THE 2004-2005 STATE BUDGET

HEALTH

Department of Health Services

The Department of Health Services' (DHS) budget supports activities and services to fulfill the State's commitment to protecting and improving the health of all Californians. DHS administers a broad range of public health programs and the California Medical Assistance Program (Medi-Cal).

For fiscal year 2004-05, the Governor's Budget provides a total of $34.3 billion for the support of DHS programs and services. Of this amount, $910.5 million is for state operations and $33.3 billion is for local assistance. This represents a total increase over the revised current year budget of 5.3%. Although the overall budget has increased, this is not due to significant programmatic expansions.

The net increase from the revised 2003-04 budget of $1.72 billion is primarily attributable to two significant augmentations associated with one-time savings realized in the current year. Specifically, the change in accrual to cash budgeting for the Medi-Cal Program and relief through the enhanced Federal Medical Assistance Percentage will end this fiscal year. The loss of enhanced Medi-Cal federal matching funds is a major component of the 17% increase in General Fund over the current year to a budget of $12.2 billion. Federal funds also increased by 2.0% to $19.5 billion. Special funds, including reimbursements, decreased by 15.3% from $3.0 billion to $2.5 billion.

MAJOR PROVISIONS

The major provisions of the proposed Department of Health Services budget include:

- **Medi-Cal Reform.** The Administration proposes to redesign the Medi-Cal program to reduce the costs to the state. The state proposes to seek a Medicaid Demonstration Waiver to redesign the Medi-Cal Program. Options available to the State to control costs of the Medi-Cal Program are primarily limited to reducing the number of people eligible, eliminating optional benefits, or reducing reimbursement to providers. With the redesign of the Medi-Cal Program, the Department of Health Services believes it will have the flexibility necessary to provide health care coverage for over 6.8 million Californians and minimize future reductions in program eligibility, benefits or provider rates. The budget projects no savings in the budget

year and $400 million General Fund in the 2005-2006 fiscal year. The elements of the redesign include:

- **Simplification.** The State may seek to simplify Medi-Cal eligibility by aligning Medi-Cal's eligibility standards and processes with those of CalWORKS and the Supplemental Security Income/State Supplementary Payment Program (SSI/SSP). Income standards and property tests could be aligned with CalWORKS for children and families and with SSI/SSP for the aged blind and disabled.

- **Multi-Tiered Benefit/Premium Structure.** Under federal law states have flexibility to modify their current benefit packages for optional Medicaid populations. With a federal waiver, California could structure a tiered benefit program that provides comprehensive benefits to the mandatory populations and basic benefits to optional eligibles, with more comprehensive benefits available to those willing to pay more.

- **Co-Payments.** The state may require co-payments from Medi-Cal beneficiaries for various services, deduct the co-payment from the provider reimbursement and give providers legal authority to require the co-payment as a condition of providing non-emergency care.

- **Conform Benefits to Private Plans.** The state may conform the basic Medi-Cal optional benefits package to private health plans and exclude some benefits such as chiropractic and acupuncture services.

- **Managed Care Reform.** The state may expand managed care into additional counties, review and reform managed care reimbursement policy to ensure access and appropriate utilization and encourage enrollment of the Aged, Blind and Disabled into managed care. This aspect of reform will take time to implement and budget savings will not accrue until the 2005-2006 fiscal year.

- **Medi-Cal Anti-Fraud.**

  - **Enhance Medi-Cal Estate Recoveries and Increase Long-Term Care Insurance Purchases.** The budget proposes to make statutory changes to authorize the Department of Health to recover Medi-Cal costs from annuities included in deceased beneficiaries' estates. The Department also would continue its efforts to increase the number of middle-income persons purchasing long-term care insurance, which serves to control Medi-Cal costs.

  - **Expand Hospital Billing Audits.** The Department would increase the number of field audits of fee-for-service (non-contracting) hospital cost reports; home office cost reports and related billings. The budget would increase staffing by 41 at an annual cost of $2.4 million General Fund. It is projected the state would save a net $1.4 million in the budget year $15.3 million in 2005-2006 from the increased number of audits.

- **Provider Feedback.** In order to ensure that providers understand the amount that they have been paid by Medi-Cal, mid-year IRS 1099 forms will be sent to them at their home address. Utilization and billing profiles will also be developed and providers will be notified if their profiles are significantly different than those of their peers. These activities are expected to generate savings of $2.5 million General Fund in 2004-05.

- **Beneficiary Confirmations.** The Department will institute two methods of verifying that beneficiaries actually received the benefits that providers billed to Medi-Cal. The first method will be to contact a random sample of Medi-Cal beneficiaries by phone or by mail. The second method will be to contact a beneficiary in person or by mail when a review indicates the provider's billing patterns and diagnosis for the beneficiary do not appear to match. Savings in 2004-05 are expected to be $1.0 million General Fund.

- **Restrict Electromyography and Nerve Conduction Tests to Specially Trained Physicians.** The Department will restrict billing to neurologists, physical medicine and rehabilitation trained physicians who have received specialized training in electromyography and nerve conduction tests. The proposal would save $652,000 General Fund in 2004-2005 and $1.1 million General Fund annually thereafter.

- **Implement Counterfeit-Proof Prescription Pads.** The Department would require that all prescriptions for Medi-Cal beneficiaries be written on prescription blanks obtained from State printing vendors. It would reduce forging and/or altering of prescriptions and provide an inventory of prescribers' drug orders. The proposal would not produce savings in the budget year but would produce between $ 7.0 million and $14.0 million General Fund annually thereafter.

- **Convert Limited-Term positions to Permanent.** The proposal requests the conversion of nine limited term positions in Payment Systems Division and six limited term positions in Audits and Investigations Division to permanent status to combat provider fraud and abuse in the Medi-Cal program. These positions are necessary to stay current with the re-enrollment of providers into the Medi-Cal program and to ensure deactivation of fraudulent providers thorough pre-screening and background checks of new re-enrollment applications. These limited term positions were established by the 2002-03 Budget Act to re-enroll approximately 140,000 current providers. These permanent positions will extend the cost savings associated with the re-enrollment efforts. The deactivation of unqualified providers resulting from re-enrollment activities terminates Medi-Cal payments, with subsequent savings to the Department. This proposal is expected to generate Medi-Cal savings of $15.2 million.

ADDITIONAL HIGHLIGHTS

Additional Highlights of the proposed Department of Health Services Budget:

- **Quality Improvement Fee on Medi-Cal Managed Care Plans.** The 2003-04 Budget assumed that the Medi-Cal managed care plans would pay a quality improvement assessment fee of 6% of their gross revenues from their Medi-Cal lines of business. This fee would be paid directly to the General Fund. The cost of the fee would be reimbursed through a Medi-Cal rate increase, which would also provide an additional rate increase of approximately 3% to the plans. The fee and rate increases were not approved at the federal level for implementation in 2003-04; therefore, there is a saving of $112.5 million General Fund in the Medi-Cal budget in 2003-04. The net impact to the state General Fund is a loss of $37.5 million. The Department is proposing to change state law to make it compatible with the requirements of federal law and to work with managed care plans to implement the fee in 2004-05. The cost to Medi-Cal is expected to be $225.0 million General Fund, with a net savings to the state General Fund of $75.0 million.

- **Medi-Cal County Administration Costs.** The Department will formally implement a county cost control plan that ensures that counties have sufficient staff to complete required eligibility activities, including annual re-determinations, in the most cost effective manner. The plan will include staffing guidelines, policies to control overhead costs, and language that controls wage increases, while still maintaining the integrity of the eligibility determination process. Savings in 2004-05 is expected to be $10.0 million General Fund.

- **Transfer of Breast and Cervical Cancer Treatment Program to Counties.** This proposal requests approval to transfer the Breast and Cervical Cancer Treatment Program (BCCTP) eligibility determinations and re-determinations to the counties, effective January 1, 2005. The Department currently does the eligibility determinations for this program. It is the only eligibility determination done by the state in the Medi-Cal Program, and with current staffing levels is unable to perform this process in a manner that meets federally required timeframes. One of the existing twelve positions will be eliminated on January 1, 2005 and nine positions will be retained through June 30, 2005, for the six-month transition period of the BCCTP to the counties. This will leave two permanent positions to ensure that the counties are performing BCCTP eligibility determinations and re-determinations consistent with State and Federal BCCTP program requirements.

- **Adult Day Health Care Reform.** Effective October 1, 2004, a twelve-month moratorium will be placed on the certification of new Adult Day Health Care centers (ADHCs). In addition, changes will be made to the way ADHC services are paid, ADHC centers will be required to bill separately for the physical, speech and occupational therapy and transportation services they provide. Savings in 2004-05 is expected to be $12.7 million General Fund.

- **Interim Rates for Cost-Reimbursed Hospitals.** Effective December 2003, the Department is reducing the interim rate it pays non-contract hospitals by 10%. This will result in savings of $18.1 million General Fund in 2003-04 and $31.0 million in 2004-05. The hospitals' actual costs will be reconciled in 2005-06, using audited hospital cost reports, and any necessary payments/collections will be made.

- **Rate Methodology for Federally Qualified Health Centers (FQHC) and Rural Health Clinics (RHC).** Federal law requires that a rate increase be given each year to FQHCs and RHCs whose rates are set under the federally mandated Prospective Payment System (PPS). The rate increase is based on the Medicare Economic Index (MEI) and is 3% effective October 1, 2003. The 2003-04 cost of the increase is $5.8 million General Fund. The 2004-05 cost of this increase, and the impact of an additional 3% increase anticipated in October 2004, is $16 million General Fund.

  Additionally, federal law requires that rates established for FQHCs and RHCs under the PPS be adjusted for changes in scope of service. In addition, the interim payments made to clinics must be adjusted for Medicare crossover claims and managed care actual costs. These adjustments, which have not yet been made, will be retroactive to January 1, 2001; it is expected that the retroactive payments will be made in 2004-05. Those payments, plus the ongoing costs for these adjustments, are expected to increase costs in 2004-05 by $102.4 million General Fund.

  Also, the Benefits Improvement and Protection Act (BIPA) of 2000 required the Department to implement a PPS for FQHCs and rural health clinics (RHCs). Under an alternative rate methodology, the rates were set based on the facilities' 2000 cost reports. Effective April 1, 2004, the Department proposes to eliminate the alternative rate methodology and set the base rates for the facilities based on averages from audited cost reports from 1999 and 2000. This is expected to result in savings of $7.4 million General Fund in 2003-04 on an accrual basis, $3.8 million General Fund on a cash basis. On a cash basis, savings will increase by 28.4 million General Fund in 2004-05 to $32.3 million General Fund.

  Overall, the clinics will see a net increase in payment of $14.0 million in total funds in 2003-04 and $182.3 in total funds in 2004-05.

- **Treatment Authorization Requests Workload.** This proposal will augment staffing in the Medi-Cal Operations Division (MCOD) to address a workload increase associated with a 17% annual increase in Treatment Authorization Requests (TAR) based on Calendar Year 2001 to 2002 data.

  Approval of these positions is expected to enable MCOD to adjudicate medically necessary services for Medi-Cal beneficiaries in a timelier manner. This, it is hoped, will reduce beneficiary and provider complaints, increase the ability to meet the mandatory 24-hour turnaround requirement for drug TARs, assist in identifying and preventing fraud and abuse, and, thereby, reducing state General Fund expenditures for excess or inappropriate drug usage. The staff augmentation alone

will not meet workload increases. Budget trailer bill is being proposed to permit the sampling of TARs for review.

- **Sunset Date for California Partnership for Long-Term Care.** This proposal would amend current statute in the Welfare and Institutions Code, Section 22003(c), to remove the January 1, 2005 sunset date for the California Partnership for Long-Term Care (the Partnership) and remove language referring to the termination of the program from Welfare and Institutions Code, Section 22009(c)(1). Additionally, the proposal requests the conversion of five limited-term positions to permanent status. Implementation of this proposal would preserve the State's program that promotes the purchase of high quality long-term care (LTC) insurance policies. The Partnership is necessary for the continued availability of Partnership-certified LTC insurance policies designed for people with moderate income who would otherwise rely on Medi-Cal to pay their future LTC costs.

- **Shift from Accrual to Cash Accounting.** AB 1762, the Health Trailer Bill to the 2003 Budget Act, included the requirement that Medi-Cal change from an accrual to cash budgeting/accounting system, effective with the 2003-04 fiscal year. The 2003-04 Budget assumed savings of $930 million General Fund for this change, which is one-time only and does not continue into Fiscal Year 2004-05. Under the provisions of AB 1762, costs for 2001-02 and 2002-03 paid in 2003-04 remain in the 2001-02 and 2002-03 fiscal years on an accrual basis. This makes 2003-04 a modified cash year. In 2004-05 all costs will be budgeted on a cash basis. Based on the appropriations for 2001-02 and 2002-03 that were still to be expended at the end of the 2002-03 fiscal year, the savings in 2003-04 from shifting to cash budgeting is expected to be $994 million. This is $64 million more savings in 2003-04 than originally anticipated. In 2004-05, there will be increased costs of $994 million General Fund due to the end of this one-time savings: $957.6 million General Fund for benefits, $17.4 million General Fund for county administration and $19.0 million General Fund for fiscal intermediary costs.

- **Federal Matching Assistance Percentage (FMAP).** The federal Jobs and Growth Tax Relief Reconciliation Act of 2003 provided federal fiscal relief to the states for the period April 2003 through June 2004. During this period California will receive enhanced federal financial participation (FFP) in the costs of the Medi-Cal Program, 54.35% from April 2003 through September 2003, and 52.95% from October 2003 through June 2004; in July 2004 it will return to 50%. The loss of this enhanced FFP in 2004-05 results in increased General Fund costs of $655.4 million General Fund.

- **Five Percent Provider Rate Reduction.** In the Budget Act of 2003, the Legislature reduced selected Medi-Cal provider rates by 5%, effective January 1, 2004. This includes fee-for-service (FFS), Family PACT and managed care rates. Some services, including hospital inpatient and outpatient, nursing facility and FQHC services are exempt from the reduction. Savings are estimated to be $102.8 million

General Fund in 2003-04 and $236.8 million General Fund in 2004-05. On December 23, 2003, the U.S. District Court issued a preliminary injunction prohibiting the Department from implementing the FFS reductions. On January 8, 2004, the department filed a Motion for Reconsideration, asking the court to reconsider its decision as to all of the 5% rate cuts, the court is expected to rule on the motion in mid-February.

- **End of Fiscal Year Checkwrite.** In order to maximize FFP and take advantage of the 52.95% FFP available through June 30, 2004, the checkwrite that would otherwise be paid on July 1, 2004 will be paid on June 30, 2004. Shifting this checkwrite to June increases costs in 2003-04 by $135 million General Fund, but saves $8.5 million in General Fund costs because of the enhanced FFP. Costs in 2004-05 will be $143.5 million General Fund less than they would otherwise have been without the shift, a reduction of $278.5 million General Fund from 2003-04.

MID-YEAR REDUCTION PROPOSALS

- **10 Percent Provider Rate Reduction.** The Governor's Mid-Year Reduction Proposal includes a 10% reduction in provider rates for Medi-Cal fee-for-service, managed care and Family PACT, proposed to be effective January 1, 2004. Some services, including hospital inpatient and outpatient, nursing facility, and federally qualified health center services are excluded from the reduction. Savings in 2003-04 is expected to be $160.1 million General Fund, increasing by $299.9 million General Fund in 2004-05 to $460.0 million General Fund.

- **Wage Rate Adjustment.** The Budget Act of 2003 included funding for a wage rate adjustment for LTC providers who have collective bargaining agreements or contracts that increase wages for their staff. $46 million General Fund was included in 2003-04, $21 million General Fund for wage increases in 2002-03 and $25 million General Fund for wage increases in 2003-04. The Governor's Mid-Year Reduction Proposal eliminates this funding.

- **Cap on State Only Services for Aliens: Breast and Cervical Cancer Treatment Services for Undocumented Aliens; Non-Emergency Services for Newly Qualified Aliens; and Non-Emergency Services for Undocumented Aliens.** The Governor's Mid-Year Reduction Proposal includes capping the number of persons that can be eligible for state-only services for aliens in any given month to the number that were eligible on January 1, 2004. This requires the establishment of statewide waiting lists for these programs. It is expected that the system changes needed to establish the waiting lists will be completed by July 1, 2004. Savings in 2004-05 is expected to be $1.8 million General Fund for Breast and Cervical Cancer Treatment services for undocumented aliens, $5.6 million General Fund for non-emergency services for newly qualified aliens and $9.8 million General Fund for non-emergency services for undocumented aliens.

Public Health Programs

MAJOR PROVISIONS

The major provisions of the proposed Public Health Programs Budget include:

- **AIDS Drug Assistance Program.** This proposal partially backfills one-time rebate augmentations included in the 2003-04 budget with $8.3 million for the AIDS Drug Assistance Program in fiscal year 2004-05. This request is comprised of $3,032,000 in on-going reimbursements (drug rebates), $5,822,000 in one-time reimbursements (drug rebates), and a reduction in General Fund of $550,000 associated with a cap on the ADAP caseload, proposed to be effective January 2004.

- **Elimination of Community Challenge Grant Program.** The Community Challenge Grant (CCG) Program is funded through the Temporary Assistance to Needy Families (TANF) High Performance Awards received as reimbursements from the Department of Social Services. TANF funding for CCG will end June 30,2004. Therefore, this proposal reduces reimbursements by $19.878 million ($866,000 in state operations and $19,012,000 in local assistance) and eliminates seven positions.

- **Federally Funded Bioterrorism.** The Department of Health Services requests the limited-term positions and federal budget authority of $76.509 million; $29.270 million state operation; and, $47.239 million local assistance in Fiscal Year 2004-05 continue implementation of the Centers for Disease Control and Prevention (CDC) cooperative agreement and administer the expanded Health Resources and Services Administration (HRSA) cooperative agreement for activities relating to bioterrorism preparedness and response.

  The CDC cooperative agreement includes additional efforts to prepare to deploy the strategic national pharmaceutical stockpile, the smallpox vaccination program and technical support for the local Health Jurisdictions.

  The HRSA cooperative agreement includes the following new workload: upgrade or maintain airborne infectious disease isolation capacity; establish a response system that allows immediate deployment of additional patient personnel that would meaningfully increase hospital patient care surge capacity; develop a system that allows the credentialing and supervision of clinicians not normally working in facilities responding to a terrorist incident; establish operational relationships among the various types of analytical laboratories within the State; and, adopt standard coding for electronic exchange of laboratory results and associated clinical observations between and among clinical laboratories of public health departments, hospitals, and other entities.

- **California Nutrition Network.** This proposal requests augmentation of $39.7 million in reimbursement and local assistance expenditure authority for the social marketing campaign of the California Nutrition Network for Healthy, Active Families (Network) in the Cancer Prevention Branch. The Network is principally funded through federal funds awarded by the U.S. Department of Agriculture to the California Department of Social Services. Through an annual interagency agreement, DSS reimburses DHS for activities identified in the USDA approved plan.

- **Tissue Bank Licensure Program.** This proposal will increase spending authority of the Tissue Bank Special Fund from $166,000 to $259,000 to allow the program to hire an additional Examiner to conduct onsite inspections. California currently licenses 300 tissue banks that supply reproductive tissue, human milk and bone marrow from living donors, and ocular tissue, bone, veins, tendons and heart valves from deceased donors to recipients dependent on human tissue. Onsite inspections must be conducted to assure that this tissue is safely collected, processed, stored and distributed to protect living donors and patients dependent on human tissue. One additional full time position would enable the program to visit the 300 existing banks about once every three years to assure the safety of the public. Currently, the program has a 0.6 position for field inspections, and can only inspect about 30 banks annually.

MID-YEAR REDUCTION PROPOSALS

- **Capped Caseloads.** To control costs, the budget proposes to cap enrollment in the California Children's Services (CCS) program and the Genetically Handicapped Persons Program (GHPP), within the Children's Medical Services Branch. CCS ensures that low-income children with physically disabling conditions receive medical care appropriate for their CCS eligible condition. GHPP provides medical care for individuals with specific conditions such as hemophilia, cystic fibrosis, sickle cell anemia, and degenerative neurological diseases.

  The CCS caseload is proposed to be capped at 37,600 resulting in estimated General Fund savings of approximately $120,800 in 2003-04 and $1,895,000 in 2004-05. The GHPP would continue to serve the current caseload of 1,679 (50% are Medi-Cal eligible), resulting in General Fund savings in 2004-05 of $245,000.

- **Genetically Handicapped Persons Program.** The budget proposes to implement co-payments in the Genetically Handicapped Persons Program (GHPP) beginning in fiscal year 2004-05. General Fund costs have increased nearly 82% since fiscal year 1998-99. Over 70 percent of the increase in program expenditures are due to the higher costs of blood factor products for persons with hemophilia. By implementing co-payments, there will be a $567,000 in GF savings from this proposal.

Managed Risk Medical Insurance Board

The Managed Risk Medical Insurance Board (MRMIB) administers several programs designed to provide health care coverage to adults and children. The Major Risk Medical Insurance Program provides health insurance to California residents unable to obtain it for themselves or their families because of pre-existing medical conditions. The Access for Infants and Mothers (AIM) program currently provides coverage for pregnant women and their infants whose family incomes are between 200 percent and 300 percent of the federal poverty level (FPL). The Healthy Families Program provides health coverage for uninsured children in families with incomes up to 250 percent of the FPL who are not eligible for Medi-Cal.

MAJOR PROVISIONS

The major provisions of the Healthy Families Budget include:

- **Capping Healthy Families Enrollment.** The Mid-Year Reductions proposed by the Governor would establish a limit on the enrollment in Healthy Families of 712,000 children. The state would achieve a $31.5 million General Fund savings while 112,000 children were on a waiting list.

- **Establishing a Two-Tiered Benefit Structure.** The Mid-Year Reductions proposed by the Administration also included a two-tier benefit package for children in families with incomes between 201 and 250 percent of the Federal Poverty Level. If families chose to pay current premium levels they would receive a benefit package that did not include dental and vision coverage. If families chose to pay the higher premium they would be able to provide vision and dental coverage to their children. No savings would be achieved in the budget year from the proposal; it would require $263,000 General Fund in the Budget Year to modify the administrative system to accommodate the two benefit packages.

- **Block Grant.** The budget proposes to include the Healthy Families for Documented Immigrant Children in a block grant to the counties. The accompanying programs in the block grant include CalWORKs Benefits for Recent Documented Immigrants; California Food Assistance Program; and Cash Assistance Program for Immigrants. The budget reflects $6.6 million General Fund savings, including $849,000 General Fund from Healthy Families, from the block grant. The reduction results from an unspecified increase in efficiencies. The block grant would be provided to counties effective October 1, 2004. The budget does not reflect a single appropriation for these programs; the Administration will develop the proposal in further detail and include it in the May Revision.

Department of Developmental Services

The Department of Developmental Services is responsible under the Lanterman Developmental Disabilities Services Act (Lanterman Act) to ensure that persons with developmental disabilities receive the services and supports they need to lead more independent, productive and normal lives and to make choices and decisions about their own lives. The Department ensures coordination of services to persons with developmental disabilities; ensures that such services are planned, provided, and sufficiently complete to meet the needs and choices of these individuals at each stage of their lives, regardless of age or the degree of their disability and, to the extent possible, accomplishes these goals in the individual's home community.

The Department sets broad policy and provides leadership for developmental services statewide; establishes priorities, standards and procedures within which the developmental services program: operates and monitor's, reviews and evaluates service delivery and ensures remediation of problems that arise. Services are delivered directly through Developmental Centers and state-operated community facilities, and under contract with a statewide network of 21 private, nonprofit, locally based community agencies, known as Regional Centers. The Department's goals are:

- Expand the availability, accessibility and types of services and supports to meet current and future needs of individuals and their families;
- Transition to an outcome-based service system for all people with developmental disabilities served by the Department of Developmental Services;
- Develop systems to ensure that quality services and supports are provided;
- Facilitate the dissemination of information and deployment of assistive and information technology to improve services and supports and the lives of people with developmental disabilities;
- Establish a system to ensure the Department, State developmental centers, regional centers and service providers are in compliance with all applicable federal and state laws, regulations and contracts, including accounting for their funding in an appropriate manner.

The Governor's Budget for 2004-05 proposes an increase of $154.4 million (from $2.6 billion in 2003-04 to $2.7 billion in 2004-05), a 6 percent increase in funding for regional centers. The proposed budget decreases the Developmental Centers Program by $24.7 million (from $714.8 million to $690.1 million), a 3.5 percent decrease in funding for the developmental center system. The total number of positions proposed for the Developmental Centers Program in 2004-05 is 7,883.8, a net decrease of 669.3 positions.

MAJOR PROVISIONS

The major provisions of the Department of Developmental Services Budget include:

- **Habilitation Services Program Transfer.** The Department's budget will increase by $126.6 million as a result of the transfer of the Habilitation Services Program transfer from the Department of Rehabilitation. The transfer was authorized in the 2003-2004 budget and scheduled for the beginning of the 2004-2005 fiscal year.

- **Purchase of Services Cost Containment.** The proposed budget would impose statewide standards on the purchase of services by the Regional Center System. The statewide standards were first proposed for the 2002-2003 fiscal year. The Legislature rejected the standards and adopted other cost reductions. The Legislature again rejected the statewide purchase of service standards in the 2003-2004 budget. The 2004-2005 and 2005-2006 budgets would have the State reduce expenditures by $100 million through statewide standards, share of cost liability, standardized rate structure and an alternative rate structure.

- **Continuation of 2003-2004 Regional Center Reductions**. The budget assumes the continuation of various reductions made for the 2003-2004 budget year. They include: continuation of the Purchase of Services unallocated reduction; the Day Program Rate Freeze; the Contracted Services Rate Freeze; the Community Care Facility Service Level Freeze; the SSI/SSP Pass-Through Elimination; the Non-Community Placement Plan Start-Up Suspension; Intake and Assessment Time Extension and; Eligibility Definition Update.

- **Operations Cost Containment**. The budget proposes to reduce the Regional Centers operations budget by $6.5 million General Fund to reflect reduced funding for the administrative activities of regional centers.

Department of Mental Health

The Department of Mental Health (DMH) administers State and federal statutes pertaining to mental health treatment programs. DMH is also responsible for the direct operation of the state hospitals: Atascadero, Metropolitan, Napa and Patton, in addition to the Acute Psychiatric Program at the California Medical Facility in Vacaville, the Salinas Valley State Prison, and the new Coalinga State Hospital.

The DMH budget proposes expenditures of $2.542 billion ($910.7 million General Fund) for mental health services. This reflects an increase of $165.9 million, or 0.07 percent, over the 2003 Budget Act. Of the total amount, $1.807 billion is for local assistance, $735.6 million is for state hospitals, $18.4 million is for department support, and $7,000 is for state mandated local programs.

The DMH promotes access to appropriate statewide mental health services for California residents. As the State's mental health authority, the Department invites the participation of numerous persons and organizations.

Chapter 89, Statutes of 1991, established the State-Local Realignment which realigned to counties the funding and programmatic responsibility for the majority of local mental health programs, the Institutions for Mental Disease (IMD) program, and the use of Lanterman-Petris-Short (LPS) State Hospital beds. In 1991-92, the counties took full responsibility for the realigned local mental health programs. In addition, the IMD programs were transitioned to the counties beginning July 1, 1992. The DMH will continue to administer the State Hospitals. However, annual contacts are entered into between the DMH and the counties for the use of LPS beds at the hospitals.

Under the provisions of State-Local Realignment, and in keeping with the transfer of responsibility and funding for mental health services, counties are responsible for the provision of mental health services to their residents. Services include prevention and control of mental illness through community education and consultation, crisis evaluation and emergency care, 24-hour acute care. 24-hour residential treatment, day care treatment, outpatient care, case management, and resocialization. The Department sets overall policy for the delivery of mental health services statewide: executes and oversees performance contracts with county mental health departments, monitors compliance with state and federal statutes, and oversees various state-funded programs, and projects consistent with specific departmental objectives.

Within the DMH's overall goal of upgrading, balancing and integrating community and State-operated services, the objective of the Long-Term Care Services program is to complement mental health services in the community. Under State-Local Realignment, the Department provides hospital services to civilly committed patients under contract with local mental health departments. Judicially committed patients continue to be treated through state-funded programs.

DEPARTMENT OF MENTAL HEALTH BUDGET SUMMARY				
Fund Sources (Dollars in Thousands)	**2003-04**	**2004-05**	**$ Change**	**% Change**
General Fund	$878,929	$910,658	$31,729	%3.6
Restitution Fund	0	0	0	0
Traumatic Brain Injury Fund	1,575	1,422	-153	-10.0
California State Lottery Education Fund	1,397	1,397	0	0
Federal Trust Fund	61,993	61,917	-76	-0.1
Reimbursements	1,432,942	1,567,332	134,390	9.4
Total	**2,376,836**	**2,542,726**	**165,890**	**7.0**

MAJOR PROVISIONS

The major provisions of the proposed Department of Mental Health budget include:

- **State Hospitals.** The Governor's Budget includes $702.4 million ($560.8 million General Fund), a net increase of $31.6 million ($36.4 million General Fund) above the 2003 Budget Act for state hospitals. This funding level will support a total caseload of 4,605 state hospital commitments.

  The Administration has found that over the last ten years, the General Fund of operating the four state hospitals has increased 124 percent. The Governor's solution to the increased per patient costs and General Fund expenditures is to reform how state hospital services and related clinical functions are provided to mentally ill individuals with criminal histories. The following are the significant reforms proposed for judicially committed patients and Sexually Violent Predators:

  - **Indeterminate Commitment of Sexually Violent Predators (SVPs).** The Governor's Budget includes a reduction of $2 million General Fund by changing the SVP commitment from two years to an indeterminate length in order to eliminate unnecessary evaluations and recommitment trials.

  - **SVP Treatment Reform.** The Budget proposes a decrease of $823,000 General Fund to reflect proposed restructuring of the supervision and treatment services

provided to SVP patients. The Administration estimates that savings from this reform, would be $9.2 million beginning in 2005-06.

- **Civil Commitment Trials Held Prior to Release from Prison.** The Budget proposes holding SVPs in local custody if they have completed a prison sentence and are awaiting a commitment hearing. This appears to be a fund shift from the state to the counties, which would be required to pay for judicially committed patients between their prison terms and their civil commitments in state hospitals. This could also create additional, unnecessary levels of bureaucracy by moving individuals between the state and local jurisdictions and back again. The Administration is estimated a savings of $10.7 million General Fund in 2004-05.

- **Maintain State Hospital Population.** The Governor's Budget includes anticipated savings of $2.8 million ($3.7 million General Fund) to reflect a proposal to prioritize patient intake based on the need for treatment. The Administration argues that the proposal is necessary to curtail the un-sustainable growth in General Fund expenditures for judicially committed patients. However, it will be important to understand the actual proposals on how to achieve this savings and on what basis the prioritization would take place. The Governor's Budget also includes augmentations for the SVP Program.

- **Sexually Violent Predator Evaluations.** The Administration requests a General Fund augmentation $1.1 million in the budget year in the DMH's support appropriation to reflect an increase in the number of SVP evaluations to be performed by private contractors, as well as costs for evaluator court testimony. It will be important to understand how the reforms related to indeterminate commitment will impact the caseload of evaluations.

- **Early and Periodic Screening Diagnosis and Treatment (EPSDT) Program.** This program entitles approximately 170,000 Medi-Cal eligible children and young adults to receive services that ameliorate a diagnosed mental illness. The total budget for EPSDT includes $787 million ($365 million General Fund) to continue these services.

  EPSDT is a federal entitlement under the State's Medi-Cal Program. To meet the requirement of the TL. v. Belshe' lawsuit, in 1995-96 the Department of Health Services requested that county mental health programs expand the Short-Doyle/Medi-Cal mental health services to eligible Medi-Cal beneficiaries under EPSDT. Consequently, the program has been in effect for less than 10 years. In 2002-03, a 10 percent county match on the growth of the total state matching requirement above the Fiscal Year 2001-02 funding level was implemented to establish a financial incentive at the county level to ensure that funds are spent efficiently for medically necessary services to the EPSDT eligible population.

However, due to an increase rate of General Fund expenditures, the Governor's Budget proposes to curb expenditures in EPSDT through the following means:

- **Update Maximum Rates.** The Budget includes an estimated savings of $60 million ($40 million General Fund) based on a survey of actual costs as indicated under the State's federal plan. The adjustment of rates would occur after the survey is completed.

- **Increased Oversight.** The Governor's Budget includes a net savings of $5.7 million General Fund to reflect the implementation of targeted audits of claims. The DMH requests an augmentation of $1.7 million ($844,000 General Fund and $844,000 in FFP from DHS) to support contractual assistance for additional review and oversight of EPSDT expenditures. The Administration estimates that this effort will result in the recuperation of $13 million annually ($6.5 million General Fund) and expects to further slow program growth.

  Prior efforts have been made to slow program growth. Budget Trailer Bill for Fiscal Year 2002-03 required DMH to ensure statewide application of managed care principles to the EPSDT Program caseload growth. Regulations to initially implement this requirement have been approved by the Office of Administrative Law and were endorsed by the Secretary of State on November 18, 2003. The 2002 Budget Act also implemented a 10 percent county match on program growth. These efforts have resulted in a reduction in the rate of growth from about 30 percent annually to about 16 percent in the budget year. The rate of program growth has been reduced by almost half, but the Administration is concerned about that the overall program is still growing.

- **Federal Relief.** Consistent with the larger Medi-Cal reform effort, the State will also pursue federal authority to narrow the very broad medical necessity criteria. The DMH is requesting $472,000 ($236,000 in reimbursements from DHS as FFP and $236,000 General Fund) to support two limited term positions, as well as the contracted assistance needed to develop an application for a federal 1115 Demonstration Project waiver.

  DMH is collaborating with DHS in exploring options to increase state flexibility regarding the federal requirements for the EPSDT specialty mental health benefit that would meet the mental health needs of EPSDT beneficiaries while possibly lowering program costs. The current federal regulations and statutes require states to provide any medically necessary health or mental health treatment services needed to correct or ameliorate the mental or physical health condition of full-scope Medi-Cal beneficiaries under the age of 21.

  Currently, no DMH staff is assigned to collaborate with DHS on a federal waiver application of this complexity. DMH staffing levels have already been significantly restricted to meet required budget reductions. The requested DMH positions' focus will be providing DHS with the assistance and information needed in the waiver application that will continue to maintain essential EPSDT mental health services for

Seriously Emotionally Disturbed children and youth while determining ways to improve program effectiveness and accountability.

The Governor's Budget also includes funding adjustments to the EPSDT Program.

- **Program Cost Adjustment.** The DMH requests an increase in local assistance reimbursements from the Department of Health Services of $13.1 million in the current year to reflect additional costs for the provision of services through the EPSDT Program. The Department also requests an increase in the budget year of $317.6 million to reflect additional program costs.

- **Community Mental Health Services.**

  - **Children's System of Care (CSOC) Program.** The Governor's Budget includes the total elimination of the CSOC Program. The Administration's reasoning is that there is both a wide range of medically necessary services available to Medi-Cal eligible children and a large amount of Medi-Cal children receiving EPSDT services. However, a significant proportion of the population served by the CSOC is not eligible for necessary services within Medi-Cal's EPSDT program.

  - **Early Mental Health Initiative.** The Governor's Budget includes a reduction of $5.0 million to reflect the elimination of second round grants for the Early Mental Health Initiative. This grant cycle is completing their final year of a three-year program in the current year. After two years of budget reductions, this program would be at one-third its initial size, serving one-third of the children previously served for mental health issues related to school adjustment.

ADDITIONAL HIGHLIGHTS

Additional highlights of the proposed Department of Mental Health Budget include:

- **Medi-Cal Mental Health Managed Care.** The Governor's Budget includes an increase of $10.0 million ($5.1 million General Fund) to reflect an increase in caseload in county managed care patients.

- **Preadmission Screening and Residential Review.** The Budget reflects an increase of $1.9 million ($470,000 General Fund) for the proposed expansion of the Preadmission Screening and Residential Review Program. Through this program, individuals admitted to nursing homes are evaluated to determine if specialized mental health treatment alternatives, that are available in communities at lower costs, can better meet their needs.

- **Coalinga State Hospital.** The Governor's Budget reflects an increase of $24.9 million General Fund and 166.8 Personnel Years for continued activation of

Coalinga State Hospital, which is scheduled to open in August 2005. This funds the Phase IV and V for non-level-of-care staff, Phase V of level-of-care staff, operating expenses and equipment, recruitment and retention pay differentials, hiring above minimums, and non-level-of-care staff for Atascadero and Patton State Hospitals to accommodate the over- bedding that will occur until Coalinga State Hospital is completed.

The Administration argues that this request should be viewed as the fourth and fifth phase of a long-term, ongoing ten-phase effort that is required to meet the intent of the Governor and the Legislature in developing a new state hospital for the SVP population. As the hospital census expands beyond the 175 beds associated with Phase V, additional non-level-of-care and level-of-care staffing resources will be needed. This request is coordinated with the hospital population projection to ensure there is no duplication of level-of-care positions between Coalinga, Atascadero, and Patton State Hospitals. To this point, the State has committed approximately $394 million for construction and staffing of this project.

- **Health Insurance Portability and Accountability Act (HIPAA).** The Governor's Budget requests a General Fund augmentation of $246,000 for support of 3.0 associate level positions and operating expense costs to absorb the workload required to successfully implement and maintain HIPAA regulation standards primarily in the state hospitals and inpatient psychiatric programs.

- **State Hospital Population Adjustment.** The Governor's Budget includes a net reduction of $6.8 million (a decrease of $4.7 million General Fund and $4.1 million in realignment reimbursements and an increase of $2.0 million in reimbursements from the California Department of Corrections) to reflect a net decrease of 96 state hospital beds. Also included in this request is an increase of $3.5 million for operating expenses and equipment.

- **Forensic Conditional Release Program (CONREP).** The Governor's Budget includes a proposal to augment General Fund expenditures for the Forensic Conditional Release Program by $657,000 to support: 1) increased costs for patient services ($464,000); 2) full-year costs for five additional patients ($105,000); and 3) additional costs for state hospital liaison visits ($88,000).

  Program funding provides outpatient services to patients in the community and hospital liaison visits to patients continuing their in-patient treatment at the state hospitals, who may eventually be admitted into CONREP. The patient population includes Not Guilty by Reason of Insanity, Mentally Disordered Offenders, and Sexually Violent Predators. These services are provided in the state by either county operated or private non-profit organizations under contract with DMH.