

State Budgeting Matters

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Highlights

- *Funding is preserved for some key services, such as the children's Medicaid expansion, adult and child protective services, food banks, and the Unified Long Term Care Budget.*
- *The Senate reduces GRF appropriations by \$617 million, but Conference Committee revenue estimates are expected to be even lower.*
- *It will be difficult for state agencies to meet statutory obligations at current funding levels.*
- *Spending on Ohio's nursing homes and hospitals is increased.*
- *Without significant change, the state faces a deficit in the FY 2012-2013 budget of more than \$8 billion.*

The Good, the Bad, and the Ugly

Highlights from the Senate Version of H.B. 1

As the national recession continues, states are finding that tax revenues continue to fall far short of expectations. Ohio is no exception. Policymakers have reacted to news that Ohio's financial troubles for the current budget year have worsened by using reserves to fill the gap that had been allocated to the Fiscal Year (FY) 2010-2011 budget.

The Senate-passed version of H.B. 1, the FY 2010-2011 operating bill, lowers state spending to offset revenue reductions resulting from the recent federal cigarette tax increase and the planned use of the state's Rainy Day Fund in FY 2009. It reduces biennial appropriations in the General Revenue Fund (GRF) by \$417 million and across all funds by \$967 million. In addition, the Senate assumed biennial savings of an additional \$200 million in GRF cuts by codifying a recent Executive Order requiring state agencies to reduce spending on contracts and other services and through \$42 million in state share GRF from newly added Medicaid cost-containment initiatives.

When the next estimates are released, it is expected that state revenues could fall by as much as \$2 billion more over the biennium than was expected when the budget was released in February. The Conference Committee has the unenviable responsibility of figuring out how to close this gap. While the Senate bill preserved many key human services initiatives, the depth of cuts to state agencies will make it difficult if not impossible to meet the growing demands on the state over the next two years. The revenue gap cannot be closed by cuts alone without causing more harm to individuals and the state economy; the tax changes made in H.B. 66 must be revisited as well. This issue of *State Budgeting Matters* will review the current version of the bill and identify the challenges ahead for the Conference Committee.

The Good: Protects Some Key Services and Contains Costs

The Senate budget maintains the Medicaid expansion for children with family incomes between 200 and 300 percent of the Federal Poverty Level. The budget also retains the \$50 million per year that the House added for child and adult protective services (reduction of \$12 million from FY 2009 budgeted levels) and \$13 million per year in funding for Ohio's food banks.

The Senate bill keeps changes to the Unified Long Term Care Budget that will increase home- and community-based care options by expanding the PACE and Choices programs statewide, eliminating the cap on assisted living waiver slots, and increasing flexibility in care settings by allowing the department to seek federal approval to combine all of its Medicaid waivers into one.



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The Senate eliminated a controversial Strickland administration proposal that would have allowed the use of loaned executives and the creation of nonprofits by state agencies.

To begin to address the state's longer-term gap between revenue and expenses, the Senate bill includes a number of initiatives to reduce the cost of Medicaid. The bill:

- requires prior authorization for high technology radiological services such as MRIs;
- creates an e-prescribing system for the 10 providers who write the most prescriptions;
- creates a disease management program aimed at improving health outcomes using proven prevention strategies; and
- pilots the use of various alternative care management models for patients with multiple chronic conditions.

Limiting potential growth in debt service payments, the Senate excludes federal stimulus funds from the calculation of the state's 5 percent limit on debt and prohibits the use of certificates of participation and other debt instruments that enable state agencies to enter into lease-purchase agreements for buildings, equipment, information technology, and other non-highway projects without the approval of the General Assembly.

The Bad: Makes Additional Cuts and Further Erodes State Revenues

Spending cuts made by the Senate are significant. The Senate bill reduces GRF appropriations in the Disability Financial Assistance program by \$24 million over the biennium. This program provides a subsidy of \$115 per month to persons at or below the Federal Poverty Level¹ who have been determined disabled by the Department of Job and Family Services and are awaiting Social Security disability determination. As the wait for federal benefits has increased, people tend to stay in this program longer. Unless more money is found, reductions in eligibility or benefits levels will result.

The Senate bill replaces \$31.5 million over the biennium in GRF dollars for kinship care and Help Me Grow with TANF dollars. While Ohio had a surplus balance for many years, Ohio's TANF grant is currently overspent by \$50 million and is fully committed for the next biennium. To

fund these two initiatives, then, TANF funding for other services would have to be reduced. The TANF grant funds are primarily used for cash assistance; county prevention, retention, and contingency programs; and subsidized child care.

Even though extensive research has shown that disease prevention and health promotion reduces health care treatment costs, the Senate bill eliminates all state funding in the Department of Health for prevention, including tobacco cessation.

Further weakening Ohio's revenue structure, the Senate bill adds a transferrable film tax credit of up to \$100 million per year at a time when the state cannot meet the demand for the basic needs of its citizens. Forty-one other states offer some type of credit, which creates competition and bidding wars between states that seems to benefit Hollywood moguls more than the states where they come to film.²

And the Ugly: Increases the State's Structural Deficit

As bad as the FY 2010-2011 budget is looking, without significant revenue increases now, the FY 2012-2013 budget will look worse. With the loss of federal stimulus and other one-time funds and even with only limited growth in spending, the state faces a deficit in the FY 2012-2013 budget of more than \$8 billion. Several provisions added to H.B. 1 will make the FY 2012-2013 budget problem even worse.

Since its introduction, H.B. 1 has contained cash management actions that increase available funds for the FY 2010-2011 biennium but at greater cost to the state over the long run. One such action is to refinance state debt to reduce debt service payments by \$453 million over fiscal years 2009, 2010 and 2011. This action is expected to raise debt service payments by \$61.3 million in the FY 2012-2013 biennium plus more after that. The Executive Budget included use of \$200 million from cash currently held by the School Facilities Commission.³ The Senate bill borrows an additional \$50 million from this pot, bringing the total to \$250 million for this biennium. In addition, the Senate has added a provision requiring the school facility funds to be repaid in the FY 2012-2013 biennium.

While the budget process has been challenging for most, Ohio's nursing homes and hospitals have done well and

emerged relatively unscathed. The Executive Budget had imposed additional franchise fees on nursing homes and hospitals to support the Medicaid program. The cost of the new fees, net rate increases, was \$332 million to hospitals and \$117 million to nursing homes.⁴ The nursing homes were also facing a \$112 million reduction tied to the final phase-in of the price-based formula implemented in FY 2006. The House increased spending on nursing homes by \$233.7 million over the biennium, and the Senate followed with an additional \$143.3 million. On the hospital side, the House increased spending by \$527.4 million and the Senate by an additional \$70 million.

The changes made to benefit hospitals and nursing homes increase state spending without covering additional people or improving quality of care. The actions taken will also add to Ohio's structural deficit—the gap between what the state needs to spend and the money it expects to have.

Nursing homes

Ohio's supply of nursing home beds exceeds demand. The Executive Budget was on the right track to reign in long-term care costs; however, progress has been derailed by strong lobbying by Ohio's skilled nursing coalition. Instead of following through on the final phase-in of the price-based reimbursement system that the industry has had four years to prepare for, the House and Senate increase facility rates and slow migration to the price-based formula.

In addition to rate increases, the Senate adds provisions that will increase future costs as well. First, beginning in FY 2013, state law will require nursing home rates to be adjusted annually for inflation. The Senate creates conditions under which nursing homes could convert to intermediate care facilities for the mentally retarded (ICFs). While the occupancy rate in Ohio's ICFs hovers close to 100 percent, the investment in this system has been in home- and community-based alternatives. Finally, the Senate weakened proposed changes to the state's certificate of need program for nursing facilities even though the occupancy rate in FY 2007 in Ohio's nursing homes was 84 percent.

Hospitals

The Senate tweaked changes made by the House to increase the amount returned to the industry to equal the amount of revenue collected under the franchise fee. The Senate accelerated the effective date of the 5 percent Medicaid hospital rate increase from January 1, 2010, to July 1, 2009, increasing state costs by \$70 million in FY

2010. The Senate also provided rate increases for businesses affiliated with hospitals including home health care, hospice, and ambulance services. This provision favors members within a Medicaid provider class based only on ownership. Home care providers are already paid different rates for providing the same service by the three state agencies that purchase their services. Further fracturing the provider base could destabilize this market. The Senate maintained the Supplemental Upper Payment Limit Program, which will redistribute franchise fee dollars back to hospitals. Finally, the Senate moved the franchise fee to temporary law and called for it to expire at the end of the next biennium. Between the fee and the federal revenue generated from the fee, the hospital tax raises about \$1 billion per year.

Neither the House nor the Senate chose to retain the executive proposal to control Medicaid costs by requiring hospitals to contract with managed care at Medicaid fee-for-services rates. Medicaid managed care companies are required to contract with providers, including hospitals. In some areas of the state where the number of providers is limited, some providers were able to leverage their market share by requiring that they be paid higher rates. Closing this loophole would have saved the state \$146 million in this biennium and more in the next. This practice has uneven benefits across the system and has no connection to the quality of services provided.

Concerns as the Bill Moves to Conference Committee

Many agency appropriations are at the lowest level in a decade, raising concerns about how they will meet their statutory responsibilities. Of particular concern is the impact on the Department of Job and Family Services (JFS). The bill also assumes savings from agency cuts that have yet to be identified, making it impossible to assess the impact on programming.

Impact of Deep Cuts to the Department of Job and Family Services

Over the years, JFS has been the punching bag of state government and, in some cases, rightfully so. But many of its missteps have been corrected, and the importance of the agency's role during an economic downturn cannot be overstated. Major programs administered by JFS include:

child welfare, child support, Medicaid, food stamps, cash assistance, unemployment compensation, and workforce development.

At each step in the process, funding for Ohio's largest GRF-funded agency has been reduced. As the budget currently stands, in FY 2011, GRF funding for JFS administration will be \$69 million less than it was in FY 2006, and it will be \$36 million less than it was in FY 2009, which followed three rounds of budget cuts. In addition, much of JFS's GRF administrative funding is matched with federal dollars, making the impact of these cuts even greater. It is doubtful that this agency in its weakened state or its county partners will be able to respond to the needs of an increasing number of Ohio's citizens.

State Impact

Most of Ohio's human service programs are state supervised and county administered. Both pieces are integral to ensuring the delivery of services in an efficient and cost-effective manner. Many program requirements are set by the federal government, which also provides the lion's share of the funding. Federal officials often employ a one-size-fits-all approach for the 50 states, which makes management across multiple levels of government complex for states such as Ohio that favor local control.

JFS has been struggling for years to keep its multiple ancient Information Technology (IT) systems up-to-date and functional, manage substantial policy changes at the national and state levels, and realign service delivery following the merger of the Department of Human Services and the Bureau of Employment Services.

The age and condition of many of JFS's IT systems has been a concern for years. Many of the workforce and unemployment compensation systems have been improved, and SACWIS, the state's child welfare system, is now operational in all counties. The Medicaid Information Technology System (MITS) is expected to be implemented in December, 2010, and stands to significantly improve the efficiency and management of the Medicaid program. However, the system at the core of human service programming is CRIS-E, the "front door" for most public benefits and Ohio's eligibility determination system since 1989. Data from CRIS-E are used by many other programs and IT systems. To put this into a technological and policy perspective, this system predates Microsoft Windows (1990) and welfare reform (1996), both of which have revolutionized the way business is done in this arena. The system has been scheduled for replacement, but this has been prevented by a lack of available funding over the past three biennia. The current system is very cumbersome to use for programmers who have to keep it up to date to reflect current policy and by caseworkers who find the current design increases errors that multiply as the data are spread through other systems.

Table 1. JFS Central Administration Spending (\$ in millions)³

Line Item	Line Item Name	Actual FY 2006	Actual FY 2007	Actual FY 2008	Estimate FY 2009	Senate FY 2010	Senate FY 2011	FY 2011 Compared to FY 2006	FY 2011 Compared to FY 2009
600-321	Support Services	\$58.4	\$60.4	\$56.3	\$54.2	\$46.6	\$46.6	(\$11.7)	(\$7.6)
600-416	Computer Projects	\$132.5	\$130.5	\$137.6	\$106.2	\$87.5	\$87.7	(\$44.8)	(\$18.5)
600-417	Medicaid Provider Audits	\$ –	\$ –	\$1.3	\$1.6	\$2.8	\$2.8	\$2.8	\$1.2
600-420	Child Support Administration	\$4.2	\$4.9	\$6.7	\$7.7	\$7.4	\$7.4	\$3.2	(\$0.3)
600-421	Office of Family Stability	\$4.1	\$2.9	\$3.5	\$2.7	\$2.7	\$2.7	(\$1.3)	\$ –
600-423	Office of Children and Families	\$4.8	\$5.3	\$5.3	\$4.8	\$4.8	\$4.8	\$0.0	\$ –
600-425	Office of Ohio Health Plans	\$40.7	\$46.0	\$40.5	\$34.7	\$30.0	\$23.4	(\$17.3)	(\$11.3)
TOTAL		\$244.6	\$250.1	\$251.1	\$211.9	\$181.8	\$175.5	(\$69.1)	(\$36.5)

Note: Numbers may not add due to rounding.

To implement the policy changes included in this bill that affect JFS or other state agencies that administer portions of the Medicaid program, activities that will be required of JFS staff include:

- Draft rule changes, notify affected parties, hold hearings;
- Draft State Plan Amendments, negotiate changes with the federal government;
- Draft and enter into interagency agreements with one or more state agencies to administer parts of JFS programs;
- Update and test all IT systems, enter policy changes, and ensure that they are effective on the proper date;
- Provide training and technical assistance to affected parties, including providers and county partners, on policy changes and how they will be implemented; and
- Provide oversight and audit functions to ensure program integrity and protect against fraud, waste, and abuse.

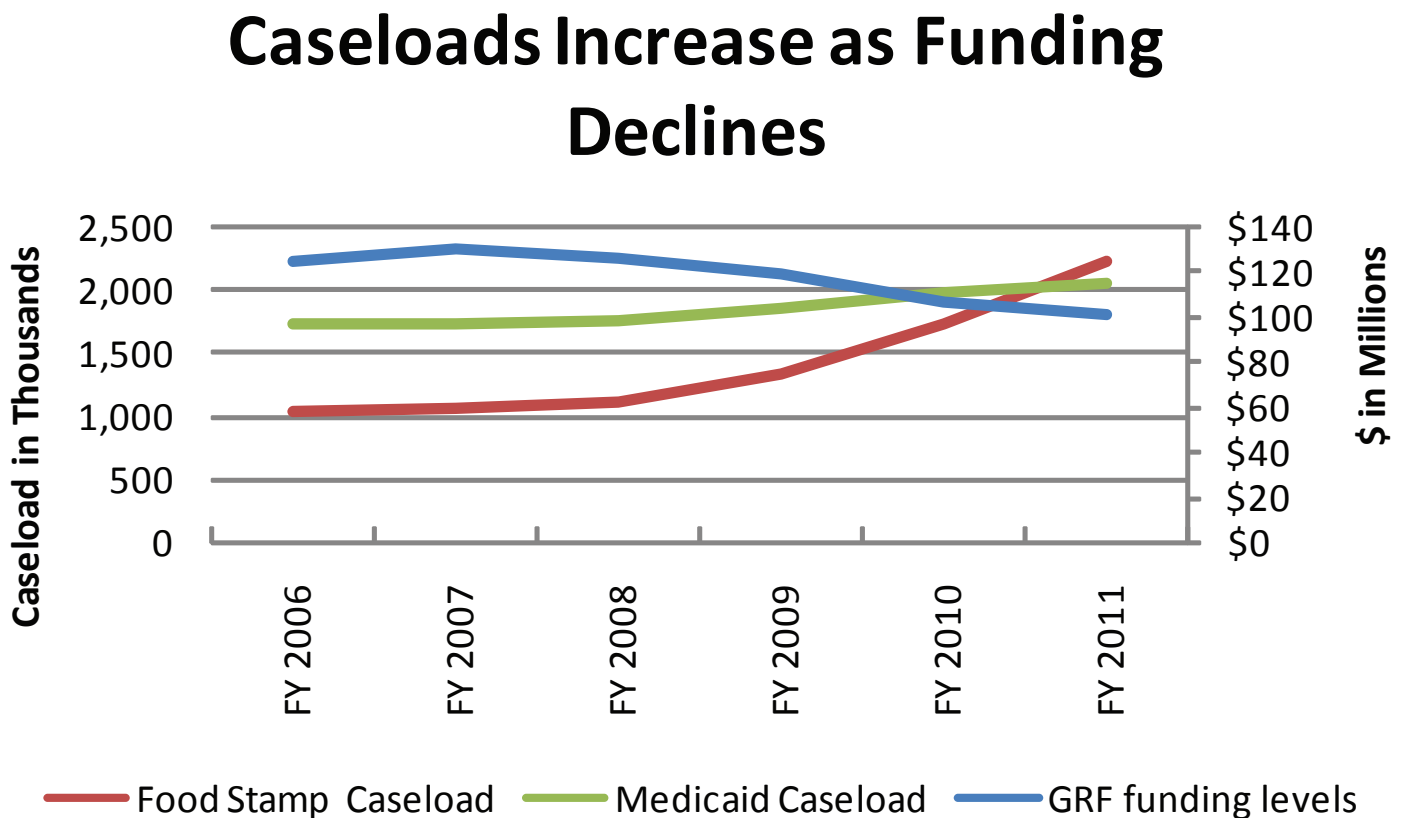
At the same time, given the funding levels in H.B. 1, the agency will need to undergo a significant restructuring and reduction in workforce in order to remain within appropriated levels.

As of December, 2008, JFS had 3,688 employees, almost half of whom were assigned to Department of Labor (DOL) programs including workforce development, unemployment compensation, and local operations and were paid with federal funds. Since FY 2006, non-DOL staffing levels have been reduced by 15 percent.⁶

County Impact

As policy changes are made at the state level, they must be implemented at the county level. Counties have seen record growth in caseloads, while state support has fallen. Figure 1⁷ shows the decrease in funding compared to the increase in caseloads supported by the funds.

Figure 1.



In addition to reductions in funding for eligibility determinations, counties are also facing reductions in TANF funding. As the state has spent the TANF surplus balance and as cash assistance caseloads have increased, TANF funding for county prevention, retention, and contingency (PRC) programming has declined over the past biennium and will be reduced further in the next as well. (PRC helps families maintain self-sufficiency and assists families with emergencies.)

Inadequately funding this system as caseloads increase will likely lead to lower-quality services, decreased accuracy, missed federal performance requirements, and potential federal lawsuits over case processing times. Over the long run, this will lead to higher costs and federal penalties.

Unidentified Cuts and Cash Raids

As the bill currently stands, balancing the FY 2010-2011 budget will mean more than \$500 million has to be reduced from GRF appropriations and non-GRF fund cash raids. Because the programs and funds that will be affected by these reductions have not yet been identified, it is impossible to know the impact of these changes. The reductions would come on top of three rounds of budget cuts in fiscal years 2008 and 2009, as well as significant reductions to agency spending taken along each step in the budget process. Additional cuts likely will hinder basic operations.

H.B. 1 includes broad rotary® raid authority that supersedes state statute to allow the Ohio Budget and Management director to transfer funds from any non-GRF account to the GRF. The Senate eliminates appropriations in the Departments of Development and Health that were backed with cash taken following the closure of the Tobacco Use Prevention and Control Foundation. This cash transfer of roughly \$230 million is currently the subject of a lawsuit. Should the judge release these funds to the state, they likely will be used to shore up the GRF.

The Senate codifies Executive Order 2009-07S, Implementing Additional Spending Control Strategies, and assumes \$100 million per year in GRF savings from appropriated levels. The Executive Order required agencies to develop plans to reduce spending on contracted services and supplies by 30 percent by placing limitations on travel and use of personal electronic devices, and required increased use of central administrative services such as printing, mailing, purchasing standardization, and IT system consolidation. Following three rounds of cuts,

one would assume that discretionary spending has been curtailed, and additional reductions will result in program cuts. As this order applies to GRF savings only, the impact will be uneven across state agencies.

Challenges Lay Ahead for Conference Committee

All of this adds up to a clear need to revisit Ohio's revenue policy.

The state's economy cannot rebound fast enough to avoid disaster in FY 2012-2013. Tax changes made in FY 2005 have reduced the state's largest source of revenue and its most progressive tax—the state income tax—by 21 percent over the past five years. In addition, the state's corporate income tax on non-financial businesses has been eliminated. These taxes were replaced with a new tax on business gross receipts that brings in only enough money to reimburse schools and local governments for the phase-out of a local tax on business machinery and inventory. By design, Ohio's tax overhaul has reduced revenues in the state treasury over \$2 billion each year. It might have seemed to some like a good idea at the time, but the reality today is that Ohio cannot afford these policies.

The state is confronted with both a short-run and a long-run challenge. First, the state must get through the current recession. Second, the state must address a structural deficit extending into the future. Throughout this budget process The Center for Community Solutions has spotlighted the insufficiency of Ohio's diminished revenue structure to support state spending essential to meeting the needs of Ohio's families. It is time for action.

1. The Federal Poverty Level is \$10,830 for a single-person household.
2. Waggoner, Martha. "States Give Hollywood a Fortune in Tax Breaks." *Associated Press*, June 2, 2009.
3. The School Facilities Commission received \$4.1 billion from the securitization of the state's share of Tobacco Master Settlement Agreement that took place in October, 2007.
4. Ohio Department of Job and Family Services Projected Medicaid Expenditures FY 2009-2011, Executive Submission, February, 2009.
5. Legislative Service Commission, *Budget in Detail*.
6. Legislative Service Commission, *LSC Redbook, Analysis of the Executive Budget Proposal, Department of Job and Family Services*. March 2009, page 2.
7. Ohio Department of Job and Family Services Public Assistance Monthly Statistics Report; Ohio Department of Job and Family Services Projected Medicaid Expenditures FY 2009-2011, Executive Submission, February, 2009; and updated growth assumptions for food stamps from the department.
8. Rotary funds are non-GRF accounts that contain revenues for a specific purpose such as hunting and fishing licenses.