Ohio Legislative Service Commission

Baseline Forecast of GRF Revenues and Medicaid Expenditures for the FY 2014-FY 2015 Biennial Budget

Testimony before the House Finance and Appropriations Committee

February 5, 2013

Chairman Amstutz and members of the House Finance and Appropriations Committee, I am Mark Flanders, Director of the Legislative Service Commission (LSC). I am here to testify on LSC's forecasts for General Revenue Fund (GRF) revenues and Medicaid expenditures in fiscal years 2013 through 2015. The information in the accompanying LSC forecast book includes an overview and forecast for the economy, forecasts of GRF revenues, and forecasts of expenditures in the Medicaid Program. These are baseline forecasts, LSC's predictions for revenues and expenditures if current law were to remain unchanged throughout the next biennium.

Summary – Comparison of LSC and Executive Budget Baseline Forecasts

LSC forecasts somewhat higher baseline GRF revenues for the biennium than are forecast for the executive budget. The forecast is higher in both of the fiscal years.

The differences between LSC's forecasts of total GRF receipts and those in the executive budget are summarized in the table below. The differences in this testimony are presented as LSC's forecast minus the executive's, so a positive number corresponds to LSC forecasting higher revenue. LSC's forecast for the biennium is $293.2 million greater than the Office of Budget and Management's (OBM's). Four tables that are attached to this testimony provide more detailed forecast comparisons for fiscal years 2013 through 2015 and for the FY 2014-FY 2015 biennium as a whole.

Summary of LSC and OBM Baseline GRF Revenue Forecast Differences

	FY 2013	FY 2014	FY 2015
Dollar Difference	$77.1 million	$85.4 million	$207.8 million
Percent Difference	0.3%	0.3%	0.6%

LSC forecasts baseline Medicaid service expenditures to be lower for FY 2013, FY 2014, and FY 2015 than are forecast in the executive budget. The differences between LSC's forecasts of Medicaid service expenditures and those in the executive budget are summarized in the table below.

Summary of LSC and OBM Baseline All-Fund Medicaid Forecast Differences

	FY 2013	FY 2014	FY 2015
Dollar Difference	-$52.0 million	-$119.1 million	-$80.7 million
State Share	-$18.8 million	-$41.2 million	-$28.2 million
Percent Difference	0.3%	0.6%	0.4%

Tax revenues and Medicaid service expenditures are dependent in part on developments in the economy. In the rest of my testimony, I will focus on these topics, starting with the economy.

The Economy

U.S. inflation-adjusted gross domestic product (real GDP) decreased by 0.1% in the fourth quarter of calendar year 2012. Few economic forecasters foresaw a drop in real GDP, but most expected growth to be weak. The slight dip was due to transitory factors, i.e., reduced inventory accumulation and a decline in federal spending on national defense. Consumer spending grew by 2.2% for the quarter, slightly faster than during the preceding two quarters. LSC economists consider it unlikely that the surprise decrease in real GDP, by itself, will materially affect forecasters' views regarding the continuation of the business cycle expansion.

Aside from the fourth quarter real GDP figure, most recent indicators have implied slow but consistent economic growth. Because that growth has been slow, large numbers of people are still unemployed, both nationally and in Ohio, though unemployment has come down more in Ohio than nationwide. National employment grew by 1.6% during the year ending in December; for Ohio the comparable figure is 1.8%, representing an increase of slightly over 90,000 jobs. Most of Ohio's economic sectors experienced job gains for the year. Ohio's unemployment rate has declined slowly but steadily, from a high of 10.6% in late 2009 and January 2010, to 6.7% in December. Though the number of unemployed Ohio workers declined by nearly 235,000 from January 2010 to December 2012, it should be noted that just under 118,000 (50%) of the decline was due to workers finding jobs; the rest was due to workers exiting the labor force.

Though the LSC forecasts are based on continuation of the economic expansion, economic forecasters point to a number of risks to that continuation. Important risks are posed by federal fiscal policy. Though Congress has acted to prevent income tax increases for a substantial majority of Americans, it has provided only a very short-term delay in the expiration of the federal government's authority to borrow, and in sequestration, the term that refers to a significant reduction in federal spending that is required by current federal law. Apart from what develops in the overall economy due to either of these issues, it is worth noting that sequestration would affect the state budget directly. Other risks include continuing economic problems in Europe, and, seemingly as always, oil prices. Tension in the Middle East, perhaps centered on Iran, could lead to a sharp increase in prices despite the growth in supply arising domestically (and even here in Ohio). Some analysts foresee problems in financial markets arising from borrowers' difficulties in repaying student loan debt. Other adverse developments, not currently foreseen, could undermine the economic outlook.

As you consider the forecasts below, then, please remember that it is inevitable that economic forecasts are very uncertain things. The only thing that we know for certain is that the LSC forecast will be wrong; it is only a question of how much and in which direction. It is possible that the baseline forecast could prove significantly too optimistic regarding economic growth in the nation and Ohio. Alternatively, it could be that it will prove to be too pessimistic.

In developing a GRF revenue forecast, LSC economists have relied on the economic forecasting firm Global Insight for the economic predictions that underlie those revenue forecasts. Specifically, we have used Global Insight's January baseline forecasts for the nation and Ohio as the sources for input or explanatory variables in the models.

As is detailed in the accompanying forecast materials, this forecast shows national real GDP, the broadest measure of economic activity, growing at about a 2.0% annual rate during the period corresponding to state FY 2013, by 2.1% during FY 2014, and by 3.2% during FY 2015. Personal income in Ohio, which is not adjusted for inflation, is forecast to grow somewhat faster, by 3.5% during the current fiscal year and during FY 2014, and by 4.4% during FY 2015. These growth rates are strong enough to bring down unemployment, but only slowly. By the end of FY 2015, Ohio's statewide average unemployment rate is projected to fall only to 6.5%, from the 6.8% level expected for the current quarter.

Revenue Forecasts

The LSC baseline forecasts for FY 2014 and FY 2015 assume the current Revised Code tax structure. Among the notable implications of that is that the newly enacted financial institutions tax (FIT) begins to generate revenue in FY 2014, and the taxes that it is replacing, the corporate franchise tax and the business and property tax, are expected to produce no revenue during the upcoming biennium. The estate tax, which no longer applies to estates of individuals who died after the first of this year, is expected to yield little revenue in FY 2014 (and none in FY 2015). Also, the GRF is assumed not to receive an amount, estimated to be $140 million per year, of commercial activity tax (CAT) revenue attributable to sales of petroleum products, in accordance with an Ohio Supreme Court decision handed down in December. Finally, 1.68% of GRF tax receipts are forecast to be transferred to the Local Government Fund (LGF) and 1.69% to the Public Library Fund (PLF) starting in FY 2014, based on the LSC estimate of tax receipts for FY 2013.

For FY 2013, LSC estimates total GRF tax revenue to be $20.71 billion, after distributions to the local government funds. This is $107 million more than the current estimate by OBM. LSC estimates that this expected positive variance in revenues will be augmented slightly by earnings on investments, which combined with revenues from license fees are estimated to be $3 million above the OBM estimate.

For FY 2014, LSC forecasts total GRF tax revenue to be $21.23 billion, a $523 million (2.5%) increase from FY 2013. Economic growth forecast by Global Insight is expected to lead to moderate growth in most tax sources. Income tax revenue is forecast to grow by 2.0% due to improved labor markets, proprietors' income, and income from investments. The growth is restrained due to an assumption that some revenue realized in FY 2013 was due to one-time payments intended to avoid increases in federal income tax rates that, as of late last year, were to have gone into effect on January 1. Revenue is expected to increase strongly from the nonauto sales tax, primarily due to increasing revenue from Medicaid health insuring corporations (HICs). A projected decline in cigarette tax revenue is due to the continuation of a long-term trend. A projected decline in revenue from the kilowatt hour tax is due to weak growth in all funds revenue being more than offset by growing allocations to the PLF, which are debited in part against this tax.

For FY 2015, LSC forecasts total GRF tax revenue to increase to $22.30 billion, representing growth of $1.07 billion (5.0%) from FY 2014. Revenue growth is forecast to continue for most taxes, again with the exception of the cigarette tax.

Tax revenue for the biennium is forecast to be $43.54 billion. That is approximately $3.82 billion greater than tax revenue during the current biennium.

Medicaid Expenditure Forecast

Medicaid services are an "entitlement" for individuals who meet eligibility requirements. This means that if eligible for Medicaid, the individual is guaranteed the benefits and the state is obligated to pay for them. It is for this reason that the executive and LSC forecast Medicaid expenditures.

LSC's baseline forecast shows the expected cost of this entitlement program given current policies. It does not take into account the optional expansion under ACA

(Affordable Care Act). However, the "woodwork" effect of ACA and the ACA physician rate increases are added to LSC's baseline expenditure forecast.

All Medicaid figures that I am about to present are "all funds," also referred to as combined state and federal dollars. For FY 2013, Medicaid expenditures are projected to be $16.3 billion. For FY 2014, Medicaid expenditures are estimated to be $18.8 billion, a $2.5 billion (15.3%) increase from FY 2013. For FY 2015, Medicaid expenditures are projected to be $19.7 billion, an $872 million (4.6%) increase from FY 2014.

As the economic growth in Ohio is expected to continue through 2015 and also the unemployment rate in Ohio is projected to fall slowly through the end of 2015, the Medicaid caseload for families and children is projected to decrease. On the other hand, due to the aged population, the Medicaid caseload for the aged, blind, and disabled population is projected to grow in the upcoming biennium.

In general, the increases in Medicaid expenditures are being driven by the caseload growth in the aged, blind, and disabled population and increases in monthly per member costs. However, the large projected increase in expenditures from FY 2013 to FY 2014 is mostly due to the "woodwork" effect, the physician rate increase under ACA, and the implementation of the Integrated Care Delivery System (ICDS) and Health Homes authorized under H.B. 153.

The ACA increases access to health insurance beginning in 2014 through a coordinated system of "insurance affordability programs," including an optional expansion of Medicaid to all individuals under age 65 whose family income is at or below 138% federal poverty guidelines (FPG), and the creation of health insurance exchanges. Whether or not a state implements the optional Medicaid expansion, states will see increased enrollment among currently eligible people, most of whom were previously uninsured. This is sometimes called the "woodwork" effect.

The ACA requires states to raise their Medicaid physician fees to at least Medicare levels for family physicians, internists, and pediatricians for many primary care services. Physicians in both fee-for-service and managed care environments get the enhanced rates. The primary care fee increase, which applies in 2013 and 2014, is fully federally funded up to the difference between a state's Medicaid fees in effect on July 1, 2009 and Medicare fees in 2013 and 2014.

Ohio will partner with the Centers for Medicare & Medicaid Services (CMS) to test a new model for providing Medicare and Medicaid dual enrollees with a more coordinated, person-centered care experience. Under this model, Ohio and CMS will contract with ICDS plans that will coordinate the delivery of and be accountable for all covered Medicare and Medicaid services for participating dual enrollees. ICDS plans will be responsible for conducting a comprehensive assessment of dual enrollees' medical, behavioral health, long-term services and supports, and social needs in seven regions (29 counties) of the state for 115,000 dual enrollees. Dual enrollees and their caregivers will work with a care management team to develop person-centered, individualized care plans.

H.B. 153 authorized Ohio Medicaid to implement a system under which Medicaid recipients with chronic conditions are provided with coordinated care through health homes. Beginning in October 2012, Ohio Medicaid received federal approval for enhanced federal match to pay for care coordination in serious and persistent mental illness (SPMI) focused health homes. Under the new system, care managers in Patient-Centered Medical Homes provide intensive care coordination and develop an individualized care plan for each consumer to address both medical and nonmedical needs.

Mr. Chairman and members of the Committee, thank you for the opportunity to present the LSC forecasts. My staff and I would be happy to answer any questions that you may have.

Testimony on GRF Revenue and Medicaid Expenditure Forecast.docx/

FY 2013 Revenue Estimates Millions of Dollars						
GRF	**Original Aug. 2012**	**OBM Jan. 2013**	**Change**	**LSC Jan. 2013**	**Change**	**LSC Minus OBM**
TAX REVENUE						
Auto Sales	$1,075.0	$1,070.0	-$5.0	$1,080.6	$5.6	$10.6
Nonauto Sales & Use	$7,350.0	$7,297.9	-$52.1	$7,315.4	-$34.6	$17.5
Total Sales & Use Taxes	$8,425.0	$8,367.9	-$57.1	$8,396.0	-$29.0	$28.1
Personal Income	$8,970.0	$9,250.5	$280.5	$9,263.1	$293.1	$12.6
Commercial Activity	$850.0	$831.4	-$18.6	$842.7	-$7.3	$11.3
Corporate Franchise	$150.0	$180.0	$30.0	$201.7	$51.7	$21.7
Financial Institutions						
Public Utility	$115.0	$110.0	-$5.0	$116.4	$1.4	$6.4
Kilowatt Hour Excise	$305.0	$296.9	-$8.1	$298.9	-$6.1	$2.0
Natural Gas Consumption (MCF)	$60.0	$60.0	$0.0	$58.3	-$1.7	-$1.7
Foreign Insurance	$270.0	$270.0	$0.0	$279.0	$9.0	$9.0
Domestic Insurance	$195.0	$200.0	$5.0	$206.0	$11.0	$6.0
Business & Property	$25.0	$25.0	$0.0	$25.0	$0.0	$0.0
Cigarette	$815.0	$815.0	$0.0	$820.8	$5.8	$5.8
Alcoholic Beverage	$58.0	$58.0	$0.0	$58.3	$0.3	$0.3
Liquor Gallonage	$40.0	$40.0	$0.0	$40.1	$0.1	$0.1
Estate	$66.0	$100.0	$34.0	$105.6	$39.6	$5.6
Total Tax Revenue	$20,344.0	$20,604.6	$260.7	$20,711.8	$367.9	$107.2
NONTAX STATE-SOURCE REVENUE						
Earnings on Investments	$5.5	$5.5	$0.0	$7.5	$2.0	$2.0
Licenses and Fees	$46.0	$46.0	$0.0	$47.0	$1.0	$1.0
Other Revenue	$48.0	$48.0	$0.0	$48.0	$0.0	$0.0
Nontax State-Source Revenue	$99.5	$99.5	$0.0	$102.5	$3.0	$3.0
TRANSFERS						
Liquor Transfers	$160.0	$160.0	$0.0	$160.0	$0.0	$0.0
Transfers In	$27.5	$282.4	$254.9	$282.4	$254.9	$0.0
Transfers In - Temporary	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Total Transfers In	$187.5	$442.4	$254.9	$442.4	$254.9	$0.0
TOTAL GRF Before Federal Grants	$20,631.0	$21,146.5	$515.5	$21,256.7	$625.7	$110.2
Federal Grants	$8,151.3	$7,608.6	-$542.7	$7,575.4	-$575.9	-$33.2
TOTAL GRF SOURCES	**$28,782.3**	**$28,755.1**	**-$27.2**	**$28,832.2**	**$49.9**	**$77.1**

FY 2014 Baseline Revenue Forecasts

Millions of Dollars

GRF	OBM	LSC	LSC Minus OBM Difference	LSC Minus OBM Percent	Growth from FY 2013 OBM	Growth from FY 2013 LSC
TAX REVENUE						
Auto Sales	$1,119.0	$1,128.0	$9.0	0.8%	4.6%	4.4%
Nonauto Sales & Use	$7,802.1	$7,766.2	-$35.9	-0.5%	6.9%	6.2%
Total Sales & Use Taxes	$8,921.1	$8,894.2	-$26.9	-0.3%	6.6%	5.9%
Personal Income	$9,335.7	$9,448.7	$113.0	1.2%	0.9%	2.0%
Commercial Activity	$795.1	$793.8	-$1.3	-0.2%	-4.4%	-5.8%
Corporate Franchise	$0.0	$0.0	$0.0	--	-100.0%	-100.0%
Financial Institutions	$190.0	$200.0	$10.0	5.3%	--	--
Public Utility	$110.0	$125.6	$15.6	14.2%	0.0%	7.9%
Kilowatt Hour Excise	$279.1	$289.2	$10.1	3.6%	-6.0%	-3.2%
Natural Gas Consumption (MCF)	$60.0	$60.4	$0.4	0.7%	0.0%	3.6%
Foreign Insurance	$272.0	$288.0	$16.0	5.9%	0.7%	3.2%
Domestic Insurance	$214.0	$211.0	-$3.0	-1.4%	7.0%	2.4%
Business & Property	$0.0	$0.0	$0.0	--	-100.0%	-100.0%
Cigarette	$790.0	$799.2	$9.2	1.2%	-3.1%	-2.6%
Alcoholic Beverage	$58.0	$60.7	$2.7	4.7%	0.0%	4.1%
Liquor Gallonage	$41.4	$41.0	-$0.4	-1.0%	3.5%	2.2%
Estate	$15.0	$23.0	$8.0	53.3%	-85.0%	-78.2%
Total Tax Revenue	$21,081.4	$21,234.8	$153.4	0.7%	2.3%	2.5%
NONTAX STATE-SOURCE REVENUE						
Earnings on Investments	$6.0	$8.4	$2.4	40.0%	9.1%	12.0%
Licenses and Fees	$46.0	$48.6	$2.6	5.7%	0.0%	3.4%
Other Revenue	$43.0	$47.9	$4.9	11.4%	-10.4%	-0.2%
Nontax State-Source Revenue	$95.0	$104.9	$9.9	10.4%	-4.5%	2.3%
TRANSFERS						
Liquor Transfers	$0.0	$0.0	$0.0	0.0%	-100.0%	-100.0%
Transfers In	$363.6	$363.6	$0.0	0.0%	28.8%	28.8%
Transfers In - Temporary	$0.0	$0.0	$0.0	0.0%	--	--
Total Transfers In	$363.6	$363.6	$0.0	0.0%	-17.8%	-17.8%
TOTAL GRF Before Federal Grants	$21,540.0	$21,703.3	$163.3	0.8%	1.9%	2.1%
Federal Grants	$9,423.3	$9,345.4	-$77.9	-0.8%	23.9%	23.4%
TOTAL GRF SOURCES	**$30,963.3**	**$31,048.7**	**$85.4**	**0.3%**	**7.7%**	**7.7%**

FY 2015 Baseline Revenue Forecasts Millions of Dollars						
GRF			LSC Minus OBM		Growth from FY 2014	
	OBM	LSC	Difference	Percent	OBM	LSC
TAX REVENUE						
Auto Sales	$1,172.0	$1,179.0	$7.0	0.6%	4.7%	4.5%
Nonauto Sales & Use	$8,261.5	$8,224.5	-$37.0	-0.4%	5.9%	5.9%
Total Sales & Use Taxes	$9,433.5	$9,403.5	-$30.0	-0.3%	5.7%	5.7%
Personal Income	$9,760.3	$9,951.7	$191.4	2.0%	4.5%	5.3%
Commercial Activity	$820.9	$826.9	$6.0	0.7%	3.2%	4.2%
Corporate Franchise	$0.0	$0.0	$0.0	--	--	--
Financial Institutions	$200.0	$209.0	$9.0	4.5%	5.3%	4.5%
Public Utility	$110.0	$138.6	$28.6	26.0%	0.0%	10.4%
Kilowatt Hour Excise	$270.5	$282.0	$11.5	4.3%	-3.1%	-2.5%
Natural Gas Consumption (MCF)	$60.0	$62.4	$2.4	4.0%	0.0%	3.3%
Foreign Insurance	$276.0	$299.0	$23.0	8.3%	1.5%	3.8%
Domestic Insurance	$254.0	$247.0	-$7.0	-2.8%	18.7%	17.1%
Business & Property	$0.0	$0.0	$0.0	--	--	--
Cigarette	$765.0	$778.3	$13.3	1.7%	-3.2%	-2.6%
Alcoholic Beverage	$58.0	$61.0	$3.0	5.2%	0.0%	0.5%
Liquor Gallonage	$42.5	$41.9	-$0.6	-1.4%	2.7%	2.2%
Estate	$0.0	$0.0	$0.0	--	-100.0%	-100.0%
Total Tax Revenue	$22,050.6	$22,301.1	$250.5	1.1%	4.6%	5.0%
NONTAX STATE-SOURCE REVENUE						
Earnings on Investments	$6.0	$11.3	$5.3	88.3%	0.0%	34.5%
Licenses and Fees	$46.0	$50.5	$4.5	9.8%	0.0%	3.9%
Other Revenue	$51.2	$51.2	$0.0	0.0%	19.1%	6.9%
Nontax State-Source Revenue	$103.2	$113.0	$9.8	9.5%	8.6%	7.7%
TRANSFERS						
Liquor Transfers	$0.0	$0.0	$0.0	0.0%	--	--
Transfers In	$427.9	$427.9	$0.0	0.0%	17.7%	17.7%
Transfers In - Temporary	$0.0	$0.0	$0.0	0.0%	--	--
Total Transfers In	$427.9	$427.9	$0.0	0.0%	17.7%	17.7%
TOTAL GRF Before Federal Grants	$22,581.8	$22,842.0	$260.2	1.2%	4.8%	5.2%
Federal Grants	$10,982.1	$10,929.6	-$52.5	-0.5%	16.5%	17.0%
TOTAL GRF SOURCES	**$33,563.8**	**$33,771.6**	**$207.8**	**0.6%**	**8.4%**	**8.8%**

FY 2014 - FY 2015 Biennium Baseline Revenue Forecasts

Millions of Dollars

GRF	OBM	LSC	LSC Minus OBM Difference	Percent
TAX REVENUE				
Auto Sales	$2,291.0	$2,307.0	$16.0	0.7%
Nonauto Sales & Use	$16,063.6	$15,990.7	-$72.9	-0.5%
Total Sales & Use Taxes	$18,354.6	$18,297.7	-$56.9	-0.3%
Personal Income	$19,096.0	$19,400.4	$304.4	1.6%
Commercial Activity	$1,616.0	$1,620.7	$4.7	0.3%
Corporate Franchise	$0.0	$0.0	$0.0	--
Financial Institutions	$390.0	$409.0	$19.0	4.9%
Public Utility	$220.0	$264.2	$44.2	20.1%
Kilowatt Hour Excise	$549.6	$571.2	$21.6	3.9%
Natural Gas Consumption (MCF)	$120.0	$122.8	$2.8	2.3%
Foreign Insurance	$548.0	$587.0	$39.0	7.1%
Domestic Insurance	$468.0	$458.0	-$10.0	-2.1%
Business & Property	$0.0	$0.0	$0.0	--
Cigarette	$1,555.0	$1,577.5	$22.5	1.4%
Alcoholic Beverage	$116.0	$121.7	$5.7	4.9%
Liquor Gallonage	$83.9	$82.9	-$1.0	-1.2%
Estate	$15.0	$23.0	$8.0	53.3%
Total Tax Revenue	$43,132.0	$43,535.9	$403.9	0.9%
NONTAX STATE-SOURCE REVENUE				
Earnings on Investments	$12.0	$19.7	$7.7	64.2%
Licenses and Fees	$92.0	$99.1	$7.1	7.7%
Other Revenue	$94.2	$99.1	$4.9	5.2%
Nontax State-Source Revenue	$198.2	$217.9	$19.7	9.9%
TRANSFERS				
Liquor Transfers	$0.0	$0.0	$0.0	--
Transfers In	$791.5	$791.5	$0.0	0.0%
Transfers In - Temporary	$0.0	$0.0	$0.0	--
Total Transfers In	$791.5	$791.5	$0.0	0.0%
TOTAL GRF Before Federal Grants	$44,121.8	$44,545.3	$423.5	1.0%
Federal Grants	$20,405.4	$20,275.0	-$130.4	-0.6%
TOTAL GRF SOURCES	**$64,527.1**	**$64,820.3**	**$293.2**	**0.5%**