30% over the next few years. In 1994, the patient volume growth of these hospitals declined by 4.5%. The seven Boston Teaching Hospitals could consolidate into three academic based systems in time. The networks of the teaching hospitals are expected to increase expansion in non-hospital based health care.

- BCH is recipient of special state and federal revenues for such things as graduate medical education and high levels of care provided by Medicaid, Medicare and Uncompensated or Free Care Pool recipients. These special payments totaled $44.6 million for BCH in 1994 and are expected to decline.

- Federal regulations that will take effect on July 1, 1995, may restrict the Commonwealth's ability to favorably allocate disproportionate service funds to BCH. In an effort to control its reimbursements to "disproportionate share" hospitals, the federal government approved regulations in October 1993 that

link the uncompensated care costs with disproportionate share revenues. This link also places a cap on each hospital as part of an overall state cap on reimbursements. Because BCH qualifies for four of the DMA's six disproportionate share programs, its revenues may be close to the cap. The individual hospital cap and the link between expenses and revenues will limit the DMA's flexibility in BCH funding.

- BCH's reliance on Medicaid, Medicare and the Free Care Pool for most of its revenues and the expected reductions in federal health care funding and utilization of block grants, point to the increasing funding pressures the Hospital will face over the next few years. In 1994, BCH relied on Medicaid, Medicare and the Free Care Pool for 86.1% of its total net revenues. It is these revenues that are most vulnerable to reductions as a consequence of the efforts of Congress and the President to cut federal spending. The House and Senate budget resolution would reduce Medicaid spending by $180 billion and Medicare spending by $270 billion over seven years to limit growth to 4% by 2002. For Massachusetts, the reduction in Medicaid and Medicare is estimated at $7-8 billion over this time. Earlier this month, President Clinton proposed spending reductions of $54 billion in Medicaid and $124 billion in Medicare over ten years, giving further indication that large reductions can be expected in the next few years.

2. Need To Be Competitive And Cost Efficient - The home rule petition is essential to enable the Public Health Commission and *Medical Center* to be competitive in this new environment by providing opportunities to improve service and cost efficiency. The restrictions and constraints on public institutions, such as BCH, put them at a disadvantage in responding rapidly and creatively to the changing health care market. The survival of the hospitals will depend on their ability to be competitive as price and patient volume continue to decrease. The *Medical Center* as a private, nonprofit corporation affords the best opportunity to be competitive in Boston. The merger will establish the critical mass of patient volume that will enable the new *Medical Center* to be more cost effective and viable. New physician linkages are essential to open new markets and such linkages are easier to establish in a private setting.

The costs for Boston City Hospital are among the highest in the state and aggressive cost control must continue if it is to survive. The merger offers the opportunity to achieve greater cost efficiencies. Based on 1993 data, BCH's inpatient cost per discharge is 10% higher than other Boston Teaching Hospitals and 16% higher than at comparable community hospitals. That is an indicator of the degree to which BCH must respond to the competitive rate pressures. On the other hand, the inpatient cost per discharge at BUMCH is 6% lower. Adding to these pressures is the fact that the other Boston Teaching Hospitals have set goals to reduce operating costs by 20-30% over the next few years. That will set new comparative benchmarks in the marketplace. While there are reasons for cost differences, the key to the future is the willingness of the payors to pay higher costs for special services at BCH.

3. Improves The City's Financial Position - This home rule petition will enable an agreement to be negotiated that should improve the City's financial position. Currently, the operational and capital obligation on Boston for DH&H is unlimited. It is expected that the hospital merger agreement will fix the City's financial obligations to the *Medical Center* and to certain services of the Public Health Commission in term and amount for both operational and capital expenses. Over the three years from fiscal 1992 through fiscal 1994, the City's assistance to DH&H averaged $34.2 million. The bulk of that assistance was for public health services with the balance allocated to BCH, BSRH, EMS and Long Island Shelter. The City will continue to be responsible for funding public health services and Long Island Shelter but its assistance to the other services will be defined in the merger agreement. With the approval of the home rule petition, the City's debt service obligations for the new BCH facility will transfer to the Public Health Commission and over 2,500 employees will transfer to either the Commission or the *Medical Center*.

Conclusion

The Bureau believes that this home rule petition should be approved now. Today BCH is in an equal position in negotiating with BUMCH. However, the recent news that the boards of Carney Hospital and Quincy Hospital have agreed to investigate opportunities to work together is another indicator that the health care market is moving quickly and that a delay may find BCH in a weaker position unable to forge a partnership in an effort to be competitive in this market. Representatives of the eight neighborhood health centers which have agreed to become part of this new health system, have indicated the necessity of moving quickly to establish the new public health network. They spoke of their need to associate with other hospitals if this plan is not approved soon. This home rule petition provides the framework for a new health system and should be approved by the Council. The merger agreement that follows will answer many of the questions raised in these hearings and enable the Council to vote on the specifics of the hospital merger.