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STATE FISCAL CONDITIONS CONTINUE TO DETERIORATE; FEDERAL ASSISTANCE BADLY NEEDED

By Iris J. Lav

States around the country continue to struggle with dismal fiscal conditions. State revenues have declined for four consecutive quarters. According to the Rockefeller Institute, revenues for the period April-June 2002 — the final quarter of the fiscal year in most states — were 10.4 percent below revenues for the same period in 2001.[1] This is the sharpest decline at least since the 1980s.

It is thus not surprising that states faced deficits that exceeded $50 billion as they enacted their fiscal year 2003 budgets, on top of the approximately $40 billion in deficits with which states coped in fiscal year 2002. According to the National Conference of State Legislatures, one-quarter of the states had 2003 budget deficits that exceeded 10 percent of their general fund budgets.[2] Struggling to meet balanced budget requirements, states have cut spending and imposed tax increases. Nevertheless, a combination of a continued decline in revenue collections in the current quarter in many states and a resurgence of the growth of health care costs is leading to the reopening of substantial deficits. Because most states are prohibited by constitution or statute from running deficits, most of these new gaps between revenues and budgeted spending will have to be closed during fiscal year 2003 through additional program cuts or tax increases.

At this point in the state fiscal crisis, most of the less severe ways of closing fiscal gaps have been used up. States have drawn down much of their rainy day funds and available reserves. Most states have cut government administrative expenses, frozen hiring, or instituted early retirement schemes. Many states also have postponed expenses into future years, used bonds instead of current revenue to finance certain types of expenses, and/or accelerated future revenues into the current year. There are few tactics remaining available that are not cuts in essential services such as health care, social services, and education, or tax increases. Some states already are eliminating health care coverage for large numbers of low-income children. States cannot solve this problem on their own.

In July, on a bipartisan basis, the U.S. Senate voted 75-24 to provide $9 billion in temporary state fiscal relief. The amendment to provide this relief, sponsored by Senators Jay Rockefeller, Susan Collins, Ben Nelson, and Gordon Smith, was attached to legislation expanding access to generic drugs. It now appears, however, that the generic drug bill, which is fiercely opposed by the pharmaceutical industry, will not make it through Congress this year. Fortunately, there is another opportunity to provide temporary state fiscal relief; such relief could be included in upcoming legislation to adjust reimbursement rates for Medicare health providers. If fiscal relief is *not* enacted now, state budget cuts — and consequent reductions in basic services — will become significantly deeper in the months ahead.

The Latest State Budget Cut: Terminating Health Care Coverage for Tens of Thousands of Low-income Children in Oklahoma

Faced with mounting budget deficits, Oklahoma acted this week to slash Medicaid and SCHIP coverage for low-income children, elderly, and disabled people.

For children in Oklahoma aged 1 to 5, eligibility for health insurance is being reduced from 185 percent of the poverty line to 133 percent. For children aged 6 to 18, eligibility is being cut from 185 percent to 115 percent of the poverty line. These changes nearly eliminate Oklahoma's SCHIP program. The state also is reducing Medicaid eligibility for elderly and disabled people from 100 percent of the poverty line to less than 80 percent of the poverty line and terminating its "medically needy" program. (Under the medically needy program, Medicaid coverage is provided to needy people whose gross incomes modestly exceed the Medicaid income limits but who have high medical bills that reduce their disposable income to below the income limits.) These changes together will result in approximately 80,000 low-income people in Oklahoma losing health care coverage.

Oklahoma originally planned to implement these eligibility cutbacks by November 1, 2002. It now appears likely the state will delay the eligibility cutbacks until March 1, 2003, although other cutbacks in benefits will be implemented.

State Revenues Continue to Fall

Fiscal year 2003 began on July 1, 2002 in most states. Only some of the states report revenue collections on a monthly basis, but these reports are an important indicator of state fiscal health. The early indications are not only that revenues are coming in below estimates, but also that revenue collections for July/August 2002 in some states fell below their 2001 level, which itself had been reduced by weak economic conditions.

- In Oklahoma, for example, August 2002 revenue collections were 11 percent below the forecast, and 6.3 percent below August 2001 collections. To cope with the shortfall, Oklahoma is implementing statewide budget cuts at an annualized rate of 4.75 percent. The state also is making deep cuts in Medicaid eligibility. (See box above.)

- Colorado officials recently announced that their fiscal year 2002-03 budget had fallen $400 million out of balance. The governor has directed departments to cut an additional 4.1 percent from operations, on top of cuts made during the budget process.

- August 2002 revenues in Massachusetts were 4.4 percent below August 2001 collections, and 6.9 percent below August 2000 collections.

- April-through-August personal income tax revenues in New York are 23 percent — or $2 billion — below collections in the same period last year. Corporate income tax revenue collections have declined 19 percent from last year.

- New Jersey's personal income tax revenues in July-August 2002 are 4 percent below 2001 revenues and 15 percent — or $125 million — below revenues in the same period in 2000.
- General fund revenues in Georgia for July and August are 11.5 percent below 2001 revenues for the same period and 18 percent — more than $400 million — below July-August 2000 revenue collections.
- California revenues for July and August 2002 are $686 million less than collections in the same two months in 2000.
- Delaware has acknowledged a $95 million hole in its fiscal year 2003 budget, on top of the $170 million shortfall that was closed when the budget was enacted.

While revenues collections are not declining in all states, most states are experiencing slower-than-expected revenue growth. As a result, states will have to close additional deficits during fiscal year 2003. Even where revenues are growing rather than declining, the growth generally is insufficient to support the normal inflation-related increase in the cost of providing services, and states are looking at implementing significant budget cuts.

Budget Cuts

States already have made substantial budget cuts, a number of which will have pronounced effects on low-income and vulnerable populations. The following are some examples.

Medicaid

States are having particular difficulty in maintaining funding for their Medicaid programs. A report that the Kaiser Commission on Medicaid and the Uninsured issued on September 19 notes that state Medicaid costs grew by 11 percent in fiscal year 2002 — consistent with the 12.7 percent growth in private health insurance costs — and are expected to continue to grow at double-digit rates again in 2003.[3] Yet declining revenues and budget constraints led states to appropriate only a 4.8 percent increase in funding for Medicaid for fiscal year 2003. To bridge this gap, many states have already cut their Medicaid programs; others are likely to do so later this year if they cannot find a way to increase the funds available for the program.

According to the Kaiser report:

- Medicaid benefits were reduced in 22 states in fiscal year 2002 and/or fiscal year 2003. The states reducing benefits are Arizona, California, Connecticut, Delaware, Florida, Georgia, Idaho, Indiana, Iowa, Kansas, Massachusetts, Mississippi, Missouri, Montana, New Hampshire, New Mexico, North Carolina, Rhode Island, South Carolina, Texas, Utah, and West Virginia.

State Fiscal Relief is One of Best Ways to Stimulate Economy

Economic experts such as Robert Reischauer, former director of the Congressional Budget Office, and Joseph Stiglitz, co-winner of the 2001 Nobel Prize in Economics, as well as economic experts at the Brookings Institution have noted in various reports and testimony that state fiscal relief is one of the most effective ways to stimulate a weak economy. This is because federal dollars used for fiscal relief reduce the magnitude of the budget cuts and tax increases that states otherwise would have to institute to meet balanced budget requirements. The budget cuts and tax increases that otherwise would be made reduce demand for goods and services and could contribute to delaying or endangering the economic recovery.

- Medicaid eligibility was reduced or restricted in 25 states in fiscal year 2002 and/or fiscal year 2003. The states reducing eligibility are Alaska, Arizona, California, Colorado, Connecticut, Delaware, Georgia, Illinois, Indiana, Kansas, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Nebraska, New Hampshire, New Jersey, North Carolina, North Dakota, Ohio, Pennsylvania, Utah, Washington, and West Virginia. The report notes that in four states — Missouri, New Jersey, Nebraska, and Massachusetts — the changes eliminated eligibility for thousands of people.

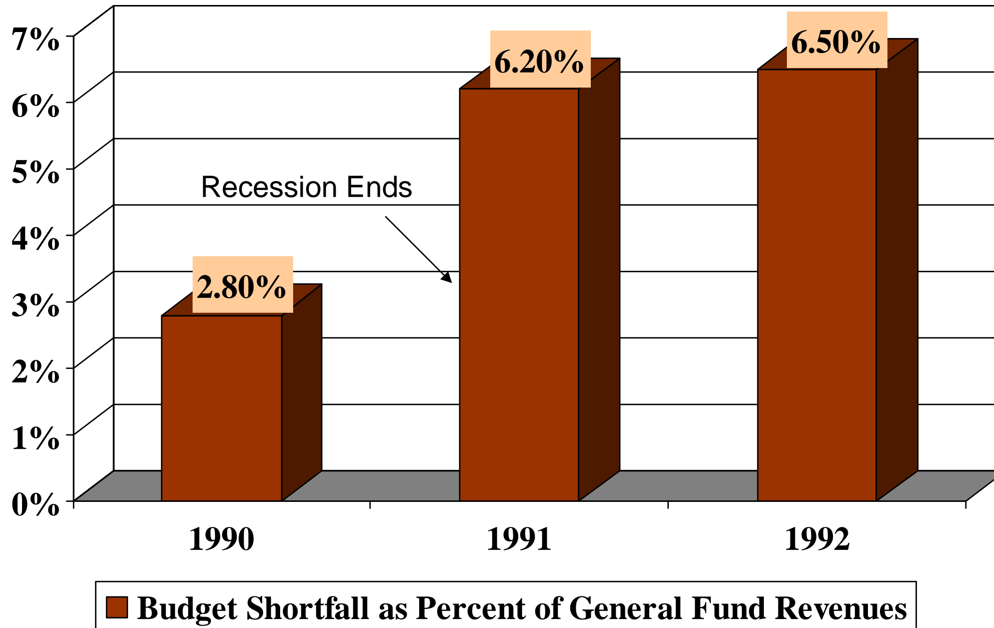
- Copayments for health care services other than prescription drugs were instituted or increased in 16 states in fiscal year 2002 and/or fiscal year 2003. The states instituting additional copayment requirements are Arizona, California, Delaware, Illinois, Kentucky, Massachusetts, Michigan, Mississippi, New Hampshire, Ohio, Oregon, Rhode Island, Texas, Utah, Vermont, and West Virginia. Research has shown that copayments are a significant deterrent to the use of essential medical care and prescription drugs among low-income populations, and that there are adverse health consequences when such treatment is foregone or delayed.

The Kaiser survey was taken in May and June of 2002. Since then, additional reductions in Medicaid for fiscal year 2003 have been announced. For example, as noted above, in mid-September, Oklahoma announced sharp reductions in Medicaid eligibility for children and seniors, as well as complete elimination of its medically needy program.

Other Areas

A recent report by the Children's Defense Fund found that states have reduced funding for child care for low-income working families.[4] Waiting lists for child care programs exist in 19 states and are growing larger. Over the past two years, Florida added more than 12,000 children to its waiting list, while Texas added more than 5,000 children. Indiana and Tennessee also have increased their waiting lists substantially. Eligibility for services has been restricted in a number of states, including Indiana, Nebraska, New Mexico, and West Virginia. Parent fees have increased in a number of states, including Indiana, North Carolina, and West Virginia.

Other programs that assist low-income working families also are being cut. For example, Indiana is reducing the amount a family can earn without losing TANF cash benefits and



reducing spending on a range of social service programs. Massachusetts' FY 2003 budget reduces funding for employment services for cash assistance recipients and eliminates both an eviction prevention program that helped about 8,000 families last year and assistance for thousands of legal immigrant families. Tennessee is cutting transportation assistance, job skills training, and substance abuse services. Ohio is cutting state housing subsidies for the elderly, emergency shelter funds that help homeless men, women, and children, funding for child welfare agencies that protect abused and neglected children, and a program that provides meals to hungry older adults.

State support of public universities also has been significantly affected by state budget deficits. Many state institutions of higher education have acted to make up for lost revenues by sharply increasing tuition, which reduces access to higher education for low- and moderate-income families. For example, freshmen at Texas A&M University will pay at least 26 percent more in tuition and fees in 2002 than in 2001. Tuition and fees at the University of Kansas will be more than 20 percent higher in 2002. Pennsylvania State University increased tuition by 13.5 percent.

More Problems on the Horizon

These examples reflect only some of the cuts to date; substantial additional cuts appear to be in store in when state legislatures reconvene. Under normal circumstances, state fiscal conditions do not recover until 12 to 18 months after a recession ends. As shown in Figure 1, state budget deficits were larger in fiscal year 1992 than in 1991 — even though the recession of the early 1990s ended in the middle of fiscal year 1991. The current continued weakness in the stock market and thus in capital gains income— which affects personal income tax revenue at both the federal and state levels — raises the question of whether the time clock on the 12 to 18 month lag has even begun to run in this downturn. A large number of states already are projecting deficits for fiscal year 2004.

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[1] Nicholas W. Jenny, *State Tax Revenue Decline Accelerates,* Fiscal Studies Program, The Nelson A. Rockefeller Institute of Government, September, 2002.

[2] National Conference of State Legislatures, Fiscal Affairs Program, *State Budget and Tax Actions 2002: Preliminary Report,* July 24, 2002.

[3] Kaiser Commission on Medicaid and the Uninsured, *Medicaid Spending Growth: Results from a 2002 Survey,* September 2002.

[4] Children's Defense Fund, *Low-Income Families Bear the Burden of State Child Care Cutbacks,* September 5, 2002.