



**London N. Breed,
Mayor**

**Jenny Louie,
Chief Financial Officer**

MEMORANDUM

December 1, 2021

To: President Dan Bernal and Honorable Members of the Health Commission

Through: Dr. Grant Colfax, Director of Health
Greg Wagner, Chief Operating Officer

From: Jenny Louie, Chief Financial Officer

RE: Updates to DPH Revenue Management Reserve

This memo outlines changes to the calculation of, deposits to, and withdrawals from the DPH Revenue Management Reserve to simplify the methodology and establish a more predictable reserve.

This reserve is established under Section 12.6 of the administrative provisions of the Annual Appropriation Ordinance which authorizes the Controller to defer surplus transfer payments, indigent health revenues, and Realignment funding to offset future reductions or audit adjustments associated with funding allocations for indigent health services. This provision was adopted by the Board of Supervisors to smooth volatile state and federal revenues that can lead to large variances between budgeted and actual amounts due to unpredictable timing of payments, policy changes which may affect projected allocations, and delays in final audit settlements.

Currently, the DPH management reserve balance is calculated by identifying known and significant revenue risks due to potential policy changes in Medi-Cal programs and federal funding programs such as Disproportionate Share Hospitals. This approach does not adequately mitigate against all the possible fluctuations in DPH revenue, which become increasingly more prevalent with the continued shift of payment models from cost reimbursement to value and performance-based payments where there is more variability in terms of level of payments. Moreover, determining the true financial impact and risk can also be challenging with pending policy changes.

DPH proposes to simplify the methodology for calculating its management reserve and determining deposits and withdrawals. Moving forward, the reserve will be based on a percentage of budgeted DPH Medi-Cal, Medicare and patient revenues rather than identifying specific potential adverse events. This will allow DPH to be able to create a stable and more predictable reserve to buffer against variability particular with an increased shift towards value based payments. Moreover, these changes will provide clear guidance on how deposits and withdrawals are made, as outlined below.

Level of Reserve and Calculation:

- Maximum reserve of 5% of revenues of DPH's budgeted net Medi-Cal, Medicare and Patient Revenues less Intergovernmental Transfer payments (IGT) for all divisions over the two-year approved budget. For FY 2021-22 the calculation is as follows:

Budgeted Revenues	Medi-Cal	Medicare	Patient Revenues	Less IGT	Annual total
21-22	933,070,146	163,838,477	143,467,856	(89,491,155)	1,150,885,324
22-23	895,154,928	168,125,980	143,833,827	(92,557,601)	1,114,557,134
			Total Revenues Over Two Years		2,265,442,458
			5% Reserve Over Years		113,272,123

Deposits:

- If DPH revenues exceed budgeted revenues in any given quarter, 50% of the balance will be deposited by the Controller up to the 5% cap.
- Should budgeted revenues drop and the calculated reserve are projected to be lower than the amount being held in the reserve for two fiscal years, the reserve will be adjusted down to reflect the updated two-year revenue budget as described above.

Withdrawals:

- When DPH's projected revenues in the quarterly reports are below budget, reserves will be released to balance shortfalls.
- Consistent with the City's Rainy Day reserve policy, up to 50% of the reserve may be used in a given fiscal year, but the withdrawal should not exceed DPH's projected revenue deficit.
- Notwithstanding this policy, the Mayor and the Board may choose to appropriate this reserve through the supplemental or budget appropriations process as outlined in the City Charter.

Use of Reserve To Address Timing of Payments

- In addition, DPH will continue to use management reserve to reflect issues regarding timing of payments to meet budgeted assumptions in a future year.
- Withdrawals will be made to meet revenue targets in the year they are projected.
- These deposits will be excess of the 5% calculation.