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COUNTY OF LOS ANGELES
DEPARTMENT OF HEALTH SERVICES
313 N. Figueroa, Los Angeles, CA 90012
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December 6, 2004

TO: Each Supervisor

FROM: Thomas L. Garthwaite, MD 
Director and Chief Medical Officer

SUBJECT: KING/DREW MEDICAL CENTER PROFIT MARGIN

At the November 30, 2004, meeting of the Board of Supervisors, the Department of Health Services (DHS) was asked to provide a response to the statement that King/Drew Medical Center is one of the most profitable hospitals in the United States.

This issue came about as a result of an article in the June 2004 issue of Managed Healthcare Executive Magazine on the subject of teaching hospital profitability, which identified King/Drew Medical Center as having a total profit margin of 36.9 percent, significantly higher than the other hospitals identified in the publication's survey.

The Department contacted Managed Healthcare Executive Magazine and obtained their calculations and source document for this information, which was the hospital's Fiscal Year 2002-03 Medicare Cost Report. Based on a review of this information, DHS Finance staff determined that the calculation incorrectly included gross revenues for the SB 855 (disproportionate share payments) and SB 1255 (supplemental Medi-Cal inpatient payments) programs, which included the hospital's intergovernmental transfer. However, the intergovernmental transfer of funds also should be recognized as an expense; not offsetting the revenue with the expense results profits being overstated. Also, Realignment funds (e.g., Vehicle License Fees and Sales Tax) and net County contribution were inappropriately reported as revenue to the hospital, as opposed to subsidies, which do not impact profit.

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The result of the incorrect reporting of these funds resulted in the impression that King/Drew Medical Center operates at a profit. Based on DHS' calculations, that included net SB 855 and SB 1255 funds and excluded Realignment and net County contribution dollars, King/Drew Medical Center's financial picture changes from a profit margin of 36.9 percent to a loss of 3.6 percent.

To avoid future confusion as to DHS hospital revenues or profitability, and to provide a more accurate presentation of revenue, DHS and facility finance staff have been instructed that in future Medicare cost reports SB 855 and SB 1255 revenues should be reported as net revenues and the Realignment and net County contribution funds should be excluded. Additionally, the Fiscal Year 2002-03 hospital cost reports are being reviewed and any that are inconsistent with this accounting will be amended.

Please let me know if you have any further questions.

TLG:ak

c: Chief Administrative Officer
County Counsel
Executive Officer, Board of Supervisors