



# CENTER ON BUDGET AND POLICY PRIORITIES

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## **ASSESSING THE ADMINISTRATION'S CLAIMS THAT EXTENDING \$1.1 BILLION IN EXPIRING SCHIP FUNDS IS NOT NECESSARY TO SUSTAIN EXISTING CHILDREN'S ENROLLMENT**

by Edwin Park and Matt Broaddus

Recent media reports indicate that the Bush Administration opposes bipartisan legislation to extend nearly \$1.1 billion in unspent SCHIP funds that are slated to expire and revert to the Treasury after September 30.<sup>1</sup>

Bipartisan legislation that the National Governors Association has endorsed<sup>2</sup> (S. 2759 in the Senate and H.R. 4936 in the House<sup>3</sup>) would extend the availability of the expiring funds and target the large majority of those funds to the states that need the funds to avert cutbacks in their children's health insurance programs.<sup>4</sup> This legislation would help lessen or defer looming cuts in children's health insurance enrollment by providing more adequate federal funding to the 18 states projected to face federal funding shortfalls over the next three years.

The Administration opposes the bipartisan legislation for three reasons.<sup>5</sup> First, the Administration claims there is unused federal funding in the SCHIP program that more than meets states' needs in fiscal year 2005, and the expiring funds consequently are not needed for this purpose. Second, some unspent federal funds from fiscal year 2002 are scheduled to be redistributed in 2005, and the Administration says it will distribute the bulk of these funds to the six states that otherwise will face federal funding shortfalls in 2005;<sup>6</sup> the Administration contends this targeted redistribution of unspent 2002 funds will eliminate the federal funding

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<sup>1</sup> See, for example, Ceci Connolly, "Words, Actions at Odds on Children's Health Care," *Washington Post*, September 25, 2004; William M. Welch, "States May Lose Funds for Kids' Health Care," *USA Today*, September 24, 2004; and Mary Agnes Carey, "HHS' Thompson Promises to 'Cover Any Gaps' in SCHIP Funding," *CQ Healthbeat News*, September 28, 2004.

<sup>2</sup> Letter from Governors John Hoeven (R-ND) and Jennifer Granholm (D-MI) to Senate Majority Leader Bill Frist and Senate Minority Leader Tom Daschle and House Speaker Dennis Hastert and House Minority Leader Nancy Pelosi, June 8, 2004 and Letter from Governors Jennifer Granholm (D-MI) and Haley Barbour (R-MS) to CMS Administrator Mark McClellan, September 28, 2004.

<sup>3</sup> The lead sponsors of S. 2759 are Senators Jay Rockefeller (D-WV) and Lincoln Chafee (R-RI). The lead sponsors of H.R. 4936 are Representatives John Dingell (D-MI) and Joe Barton (R-TX).

<sup>4</sup> For an analysis of the effects of the bipartisan legislation, see Edwin Park and Matt Broaddus, "Congress Can Preserve \$1.1 Billion in Expiring Children's Health Insurance Funds and Help Avert SCHIP Cutbacks," Center on Budget and Policy Priorities, revised September 28, 2004.

<sup>5</sup> Letter from HHS Secretary Tommy Thompson to Senator Charles Grassley (R-IA), September 28, 2004.

<sup>6</sup> The six states are Arizona, Minnesota, Mississippi, Nebraska, New Jersey and Rhode Island.

shortfalls in these states and be a better approach than the bipartisan legislation. Finally, the Administration argues that while the expiring funds should be extended, these funds should instead be used for outreach activities to find and enroll more of the eligible but uninsured children.

A careful examination of the Administration's arguments finds them to be seriously flawed.

## **Assessing the Administration's SCHIP Claims**

### **The unused federal SCHIP funds that the Administration points to are *not available* to the states that face federal funding shortfalls.**

In the aggregate, states are projected to have \$10.7 billion in federal SCHIP funds available to them in fiscal year 2005. This exceeds the \$5.2 billion in federal SCHIP funds projected to be spent in 2005.<sup>7</sup> The Administration cites these figures in arguing that states do not need the \$1.1 billion in expiring funds because a large surplus of federal SCHIP funds already exists. This argument makes a good sound-bite but is at odds with the federal rules that govern SCHIP funding.

Each state receives an annual allotment of federal SCHIP funding each year. That allotment is available to that state for three years. In any given year, a state may have some funding available from each of its three most recent annual SCHIP allotments. A state also may have some additional federal SCHIP funds that have been provided to it through the SCHIP redistribution process; funds that a state has not spent in three years are reallocated to other states. A state may thus have some funding available in 2005 from the annual allotments it received for fiscal years 2003, 2004 and 2005, as well as some unspent fiscal year 2002 funds that were redistributed to it. The total amount of these federal funds may (or may not) exceed the amount of federal SCHIP funds that a state needs to maintain its SCHIP program in fiscal year 2005.

Any funds such a state may have in 2005 that are in excess of what the state actually will use in 2005, however, are not available to the states that will face SCHIP funding shortfalls in 2005. The critical issue thus is *not* whether the total amount of SCHIP funding available nationwide in 2005 exceeds the total amount that can be used nationally in 2005, but whether there is adequate federal funding *in individual states* for them to sustain their SCHIP programs.

Under current law, 18 states are projected to have insufficient federal funding by 2007. Unless the Administration proposes legislation to alter the current federal SCHIP financing system — by taking away federal funds to which a number of states are entitled under the current rules and shifting these funds to other states to ensure no state faces a federal funding shortfall through 2007 — the total amount of aggregate funding available to the SCHIP program as a whole is somewhat beside the point.

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<sup>7</sup> Center on Budget and Policy Priorities' SCHIP financing model, updated to reflect state expenditure projections reported by states to the Centers for Medicare and Medicaid Services (CMS) in May 2004.

The bipartisan legislation mentioned above would leave the existing SCHIP financing system essentially unchanged but would extend the \$1.1 billion in expiring SCHIP funds and target a large majority of those funds to the states that most need them. A more comprehensive restructuring of the SCHIP financing system could then be considered when SCHIP is reauthorized, which is currently scheduled for 2007.

**The Administration's approach would likely *increase* the magnitude of the federal funding shortfalls that some states face in 2006 and 2007.**

Under current law, unspent funds from fiscal year 2002 are scheduled to be redistributed during 2005 to states that have fully spent their 2002 funds. Because federal law is silent on exactly how the 2002 funds are to be redistributed, the Administration believes it can use its discretion to target a large share of the estimated \$623 million in unspent fiscal year 2002 funds to the six states that are projected to face federal funding shortfalls in 2005.<sup>8</sup> The Administration claims there are more than enough unspent 2002 funds to fill the federal funding gaps in these six states. The Administration therefore argues that under its approach of targeting a large share of the unspent 2002 funds to these six states, no state would have insufficient federal funding in 2005.

The Administration's approach raises several concerns. The total amount of additional federal funding required by the six states to meet all of their needs in 2005, prior to any redistribution of unspent 2002 funds, could be as high as \$623 million.<sup>9</sup> To redistribute unspent 2002 funds as it proposes, the Administration would thus have to redistribute as much as 100 percent of the unspent 2002 funds to the six states facing shortfalls in 2005.<sup>10</sup> Some 30 states, however, are expected to qualify for a share of the redistributed 2002 funds in 2005. Under the Administration's approach, the other 24 states would get significantly less in unspent 2002 funds (and possibly no such funds at all) than they would receive under a redistribution formula consistent with the approach used in prior years. This would constitute a major departure from how previous redistributions of unspent SCHIP funds were conducted; under the previous distributions, the unspent funds were redistributed proportionally among the qualifying states,

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<sup>8</sup> Center on Budget and Policy Priorities' SCHIP financing model updated to reflect state expenditure projections reported by states to the Centers for Medicare and Medicaid Services (CMS) in May 2004. The Administration estimates the total amount of unspent 2002 funds available for redistribution at \$660 million.

<sup>9</sup> Center on Budget and Policy Priorities' SCHIP financing model updated to reflect state expenditure projections reported by states to the Centers for Medicare and Medicaid Services (CMS) in May 2004. The Administration estimates the total shortfalls among the six states in 2005 at only \$275 million. The substantial difference between the Administration's estimates and those produced by the Center's state-specific SCHIP financing model are the result of differing state spending estimates for 2005. The Administration uses fiscal year 2005 spending estimates as estimated by states in May 2004. The Center's model uses fiscal year 2004 spending trended forward by historical spending from 2001-2004 to estimate spending in 2005, principally because state-reported estimates for the coming year have tended not to be accurate indicators of actual state spending.

<sup>10</sup> Using the Administration's estimate that these six states will face a combined shortfall of \$275 million in 2005 (see footnote 9), filling the shortfalls in these states would account for 44 percent of the total unspent 2002 funds available for redistribution in 2005. That would reduce the amounts redistributed to the other 24 states by 26 percent, as compared to the amounts that would be made available through a redistribution consistent with the approach used in prior years.

based on their SCHIP expenditure levels over the prior three-year period. Many of these 24 other states likely would find this new way of allocating the redistributed funds to be highly inequitable.

Moreover, it is unclear how the Administration would estimate the federal funding shortfalls in these six states. Such estimates might not correspond to the actual spending needs in these states in 2005, as spending estimates tend to fluctuate over the course of the year. And if the distribution of funding is based on these six states' estimates of their shortfalls, these states may have an incentive to inflate their estimates of the shortfalls to gain a larger redistribution of funds.

Most important, because the Administration's approach would substantially reduce the amount of unspent 2002 funds redistributed to the other 24 states that qualify for redistributed funds (as compared to the amount of redistributed funds these states would receive if the redistribution were done in the normal manner), this approach would *enlarge the federal SCHIP funding shortfalls that many of these states face in 2006 and 2007*. One group of states that would be adversely affected consists of states in which a redistribution of unspent 2002 funds under the normal procedures would enable the states to avert any shortfalls through 2007, but the smaller redistribution of 2002 funds the states would get under the Administration's approach would cause the states to face a shortfall in 2006 and/or 2007. Another group of states that would be negatively affected consists of states that already will face shortfalls in 2006 and 2007 (but not in 2005). The smaller redistribution of unspent 2002 funds that these states would receive under the Administration's approach would cause their shortfalls in 2006 and/or 2007 to be larger than would otherwise be the case. In contrast, the proposed bipartisan legislation would increase the amount of SCHIP funds redistributed to all 30 states that qualify for the redistribution of unspent 2002 funds, since the \$1.1 billion in funds otherwise slated to revert to the Treasury on September 30, 2004 would be added to the pool of funds being redistributed.

To provide some additional background on this problem, states are projected to face federal funding shortfalls totaling \$1.4 billion in 2006 prior to any redistribution of unspent 2003 funds, and only \$199 million in unspent 2003 SCHIP funds are expected to be available for redistribution in 2006. A number of states consequently face a large funding hole in 2006. The Administration's approach would not do anything to address this problem. Similarly, states face a collective federal funding gap of \$2.0 billion in 2007 prior to any redistribution of unspent 2004 funds, while the amount of unspent 2004 funds available for redistribution is projected to be only \$153 million.

The bipartisan legislation would ease these problems by increasing the amount of SCHIP funds in the system by \$1.1 billion and targeting these funds to the states with the greatest SCHIP funding needs. This \$1.1 billion would be in addition to the modest amounts of unspent SCHIP funds expected to be available for redistribution in the next few years.

### **What about outreach funds?**

The Administration argues that the expiring SCHIP funds should be extended, but should be diverted to outreach activities. Increasing federal funding for outreach by states, community

organizations, faith-based groups, and schools, as the Administration is proposing, might help to enroll more eligible but uninsured children in Medicaid and SCHIP. A large proportion of the low-income children who are uninsured are children who are eligible for Medicaid or SCHIP but are not enrolled.

It is unclear, however, whether states at this time need or would use additional federal funding for outreach. States already have the ability to use up to 10 percent of their federal SCHIP funds for administrative costs, including outreach. Yet, nearly all states have levels of administrative and outreach spending well below the 10 percent limit. In addition, many states have scaled back or eliminated SCHIP outreach activities in recent years in order to reduce state SCHIP expenditures in the face of state budget deficits.

More importantly, the fact remains that more than one-third of the states are projected to have insufficient federal funding over the next few years just to sustain their *existing* SCHIP programs and to continue insuring the number of children *they already cover*. Shoring up federal SCHIP funding to ensure that all states have adequate federal funds to sustain their existing programs thus is a prerequisite to providing increased outreach funding to find and enroll uninsured children. Unless states have the federal funds that are necessary to sustain their existing programs in coming years, many are unlikely to spend the outreach funds the Administration proposes to provide.

In short, increased outreach funding should not come at the expense of maintaining the availability of the \$1.1 billion in expiring SCHIP funds to provide insurance coverage to children. This suggests that to maximize the enrollment of low-income children, the best approach would be to take both steps in tandem — to maintain the availability of the expiring SCHIP funds for covering children, as the bipartisan legislation would do, and to provide separate, additional funding for outreach.

## **Conclusion**

The Administration claims it is not necessary to maintain the availability of the nearly \$1.1 billion in federal SCHIP funds for covering *currently enrolled* children, because there already is sufficient federal SCHIP funding for this purpose. While acknowledging that some individual states face federal funding shortfalls in 2005, the Administration claims it can address those shortfalls without Congressional action. The Administration also argues that the focus should shift to outreach. The Administration opposes bipartisan legislation introduced in the Senate and the House to extend the availability of the expiring SCHIP funds for insuring children.

An analysis of the Administration's arguments finds them flawed. Of particular concern, the Administration's approach would do nothing to address the funding shortages that a number of states face in 2006 and 2007 and would, in fact, increase the magnitude of those shortfalls in some of these states.