Center on Budget and Policy Priorities

820 First Street NE, Suite 510
Washington, DC 20002

Tel: 202-408-1080
Fax: 202-408-1056

center@cbpp.org
www.cbpp.org

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FEDERAL GRANTS TO STATES AND LOCALITIES CUT DEEPLY IN FISCAL YEAR 2009 FEDERAL BUDGET

By Iris J. Lav and Phillip Oliff

Grants to state and local governments have long been an important way in which the federal government supports and administers programs efficiently. The new budget, however, continues to significantly erode those grants. This leaves states and localities the option of either curtailing services or increasing their own taxes to compensate for declining federal funds. These cuts would come at a particularly difficult time, when many states already are cutting programs to balance their budgets and half of the states face budget gaps for the upcoming fiscal year of more than $34 billion.

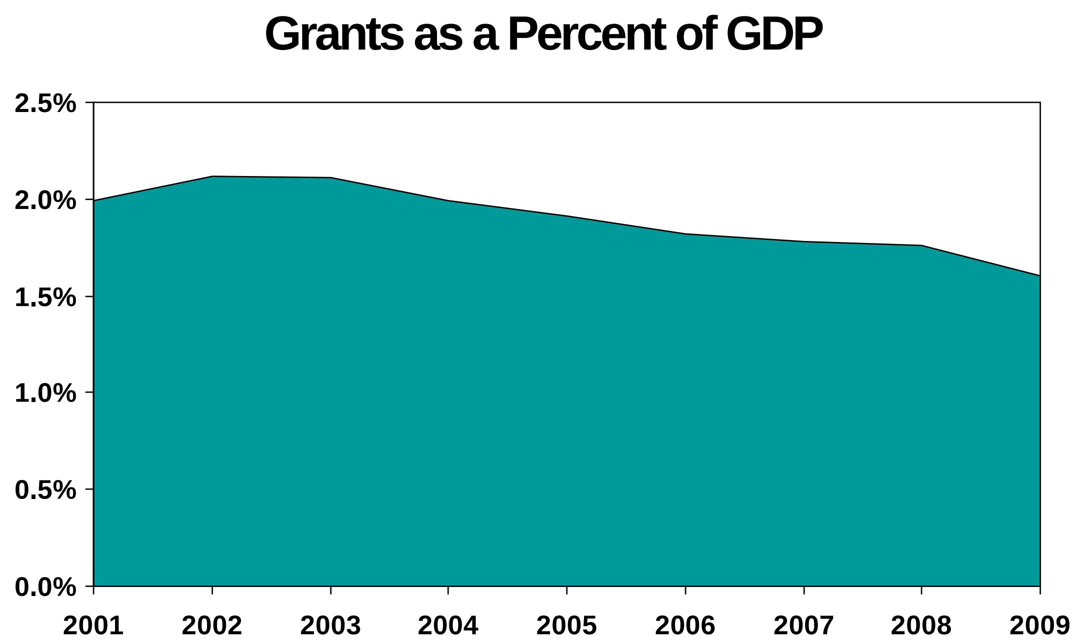
- Under the President's budget, grants to state and local government for all programs other than Medicaid would decline by $18.9 billion or 7.4 percent from fiscal year 2008 to 2009, after adjusting for inflation.[1]

- The proposed 2009 grants would be significantly lower as a percent of the economy than they were at any time since at least 2001. For 2009, the budget proposes grants to state and local government for all programs other than Medicaid that total just 1.60 percent of GDP. In 2001, such grants were 1.99 percent of GDP. Considering grant levels relative to the economy provides a somewhat better measure of whether the grants would be adequate to maintain the current level of state and local services they support, because the cost of providing services tends to grow in tandem with the economy.

- If grants for all programs for 2009 were at their 2001 to 2008 average level relative to the economy (1.94 percent), they would be $50 billion, or 21 percent, higher than their proposed 2009 level.

[1] Medicaid is traditionally excluded from this analysis because changes in Medicaid grants largely reflect inflation in health-care costs in the public and private sectors alike. Considering grants other than Medicaid gives a more accurate picture of the relative level of federal funding for state and local services. There are, however, substantial cuts in Medicaid on top of the cuts detailed in this report. The budget would cut federal Medicaid expenditures by $18.2 billion over five years (with $17.4 billion in reductions from legislative changes and another $800 million from regulatory changes). These "savings" would primarily be achieved *not* by lowering health care costs, but rather by shifting costs to the states. (See box on page 5.)

FIGURE 1



- These shortfalls are difficult for states and localities to handle, especially at a time when state and local governments are already facing considerable fiscal strain and the economy is on the verge of a possible recession. With few exceptions, state and local governments would not be able to absorb the proposed continuing reductions in federal aid without instituting program cuts or tax increases.

Discretionary and Mandatory Grants

The President's 2009 budget proposes substantial cuts in discretionary grants that are appropriated annually and only a negligible increase in entitlement programs.

- Discretionary grants to state and local governments would decline by $15.1 billion from 2008 to 2009. The decline would be $19.1 billion, or 10.9 percent, after adjusting for inflation.

- If discretionary grants had remained at their 2001 to 2008 average level relative to the economy, they would be $47.4 billion, or 30.4 percent, higher than the proposed level for 2009.

- On the entitlement or "mandatory" side of the budget, grants to state and local governments other than for Medicaid would increase by $2 billion from 2008 to 2009. After adjustment for inflation, they would increase by $200 million, or 0.2 percent.

- If mandatory grants other than Medicaid were at their 2001 to 2008 average level relative to the economy, they would be $2.7 billion, or 3.3 percent, higher than the proposed level for 2009.

TABLE 1: GRANTS-IN-AID TO STATE AND LOCAL GOVERNMENTS IN THE FY 2009 BUDGET, EXCLUDING MEDICAID BUDGET AUTHORITY (FUNDING) IN BILLIONS OF DOLLARS			
	FY 2007	**FY 2008**	**FY 2009**
Discretionary Funding	$127.1	$127.1	$114.2
Mandatory Funding	119.2	117.2	112.2
Total Funding	246.3	244.3	226.4
Total Funding adjusted for technical anomalies*	244.0	249.9	236.8
In 2009 dollars (i.e., adjusted for inflation)	257.7	255.7	236.8
Percent change after adjusting for inflation- 2008 to 2009			**-7.39%**
Funding as a percent of GDP	**1.78%**	**1.76%**	**1.60%**

* Adjustments were made to exclude disaster relief funding in all years, to reflect funding for highways and airports as the level of obligations for those programs rather than the level of "contract authority," and to remove distortions that can occur when the level of "advance" appropriations changes from year to year.

- *Total* discretionary and mandatory grants combined, other than Medicaid, would decline by $13.1 billion. After adjustment for inflation, grants would decline by $18.9 billion or 7.4 percent.

- If all grants other than Medicaid were at their 2001 to 2008 average level relative to the economy, they would be $50 billion, or 21 percent, higher than the proposed level for 2009.

What is Being Cut?

The reductions in grant funds are spread throughout a wide range of budget categories and programs. In some cases nominal funding is slated for a cut. In others, the proposed funding fails to keep pace with the cost of the program.

The cuts include a constellation of reductions that will harm the most vulnerable children in the country. There is a 30 percent nominal reduction in **the Social Services Block Grant** which helps pay for services that protect children from neglect and abuse, foster care, adoption, and related services for children and families. In addition, the budget assumes cuts in payments to states for **children and families services programs** and for the **safe and stable families** program. These cuts would come as weak economic conditions create increased need for these types programs; if the federal government cuts funding, the burden of supporting these programs is likely to fall to states and local governments.

Employment and training cuts are also particularly troublesome during weak economic conditions. The budget proposes to cut **vocational and adult education**, **training and employment services**, and funds for the operation of the **federal-state employment service**. Again, these are needed programs that states may have to continue if the federal government does not uphold its end of the funding.

Public safety programs important to states and localities are *cut by nearly two-thirds*. These include **juvenile justice programs**, the **COPS community policing program**, **prevention of violence against women**, assistance for **areas with high drug trafficking**, and other programs. In addition, grants for **homeland security**, which include reductions in support for first responders, are cut by 45 percent.

Other cuts include:

- **Energy Assistance** to help low-income households pay heating bills;

- The **Community Development Block Grant**; which provides housing and economic opportunities to low-income populations;

- The Environmental Protection Agency's **State and Tribal Assistance Grants**, which helps states implement air and water quality standards;

- Education programs including **school improvement programs** and funds for the **Safe and Drug Free Schools** program; and

- The **Commodity Supplemental Food Program**, which provides nutritional food packages to low-income elderly people.

State Fiscal Problems

These cuts come at a time when states are struggling to meet their balanced budget requirements with revenues that have been depressed by the economy and service demands beginning to rise as residents lose jobs and income. At least nine states have *already* implemented budget cuts that affect their current fiscal year spending, and five other states have proposed budget cuts for this year. The cuts affect children, pregnant women, people who are mentally retarded, the elderly, victims of domestic violence, poor and low-income families and individuals and many other vulnerable populations.

For the upcoming fiscal year that begins July 1 in most states, half of the states are facing budget gaps. In the 20 states that have made specific estimates, these gaps equal at least $34 billion. Thus the state budget cuts being implemented or proposed in the current fiscal year are just the tip of the iceberg; far deeper state cuts in health care, education, and social services are in the offing. The federal cuts proposed in the Bush Administration budget would greatly exacerbate the problem states are facing as they struggle to maintain services within their balanced budget requirements.

Unlike states, the federal government can run a deficit when the economy turns down. At a time when the economy is weak and states are facing an inability to provide services to their residents because of their balanced budget requirements, the federal government should be providing fiscal assistance to states rather than cutting back on federal funding and thereby deepening the state fiscal crisis.

Medicaid Cuts in the Budget

The President's budget would reduce Medicaid funding by $17.4 billion over the next five years. The greatest savings would come from cuts that reduce federal Medicaid spending by shifting costs from the federal government to the states. For example, the Administration would reduce the rate of federal reimbursement for certain administrative costs, such as inspecting nursing homes to ensure quality of care and safety. The costs of inspecting nursing homes would not disappear, but the state's share of the cost would increase.

The budget also includes a new proposal that would repeal a provision in the Medicaid statute under which states wishing to enroll the elderly and people with disabilities who are eligible for both Medicare and Medicaid, and children with special health care needs, in managed care plans must meet certain criteria to ensure that these individuals' health needs will be met. Without this protection, some of these vulnerable beneficiaries could be forced into managed care plans that do not include specialists or cover drugs that they need.

The Administration proposes to extract additional reductions in Medicaid through administrative action, without approval by Congress. The administrative changes proposed by the Administration would cut Medicaid spending by $800 million over the next five years, which would be on top of $12 billion in savings that would result from administrative actions the Administration has already taken over the last year. Like the legislative proposals, most of the federal savings from the Administration's new administrative proposals would be accomplished by shifting costs from the federal government to the states.

Reductions by State

Table 2 provides an illustration of what cuts of this magnitude would mean for each state. It distributes the reduction in grants other than Medicaid by the percentage of grants (other than Medicaid) that each state is expected to receive in 2009. This analysis does not take into account the distribution by state of the specific program cuts proposed in the budget. It does, nevertheless, provide a reasonable approximation of the amount by which each state might have to reduce services or raise revenues in order to achieve the level of federal deficit reduction the President seeks from cutting grants-in-aid.

Other Impacts of Budget on States

In addition to the loss of federal grants for programs, states would face the loss of significant amounts of revenue as a result of the federal tax changes proposed in the Bush budget. Federal tax changes often affect state revenues, because most states use federal definitions of income, federal depreciation allowances, and other features of the federal tax code as the basis for their own taxation. The business tax incentives included in the President's stimulus package potentially would reduce revenue a total of $2.9 billion in 36 states. Other tax provisions in the budget that would cause states to lose revenue include expensing for small businesses, expanded tax-free savings, and expanded Health Savings Accounts.

TABLE 2: ILLUSTRATION OF POTENTIAL LOSS OF GRANTS-IN AID BY STATE GRANTS OTHER THAN MEDICAID IN MILLIONS OF DOLLARS FY 2009 Compared To FY 2008 In President's Budget

State or Territory	FY 2009 Percentage of Grants Other than Medicaid	Nominal Budget Cut	Budget Cut After Adjustment for Inflation	Per Capita Budget Cut after Adjustment for Inflation (in dollars)	Rank
All States		**13,119**	**18,897**		
Alabama	1.5%	198.2	285.5	61.7	25
Alaska	0.5%	69.5	100.1	146.4	1
Arizona	1.7%	219.2	315.8	49.8	45
Arkansas	0.9%	124.3	179.0	63.1	20
California	14.0%	1833.6	2,641.1	72.3	12
Colorado	1.2%	158.7	228.6	47.0	48
Connecticut	1.3%	168.6	242.9	69.3	15
Delaware	0.3%	37.4	53.8	62.3	23
Florida	4.6%	609.6	878.1	48.1	47
Georgia	3.0%	397.0	571.8	59.9	25
Hawaii	0.4%	59.0	84.9	66.2	16
Idaho	0.4%	56.9	81.9	54.6	36
Illinois	4.3%	565.4	814.5	63.4	19
Indiana	1.8%	240.3	346.1	54.5	37
Iowa	0.8%	110.0	158.5	53.0	41
Kansas	0.8%	101.8	146.6	52.8	43
Kentucky	1.4%	188.7	271.9	64.1	18
Louisiana	1.7%	220.2	317.1	73.9	11
Maine	0.4%	56.3	81.0	61.5	26
Maryland	1.7%	221.0	318.3	56.7	32
Massachusetts	2.4%	315.3	454.1	70.4	14
Michigan	3.2%	421.0	606.4	60.2	27
Minnesota	1.5%	196.8	283.5	54.5	38
Mississippi	1.1%	143.5	206.8	70.8	13
Missouri	1.8%	232.8	335.3	57.0	31
Montana	0.4%	55.3	79.7	83.2	6
Nebraska	0.5%	70.8	102.0	57.5	30
Nevada	0.6%	77.5	111.6	43.5	50
New Hampshire	0.4%	46.5	67.0	50.9	44
New Jersey	2.9%	375.2	540.5	62.2	24
New Mexico	0.8%	106.2	153.0	77.7	8
New York	9.0%	1,186.2	1,708.6	88.5	4
North Carolina	2.6%	337.7	486.4	53.7	40
North Dakota	0.3%	42.7	61.5	96.2	3
Ohio	3.8%	498.7	718.3	62.6	22
Oklahoma	1.2%	158.5	228.3	63.1	21
Oregon	1.1%	146.8	211.4	56.4	33
Pennsylvania	4.3%	559.9	806.4	64.9	17
Rhode Island	0.4%	55.6	80.1	75.8	9
South Carolina	1.3%	164.6	237.1	53.8	39
South Dakota	0.3%	45.0	64.9	81.5	7
Tennessee	1.8%	239.8	345.4	56.1	34
Texas	7.4%	970.9	1,398.5	58.5	29
Utah	0.7%	85.8	123.6	46.7	49
Vermont	0.3%	37.5	53.9	86.8	5
Virginia	2.0%	260.2	374.7	48.6	46
Washington	1.9%	247.0	355.8	55.0	35
West Virginia	0.7%	94.1	135.5	74.8	10
Wisconsin	1.6%	205.9	296.6	52.9	42
Wyoming	0.3%	35.2	50.7	97.0	2

Notes: Percentage of grants per state from Analytic Perspectives, Tables 8-6 and 8-17 (Use FY 2009 estimated)
Analysis is illustrative of cuts states would experience if the amount of grant reductions in the budget were distributed over all non-Medicaid grants.
Per Capita cut uses Census data on estimated state population for July 1, 2007