MEMORANDUM

DATE: September 19, 2013

TO: House Appropriations Committee

FROM: Mary Ann Cleary, Director
Kyle I. Jen, Deputy Director

RE: Roads and Risk Reserve Fund, Medicaid Expansion Savings, and Potential Budget Risks

This memorandum provides information on the newly-created Roads and Risks Reserve Fund, state budget savings under the recently-enacted Medicaid expansion, and potential risks for the current state budget, including the ongoing shortfall in Health Insurance Claims Assessment collections.

Roads and Risks Reserve Fund

Section 211b of Article VIII of Public Act 59 of 2013, the FY 2013-14 General Government budget, created the Road and Risks Reserve (RRR) Fund. That section also provided for the deposit of $230.0 million in GF/GP revenue into the RRR Fund. These funds were available on a one-time basis following the May 2013 Consensus Revenue Estimating Conference. Subsection (3) of section 211b states the following:

> *Funds may only be spent from the roads and risks reserve fund upon appropriation. One-half of the reserve funds are available for appropriation for roads effective October 1, 2013. It is the intent of the legislature that the balance of the reserve funds will be appropriated for roads effective February 1, 2014 if those funds have not been appropriated for other purposes prior to that date.*

Article XVII of Public Act 59, the FY 2013-14 Transportation budget, included a one-time appropriation of $115.0 million from the RRR Fund for a Priority Roads Investment Program (above and beyond $121.3 million in GF/GP funds appropriated on a one-time basis in order to fully match available federal road funds). These funds will presumably be expended for a portion of the road maintenance or construction projects that could otherwise have been funded under a comprehensive transportation financing package. In conjunction with the FY 2013-14 Executive Budget, the Governor proposed to raise $1.2 billion in new transportation-dedicated revenue through increases in motor fuel and vehicle registration taxes. Neither that proposal, nor various alternatives that have been considered, have yet been acted upon by the Legislature.

Under the statement of intent in Sec. 211b, an additional $115.0 million will become available for appropriation for road projects on February 1 of next year if the funds have not been appropriated for other budgetary purposes.

Medicaid Expansion Savings

House Bill 4714 was recently approved by the Legislature and signed by the Governor as Public Act 107 of 2013. The bill provides for the expansion of the state's Medicaid program under the federal Affordable Care Act, with certain revisions to program requirements to be submitted as a waiver to the federal government.[1]

[1] For more detailed information on House Bill 4714, see this HFA analysis: http://www.legislature.mi.gov/documents/2013-2014/billanalysis/House/pdf/2013-HLA-4714-D0B38F1F.pdf.

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Additionally, the bill appropriates $1.7 billion in new federal funds to be received from the federal government for Medicaid costs under the expansion and includes negative appropriations to account for projected net state GF/GP savings to be realized under the expansion. Those savings will be achieved mainly by shifting current state General Fund costs for mental health services, the Adults Benefit Waiver program, and certain prisoner health care costs to federal reimbursement under the Medicaid expansion.

Based on the original estimates for the Medicaid expansion, the GF/GP savings, and associated negative appropriations in House Bill 4714, totaled $192.8 million: $168.6 million in the Community Health budget (accounting for $20.0 million GF/GP in administrative costs) and $24.2 million in the Corrections budget. For FY 2014-15, these savings will increase to an estimated $275.6 million on a full-year basis.

The bill, however, did not receive immediate effect and, therefore, will not take legal effect until sometime in late March (90 days after legislative *sine die* in December). Assuming that this delays the effective date of the Medicaid expansion until April 1, 2014, state savings will be reduced by roughly one-third. The state will realize six months of savings, rather than nine months, while up-front administrative costs remain at $20.0 million GF/GP.

As shown below, FY 2013-14 GF/GP savings due to the Medicaid expansion are now estimated to total $119.4 million: $103.3 million in the Community Health budget and $16.1 million in the Corrections budget. At some point, then, the FY 2013-14 budget will need to be adjusted through a positive supplemental bill or some other mechanism to address a GF/GP shortfall of $73.4 million: $65.3 million in the Community Health budget and $8.1 million in the Corrections budget.

Medicaid Expansion GF/GP Savings
FY 2013-14
$ in Millions

Category	**HB 4714 Appropriations**	**Estimated Savings Without I.E.**	**Positive Supplemental Required**
Non-Medicaid Mental Health Services	($152.9)	($102.0)	51.0
Adult Benefits Waiver	(21.4)	(12.7)	8.7
Plan First! Enrollees	(1.1)	(0.7)	0.4
Health Insurance Claims Assessment	(13.1)	(7.9)	5.2
Subtotal: Community Health	**($188.6)**	**($123.3)**	**$65.3**
Corrections Medical Expenses	**($24.2)**	**($16.1)**	**8.1**
Statewide Administration*	**$20.0**	**$20.0**	**$0.0**
NET GF/GP SAVINGS	**($192.8)**	**($119.4)**	**$73.4**

*Appropriated in Community Health budget

Source: Department of Community Health (figures may not add to due to rounding)

Section 33(c) of House Bill 4714 states the following (emphasis added):

> *"State savings" means any state fund net savings, calculated as of the closing of the financial books for the Department of community health at the end of each fiscal year, that result from the program described in this section. The savings shall result in a reduction in spending from the following state fund accounts: adult benefit waiver, non-Medicaid community mental health, and prisoner health care. Any identified savings from other state fund accounts shall be proposed to the House of*

Representatives and Senate appropriations committees for approval to include in that year's state savings calculation. ***It is the intent of the legislature that for fiscal year ending September 30, 2014 only, $193,000,000.00 of the state savings shall be deposited in the roads and risks reserve fund created in section 211b of Article VIII of 2013 PA 59.***

Because the deposit into the RRR Fund is framed only as a statement of intent, additional legislative action will be necessary to effectuate it. Assuming the deposit is, in fact, made and is adjusted based on the lowered savings amount, the RRR Fund will have a total balance of $349.4 million, as shown below.

Road and Risks Reserve Fund
FY 2013-14
$ in Millions

Initial Deposit: FY 2013-14 Budget	$230.0	
House Bill 4714 (intent only)	192.8	
Lowered savings without immediate effect	(73.4)	
Total Potential Balance	**$349.4**	
Initial Appropriation: Priority Road Investment	$115.0	
Potential remaining appropriations	234.4	
Additional immediate appropriation (HB 4714)		59.7
Appropriation from initial deposit available 2/1/14		115.0
Additional appropriation available 2/1/14 (HB 4714)		59.7
Total Potential Appropriations	**$349.4**	

Assuming that the initial provisions governing the RRR Fund are not amended when the additional deposit is made, of the total balance, $234.4 million would still be available for appropriation (accounting for the $115.0 million already appropriated for priority road projects). Of that amount, half of the savings from Medicaid expansion, or $59.7 million, would be available for immediate appropriation for road projects. The remaining $174.7 million, half of the total fund balance, would become available for such projects on February 1 of next year if the funds have not been appropriated for other budgetary purposes.

Potential Budget Risks

Several significant risks that could potentially require additional state appropriations above budgeted FY 2013-14 levels, from the RRR Fund or other available funding sources, currently exist.

<u>Health Insurance Claims Assessment</u>

The most immediate risk for the FY 2013-14 budget relates to the Health Insurance Claims Assessment (HICA). This assessment was created in 2011 to replace a previous Use Tax on Medicaid-contracted Health Maintenance Organizations. The assessment is charged as a 1.0% tax on claims paid by health insurance providers and was initially projected to generate $400 million in revenue per year, to be used to offset state GF/GP funding appropriated for the state's Medicaid program and draw down federal matching funds.

For several technical and legal reasons, actual HICA revenue collections have been well below that level, creating a roughly $130 million annual shortfall. For FY 2011-12, this shortfall was eliminated at year-end with savings from appropriation lapses in the Community Health and other budgets. For FY

2012-13, one-time resources in the Merit Award and Medicaid Benefits trust funds were utilized to cover the shortfall.

For FY 2013-14, the full $400 million in HICA revenue was again appropriated, but to date the Legislature has taken no action to increase HICA collections.[2] The FY 2013-14 Executive Budget proposed to make the assessment rate adjustable to generate the full $400 million; this would require a rate of roughly 1.4 to 1.5%.

Alternately, House Bill 4612 would create a new HICA charge of $25 per vehicle as part of revisions to Michigan's no-fault insurance system. That would generate an estimated $175.5 million in new revenue per year. The bill has been reported from the House Insurance Committee but has not been acted upon by the full House.[3]

Absent legislative action to increase HICA revenue, either GF/GP funds or some other external source of revenue will need to be appropriated to offset the HICA shortfall, or Medicaid expenditures will need to be reduced through program changes.

Federal DSH Payment Disallowance

An additional significant budget risk is the potential liability related to a disallowance of certain Disproportionate Share Hospital (DSH) payments, primarily for the state psychiatric facility, that were charged to the federal government in FYs 2007-08 and 2008-09. This issue was initially raised in a financial audit released by the Legislative Auditor General in 2010. The disallowance potentially totals $195 million, although the amount and terms of repayment remain subject to discussions between the state and the federal Department of Health and Human Services.

Legal Proceedings Regarding Retirement Contributions

There are two ongoing legal cases related to retirement system revisions adopted by the Legislature in recent years that could have state budget ramifications:

- A recent Court of Appeals ruling found that the 4% pension contribution created by the Legislature in 2011 for state employees who are still part of the State Employees' Retirement System pension plan was unconstitutional. Since April 2012, when collections began, the state has collected an estimated $62.5 million through the 4% charge to employees (based on salary), or about $44.2 million on an annual basis. If the state Supreme Court confirms the ruling, the state would presumably need to refund the contributions made by employees to that point and increase state funding in the ongoing annual state budget to offset the loss of the 4% charge. Roughly half of state contributions for pension costs are made from GF/GP funds.

- For the FY 2014-15 state budget, a major consideration is the disposition of roughly $500 million in funds collected from employees in the Michigan Public School Employees' Retirement System (MPSERS) revisions through a 3% employee health benefit contribution (based on salary) created in 2010 that is currently under legal dispute. Those funds are being held in escrow pending a state Supreme Court review of a Court of Appeals ruling against the state. If those funds do not become available to pay the state's contribution to the retirement system under recent MPSERS revisions (to allow for a cap on local employer contributions for unfunded accrued liability charges), the state School Aid budget will face a shortfall of roughly

[2] House Bill 4714 also appropriated an additional $13.1 million in HICA revenue, utilized to general additional GF/GP savings. This amount will be reduced to an estimated $7.9 million by the delay in the Medicaid expansion implementation.

[3] For more detailed information on House Bill 4612, see this HFA analysis: http://www.legislature.mi.gov/documents/2013-2014/billanalysis/House/pdf/2013-HLA-4612-155E72F3.pdf.

$250 million for FY 2014-15, requiring either additional revenue to be identified or reductions to be made from FY 2013-14 appropriation levels.[4]

Revenue Collections

Finally, the most recent revenue collection data indicates that year-to-date FY 2012-13 revenues are approximately $95.0 million GF/GP and $125 million School Aid Fund higher than the May Consensus Revenue Estimating Conference estimates.[5] There is still one month of collections remaining plus annual accruals before FY 2012-13 revenues will be final, but revenue collections do not currently appear to be a risk to the state budget.

Please call if you have any questions about this information.

[4] For more detailed information on recent MPSERS revisions, see this HFA report: http://www.house.mi.gov/hfa/PDFs/MPSERS%20report%20Apr2013.pdf.

[5] For more detailed information on current revenue collections, see this HFA report: http://www.house.mi.gov/hfa/PDFs/revreview_Sep13.pdf.