



CENTER ON BUDGET AND POLICY PRIORITIES

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July 8, 2004

WILL THE NEW TENNCARE CUTBACKS HELP TENNESSEE'S ECONOMY?

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The state of Tennessee recently enacted legislation that would make major cutbacks in the state's Medicaid program, called TennCare. The new law would make numerous changes in the health insurance program for low-income people, including limiting the number of doctors' office visits to ten per year, limiting the number of prescriptions to six per month, eliminating coverage for antihistamine and gastric acid reducing medications, mandating the use of the lowest cost prescription drugs, and creating a new definition for "medical necessity," which will be used to determine which medical treatments are permitted under the insurance plan.¹ The state plans to submit a waiver to the federal Medicaid agency to approve most of these changes in the near future.

Gov. Bredesen's office has stated that the new TennCare policies will substantially reduce state expenditures in the coming years. The cutbacks are estimated to lower state expenditures by \$300 million in FY 2005, an amount which rises to \$1.0 billion by FY 2008.² While these policies would lower state budget expenditures, they also would adversely affect Tennessee's economy and job creation because they would lead to a substantial reduction in federal revenue flowing into the state. Every TennCare dollar saved by the state also would lead to the loss of almost \$2 in federal matching funds.

The combined loss of state and federal dollars means that hospitals, physicians, pharmacists, nursing homes and other health care providers throughout the state would have lower TennCare revenues in the coming years. In turn, this means that these providers would employ fewer staff, purchase fewer medical supplies, and so on. In many parts of the state, particularly rural areas, the reduction in TennCare revenues would make it harder for clinics or other health care facilities to keep their doors open or to offer the breadth of services they now provide. For many health care providers, TennCare is a major revenue source, and a reduction in TennCare funds can have substantial repercussions for their operations.

Additional ripple effects would be felt in other parts of Tennessee's economy. Health care workers use income earned directly or indirectly from TennCare payments to pay their mortgages, buy food, fuel their cars, etc. While the budget savings from the state's share of TennCare spending arguably might be used in ways that create alternative jobs and income in the

¹ William Welch and Julie Appleby, "States Watching Tennessee's Health Care Plan for the Poor," *USA Today*, July 6, 2004.

² These are rough estimates presented by the Governor's office. They do not include savings attributable to changes in the definition of medical necessity. If additional savings due to the definition change were included, then all the estimates in this paper would be even larger.

Estimates of the Impact of TennCare Budget Reductions on the Tennessee Economy and Employment

		FY 2005	FY 2006	FY 2007	FY 2008
Estimated State Savings	(mil. \$)	\$300	\$500	\$700	\$1,000
Estimated Loss of Federal Matching Funds	(mil. \$)	\$553	\$897	\$1,256	\$1,795
Estimated Total Reduction in TennCare Expenditures	(mil. \$)	\$853	\$1,397	\$1,956	\$2,795
Economic Activity and Jobs Lost Due Solely to the Reduction in Federal Funds					
Economic Activity Lost	(mil. \$)	\$762	\$1,217	\$1,704	\$2,434
Estimated Jobs Lost		6,800	10,600	14,500	20,200

state, the loss of the *federal* Medicaid revenue that matches the state dollars would create economic losses that would multiply through other parts of the state economy.

This analysis uses information about Tennessee’s Medicaid matching rate and economic multiplier estimates derived from an economic model developed by the U.S. Department of Commerce’s Bureau of Economic Analysis to estimate the impact of the TennCare budget reductions on the state’s economy. These are rough approximations of the actual impact. We have not tried independently to estimate the budget savings due to the new policies, but simply based our calculations on the Governor’s budget estimates. The economic multiplier estimates are approximations based on general reductions in health care spending, rather than being tailored specifically to the components of the new TennCare strategy.

Given those caveats, our analyses indicate the new TennCare cutbacks would result in:

- A loss of federal matching funds that rises from \$550 million in FY 2005 to \$1.8 billion in FY 2008.
- A total reduction in TennCare expenditures of \$850 million in FY 2005 and \$2.8 billion in FY 2008.
- A substantial reduction in total economic activity in Tennessee. The economic activity lost caused by the reduction in federal matching funds alone is almost \$800 million in FY 2005 and rises to \$2.4 billion by FY 2008.
- Thousands of jobs lost in Tennessee. The number of jobs lost due to the reduction in federal matching funds would be almost 7,000 in 2005 and about 20,000 by 2008.

These analyses should be considered conservative. They do not account for reductions in the state’s share of TennCare spending that could affect economic activity, or for further budget

reductions that might occur due to changes in the definition of medical necessity in determining whether TennCare will cover certain health care services provided to beneficiaries.

Our estimates also do not account for the possibility that some patients' medical conditions will worsen because they do not receive the most appropriate medical care or are unable to get needed prescription drugs in TennCare and therefore could require more intensive or expensive medical treatment at a later time.³ A recent study found, for example, that patients who limited their use of medications because they could not afford them were more likely to have heart attacks or strokes, and another study found that increased copayments for prescription drugs led poor patients to use fewer medications but resulted in increased hospital and emergency room use.⁴ If we accounted for these factors, the estimated harm to Tennessee's economy and employment would be significantly larger.

Finally, our estimates do not account for the potential harm or cost to other public services in Tennessee. Tennessee used TennCare to gain federal matching funds for certain services that were previously supported only with state funds, such as coverage of public mental health care costs, case management services for foster care children, etc.⁵ If TennCare benefits are limited and services like these lose their federal matching status, the state will either have to make substantial cuts in these services or have to use state-only funds to maintain services. If the services are cut, the TennCare reductions could have negative repercussions for other needy individuals and public institutions. If the state instead maintains these services with state dollars, the state's TennCare budgetary savings would be offset by increases in other state services without the support of federal matching funds.

Technical Notes

For FFY 2005, the Medicaid matching rate for Tennessee will be 64.81 percent — that is, the federal government covers 64.81 percent of medical benefit costs for Tennessee, while the state is responsible for 35.19 percent of the total costs. In FFY 2006, a preliminary analysis by the Federal Funds Information Services indicates the matching rate will fall slightly to 64.22 percent. We used that rate for calculations in FFY 2007 and 2008 as well as for 2006.

³ See, for example, S. Soumerai, "Benefits and Risks of Increasing Restrictions on Access to High Cost Drugs in Medicaid", *Health Affairs*, 23: 135-146 (Jan./Feb. 2004).

⁴ M. Heisler, et al., "The Health Effects of Restricting Prescription Medication Use Because of Cost", *Medical Care*, 42(7):626-34, July 2004 and Robyn Tamblyn, et al., "Adverse Events Associated with Prescription Drug Cost-Sharing among Poor and Elderly Persons," *Journal of the American Medical Association*, 285(4): 421-429, January 2001.

⁵ Christopher Conover and Hester Davies, *The Role of TennCare in Health Policy for Low-income People in Tennessee*, Urban Institute, Feb. 2000.

The economic multiplier analyses were derived from analyses for Tennessee published by Families USA.⁶ We adapted those data to: isolate the effect of the loss of federal matching funds (as compared to the loss of both state and federal funds), to account for changes in the federal Medicaid matching rate and to account for projected changes in wage rates.

⁶ Families USA, *Medicaid: Good Medicine for State Economies: 2004 Update*, May 2004. That report's analysis was performed by Richard Clinch, Director of Economic Research at the Jacob France Institute of the Merrick School of Business at the University of Baltimore and is based on the most recent update of the Bureau of Economic Analysis' RIMS II input-output model.