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## ***Analysis of Missouri Governor's Additional \$239 Million Budget Reductions & Revenue Increases, Announced March 25, 2005***

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On March 25, Governor Blunt announced a detailed plan to balance the remaining hole in the Fiscal Year 2006 budget with a package of spending reductions and revenue enhancements that equal \$239.2 million. The \$239.2 million is in addition to spending cuts of \$362 million in General Revenue (\$1.1 billion in combined General Revenue and Federal Funds) reductions submitted in the Governor's original budget proposal in January. It was initially assumed these cuts would be made by Department Directors at the beginning of FY 2006. Instead of waiting until July to make these reductions, the Governor's Office has released this plan. The purpose of this report is to review and analyze these recommendations.

In order to emphasize the severity of the cuts, it is essential to note that they come on the heels of the substantial cuts in vital programs that were proposed in January. The new cuts would be in addition to ones already being debated by the Missouri Legislature. The bulk of the original proposed cuts would be to Medicaid which now is embodied in Senate Bill 539, as well as HB 11. Also garnering considerable attention has been the cuts to or restructuring of the "First Steps" program. It is also important to note that the FY 2006 budget cutting proposed in January and now in March comes on top of four years of massive budget cuts. The budget cuts enacted since FY 2001 have already had severe negative consequences which include:

- State support for Elementary and Secondary Education is now underfunded by an estimated \$600- \$800 million, resulting in lawsuits;
- State support for colleges and universities has declined about 10% since FY 2001 which has led to tuition increases of over 50% at most institutions;
- Substantial cuts to the State Medicaid program have already occurred and funding for state Mental Health facilities has also been severely reduced, impacting more than 135,000 Missourians, and
- Since FY 2001, Missouri state employees have received only one significant pay increase and have become the lowest paid in the nation.

### **Section I: \$108 million generated through Additional Revenue Increases / Savings:**

Five major elements in the Governor's plan account for about 45% of the \$239.2 million needed to balance the FY 2006 budget. These changes result in revenue increases by making tax changes, and free up funds through cost containment measures.

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### **I. Managed Care Savings - \$9 million**

Many of the State's Medicaid consumers are enrolled in a "Managed Care" program which is the equivalent of a Health Maintenance Organization. This generally saves the state money relative to paying on a "fee for service" basis. The state negotiates a pay rate per person with the managed care companies. The rate must be actuarially sound, in that the pay rate must be sufficient for the provider to meet its costs and provides the medical services that the contract requires. These costs increase annually with the rise of rates to provide health care services.

To meet the increased costs, the State must budget in anticipation of the requirement to pay a higher rate. Due to the fact that cost increases cannot be known with certainty, the state determines a range of rates that are deemed to be actuarially sound. The Department of Social Services (DSS) set the amount in January of 2005 but has since then determined that a lower increase than expected for managed care costs will be achievable. This change in what the state will pay for managed care will save the state about \$9 million in FY 2006.

### **II. Managed Care Provider Taxes - \$31 million**

The remaining \$31 million in "savings" within Managed Care specifically is expected to come about by the imposition of a "provider tax" on Managed Care providers. This tax will be paid to the state by the providers who will in turn be reimbursed by the Federal government through additional Federal matching funds. A similar system of provider taxes is used by hospitals and nursing homes to maximize Federal Medicaid funds. There is little doubt that a "provider tax" on Managed Care providers could provide revenues/savings to the state. For this to occur, the following is required:

- An explicit change in Missouri law to allow for this
- The cooperation of Managed Care providers
- Continued acquiescence on the part of the Federal government for this sort of approach

It is certainly possible that the state may be able to realize \$40 million in combined Managed Care savings in FY 2006 from these actions. This is with the caveat that certain assumptions have been made, and must come true. Some caution may be in order, particularly with the Federal government known to be looking to reign in its Medicaid costs. Missouri is under increased scrutiny of its matching funds mechanisms and was required several years ago to enter into a consent agreement with the federal government. In the agreement, the state it required to report and identify any new provider taxes being considered before they are implemented. This allows the federal government to review and approve such changes in advance. The administration must obtain Federal support for this plan. In the event that the provider tax fails to achieve federal support additional cuts will simply have to be made.

### **III. Pharmacy Cost Savings - \$18.8 million**

As is the case with Managed Care, the state budgets for increased costs in its Pharmacy program each year. Since the budget was released in January, DSS officials believe that a lower cost increase rate is achievable, resulting in the savings of \$18.8 million. As with any budget estimate that is more optimistic, it could lead to problems later on should pharmaceutical prices spike or other unforeseen events occur.

### **IV. FY 2005 "Confirmed Lapse" - \$20 million**

The Governor expects to generate an additional \$20 million by implementing some of the FY 2006 proposed budgets cuts in the current fiscal year, beginning in April. The money "saved" would become, in essence, "revenue" for FY 2006. There is little doubt that the state could

realize these savings in FY 2005. However, there is a problem counting these funds as revenue. The FY 2006 “revenue” that results from this is one-time revenue that is being used in effect to fund an ongoing budget in FY 2006 and beyond. This use of one-time funds in past years has been severely criticized by the Legislative leadership and the Governor’s office.

Such accounting will militate toward additional reductions in FY 2007 and beyond, because the savings only actually occurred in one year. In addition, current projections for the FY 2005 revenues indicate the state will be short of the consensus revenue estimate. If that is the case, then these “savings” will be eaten up by filling the shortfall, thus necessitating additional FY 2006 budget cuts.

**V. State Pharmacy Assistance - \$30 million**

The Governor proposes to save \$30 million by establishing an arrangement with pharmaceutical companies under the new Medicare Part D prescription drug program in 2006. Under this plan, the state could negotiate rebates on prescriptions through the continuation of the Senior Rx Program. There is certainly the potential for the state to garner some revenues from this approach. This would, however, be a new program in 2006 and some experts believe that assuming a \$30 million gain may be optimistic.

**Section II: Major Components of \$130.2 million Additional Program Cuts:**

One \$130.2 million of the Governor’s announced plan to fill the budget hole comes through additional program and service reductions. These reductions would be made in the current fiscal year, as soon as late April. The cuts proposed would be in addition to the cuts currently being debated in the Legislature. They are discussed by department below:

**1. Dept. of Elementary and Secondary Education<sup>2</sup>**

Total Proposed Reduction	\$708,512
FTEs Cut (Staff)	9.48

Major Components:

▪ Cuts to Sheltered Workshops	\$360,510
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**Impacts:** Many sheltered workshops are hand to mouth operations. Cuts will simply cause the workshops to cut the number of the disabled employed leading to less economic capacity for the participants and less dignity as well.

**2. Dept. of Higher Education**

Total Proposed Reduction	\$4,517,454
FTEs Cut	0

Major Components:

▪ University of Missouri Hospitals and Clinics	\$1,313,546
▪ Missouri Rehabilitation Center	\$1,011,669

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<sup>2</sup> It is appropriate to mention that Governor’s statements about cutting the budget in order to provide funding for local schools do not support the budgetary plan he has proposed. Not a single dollar of the Governor’s \$170.6 million increase for local schools comes from a budget cut that he has recommended. The increase that has been recommended is the minimal amount that the Governor was required to provide under current laws and court decisions. Funding for Elementary and Secondary education will not benefit from these budget cuts. For more on this, see *Elementary & Secondary Education Funding: Increases DO NOT Require Decreases in Other Vital Services*, Missouri Budget Project April 4, 2005 available at [www.mobudget.org](http://www.mobudget.org)

- MOREnet \$1,450,440
- MOBIUS \$649,530

**Impacts: University Hospitals** – The meager funding provided by the state helps defray the cost of indigent care. With the Medicaid cuts already proposed in the budget, the amount of indigent care will increase. This cut will create significant hardship on the University and force increased costs onto other consumers and insurance companies.

**Missouri Rehab Center** – The number of employees and disabled served will have to be reduced, thus negatively affecting the economy in Mt. Vernon specifically. In small communities, state facilities are often critical, stable sources of employment that ensure the ability of the community to sustain its quality of life and the local public school system.

**MOREnet** – The Missouri Research and Educational Network is one of the state’s biggest technological successes of the past ten years. MOREnet provides internet connectivity and crucial support to K-12 schools, elementary and secondary schools throughout the state, and libraries. By bundling the purchasing power of so many users MOREnet is able to save all of these entities substantial amounts. The state’s aggressive development of internet access to these public institutions actually created the economic driver for private companies’ development of high speed lines throughout the state, thus bringing such access to businesses and private citizens much more quickly than would have been the case without it.

**Missouri Bibliographic Information User System (MOBIUS)** – Also known as the Common Library Platform, MOBIUS is a consortium of academic libraries with public and private member colleges and universities in the state of Missouri. The loss of the entire core appropriation of \$649,530, as recommended by the Governor, directly affects every higher education institution in the state of Missouri. The assessment paid by each institution will increase at least 40 percent.

- In the case of the University of Missouri, the assessment increase totals more than \$200,000;
- In the case of Southwest Missouri State, the increase is more than \$37,000.

MOBIUS is a very valuable resource to all academic libraries because it provides access to more than 17 million items contained in these libraries. Interlibrary lending among Missouri’s institutions of higher education has increased from less than 30,000 per year in 1999 to more than 200,000 in FY05. Student use of libraries’ print collections has increased significantly because of MOBIUS and public libraries are beginning to join to enable all of our citizens to have access to our over \$1 billion investment in academic libraries.

### 3. Dept. of Revenue

Total Proposed Reduction	\$5,794,663
FTEs Cut	97.5

#### Major Components:

- Staffing in Taxation/Administration \$1,065,322
- Transportation Revenue Collection Transfer \$2,735,206
- Reduction in Tax Auditors \$400,000

**Impacts:** Further reductions in staff in the Division of Motor Vehicles and Drivers Licensing, over and above what has already occurred as a result of Amendment 3. It likely the cuts will

result in degrading services to Missourians who will have to wait longer for titles and other transactions to be completed. Services to auto dealers would also be expected to decrease thus affecting the economy.

Tax Auditors generally work basically on commission for a portion of the revenues generated. Cutting staff and budget here could decrease the amount of general revenue earned. Fewer revenue auditors may discourage tax compliance as companies have less to fear about properly paying their taxes which can lead to scofflaws.

#### 4. Dept. of Transportation

Total Proposed Reduction	\$6,414,694
FTEs Cut	1.00

Major Components:

- Eliminate Amtrak Funding \$3,699,927

**Impacts:** Loss of Amtrak service would restrict transportation for the elderly, for low income residents who do not own a car and for students traveling to and from college.

#### 5. Office of Administration

Total Proposed Reduction	\$4,668,757
FTEs Cut	97.00

Major Components

- State Office Buildings Operations \$1,154,594
- Design and Construction Staff \$628,329

**Impacts:** State office building staff ensure that the buildings and the major equipment therein (HVAC systems, electrical and mechanical systems etc) are properly maintained. Elimination of these staff make it more likely that the state's physical assets will degrade, thus resulting in more repair costs in the future. This cut may be shortsighted at best.

#### 6. Information Technology Consolidation

Total Proposed Reduction	\$2,589,550
FTEs Cut	0

**Impacts:** It is likely that these IT consolidations will lead to the loss of approximately 50 jobs. These cuts will restrict the state's ability to take advantage of future technology innovations.

#### 7. Dept. of Agriculture

Total Proposed Reduction	\$1,841,897
FTEs Cut	26.85

Major Components:

- Agriculture Business Development \$131,005
- Market Info/Outreach \$274,656
- Animal Health Program \$419,522

**Impacts:** These reductions may be counter-productive should they impair Missouri farmers ability to market their products.

#### 8. Dept. of Natural Resources

Total Proposed Reduction	\$2,172,114
FTEs Cut	24.91

Major Components:

▪ Water Resource Program	\$336,124
▪ Water Protection Program	\$155,906
▪ Outreach & Assistance	\$438,605

**Impacts:** Reducing outreach and assistance may result in more costly enforcement and clean up measures later.

#### 9. Dept. of Economic Development

Total Proposed Reduction	\$10,093,020
FTEs Cut	18.00

Major Components:

▪ MO Job Development	\$1,000,000
▪ Tourism Promotion	\$4,585,929
▪ Office of Public Counsel	\$105,803

**Impacts:** Reducing job development programs and tourism promotion may be counter-productive. When Governor Holden attempted to cut the budget of the Division of Tourism, its commission pointed out that the investment was returned 15 to 1. Therefore, such cuts may simply reduce taxes collected in the tourism industry as it is unable to reach potential travelers. This is particularly a problem if the state is unable to lure out-of-state travelers since their spending is a net import of dollars to the state.

Cuts to the Office of the Public Counsel may deprive consumers of adequate representation in utility rate increase cases. Major corporations may be able to win approval for excessive utility rate hikes. These additional costs on businesses and consumers will depress economic activity as the revenues are taken out of the general economy. These cuts may also deprive consumers of adequate representation in utility rate increase cases.

#### 10. Dept. Labor and Industrial Relations

Total Proposed Reduction	\$504,290
FTEs Cut	11.35

Major Components:

▪ Commission on Human Rights	\$184,378
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Employment Discrimination and Public Housing Discrimination issues will no longer be investigated. There is no other consumer office for housing and employment issues in the state.

## 11. Dept. of Public Safety

### Major Components:

▪ State Water Patrol	\$727,554
▪ State Highway Patrol	\$195,678
▪ Adjutant General Field Support	\$444,917

**Impacts:** These reductions may jeopardize public safety and crime control. Field support cuts may also lead to a loss of Federal funds.

## 12. Dept. of Corrections

Total Proposed Reduction	\$13,901,653
FTEs Cut	260.87

### Major Components:

▪ Closing Central MO Correctional (Church Farm)	\$6,709,322
▪ Reduce Substance Abuse Services	\$1,481,591
▪ Reduce Probation and Parole Services	\$2,055,488
▪ Academic Education Services	\$1,733,122

**Impacts:** The closing of Central MO Correctional Center and subsequent transfer of inmates will likely lead to increased costs at other facilities. Scaling back rehabilitation services for prisoners will lead to increases in crime and recidivism. Reduction of services within the institutions will lead to more idle time for inmates and therefore more violence and other disruptive behaviors.

## 13. Dept. of Mental Health

Total Proposed Reduction	\$16,598,312
FTEs Cut	112.6

### Major Components:

▪ Community & Family Directed Supports	\$6,034,694
▪ Alcohol and Drug Abuse Treatment	\$960,562
▪ School Based Prevention Programs	\$435,540
▪ Youth Community Programs	\$1,123,035
▪ Most of remaining reductions are staffing and E&E reductions at various facilities	

**Impacts:** Note that the DMH has already been subjected to severe across the board cuts. These additional reductions will hinder the ability of the department to provide services for adults, families and children with significant mental illness and efforts to curtail alcohol and drug abuse, particularly among youths. Additional staffing cuts at institutions may negatively affect quality of care.

## 14. Dept. of Health and Senior Services

Total Proposed Reduction	\$14,988,613
FTEs Cut	136.27

### Major Components:

▪ Environmental Health Services	\$860,691
▪ Senior Services	\$3,500,257
▪ In Home Services	\$2,000,000
▪ Community Health Services	\$1,361,753

**Impacts:** The Governor's reduction in staff for Senior Services is understated by roughly half because the loss in general revenue will also mean the loss of federal funds as well. Total staff

losses will likely be closer to 200 FTE. Seniors should expect significant delays in receiving services. The state's emergency medical system personnel may be in jeopardy. Response to environmental health outbreaks will be delayed and significantly less state assistance and coordination will be provided.

### 15. Dept of Social Services

Total Proposed Reduction	\$94,147,120
FTEs Cut	434.07

#### Major Components:

▪ Reduced Costs + Provider Tax in Managed Care	\$39,962,714
▪ Reduced Costs in Pharmacy Program	\$18,766,189
▪ Reduced Costs in Youth Treatment	\$6,062,132
▪ Juvenile Court Services	\$2,657,994
▪ Adoption Subsidy Payments reduced	\$2,550,000
▪ Income Maintenance Staff reduced	\$2,713,168
▪ Grandparents as Foster Parents	\$1,030,978
▪ Supplemental Nursing Care	\$1,000,000
▪ Child Support Enforcement	\$1,466,590
▪ Foster Care Payments	\$1,781,780

**Impacts:** The number of staff that will be laid off in income maintenance and child support enforcement is likely substantially understated as significant federal funds will be lost as well. The Governor's proposal to demand yearly review of Medicaid eligibility, and the savings supposedly generated, will be harder to achieve with fewer staff doing the work. Custodial parents will find it harder to get support from non-custodial parents as fewer staff are available for follow-up and contact to work the cases. This will put substantial economic pressure on some families while they wait for the assistance they need.

The above reductions will also lead to less assistance for troubled youth and make it more difficult for children in foster care to be placed with adoptive parents: Cuts to Grandparents as Foster Parents will result in more children in non-relative foster care as Grandparents struggle with fixed incomes. Reductions in Youth Treatment and Juvenile Court Services may lead to fewer troubled young offenders receiving assistance with a variety of situations. This will make them more likely to be repeat offenders and possibly become adult criminals. This will result in greater costs in subsequent years.

Reducing the Adoption Subsidy will make it more difficult for qualified couples to adopt children. If fewer children are adopted from the State Foster Care system, the state will incur even greater costs in later years. Reducing the affordability of adoption in general may lead to more women who are experiencing an unwanted pregnancy to choose an abortion as opposed to placing the baby for adoption.

### **THE REVENUE SITUATION - IS THIS A BEST CASE SCENARIO?**

It is and will be evident that the cuts associated with the Governor's current budget plan are severe by almost any standard. In addition, in recent weeks, it has become apparent that FY 2005 General Revenue Collections are not at levels that are consistent with the Consensus Revenue Estimate (CRE) on which current year appropriations are based. An analysis prepared by the MBP on March 15<sup>th</sup>, shows that actual net GR collections for FY 2005 will likely fall short of the

CRE by \$75 to \$100 million even if the growth rates for the major tax sources improve over the last four months of the fiscal year. Should this occur, it is likely that the FY 2006 CRE will have to be revised downward by a significant amount. In the absence of discussion of revenue options, a decrease in revenue receipts would necessitate even greater budget cuts in FY 2006 than are being analyzed by this report.<sup>3</sup>

### **One-Time Revenues Fund Ongoing Programs**

Another quandary that has yet to be thoroughly discussed is that the FY 2006 budget contains significant one-time revenues that will not be available in FY 2007. The table below shows that, even before the Governor's actions, the FY 2006 budget is based on at least \$146.3 million in revenues that will not be available next year. The Governor's newly announced plan adds another \$20 million in one-time funds. Revenue growth would have to be 2.5% in the following year just to replace these one-time revenues – or more growth in total than this year's revenue estimate. The effect could be substantial additional cuts proposed through FY 2006 withholdings or significant reductions in the FY 2007 fiscal year. (Again, these assumptions are made in anticipating the absence of legislative discussions to ameliorate the revenue crisis.)

*Table 1: One Time Funds*

<i>Revenue Stream</i>	<i>Cost to General Revenue (GR)</i>	<i>Comments</i>
Amendment 3	\$30 million	Expected Loss to GR in FY 2007
Outstanding Schools Trust Fund	\$26 million	Amount of FY 2006 school revenues being used for other programs. The funds will have to be replaced in FY 2007
Dedication of a portion of Tobacco Settlement Proceeds to Life Sciences	\$40 million	Legislation with this requirement passed in 2004
Gaming Revenues one-time Sources	\$50.3 million	Will not be available in FY 2007
Additional funds "generated" by implementing above cuts in the last quarter of the current fiscal year	\$20 million	
<b>Total One-Time Funds</b>	<b>\$166.3 million</b>	

### **SUMMARY**

1. State programs that exist to help people in poverty, elderly, and at-risk children are being asked to absorb the lion's share of the combined budget cuts.
2. The FY 2006 budget will rely heavily on one-time funding sources and a somewhat optimistic General Revenue forecast.
3. A considerable share of the budget cuts are almost certainly counter-productive in that they may preclude job creation or revenue generating. Other cuts may well lead to increased future costs to the state.
4. A balanced budget is predicated on substantial savings in Pharmacy and Managed Care costs. While these saving are certainly attainable, the amounts now forecast may at the optimistic end of the spectrum.

<sup>3</sup> Figures are based on the Consensus Revenue Estimate published in the State FY 2006 Executive Budget

