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Budget Footnotes

A NEWSLETTER OF THE OHIO LEGISLATIVE BUDGET OFFICE MARCH, 1999

FISCAL OVERVIEW

— Frederick Church

Some of the timing issues that distorted the state's fiscal picture as of the end of January were cleared up by the end of February. However, a new timing issue, and thus a new distortion, was introduced. Matters cleared up include the following:

(i) The huge shortfall in the corporation franchise tax was partly erased by February's collections. Unfortunately, there was still a $23.2 million shortfall by the end of February, and this shortfall cannot be explained away as timing. Combined January-February revenues for the first of the three FY 1999 franchise tax payments were $6.9 million below estimate, which suggests that the other two payments will fall short also. The year-end shortfall will probably exceed $23.2 million.

(ii) OBM transferred the GRF's share of the FY 1998 surplus that goes to pay for the tax year 1998 income tax reduction. This transfer was originally supposed to be made in January, but was in fact held until February. The share of the year-end surplus going to the tax cut was $701.4 million. The GRF share of this amount is 89.5%, or $627.7 million. This money was transferred from the GRF to the Income Tax Reduction Fund (ITRF) in July. It has now been transferred back to the GRF to help offset the lost income tax revenue from the 9.34% cut in income tax rates, which affects tax filings from January through April (or August, given filing extensions).

(iii) Bucking the yearlong trend, February Medicaid payments were $4.8 million over estimate. This was due to payments originally scheduled in January being delayed until February. Medicaid disbursements in January were lower than they should have been due to a delay in payment for certain service categories. The underspending in January was particularly large (negative $55.6 million), when it probably should have been more like $33.0 million. The late payment of claims affected reported disbursements in hospital care, prescription drugs, and physician services. January and February disbursements combined were $50.8 million below estimate. The monthly average of $25.4 million was close to the year's monthly average of $23.7 million.

Unfortunately, just as some matters were cleared up, others became murkier. The income tax, all year the leader in revenue overages, suddenly plunged $38.4 million below estimate, dragging the year-to-date overage down to $5.8 million. However, this seems to be the result of early processing of tax refund payments. The Ohio Department of Taxation's electronic-filing initiative has been more successful than imagined, with almost 450,000 electronic returns (not counting school district

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STATUS OF THE GRF

ISSUES OF INTEREST

Due to the pressures of the budget, this month's issue of ***Budget Footnotes*** diverges from its usual format. In place of the usual analysis of GRF revenues and spending, we have reproduced our budget forecasting testmony before the House Finance Committee.

This covers much of the same ground as the usual revenue and expenditure analysis, and includes our forecasts for the upcoming biennium as well. ***Budget Footnotes*** will return to its standard format next month.

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Budget Footnotes is issued monthly by the Legislative Budget Office (LBO), a non-partisan fiscal research agency serving the Ohio General Assembly.

Budget Footnotes examines the fiscal position of the state GRF on a monthly basis. Each issue also contains summaries of Controlling Board actions that have policy implications, and articles on fiscal issues of current interest.

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TABLE 1
General Revenue Fund
Simplified Cash Statement
($ in millions)

	Month of January	Fiscal Year 1999 to Date	Last Year	Difference
Beginning Cash Balance	($94.2)	$1,649.0		
Revenue + Transfers	$1,975.5	$12,095.5		
Available Resources	$1,881.3	$13,744.5		
Disbursements + Transfers	$1,303.5	$13,167.0		
Ending Cash Balances	**$577.8**	**$577.8**	**$120.9**	**$456.9**
Encumbrances and Accts. Payable		$700.2	$449.3	$250.9
Unobligated Balance		**($122.4)**	**($328.4)**	**$206.0**
BSF Balance		$906.9	$862.7	$44.2
Combined GRF and BSF Balance		**$784.5**	**$534.3**	**$250.2**

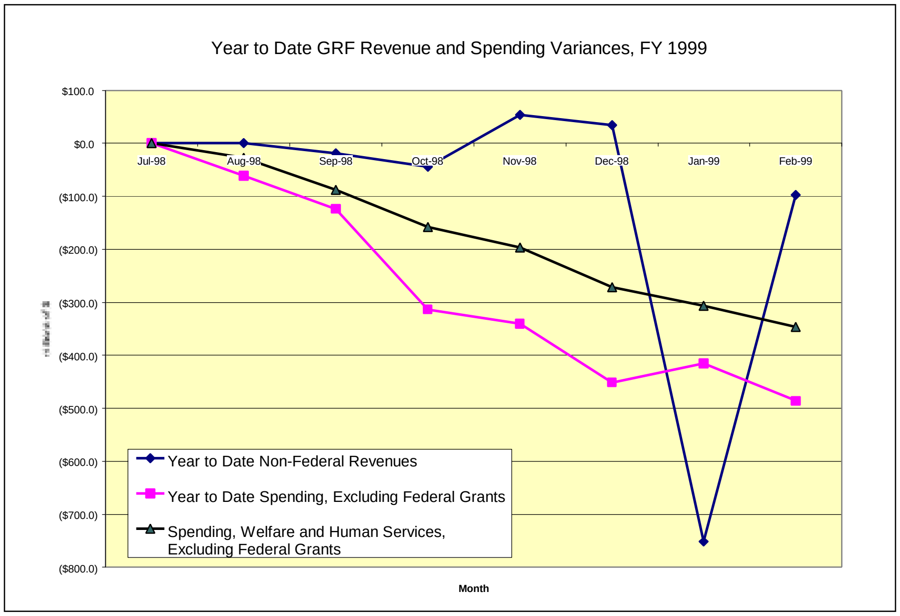
income taxes) filed through February. Most of these early electronic filers are owed refunds, so the volume of refunds has been much higher than normal through the first two months. This situation is expected to turn around in March, when a big revenue overage is expected.

The non-auto sales and use tax also tanked in February, with collections falling $14.8 million below estimate. The betting here is that at least some of this shortfall was due to poor weather in the first half of January, since non-auto sales tax collections are based primarily on the prior month's retail sales activity. LBO expects collections to hit the estimate in March, although it is unclear whether the state will regain any of February's lost ground.

In general, the shortfall in the non-auto sales tax makes us more cautious about state revenues. It now appears that by year's end, the franchise tax, sales tax, and public utility tax will all be below the revised estimates. The question then becomes how large the income tax overage will be, and how much of those shortfalls it will offset.

The state is getting a boost in non-tax revenues. Discounting the shortfall in transfers, non-tax revenue is $20.8 million over estimate, led by a $27.8 million overage in investment earnings. Federal revenues have also picked up slightly. A small overage in February reduced the year-to-date shortfall to $54.4 million.

On the spending side, welfare and human services programs continue to fall sharply below estimate. Medicaid's small $4.8 million overage in February was more than offset by $29.9 million in TANF underspending. For the year, both categories are well below the forecast. TANF disbursements are $129.8 million below estimate, 19.3% below estimate and 11.7% below last year's level. Medicaid is $189.8 million below estimate, a variance of 5.2%. Spending has increased by only 0.6% from last year. Furthermore, this 0.6% increase is the only increase among the five spending categories classified as "welfare and human services." (See Table 3.)



In both the text and the tables, LBO's comparison of actual and estimated revenues and spending, both monthly and year-to-date, are based on OBM's revised forecasts from July, not the original projections. Thus, when we say that revenues are above the estimate and that spending is below, it is with respect to the revised forecasts. The variances would be even larger if the original estimates were being used. ❑

TRACKING THE ECONOMY

— Frederick Church

The Japanese model—government-sanctioned cartels, price-fixing, forced savings, import barriers, cheap loans to targeted industries, and cross shareholding—forged the world's preeminent exporter of manufactured goods in the post-war period. As a recipe for success, it's hard to argue with. It also runs counter to nearly every prescription that has come out of the major multilateral lending institutions—the World Bank and International Monetary Fund—for the last two decades.

—"How Asia Got Rich: World Bank vs. Japanese Industrial Policy", by Edith Terry – Japan Policy Research Institute, Working Paper #10, June 1995.

When Michael Crichton published his novel ***Rising Sun*** in 1992, the U.S. was coming out of a recession but didn't know it yet. The National Bureau of Economic Research (NBER) didn't put the official ending date of the last recession at March 1991 until December 22, 1992. (This led to a ***New York Times*** headline "This Just in: Recession Ended 21 Months Ago"). The recovery was very slow, employers and employees were worried, and there were fears that Japan was supplanting the U.S. as the world's biggest economic power. The Maastricht Treaty and the proposed "Europe 92" elimination of internal trade barriers and movement toward a common currency was also stirring fears that Europe would grow quickly and leave the U.S. behind.

Right now, with the benefit of hindsight, those fears seem ridiculous. Most European countries are growing rather slowly, and Japan is reeling from the impact of a very long recession. The U.S. is finishing the century as the world's greatest economic power, and the leader in information-age technology.

Table 2
General Revenue Fund Income
Actual vs. Estimate
Month of February, 1999
($ in thousands)

REVENUE SOURCE			
TAX INCOME	Actual	Estimate*	Variance
Auto Sales	$49,158	$44,835	$4,323
Non-Auto Sales & Use	294,320	309,075	(14,755)
Total Sales	$343,478	$353,910	($10,432)
Personal Income	$302,380	$340,743	($38,363)
Corporate Franchise	346,226	222,460	123,766
Public Utility	1,655	6,750	(5,095)
Total Major Taxes	**$993,739**	**$923,863**	**$69,876**
Foreign Insurance	$19,810	$70,200	($50,390)
Domestic Insurance	1,400	225	1,175
Business & Property	0	70	(70)
Cigarette	23,102	20,790	2,312
Soft Drink	0	0	0
Alcoholic Beverage	4,113	4,264	(151)
Liquor Gallonage	1,966	2,063	(97)
Estate	0	0	0
Racing	0	0	0
Total Other Taxes	$50,392	$97,613	($47,221)
Total Taxes	**$1,044,131**	**$1,021,475**	**$22,656**
NON-TAX INCOME			
Earnings on Investments	$0	$0	$0
Licenses and Fees	2,479	3,200	(721)
Other Income	7,757	5,880	1,877
Non-Tax Receipts	$10,236	$9,080	$1,156
TRANSFERS			
Liquor Transfers	$8,000	$6,000	$2,000
Budget Stabilization	0	0	0
Other Transfers In	627,744	0	627,744
Total Transfers In	$635,744	$6,000	$629,744
TOTAL INCOME less Federal Grants	**$1,690,111**	**$1,036,555**	**$653,556**
Federal Grants	$285,374	$278,000	$7,374
TOTAL GRF INCOME	**$1,975,485**	**$1,314,555**	**$660,930**

* July, 1998 estimates of the Office of Budget and Management.

Detail may not add to total due to rounding.

LBO is rather surprised that a significant milestone was recently reached with relatively little fanfare here at home, although it was big news in Asia. In February, Japan's unemployment rate exceeded the rate for the United States. Japan's Management and Coordination Agency reported that the Japanese unemployment totaled 4.6 percent in February, exceeding the U.S. level of 4.3 percent. It estimated that a record 3.13 million people were out of work. This announcement was a bitter pill for a country long renowned for "lifetime employment". Actually, since the Japanese government revised its estimate of the January jobless rate from 4.3 percent to 4.4 percent, Japan's unemployment rate has actually exceeded America's for two months. (The situation in Japan is really much worse than the official numbers indicate since several million more are still "employed," but are thought to have no real work.)

More than a third of Japan's recently unemployed, or about 1 million people, have lost their jobs because of restructuring and corporate bankruptcies, the government estimated. Japanese officials admit that even higher jobless figures are inevitable in coming months as more corporations announce plans to lay off workers.

Table 3
General Revenue Fund Income
Actual vs. Estimate
Fiscal Year-to-Date 1999
($ in thousands)

REVENUE SOURCE *TAX INCOME*	Actual	Estimate*	Variance	FY 1998	Percent Change
Auto Sales	$465,263	$459,906	$5,357	$447,745	3.91%
Non-Auto Sales & Use	3,205,706	3,236,780	**(31,074)**	3,080,996	4.05%
Total Sales	$3,670,968	$3,696,686	**($25,718)**	$3,528,741	4.03%
Personal Income	$4,204,703	$4,198,862	**$5,841**	$3,973,644	5.81%
Corporate Franchise	376,169	399,417	(23,248)	410,267	-8.31%
Public Utility	203,723	236,250	**(32,527)**	240,486	-15.29%
Total Major Taxes	$8,455,564	$8,531,215	($75,651)	$8,153,138	3.71%
Foreign Insurance	$168,192	$206,700	($38,508)	$223,924	-24.89%
Domestic Insurance	1,442	462	980	678	112.85%
Business & Property	169	738	(569)	485	-65.23%
Cigarette	183,817	182,358	1,459	181,718	1.16%
Soft Drink	0	0	0	0	#N/A
Alcoholic Beverage	35,123	34,580	543	34,606	1.49%
Liquor Gallonage	18,903	18,810	93	18,753	0.80%
Estate	61,941	49,875	12,066	51,912	19.32%
Racing	0	0	0	0	#N/A
Total Other Taxes	$469,586	$493,524	($23,938)	$512,075	-8.30%
Total Taxes	**$8,925,150**	**$9,024,739**	**($99,589)**	**$8,665,212**	**3.00%**
NON -TAX INCOME					
Earnings on Investments	$85,270	$57,500	$27,770	$65,400	30.38%
Licenses and Fees	22,120	26,580	(4,460)	24,520	-9.79%
Other Income	61,900	64,373	(2,473)	68,501	-9.64%
Non-Tax Receipts	$169,289	$148,453	$20,836	$158,421	6.86%
TRANSFERS					
Liquor Transfers	$59,000	$54,000	$5,000	$56,000	5.36%
Budget Stabilization	0	0	0	$0	#N/A
Other Transfers In	647,392	671,148	(23,756)	269,308	140.39%
Total Transfers In	$706,392	$725,148	($18,756)	$325,308	117.15%
TOTAL INCOME less Federal Grants	**$9,800,830**	**$9,898,340**	**($97,510)**	**$9,148,942**	**7.13%**
Federal Grants	$2,294,715	$2,349,102	($54,387)	2,206,357	4.00%
TOTAL GRF INCOME	**$12,095,545**	**$12,247,442**	**($151,897)**	**$11,355,299**	**6.52%**

* July, 1998 estimates of the Office of Budget and Management.

Detail may not add to total due to rounding.

Recently, the Oji Paper Co. announced it will cut 2,000 workers from its payroll in the next two years, after recording its first annual loss since World War II. Electronics giant NEC has said it would slash 15,000 jobs to improve its balance sheet, and Oki Electric has said that it would cut 2,700 workers. Japan's debt-laden banks also are being forced to reduce their staffs.

The number of jobholders declined for the 12th straight month in February, reflecting Japan's deep recession. The prospect of even greater unemployment threatens to slow efforts to reform the Japanese economy and to aggravate growing trade friction with the United States and other countries. The Japanese government is already spending more than $1 trillion on public-works projects, guaranteed loans, tax breaks and other jobs programs. And in an effort to boost consumer spending, it is even giving coupons worth $180 to elderly pensioners and families with children.

Table 4
General Revenue Fund Disbursements
Actual vs. Estimate
Month of February, 1999
($ in thousands)

USE OF FUNDS			
PROGRAM	Actual	Estimate*	Variance
Primary & Secondary Education (1)	$355,325	$414,530	(59,205)
Higher Education	171,469	171,086	383
Total Education	$526,794	$585,616	(58,822)
Health Care/Medicaid	$458,734	$453,932	4,802
Temporary Assistance to Needy Families	43,786	73,696	(29,910)
General/Disability Assistance	4,895	4,900	(5)
Other Welfare	28,903	21,187	7,716
Human Services (2)	74,941	89,296	(14,355)
Total Welfare & Human Services	$611,259	$643,012	(31,753)
Justice & Corrections	$105,347	$100,638	4,710
Environment & Natural Resources	5,930	6,337	(407)
Transportation	3,936	2,708	1,228
Development	5,078	7,281	(2,203)
Other Government (3)	16,947	19,116	(2,169)
Capital	91	224	(133)
Total Government Operations	$137,330	$136,304	1,027
Property Tax Relief (4)	$163	$0	163
Debt Service	1,728	1,812	(84)
Total Program Payments	**$1,277,275**	**$1,366,744**	**(89,469)**
TRANSFERS			
Local Govt Distribution	$0	$0	0
Budget Stabilization	0	0	0
Other Transfers Out	26,200	0	26,200
Total Transfers Out	$26,200	$0	26,200
TOTAL GRF USES	**$1,303,475**	**$1,366,744**	**(63,269)**

(1) Includes Primary, Secondary, and Other Education.
(2) Includes Mental Health, Mental Retardation and Developmental Disabilities, and Other Human Services.
(3) Includes Regulatory and Nonregulatory agencies, Pension Subsidies, and Reissued Warrants.
(4) Includes property tax rollbacks, homestead exemption, and tangible property tax exemption.

* August, 1998 estimates of the Office of Budget and Management.

Detail may not add to total due to rounding.

What all this means in the long run is still anybody's guess. Despite its recent poor performance, Japan is still a country with formidable economic resources. However, the longer the recession goes, and the worse the prospects for its young people become, the more vulnerable Japan becomes to depletion of its greatest resource: its human capital. Younger Japanese are increasingly thinking about going elsewhere to find employment, and an outflow of talented young labor at this point could be a severe blow to the economy's long-run potential, especially given their overall low number of young people. Certainly, the "Japanese model" referred to in the quote at the beginning of this section, the model that was so much discussed and so widely emulated, is now in disrepute. Given the rather discouraging performance of the other Asian economies that followed the Japanese model, it may stay in disrepute for some time. ❑

Table 5
General Revenue Fund Disbursements
Actual vs. Estimate
Fiscal Year-to-Date 1999
($ in thousands)

USE OF FUNDS

PROGRAM	Actual	Estimate*	Variance	FY 1998	Percent Change
Primary & Secondary Education (1)	$3,282,714	$3,381,483	($98,769)	$3,077,369	6.67%
Higher Education	1,545,106	1,540,337	4,769	1,487,225	3.89%
Total Education	$4,827,820	$4,921,820	($94,000)	4,564,594	5.77%
Health Care/Medicaid	$3,447,622	$3,637,418	(189,796)	$3,426,842	0.61%
Temporary Assistance to Needy Families	541,618	671,416	(129,799)	613,301	-11.69%
General/Disability Assistance	38,134	48,293	(10,159)	38,478	-0.89%
Other Welfare	279,055	334,044	(54,989)	289,108	-3.48%
Human Services (2)	793,586	809,323	(15,737)	817,173	-2.89%
Total Welfare & Human Services	$5,100,014	$5,500,496	(400,482)	$5,184,902	-1.64%
Justice & Corrections	$1,084,362	$1,131,383	(47,020)	$1,033,971	4.87%
Environment & Natural Resources	94,805	90,671	4,133	94,641	0.17%
Transportation	23,172	18,581	4,591	17,205	34.68%
Development	79,963	82,232	(2,269)	80,442	-0.60%
Other Government (3)	252,247	287,819	(35,572)	241,980	4.24%
Capital	2,544	3,743	(1,199)	3,053	-16.66%
Total Government Operations	$1,537,094	$1,614,430	(77,336)	$1,471,291	4.47%
Property Tax Relief (4)	$536,423	$538,489	(2,065)	$515,545	4.05%
Debt Service	120,100	120,263	(163)	102,138	17.58%
Total Program Payments	**$12,121,451**	**$12,695,497**	**(574,046)**	**$11,838,471**	**2.39%**
TRANSFERS					
Capital Reserve	$0	$0	0	$0	—
Budget Stabilization	44,184	44,184	(0)	34,400	28.44%
Other Transfers Out	1,001,349	967,560	33,789	729,351	37.29%
Total Transfers Out	$1,045,533	$1,011,744	33,789	$763,751	36.89%
TOTAL GRF USES	**$13,166,984**	**$13,707,241**	**(540,257)**	**$12,602,222**	**4.48%**

(1) Includes Primary, Secondary, and Other Education.
(2) Includes Mental Health, Mental Retardation and Developmental Disabilities, and Other Human Services.
(3) Includes Regulatory and Nonregulatory agencies, Pension Subsidies, and Reissued Warrants.
(4) Includes property tax rollbacks, homestead exemption, and tangible property tax exemption.

* August, 1998 estimates of the Office of Budget and Management.

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Issues of Interest

LBO recently presented it's forecast of revenues and public assistance on the state's 2000-2001 biennial budget to members of Ohio's House Finance Committee. We have reproduced our staffs' testmony within the *Issues of Interest* section this month.

FORECAST OF REVENUES AND PUBLIC ASSISTANCE

TESTIMONY OF DENNIS MORGAN
LEGISLATIVE BUDGET OFFICER

Mr. Chairman, members of the House Finance and Appropriations Committee, I am here today to present the Legislative Budget Office's (LBO) forecast of revenues for the FY 2000-2001 biennium. This includes our forecast for the Medicaid program, as well as Temporary Assistance for Needy Families (TANF) and the Disability Assistance (DA) program.

Because of the compressed timing of the budget, we have not been able to develop an estimated ending fund balance for FY 1999 that we could compare to the executive's forecast. We intend to complete this as soon as possible. Likewise, we have not had time to explore all the assumptions made in the budget concerning the various programs in the Department of Human Services. We plan to make such a comparison and present the information to the Human Services Subcommittee when they begin budget hearings on the Department of Human Services.

Our forecasts project slightly higher revenues for the forecast period than is assumed in the executive budget. These estimates are greater by the following amounts:

FY 1999	$ 54.6 million
FY 2000	$ 19.1 million
FY 2001	$ 83.4 million

Before we begin to look at the detail supporting these numbers, as well as our forecast of human service caseload numbers, I would like to briefly discuss a number of issues that I feel the committee should keep in mind as it considers the FY 2000-2001 biennium.

The Economy

Any consideration of the state's revenue forecast must begin with a discussion of the national economy. And the watchwords for the economy and our forecast have to be uncertainty and caution.

Two years ago we stood before this committee and testified that our forecast for the current biennium would lead us into the fourth longest economic recovery in U.S. history (and the second longest recovery since WW II). And further that some economists were speculating that the economy might go another five years without a cyclical downturn.

What began in 1991 has led us today to the 96th month of the current expansion, the longest peacetime expansion on record. The longest previous expansion was from December 1982 to July 1990. Indeed, December 1982 through today marks a period of 16 years of expansion interrupted only by a mild eight month recession in the middle. Even when wartime expansions are included, the current expansion is the second longest on record, trailing only the 106 month expansion that occurred from March 1961 to December 1969.

Like two years ago, we are not forecasting a recession in the upcoming biennium. But had we held this meeting six months ago, our forecast discussion would almost certainly have included a recession scenario early in our forecast. At that time the two major forecasting firms we contract with were forecasting either a 30% or 50% chance of a recession in 1999 or 2000. Now, both firms include a 30 percent probability of a recession sometime in calendar year 2000.

Have the economic underpinnings of our economy changed much since then? No. Pushing the smaller recession scenarios further into the future seems to simply represent forecasters general concern about the length of the expansion and the belief in the inevitability of business cycles. The problem last year and one of the chief risks now is financial instability in the international economy.

The most recent round of financial instability began when Thailand devalued its currency in July 1997. This led to banking and financial crises in most of the Asian rim countries, Russia and most recently Brazil. During this time, the most commonly discussed scenario was that a financial crisis would lead to a major stock market adjustment and a crisis in consumer sentiment. Since the consumer has driven the US economy for years now, a major consumer retrenchment would likely lead the US into recession. Fortunately the crisis in Brazil was slow moving and did not create an investment panic similar to the earlier crises.

But what of the future? Worldwide currency trading is approximately $1.5 trillion dollars a day and money moves in and out of countries on short notice. Globalization of the international economy is real and it leaves you wondering where will the next crisis originate from and what its impact will be?

The U.S. Economy

The U.S. economy is undeniably robust. But you have to seriously question how long the United States can remain an oasis of prosperity in the face of modest to bad economic news in the rest of the world.

In this extended economic expansion, the “rules” of economics are being constantly challenged. Two years ago we testified that unemployment rates were extremely low, possibly unsustainably low. This seemed true for the US, and more so for Ohio. Yet employment remains at record highs and wage and price inflation remain under control.

Last year, economic growth was similar to what it was in 1997, but the U.S. economy generated 500,000 fewer jobs. Job growth in our current forecast is expected to slow further. One of the variables inhibiting job growth in Ohio is the question of where will we find additional workers.

Other than people intentionally between jobs, there aren’t that many people left in the work force pool. At this point in the expansion, “discouraged” workers that are unemployed either are probably low skilled or are unable to find jobs in their current profession.

Public assistance recipients are also at an all-time low. Out of 80,000 adult recipients in the Temporary Assistance to Needy Families program, about 30% to 35% are working at least part-time. This leaves a little over 50,000 people who might be employed or employable. If 20,000 of them were to find jobs, employment would only grow by four-tenths of one percent. Limits on additional employment are one of the main reasons we have a conservative estimate in the growth of the personal income tax.

Y2K

In considering our economic forecast, I believe that a few words about the Y2K issue are justified. Y2K is not the end of the world as we know it, yet it is big and it is real. My concerns are not based on immediate impacts in the United States. Disruptions here are likely to be isolated or of short duration. They may create inconveniences, but probably not much more. The best analogies seem to be likening it to recent natural disasters.

I should point out that no one “knows” what the impacts will be, and when you are talking about Y2K issues, you are always looking at a moving target. Problem identification and progress changes daily and the time event for Y2K issues extend from now through the year 2002.

Two weeks ago the bipartisan U.S. Senate Special Committee on the Year 2000 Technology Problem released it’s interim report, *Investigating the Impact of the Year 2000 Problems.* In releasing the report, committee chair Senator Bob Bennett, R, Utah stated that the Y2K issue created a high probability of economic impact in Latin America, South America, Asia and Africa. Consequences - unknown.

In the section on International Preparedness, the report states, "According to Gartner, the majority of disruptions will be minimal. Only 10% of failures are expected to last more than 3 days. The question then becomes, which areas will face disruptions longer than 3 days and how severe will the impact of these failures be?"

I bring this to the discussion today to point out that in our globalized and interconnected world, this kind of disruption could be critical. A serious disruption in the global just-in-time manufacturing system could result in a recession.

Consider how quickly the UPS strike in 1997 rippled though the US economy. Consider also that in the spring of 1998, two GM plants went on strike and within weeks GM was shut down. Analysts believe that this alone took two-tenths of a percent off of U.S. economic growth in the second quarter of 1998.

Consider then if you will that various estimates have placed the number of microchips at work in the United States at around five billion. If only one percent fail, that is five million computer chips at risk. Extend that to the international community and you see that the risk could be significant. As I mentioned earlier, the consequences are totally unknown and probably unknowable. It does add another element of uncertainty to our forecast.

Federal Budget and the Tobacco Settlement

A number of years ago, the U.S. Congress passed the Budget Enforcement Act (BEA) in an effort to repair the federal budget process. The BEA put separate caps on domestic and military spending and put in place a "pay-go" process, whereby all non-emergency spending that exceeded the caps had to be offset by reductions in other spending programs or increased taxes. It furthered required the Congressional Budget Office (CBO) to "score" budget bills to make sure that the "pay-go" process was appropriately implemented.

In the proposed federal budget, the wall between the caps on domestic and military spending disappear. So the appropriations for the two areas will compete against each other. For example, spending for military pay raises could be offset by reductions in domestic spending.

This becomes an important issue as we monitor federally funded programs and dollars that come to the state. It is also important to keep this process in mind as Congress tries to find ways to fund new programs and looks at pools of money like the tobacco settlement and untouched TANF reserves that continue to increase at the federal level.

As it relates to the tobacco settlement, it is clear that federal law requires the U.S. Department of Health and Human Services to engage in recoupment. States must share Medicaid recoveries from liable third-parties with the federal government.

In Congressional action, the Senate this week is considering S. 544, which contains a provision prohibiting the federal government from attaching the state tobacco settlement funds. (The same bill also proposes a $350 million reduction in the TANF block grant.) However last week, the House Appropriations committee marked up a supplemental appropriations bill that does not prohibit recoupment.

Current law requires recoupment. Any initiative that prohibits this would have to be scored by the Congressional Budget Office as foregone revenue, meaning the Congress would have to offset the lost revenue either through spending cuts or increased taxes.

In January, the Congressional Budget Office announced its plan for scoring the tobacco settlement. Their assumption is that the loss of the recoupment dollars will cost the federal government $2.9 billion through federal fiscal year 2004. This will require the offsets that have been mentioned above. While no source for these offsets have been determined, discussions last year included reducing Medicaid administration monies.

Revenues

In developing our forecast of state revenues, the performance of the personal income tax over the last several years has created significant uncertainty about how it may perform in the future. It's no secret that forecasters have been surprised by the growth in the personal income tax in the last two years. Virtually all of the states that collect a personal income tax, as well as the federal government, experienced far stronger growth than anticipated.

The withholding portion of the personal income comprises approximately 80% to 85% of collections. The withholding on salary and wages can be forecasted with some confidence by estimating employment numbers and wage growth. However, there is a great deal of uncertainty about the income tax on capital gains, which makes up an increasing share of the remainder of the personal income tax.

As you look at the history of the personal income tax in this decade, actual collections only exceeded the forecast once through FY 1995. They exceeded the estimate again in 1996 and then virtually exploded in 1997 and 1998. This we believe is a result of the realization of capital gains related to the strong performance of the stock market.

In forecasting the future of the personal income tax, it then becomes important to be able to separate collections from withholding versus taxes collected through the capital gains. Unfortunately we only have actual capital gains data through tax year 1996. We have attempted to estimate the difference between withholding and capital gains for tax years 1997 and 1998, but those estimates are based on limited information and should be used with caution.

Using this as a base, we then calculated the capital gains in the personal income tax using estimated corporate profits as well as expert forecasts of stock market activity. While there is always some uncertainty in forecasting corporate profits, attempts to forecast stock market activity are even more difficult.

We know that this kind of forecast is not satisfactory. But until we get "hard" information in the next year or two, we are left with little other information to use in our forecast. If our assumptions are correct, then wide fluctuations in the stock market could cause a swing in personal income tax collections of several hundred million dollars over the biennium. Most of this risk is probably in FY 2001. For this obvious reason, we would urge caution in developing the spending plan in the budget.

Human Services

Our human services' caseload forecasts reflect what has been happening in the economy in several ways. Temporary Assistance for Needy Families (TANF) caseloads continue to decline, as individuals become employed or simply do not seek cash assistance. We have seen a marked downward trend in caseloads since hitting a high in 1992.

We are forecasting a further reduction in caseloads of 13.1 percent in FY 2000 and 14 percent in FY 2001. This will occur even with slightly higher unemployment levels that should be offset by the imposition of the three year time limit on benefits that begins to have an effect in October, 2000.

In the Disability Assistance Program we anticipate a continuing but slowing decline in caseload, in fact staying nearly level in FY 2001. However, costs will be going down at a slower rate due to medical inflation.

Medicaid expenditures are influenced by TANF caseload estimates, but we see a growing number of non-cash assistance individuals now qualifying for Medicaid benefits. We have experienced a shift in beneficiaries to Transitional, Low Income, Healthy Start and CHIP eligibles – and in the case of CHIP using funding sources other than the GRF.

We have benefited from a change in the federal matching rate that increased the federal share of Medicaid costs from what we originally anticipated, and we have suffered some at the hands of Medical CPI rates. Both of these continue into the upcoming biennium, with the medical inflation rate having the strongest negative effect. Overall, we believe these trends will lead to expenditure growth in Medicaid of 5.36 percent in FY 2000, and 3.85 percent in FY 2001.

Summary

To summarize, we forecast an additional $157.1 million in General Fund Revenue tax collections compared to the estimates of the executive. Like the executive, we are forecasting continued growth in the economy and falling caseloads, albeit slower than the last several years, but have reservations about a number of aspects of the forecast. ❑

REVENUE FORECASTS

TESTIMONY OF FREDERICK CHURCH
SENIOR ECONOMIST

Mr. Chairman, members of the House Finance and Appropriations Committee, I am here today to present somewhat more detailed testimony about the economic outlook and the LBO revenue forecasts. LBO and OBM probably need to have some further discussions about our underlying assumptions about particular revenue sources, to make sure that our comparisons are based on the same premises. However, at this point, it looks like LBO's forecasts of state revenues exceed OBM's by $54.6 million in FY 1999, $19.1 million in FY 2000, and $83.4 million in FY 2001. At the back of my testimony are three tables that show the LBO forecasts, the OBM forecasts, and the difference between the two, by revenue source. The total revenue forecasts and differences are summarized in the table below.

Comparison of LBO and OBM forecasts, FY 1999-2001

	FY 1999	FY 2000	FY 2001
LBO			
Tax Revenue	$14,363.3	$15,208.8	$15,962.5
Non-Tax Income	$313.0	$300.0	$290.0
Transfers	$773.7	$90.0	$91.0
Total State Revenue	$15,450.0	$15,598.8	$16,343.5
OBM			
Tax Revenue	$14,338.1	$15,196.0	$15,885.6
Non-Tax Income	$293.6	$279.7	$275.5
Transfers	$763.7	$104.0	$99.0
Total State Revenue	$15,395.4	$15,579.7	$16,260.1
LBO minus OBM	$54.6	$19.1	$83.4

Most of the difference between LBO and OBM is in our forecasts of the personal income tax. In fact, except for the income tax, LBO's forecast is lower than OBM's in FY 2000 and FY 2001. LBO projects lower revenues in the corporate franchise tax, the combined insurance taxes, and the cigarette tax. We have adjusted our estimates of the cigarette tax downward because of the price increases resulting from the tobacco settlement. These price increases will reduce consumption, reduce the tax base, and thereby reduce revenue.

The Economy

LBO's revenue forecasts begin with our forecasts of the national and Ohio economies. In the past two years we have had almost an embarrassment of riches: low unemployment, low inflation, low interest rates, strong investment, high profits, a booming stock market, increasing income, increasing consumption. There are several factors that have led many economists to call this economy "the best in a generation." Some of them are:

February 1999 was the 95th consecutive month of the current economic expansion. It is the longest peacetime expansion on record, and the second longest expansion overall. The only longer expansion was the Vietnam era boom, which ran 106 months, from March 1961 to December 1969.

The U.S. economy has been in expansion for 187 of the last 195 months. In more than 16 years, starting from December 1982, we have had one 8-month recession (July 1990 through March 1991).

The core inflation rate is the lowest it has ever been in a recovery of approximately this length, and has not shown signs of increasing. Inflation not only remained in check in CY 1998, it actually decelerated somewhat. The GDP deflator increased by only 1.0 percent, while the CPI-U increased by 1.6 per-

Table 1 - Revisions to GDP Growth Forecasts, CY 1999-2001

	1995	1996	1997	1998	1999	2000	2001
Real GDP							
DRI Jan99					2.7%	2.0%	2.0%
DRI Feb99					3.4%	1.9%	2.3%
WEFA Jan99	2.3%	3.4%	3.9%	3.9%	2.4%	1.7%	2.2%
WEFA Feb99					3.2%	1.4%	1.8%
GEAC Jan99					2.4%	2.5%	2.5%

cent. The GDP inflation number was the lowest since 1959.

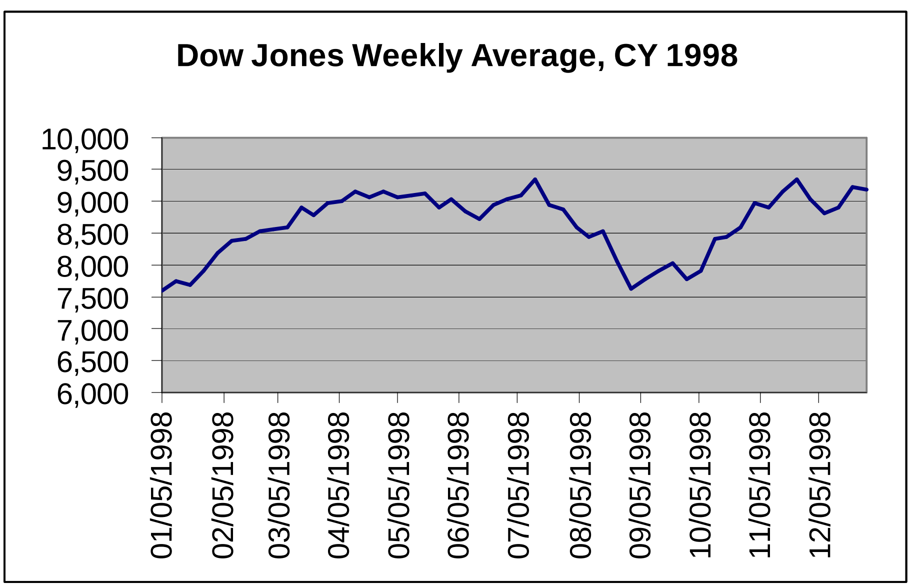
Real consumer spending increased by 4.8 percent, the fastest increase in 14 years. Housing construction, already at a high level, rose 10.4 percent, also the biggest increase in 14 years.

There were three months during CY 1998 where the U.S. unemployment rate was 4.3 percent, the lowest rate since 1970. For the year, unemployment averaged 4.5 percent, the lowest since the 3.5 percent mark in 1969 during the Vietnam War. The 1998 figure was the lowest peacetime rate since 1957, when it averaged 4.3 percent. Employment increased by 2.9 million jobs in 1998, below the 3.4 million figure of 1997, but remarkable in the face of low world demand that caused job losses of almost 300,000 in mining and manufacturing.

The effective home mortgage rate in 1998 averaged 7.1%, the lowest rates in three decades. The huge volume of mortgage refinancing put additional money in consumers' pockets and helped fuel the boom in spending.

There's more, but these examples are enough to convey the strength of the economy. The seeming paradox is that the U.S. has enjoyed all this prosperity in the midst of slow worldwide economic growth, with outright recession in Japan and in other Asian countries. A couple of years ago, when U.S. exports were a major growth engine for the U.S. economy, we probably would not have believed that export growth would slow to 1.5% and the U.S. would experience a boom, but that is precisely what we have seen.

Some forecasters have stated that if only exports had kept up their previous pace, with all other factors constant, real GDP growth would have exceeded 5%. Possibly so, but it is not at all clear that with higher world demand other factors would have remained constant. In particular, higher world demand for capital probably would have led to higher interest rates worldwide, which would have dampened U.S. investment and reduced the stock market gains that have added so much to U.S. household wealth and driven consumption increases. Instead, our merchandise trade outflows were matched by capital inflows that have helped fuel an investment boom that is increasing labor productivity and helping to restrain output price inflation even as wages and compensation move higher.



Dow Jones Weekly Average, CY 1998

Governor's Council Forecast of key variables
% change, unless otherwise indicated

	CY 1999	CY 2000	CY 2001
Real GDP	2.4	2.5	2.5
CPI inflation	2.2	2.4	2.4
U.S. personal income	4.4	4.7	4.9
Ohio personal income	3.9	4.2	4.5
U.S. corp. profits	-1.0	2.0	4.0
light vehicle sales (millions)	14.9	15.0	15.0
housing starts (millions)	1.52	1.45	1.45
U.S. unemployment rate	4.6	4.7	4.9
Ohio unemployment rate	4.4	4.5	4.6

Finally, no recap of the U.S. economy in the past two years would be complete without mentioning the financial panic that we averted in the Fall of 1998. From mid-July to the end of August, a wave of currency devaluations and economic crises in Asia (e.g. Korea, Indonesia) Russia, and Brazil panicked Wall Street and led to sharp stock market declines. DRI estimated that the value of U.S. stock holdings declined by $2 trillion in that 1.5 months. In response, the Federal Reserve reduced the target federal funds rate from 5.5% to 4.75% in three discreet moves from September 29th to November 17th. This and the concerted efforts of Fed chairman Greenspan and Treasury Secretary Rubin calmed financial markets, and by year's end the U.S. stock market had made back its losses.

In September, I and another LBO tax analyst attended a revenue estimating and forecasting conference where economists from the major forecasting firms were privately saying that recession probabilities for CY 1999 might be as high as 50%. To have that high a probability of a downturn at a time when most of the economic statistics were the strongest in a generation was eye-opening. Since then, forecasting firms such as WEFA, DRI, and RFA have scaled their recession probabilities back to about 30%, and pushed off the starting date to CY 2000.

The major forecasting firms are all predicting slower growth in CY 1999 – 2001 than we have just experienced in CY 1997-1998. Of course, they were forecasting slower growth two years ago, also. Forecasters still believe that 3.9% GDP growth is well above trend, although there is some admission within the economics profession that the official productivity numbers are rather poor estimates and thus the estimate of the trend is partly guesswork. There are some forecasters now willing to estimate trend growth that is higher than the 2.25% to 2.5% that was the received wisdom for so long. So, the slower real GDP growth in professional forecasts is really a forecast of a movement back toward trend, or in the short run, below trend.

In reality, it may be that the U.S. economy is faced with more of a knife-edge problem: either strong growth or very weak growth (or recession) if world instability destabilizes the stock market. However, the mainstream forecasts all point toward a stable, but slower growth environment.

Finally, the Governor's Economic Advisory Council (GEAC) forecast, which is the main driver for LBO's revenue and caseload forecasts, projects essentially trend growth over the CY 1999-2001 period, although the forecast for CY 1999 might well be higher if it were redone today, in light of how strong U.S. economic growth turned out to be in the 4th quarter of CY 1998.

REVENUES

LBO is keenly aware that the state has run large budget surpluses in FY 1994 -1998, and will probably have another sizable surplus at the end of FY 1999 as well. What may surprise you is that the source of these GRF surpluses has shifted markedly over that time period. As Table 1 shows, in FY 1994-1996, the bulk of the budget surplus stemmed from underspending. The income tax actually fell short of the estimate in FY 1994 and FY 1995, before posting a relatively modest overage in FY 1996. It is only in FY 1997 and FY 1998 that tax revenue overages, particularly in the income tax, were the driving force behind the state's large ending balances.

Nevertheless, the past two years have turned a spotlight on the income tax. OBM and LBO's task in analyzing and forecasting the tax and presenting the results to the General Assembly is not made any easier by the tax rate cuts, personal exemption increases, and pass-through entity withholding changes that we have made in the last three years.

Table 1 - Sources of GRF Surplus, FY 1994 - 1998

	FY 1994	FY 1995	FY 1996	FY 1997	FY 1998
Income Tax Overage	($83.3)	($38.9)	$77.2	$280.0	$567.3
Total Tax Overage	$170.3	$332.7	$174.7	$334.3	$737.7
Non-Federal Revenue	$234.6	$355.5	$238.1	$436.8	$852.6
Underspending	$459.7	$931.3	$411.5	$726.4	$651.3
Federal Revenue Shortfall	($176.9)	($445.9)	$3.1	($393.3)	($472.7)
Net Underspending	$282.7	$485.4	$414.6	$333.1	$178.6
Annual Budget Surplus*	$517.4	$840.9	$652.7	$769.9	$1,031.2
Ending GRF Fund Balance	$560.3	$928.0	$781.3	$834.9	$1,084.4
Income Tax % of Surplus	-16.1%	-4.6%	11.8%	36.4%	55.0%
Underspending % of Surplus	54.7%	57.7%	63.5%	43.3%	17.3%

amounts are in millions of $

* The term "surplus" is used here in an inexact way. The sum of the revenue overage and the underspending is not necessarily eaxctly equal to a budget surplus. The revenue overage and underspending are deviations from plan, and the plan itself may have incorporated a surplus or deficit.

Based on our conversations with federal tax officials and officials in other states, we believe that gains rose another 50% in tax year 1997, pushing up tax revenues by another $220 million, for a cumulative impact of $345 million in FY 1998. This goes a long way toward explaining the FY 1997 and FY 1998 overages of $280 million and $567 million. In tax year 1998, if capital gains increased another 20% (the Dow Jones increased by 27%), then LBO estimates that this pushed up tax revenues by another $95 million for FY 1999, for a cumulative increase of $440 million since FY 1996.

What is the source of the income tax boom that we have seen in FY 1997 and FY 1998? While employer withholding growth was very strong in FY 1998 (9.1%), the growth in quarterly estimated payments and the strength of annual return payments in spite of the rate cuts suggest that non-wage income is behind the big increases and big overages that we have seen. Indeed, even on the withholding side, it may be the case that something other than ordinary wage payments led to the 9.1% growth. BLS data indicate that Ohio payroll employment grew by 1.9% in FY 1998, while average hourly earnings (national) of production workers grew by about 4%, while earnings in other occupations grew about 3%. This is not quite enough to explain 9.1% growth in withholding, so there may well have also been bonus income or other lump-sum payments helping withholding collections.

On the non-wage income side one does not have to look far to see a star performer. The stock market has been soaring, and capital gains income has been rising along with it. Unfortunately, the last hard data on Ohio capital gains is still from tax year 1996, although tax year 1997 data will be available this Spring. We know that in tax year 1996, Ohio capital gains income increased by 52%, pushing up FY 1997 income tax collections by about $125 million.

We expect additional capital gains increases in FY 1999, but not as big a revenue overage, because OBM and LBO built some of this additional income into the base revenue figure. LBO's forecast of FY 1999 income tax revenue is $174.1 million higher than the revised forecast from July 1998, and about $50 million higher than OBM's latest forecast.

There is also additional income tax revenue from changes in business organization. More businesses are being organized as S-corporations, partnerships, and limited liability companies (LLCs) where the business does not pay the corporate tax, but instead the owners pay the income tax on their share of profits. We cannot put a hard number to the amount of tax collected from these businesses, but we know that it is growing. In tax year 1985, when Ohio last imposed the corporate-level tax on S-corporation earn-

History and Forecasts for FY 1997-2001, Baseline and Adjusted

in millions of $

	1997	1998	1999	2000	2001
Total Collections	$6,013.8	$6,941.3	$7,066.7	$8,007.2	$8,525.1
GRF Share	$5,382.3	$6,212.5	$6,324.7	$7,166.5	$7,629.9
Addback or Subtract:					
Tax Cut Impacts	($352.8)	($301.1)	($638.3)	($105.2)	$0.0
Exemption Increases	($40.0)	($89.0)	($111.0)	($145.0)	($168.0)
Pass-Through Entities			$39.0	$39.0	$39.0
Total	$6,406.6	$7,331.4	$7,777.0	$8,218.4	$8,654.1
growth rate		14.4%	6.1%	5.7%	5.3%

ings, there were an estimated 10,000 to 15,000 S-corporations in Ohio. In 1999 there are more than 100,000 (estimated).

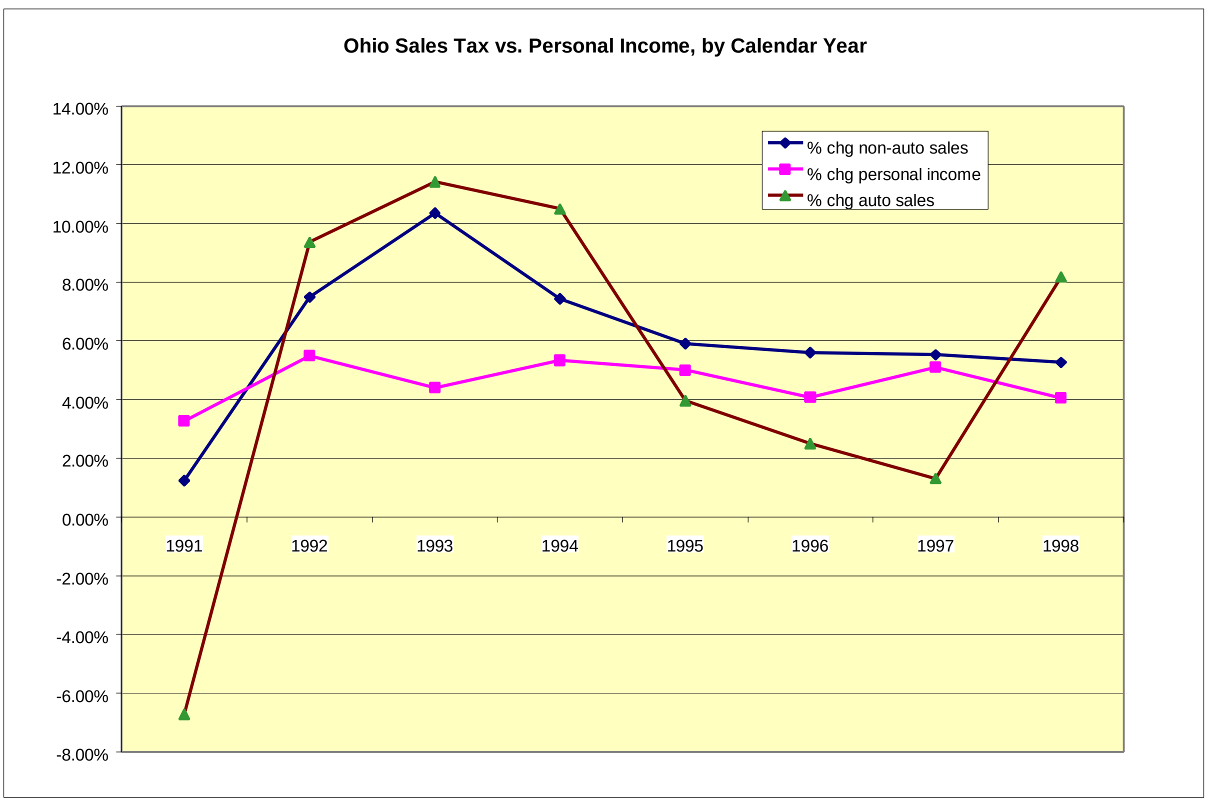
Corporate profit growth is slowing down, and is predicted to be negative in CY 1999, with small growth in CY 2000 and CY 2001. Although price/earnings ratios are at levels we probably would not have believed a few years ago, we do not believe that stock prices can continue their rapid growth with much smaller earnings growth. This will reduce income tax growth from unincorporated businesses, and income tax growth from capital gains.

If we are right about FY 1999, then the income tax is already slowing significantly from the pace of FY 1997 and FY 1998. It is not easy to construct a baseline growth figure for collections once the rate cuts and other law changes are taken into account, but we have tried to do so. FY 1999 growth in baseline collections is only 6.1%, slowing to 5.7% in FY 2000 and 5.3% in FY 2001.

Sales Tax

LBO projects that sales tax growth will be slightly slower than personal income growth over the FY 2000-2001 biennium. As the figure below illustrates, this has not been the case for the past few years (at least in non-auto sales). Consumers have been spending out of their additional real-estate and stock market wealth, refinancing their mortgages and spending the savings, and borrowing against their higher wealth. If the major forecasters are right that company earnings will be flat and stock prices will grow slowly, if at all, then this spending out of wealth should also slow down. We expect personal savings rates to resume being positive, and taxable retail sales to trail personal income.

LBO has also been thinking hard about the impact of Internet commerce on sales tax collections, trying to separate hype from reasonable estimates. LBO recently estimated that Ohio lost about $22 million in sales tax in CY 1998 from Internet sales, although the amount could have been as much as $45 million (and other state analysts apparently have even bigger numbers). The estimated GRF loss was about $18 million. If Internet sales triple again in CY 1999, the GRF tax loss increases to $54 million, or an additional $36 million. This would be enough to shave about 0.7% of growth from the non-auto sales tax. Interestingly, some Merrill Lynch analysts recently projected that store-based retail sales growth over



the next few years will be reduced from 4% annually to 3.5% annually by the substitution of Internet sales for store sales.

While these Internet estimates are speculative at this point, they provide a good reason for caution about future growth of the sales and use tax.

Corporation Franchise Tax

Corporate franchise tax revenues – GRF only - FY 1997-2001

Fiscal year	Actual revenues and original baseline	Adjustments to baseline	New baseline
1997	$1,150.8		
1998	$1,196.6		
1999	$1,184.0	($98.0)	$1,086.0
2000	$1,177.0	($124.6)	$1,052.4
2001	$1,191.1	($136.5)	$1,054.6

LBO's franchise tax estimates are lower than OBM's, and show a decline in FY 2000 and an extremely small increase in FY 2001. When LBO estimated the revenue impacts of the corporate franchise tax reform enacted by HB 215, we found that the losses from the reform increased in FY 2000 and FY 2001 (in part due to the continued phasing down of the net worth millage on financial institutions). Our forecast represents essentially a flat baseline, with increasing reductions due to the prior law changes.

Insurance Taxes

The insurance taxes were also restructured by HB 215, and there is consequently uncertainty about whether LBO's estimated impacts of the law changes will be met in reality. We have already made adjustments to our HB 215 estimates based on what has happened so far in FY 1999. Foreign insurance premium tax collections for FY 1999 have been below the estimate that LBO made when H.B. 215 passed. As a result, LBO has adjusted the estimate of FY 1999 collections downward, and then re-run the insurance tax model with lower projected growth rates for premiums in future years. This has resulted in downward adjustments to our baseline forecast of foreign insurance premium taxes.

Cigarette Taxes

Forecasted collections for FY 2000 – 2001 have been adjusted for the impact of the recent tobacco settlement between the states and the participating tobacco product manufacturers. The settlement agreement requires the tobacco companies to make payments to the states *in perpetuity*, with the payments totaling an estimated $206 billion through calendar year (CY) 2025 nationally. The settlement is expected to provide Ohio $9.87 billion in payments through CY 2025. In order to pay for the settlement, the tobacco companies have raised the price per pack of cigarettes by 45 cents.

Raising the price of a pack of cigarettes by 45 cents obviously will reduce consumption. The impact is a lot like that of a federal excise tax increase: it will operate across the board and raise prices generally, but will not exacerbate cross-state price differentials. This has two impacts: the reduction in national sales volume will reduce settlement payments to states over time, and cigarette tax collections will fall somewhat.

LBO estimates that manufacturers have raised prices by about 20%. There seems to be consensus that the price elasticity of demand for cigarettes and tobacco products is about –0.4. So, the price increase should result in a consumption decline of about 8% annually. Baseline collections have been adjusted downward by $23.4 million in FY 2000 and $23.3 million in FY 2001 to reflect this change.

Other

Finally, there are some tables attached to my testimony, after the forecasts, that I think may be of interest. The first one shows the use of the ending GRF fund balance for FY 1995-1998. This shows clearly that the bulk of the $3.63 billion in unobligated ending fund balances over that 4-year period, the biggest share has been used for income tax cuts ($1.37 billion), with transfers to schools second ($0.82 billion), and transfers to the BSF third ($0.61 billion). The remaining $0.83 billion has gone for a variety of other purposes.

The second table tries to isolate the current operating surplus or deficit for FY 1989-1998, by looking at current year revenues vs. current year spending, and excluding the impacts of carryover balances between years and inter-fund transfers to and from the GRF. ❑

Assumed Zero Tax Cut for Tax Years 1999 and 2000
Differences, LBO minus OBM, FY 2000 - FY 2001

GRF Amounts by Revenue Source
dollar amounts in millions

TAX INCOME	Estimated FY 1999	Baseline FY 2000	Adjustments	Total FY 2000	Baseline FY 2001	Adjustments	Total FY 2001
Auto Sales	$0.0	$11.0		$11.0	$11.2		$11.2
Non-Auto Sales & Use	$0.0	$10.2		$10.2	($7.0)		($7.0)
Total Sales	$0.0	$21.2	$0.0	$21.2	$4.2	$0.0	$4.2
Personal Income	$49.7	$39.1	($8.2)	$30.9	$142.8	($8.4)	$134.4
Corporate Franchise	($10.0)	($25.3)		($25.3)	($54.6)		($54.6)
Public Utility	($1.0)	$23.9		$23.9	$16.3		$16.3
Total Major Taxes	$38.7	$58.9	($8.2)	$50.7	$108.7	($8.4)	$100.3
Foreign Insurance	($20.0)	($29.0)		($29.0)	($32.0)		($32.0)
Domestic Insurance	$0.0	$10.5		$10.5	$18.9		$18.9
Business & Property	$0.0	($1.0)		($1.0)	($1.0)		($1.0)
Cigarette	$7.0	($14.4)		($14.4)	($7.1)		($7.1)
Alcoholic Beverage	($0.5)	($1.4)		($1.4)	($2.3)		($2.3)
Liquor Gallonage	$0.0	($0.4)		($0.4)	($0.3)		($0.3)
Estate	$0.0	($2.2)		($2.2)	$0.4		$0.4
Racing	$0.0	$0.0		$0.0	$0.0		$0.0
Soft Drink	$0.0	$0.0		$0.0	$0.0		$0.0
Total Other Taxes	($13.5)	($37.9)	$0.0	($37.9)	($23.4)	$0.0	($23.4)
Total Taxes	**$25.2**	**$21.0**	**($8.2)**	**$12.8**	**$85.3**	**($8.4)**	**$76.9**
% growth							
Non-Tax Income							
Earnings on Investments	$25.0	$20.0		$20.0	$15.0		$15.0
Licenses and Fees	($2.0)	$1.4		$1.4	$0.6		$0.6
Other Income	($3.6)	($1.1)		($1.1)	($1.1)		($1.1)
Non-Tax Receipts	$19.4	$20.3	$0.0	$20.3	$14.5	$0.0	$14.5
TRANSFERS							
Liquor Transfers	$5.0	$1.0		$1.0	$2.0		$2.0
Other Transfers In	$5.0	($15.0)		($15.0)	($10.0)	$0.0	($10.0)
Total Transfers In	$10.0	($14.0)	$0.0	($14.0)	($8.0)	$0.0	($8.0)
TOTAL INCOME less Federal Grants	**$54.6**	**$27.3**	**($8.2)**	**$19.1**	**$91.8**	**($8.4)**	**$83.4**
Federal Reimbursement	($90.0)						
TOTAL GRF INCOME	**($35.4)**						

LBO Revenue Estimates FY 1999 - FY 200 Assumed Zero Tax Cut for Tax Years 1999 and 2000

GRF Amounts by Revenue Source
dollar amounts in millions

	Actual FY 1994	Actual FY 1995	Actual FY 1996	Actual FY 1997	Actual FY 1998	Estimated FY 1999	Baseline FY 2000	Adjustments	Total FY 2000	Baseline FY 2001	Adjustments
TAX INCOME											
Auto Sales	$627.9	$657.6	$668.8	$673.7	$722.8	$735.0	$746.0		$746.0	$757.2	
Non-Auto Sales & Use	$3,623.0	$3,854.3	$4,070.7	$4,295.3	$4,542.7	$4,755.0	$4,945.2		$4,945.2	$5,143.0	
Total Sales	$4,250.9	$4,511.9	$4,739.5	$4,969.0	$5,265.5	$5,490.0	$5,691.2	$0.0	$5,691.2	$5,900.2	$0.0
Personal Income	$4,538.9	$4,880.7	$5,262.8	$5,382.3	$6,212.5	$6,324.7	$7,072.3	($70.7)	$7,001.6	$7,629.9	($79.0)
Corporate Franchise	$897.3	$1,043.8	$1,114.0	$1,150.8	$1,196.6	$1,080.0	$1,052.0		$1,052.0	$1,055.0	
Public Utility	$608.9	$673.3	$621.6	$639.8	$673.0	$635.1	$653.9		$653.9	$641.3	
Total Major Taxes	$10,295.9	$11,109.7	$11,737.9	$12,141.8	$13,347.7	$13,529.8	$14,469.4	($70.7)	$14,398.7	$15,226.4	($79.0)
Foreign Insurance	$272.2	$267.9	$276.1	$283.5	$280.9	$260.0	$246.0		$246.0	$238.0	
Domestic Insurance	$47.6	$50.9	$55.3	$56.4	$63.2	$75.0	$90.5		$90.5	$102.9	
Business & Property	$8.9	$6.7	$9.1	$8.9	$6.4	$7.0	$7.0		$7.0	$7.0	
Cigarette	$287.0	$295.7	$294.5	$298.4	$296.6	$297.0	$269.6		$269.6	$267.9	
Alcoholic Beverage	$51.6	$51.5	$50.8	$51.9	$52.4	$52.0	$51.6		$51.6	$51.2	
Liquor Gallonage	$27.7	$27.4	$27.3	$27.1	$27.3	$27.5	$27.6		$27.6	$27.7	
Estate	$86.5	$83.4	$89.9	$102.0	$114.8	$115.0	$117.8		$117.8	$120.4	
Racing	$2.5	$0.8	$0.0	$0.0	$0.0	$0.0	$0.0		$0.0	$0.0	
Soft Drink	$59.3	$34.2	$0.0	$0.0	$0.0	$0.0	$0.0		$0.0	$0.0	
Total Other Taxes	$843.4	$818.5	$802.9	$828.3	$841.8	$833.5	$810.1	$0.0	$810.1	$815.1	$0.0
Total Taxes	**$11,139.3**	**$11,928.2**	**$12,540.8**	**$12,970.1**	**$14,189.4**	**$14,363.3**	**$15,279.5**	**($70.7)**	**$15,208.8**	**$16,041.5**	**($79.0)**
% growth		**7.1%**	**5.1%**	**3.4%**	**9.4%**	**1.2%**			**5.9%**		
Non-Tax Income											
Earnings on Investments	$28.5	$33.5	$76.6	$102.5	$129.0	$145.0	$130.0		$130.0	$120.0	
Licenses and Fees	$63.3	$61.2	$65.0	$66.2	$36.3	$38.0	$40.0		$40.0	$40.0	
Other Income	$140.2	$132.7	$101.0	$99.3	$123.6	$130.0	$130.0		$130.0	$130.0	
Non-Tax Receipts	$232.0	$227.4	$242.7	$268.1	$288.9	$313.0	$300.0	$0.0	$300.0	$290.0	$0.0
TRANSFERS											
Liquor Transfers	$53.6	$58.0	$61.0	$66.5	$88.0	$90.0	$90.0		$90.0	$91.0	
Other Transfers In	$27.4	$15.1	$27.1	$417.6	$280.8	$683.7	$0.0		$0.0	$0.0	$0.0
Total Transfers In	$81.0	$73.1	$88.1	$484.1	$368.8	$773.7	$90.0	$0.0	$90.0	$91.0	$0.0
TOTAL INCOME less Federal Grants	**$11,452.4**	**$12,228.7**	**$12,871.6**	**$13,722.2**	**$14,847.1**	**$15,450.0**	**$15,669.5**	**($70.7)**	**$15,598.8**	**$16,422.5**	**($79.0)**
		6.8%	**5.3%**	**6.6%**	**8.2%**	**4.1%**	**1.4%**			**4.8%**	
Federal Reimbursement	$3,476.4	$3,482.0	$3,703.5	$3,531.6	$3,290.8	$3,385.0					
TOTAL GRF INCOME	**$14,928.8**	**$15,710.7**	**$16,575.1**	**$17,253.9**	**$18,137.9**	**$18,835.0**					

OBM Revenue Estimates FY 2000 - FY 2001

Assumed Zero Tax Cut for Tax Years 1999 and 2000

GRF Amounts by Revenue Source
dollar amounts in millions

TAX INCOME	Actual FY 1994	Actual FY 1995	Actual FY 1996	Actual FY 1997	Actual FY 1998	Estimated FY 1999	Baseline FY 2000	Adjustments	Total FY 2000	Baseline FY 2001
Auto Sales	$627.9	$657.6	$668.8	$673.7	$722.8	$735.0	$735.0		$735.0	$746.0
Non-Auto Sales & Use	$3,623.0	$3,854.3	$4,070.7	$4,295.3	$4,542.7	$4,755.0	$4,935.0		$4,935.0	$5,150.0
Total Sales	$4,250.9	$4,511.9	$4,739.5	$4,969.0	$5,265.5	$5,490.0	$5,670.0	$0.0	$5,670.0	$5,896.0
Personal Income	$4,538.9	$4,880.7	$5,262.8	$5,382.3	$6,212.5	$6,275.0	$7,033.2	($62.5)	$6,970.7	$7,487.1
Corporate Franchise	$897.3	$1,043.8	$1,114.0	$1,150.8	$1,196.6	$1,090.0	$1,077.3		$1,077.3	$1,109.6
Public Utility	$608.9	$673.3	$621.6	$639.8	$673.0	$636.1	$630.0		$630.0	$625.0
Total Major Taxes	$10,295.9	$11,109.7	$11,737.9	$12,141.8	$13,347.7	$13,491.1	$14,410.5	($62.5)	$14,348.0	$15,117.7
Foreign Insurance	$272.2	$267.9	$276.1	$283.5	$280.9	$280.0	$275.0		$275.0	$270.0
Domestic Insurance	$47.6	$50.9	$55.3	$56.4	$63.2	$75.0	$80.0		$80.0	$84.0
Business & Property	$8.9	$6.7	$9.1	$8.9	$6.4	$7.0	$8.0		$8.0	$8.0
Cigarette	$287.0	$295.7	$294.5	$298.4	$296.6	$290.0	$284.0		$284.0	$275.0
Alcoholic Beverage	$51.6	$51.5	$50.8	$51.9	$52.4	$52.5	$53.0		$53.0	$53.5
Liquor Gallonage	$27.7	$27.4	$27.3	$27.1	$27.3	$27.5	$28.0		$28.0	$28.0
Estate	$86.5	$83.4	$89.9	$102.0	$114.8	$115.0	$120.0		$120.0	$120.0
Racing	$2.5	$0.8	$0.0	$0.0	$0.0	$0.0	$0.0		$0.0	$0.0
Soft Drink	$59.3	$34.2	$0.0	$0.0	$0.0	$0.0	$0.0		$0.0	$0.0
Total Other Taxes	$843.4	$818.5	$802.9	$828.3	$841.8	$847.0	$848.0	$0.0	$848.0	$838.5
Total Taxes	**$11,139.3**	**$11,928.2**	**$12,540.8**	**$12,970.1**	**$14,189.4**	**$14,338.1**	**$15,258.5**	**($62.5)**	**$15,196.0**	**$15,956.2**
% growth		**7.1%**	**5.1%**	**3.4%**	**9.4%**	**1.0%**			**6.0%**	
Non-Tax Income										
Earnings on Investments	$28.5	$33.5	$76.6	$102.5	$129.0	$120.0	$110.0		$110.0	$105.0
Licenses and Fees	$63.3	$61.2	$65.0	$66.2	$36.3	$40.0	$38.6		$38.6	$39.4
Other Income	$140.2	$132.7	$101.0	$99.3	$123.6	$133.6	$131.1		$131.1	$131.1
Non-Tax Receipts	$232.0	$227.4	$242.7	$268.1	$288.9	$293.6	$279.7	$0.0	$279.7	$275.5
TRANSFERS										
Liquor Transfers	$53.6	$58.0	$61.0	$66.5	$88.0	$85.0	$89.0		$89.0	$89.0
Other Transfers In	$27.4	$15.1	$27.1	$417.6	$280.8	$678.7	$15.0		$15.0	$10.0
Total Transfers In	$81.0	$73.1	$88.1	$484.1	$368.8	$763.7	$104.0	$0.0	$104.0	$99.0
TOTAL INCOME less Federal Grants	**$11,452.4**	**$12,228.7**	**$12,871.6**	**$13,722.2**	**$14,847.1**	**$15,395.4**	**$15,642.2**	**($62.5)**	**$15,579.7**	**$16,330.7**
		6.8%	**5.3%**	**6.6%**	**8.2%**	**3.7%**	**1.6%**		**1.2%**	**4.4%**
Federal Reimbursement	$3,476.4	$3,482.0	$3,703.5	$3,531.6	$3,290.8	$3,475.0	$3,946.0		$3,946.0	$4,164.8
TOTAL GRF INCOME	**$14,928.8**	**$15,710.7**	**$16,575.1**	**$17,253.9**	**$18,137.9**	**$18,870.4**	**$19,588.2**	**($62.5)**	**$19,525.7**	**$20,495.6**

Ending GRF Balance Uses, FY 1995-1998

amounts in millions of $		1995	1996	1997	1998	Totals
	Ending GRF Balance	$928.0	$781.3	$834.9	$1,084.4	$3,628.6
	Inter-Fund Transfers (non-BSF)					
	State Infrastructure Bank	$0.0	($100.0)	$0.0	$0.0	($100.0)
	Human Services Stabilization Fund	($100.0)	$0.0	$0.0	$0.0	($100.0)
	OPLIN One-Time Transfer	($8.0)	$0.0	$0.0	$0.0	($8.0)
	LGF One-Time Transfer	($12.0)	$0.0	$0.0	$0.0	($12.0)
Schools $821.4 M	Supplemental School Assistance Fund	($29.3)	$0.0	$0.0	$0.0	($29.3)
Schools $821.4 M	School District 1987 MCI Reimbursement	($5.0)	$0.0	$0.0	$0.0	($5.0)
Schools $821.4 M	School District Stored Natural Gas Reimbursement	($2.6)	$0.0	$0.0	$0.0	($2.6)
Schools $821.4 M	School Building Assistance	($41.0)	$0.0	($250.0)	($170.0)	($461.0)
Schools $821.4 M	SchoolNet Plus	($125.0)	($30.0)	($94.4)	$0.0	($249.4)
Schools $821.4 M	Solvency Assistance	$0.0	$0.0	$0.0	($30.0)	($30.0)
Schools $821.4 M	Textbooks and Materials	$0.0	$0.0	($35.0)	$0.0	($35.0)
Schools $821.4 M	Distance Learning	$0.0	$0.0	($9.2)	$0.0	($9.2)
	Subtotal Transfers	($322.8)	($130.0)	($388.6)	($200.0)	($1,041.4)
	Supplemental Appropriations	$0.0	($46.2)	$0.0	$0.0	($46.2)
	Other					
	BSF Transfer	($535.2)	$0.0	($34.4)	($44.2)	($613.8)
	Additional BSF Amount Needed for 5% Balance	$0.0	($0.4)	$0.0	$0.0	($0.4)
	Anticipated Operating Deficit	$0.0	($121.0)	$0.0	$0.0	($121.0)
	Capital Reserve	$0.0	$0.0	($7.2)	($10.3)	($17.5)
	Reserve Against Prior Year Income Tax Rate Cut	NA	NA	($55.5)	($37.8)	($93.3)
	Necessary 0.5% GRF Carryover	($70.0)	($82.9)	($86.3)	($90.7)	($329.9)
	Subtotal Other Obligations	($605.2)	($204.3)	($183.4)	($183.0)	($1,175.9)
	Total All Transfers and Other Obligations	($928.0)	($380.5)	($572.0)	($383.0)	($2,263.5)
	Amount Left for Tax Cut	$0.0	$400.8	$262.9	$701.4	$1,365.1
	Tax Cut %		6.61%	3.99%	9.34%	

GRF Operating Surplus, FY 1989 - 1999, different definitions
amounts in millions of $

GRF Revenue	FY 1989	FY 1990	FY 1991	FY 1992	FY 1993	FY 1994	FY 1995	FY 1996	FY 1997	FY 1998
GRF Tax Revenue	$8,698.5	$9,048.1	$9,053.0	$9,421.9	$10,124.2	$11,139.3	$11,928.2	$12,540.9	$12,970.1	$14,189.4
GRF Non-Tax Revenue	$239.3	$249.0	$230.7	$265.8	$168.9	$232.0	$227.4	$242.7	$268.1	$288.9
Liquor Transfers	$50.0	$46.0	$55.5	$57.0	$56.5	$53.6	$58.0	$61.0	$66.5	$88.0
ITRF Transfer	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$358.7	$235.3
State Revenue	$8,987.8	$9,343.2	$9,339.2	$9,744.7	$10,349.6	$11,424.9	$12,213.6	$12,844.5	$13,663.3	$14,801.6
		4.0%	0.0%	4.3%	6.2%	10.4%	6.9%	5.2%	6.4%	8.3%
Federal Reimbursement	$1,969.9	$2,204.2	$2,662.3	$3,097.7	$3,285.2	$3,476.4	$3,482.0	$3,703.5	$3,531.6	$3,290.8
Sub-Total GRF Income	$10,957.7	$11,547.4	$12,001.5	$12,842.4	$13,634.8	$14,901.3	$15,695.6	$16,548.0	$17,194.9	$18,092.3
All Other Transfers	$24.2	$39.0	$184.3	$362.9	$38.4	$27.4	$15.1	$27.1	$58.9	$45.5
Total GRF Income	$10,981.9	$11,586.4	$12,185.7	$13,205.3	$13,673.2	$14,928.8	$15,710.6	$16,575.1	$17,253.8	$18,137.8

GRF Spending	FY 1989	FY 1990	FY 1991	FY 1992	FY 1993	FY 1994	FY 1995	FY 1996	FY 1997	FY 1998
Disbursements	$10,656.4	$11,585.7	$12,501.1	$13,169.5	$13,600.2	$14,433.2	$14,978.6	$15,858.1	$16,404.0	$17,087.0
Transfers to ITRF	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$400.8	$262.9
All Other Transfers	$58.0	$108.1	$35.0	$22.5	$19.3	$47.3	$261.7	$890.7	$219.8	$506.7
All GRF Outlays	$10,714.4	$11,693.8	$12,536.0	$13,192.0	$13,619.5	$14,480.5	$15,240.3	$16,748.8	$17,024.6	$17,856.6
Operating Surplus, All Sources and Uses	$267.5	($107.4)	($350.3)	$13.2	$53.7	$448.3	$470.3	($173.7)	$229.2	$281.2
Operating Surplus, No Transfers Except Liquor	$301.3	($38.3)	($499.6)	($327.1)	$34.6	$468.1	$717.0	$689.9	$432.1	$770.0
Operating Surplus, with Liquor & ITRF Transfers	$301.3	($38.3)	($499.6)	($327.1)	$34.6	$468.1	$717.0	$689.9	$390.1	$742.4

Medicaid and Caseload Expenditure Forecasts

**Testimony of Barbara Riley
Division Chief**

Mr. Chairman, members of the House Finance and Appropriations Committee, the following are the Legislative Budget Office's forecasts for Medicaid, TANF, and Disability Assistance caseloads and expenditures. As you know, welfare reform at the state and national levels has basically changed the rules of the game, unfortunately, this makes human services forecasting considerably more complex. At one time to forecast Medicaid it was simply, "how many" and "how much", now it means that we have to be more cognizant of who we serve, what services they use, and the cost of those services. In the TANF, or Ohio Works First (OWF) program, caseload count no longer dictates expenditures, now we are working with a block grant from the federal government which allows for much greater flexibility. What do these changes mean for the upcoming biennium? Increased growth in Medicaid, (5.36 percent in FY 2000, and 3.85 percent in FY 2001), and less spent on cash assistance for OWF recipients.

Medicaid

The following is a LBO baseline forecast, which assumes no change in the Medicaid policies and program for the upcoming biennium. Of course, you have just heard that the administration does propose several Medicaid initiatives, including an expansion of the CHIP program to 200 percent of poverty and an increase in certain noninstitutional provider fees. Our forecast does not take those initiatives into account. We received the breakdown of the administration's final estimates yesterday, and will be happy to make an apples to apples comparison when the subcommittee hears the Department's budget, or at your convenience after we have had an opportunity to recalculate our estimates. In addition, our percentage and dollar changes are based on LBO's anticipated FY 1999 year end numbers. In this case, it appears that we are very close to the OBM year-end estimate; LBO estimates a year end expenditure of $12.66 million (.2 percent) less than the Executive. This difference is only $5.52 million in state share GRF.

Another complication is that we continue to forecast Medicaid as though it were a pure program entirely contained in the Department of Human Services 400-525 line item, but there are many other Medicaid funded programs within the state budget. The majority are waiver programs such as PASSPORT, and others designed to provide care in a home or community based setting. To the extent that these programs allow people to avoid institutionalization, they also divert expenditures from the 400-525 line to other places within the state budget. These waivers are growing pieces of Ohio's medical assistance for low income individuals, and should be seen as a part of our medical care policies and expenditures. However, for today's purposes, we will focus on who receives medical assistance under the traditional Medicaid program, what services they receive, and at what cost.

Who Do We Serve?

Nearly buried within the table (refer to page 26 of this testimony) is the fact that by the end of this biennium we believe that the Low Income/Transitional category of recipients will exceed the number of persons receiving Medicaid along with OWF cash benefits. In fact, if you take into account the children who receive Healthy Start and CHIP benefits, we already provide medical assistance alone to more adults and children than receive both cash and medical assistance. This is a new paradigm, and one that may lead us to consider Medicaid more as a health insurance benefit than a welfare program.

What Services Do Recipients Receive?

The primary driver of the Medicaid budget is the nursing home category, including both nursing facilities and intermediate care facilities for the mentally retarded (ICF-MRs). The population using these services is the Aged, Blind and Disabled (ABD) group, comprising 31 percent of the Medicaid eligible population, and expending 76 percent of the dollars. Expenditures in this category are expected to increase by 7.12 percent in FY 2000 to $2,497.6 million, and 6.06 percent in FY 2001 to $2,649.0 million. These increases are fueled by the heightened acuity levels, as waiver and other service programs have diverted the less frail from institutions, leaving the most ill and costly recipients in residence. Also contributing to increased costs are escalating prescription drug costs and capital costs. The average nursing home per diem has gone from $101.30 in FY 1997 to $108.64 in FY 1998. We anticipate that rate will grow by 4.1 percent in FY 1999 and by 4.5 percent in each of the next two years.

Although general inflation has been curtailed, and the overall Consumer Price Index (CPI) for medical care declined from 1991 until 1997, we began to see the medical CPI rise again in 1998. From December of 1997 to November of 1998 medical inflation accelerated from 2.8 percent to 3.5 percent; in the same time period, the general CPI had a net deceleration from 1.7 percent to 1.5 percent. Inside the medical rate is the prescription drug and medical equipment category, and the prescription drug producer price index is going through the roof with an average annual price growth in FY 1998 of 15 percent. The rate of increase for equipment is much lower, but combined, the growth rate in spending is projected to be 14.62 percent from FY 1999 to FY 2000, and 8.44 percent from FY 2000 to FY 2001.

The movement to managed care also has to be taken into account. Assumptions were that this would be a factor in controlling Medicaid expenditures, and indeed it has been. However, enrollment rates have not kept pace with our assumptions as the targeted population (OWF and OWF Related) has been steadily declining, hampering the department's ability to reach expectations. As a result, rather than having the anticipated 78 percent enrolled in HMOs by the end of this biennium, there will be only about 42 percent, although the enrollment rate was higher earlier in the biennium. Human Services is assuming that this will build back to 58 percent by the conclusion of the next biennium, and we believe that is a reasonable goal. Therefore, we are projecting HMO expenditure growth in FY 2000 of 14.62 percent and another 10.84 percent in FY 2001. This increase in HMO use will contribute to a decline in physician and hospital usage, allowing expenditures to decline somewhat in those categories. As we look at managed care, we also must recognize that there may be limits to the possible managed care cost savings, limits that we may be approaching in the broader medical market as providers exit the market, consolidate, and generally limit competition.

The final service category is the Medicare Buy-In, where we provide various levels of financial assistance in order to assure low income Medicare eligibles full access to the Medicare system. This cost category is expected to increase by 3.83 percent in FY 2000, and by only .60 percent in 2001. But, there is likely to be a much larger growth in eligible individuals, (perhaps adding up to 36,000 individuals by the end of the FY 2000/2001 biennium), with the new federal Additional Low-Income Medicare Beneficiaries (ALMB) category. This huge growth in beneficiaries is offset by the fact that the category is fully funded by the federal government.

How Much Will It All Cost?

We foresee an increase in expenditures in FY 2000 of 5.36 percent, or $277.73 million in combined state and federal GRF dollars. This is an increase of $86.28 million in state share, with an overall expenditure, state and federal, of $5.46 billion. For FY 2001, we expect total Medicaid expenditures to go up by 3.85 percent over FY 2000 to $5.67 billion which equates to an increase of $210.33 million, with a state share increase of $66.35 million.

TANF

With the funding for TANF having been transformed into a block grant you might wonder why we continue to forecast caseloads and cash assistance expenditures. There are a number of reasons, including the fact that these are used in forecasting Medicaid, and that expenditures for cash assistance dictate the amount of federal block grant and state Maintenance of Effort (MOE) moneys that are available for TANF services such as education and training, Prevention, Retention, and Contingency (PRC), transportation, child care, etc.

Clearly the purpose of cash assistance has changed from an entitlement program to one with a temporary focus designed to assist people as they move to the work force. In addition, the ancillary services provided with TANF dollars are meant to develop a strong workforce and put in place supports that will allow individuals to fully participate in employment and to enhance their income potential. Under that philosophy we have imposed time limits, the effect of which will be felt in October of 2000, and strict work requirements which are now in place and enforced with a system of sanctions.

In order to carry out the workforce development focus, we have available to us approximately $728 million per year in federal TANF block grant funds, and we are obligated to provide state funding to meet our mandated MOE level of $417 million. The federal government set the MOE rate at 80 percent of what we spent in FFY 1994 on ADC, JOBS, and Family Emergency Assistance. Current appropriations and the proposed budget have allocated only $401 million, or 77 percent of that level. However, the mandatory MOE rate can by reduced to 75 percent if a state meets work participation requirements, and Ohio's current performance should allow for us to draw our full federal block grant, without penalty. Ohio also has determined that $75 million of the federal block grant funds in each year will not be appropriated, but will be left at the federal level as a reserve for use in an economic downturn.

That said, where are caseloads now, and where are they going? The cash assistance caseload has been in a steady decline since the spring of 1992, dropping from over 250,000 cases to an anticipated average monthly caseload in FY 1999 of 117,886 assistance groups. We are projecting a decline in FY 2000 of 13.1 percent to a monthly average of 102,392, and in FY 2001 a further reduction of 14 percent, down to 88,061. This equates to cash grant funding of $383.6 million in FY 2000 (down $54.8 million from FY 1999), and $329.9 million in FY 2001, (down $53.7 million from FY 2000).

Therefore, for FY 2000 we will have available $728 million in federal funds, plus $401 million in state dollars (for a total of $1,129 million), less the $75 million left on reserve, less the $383.6 million for cash assistance which leaves $634.1 million for administration, work, education and training activities, PRC, transitional services, and various specified reserve funds. For FY 2001, a similar calculation yields $678.8 million for services other than cash grants.

To date we have been unable to expend all the available TANF federal block grant dollars. This is largely due to declining caseloads, but we also have put in place a system that allows the counties considerable flexibility in spending their TANF allocations, and they have not yet developed alternatives for TANF support services that fully tap the unspent federal dollars. At the end of FFY 1998, Ohio's TANF reserve was $544.9 million and is expected to increase to about $693.5 million by the end of June 1999. As you may know, there is great interest at the federal level in seeing some of these unspent dollars returned to the federal coffers, and several weeks ago a U.S. Senate committee voted to do just that.

There are a number of interesting outcomes of the declining caseloads, including an increasing share of "child only" cases, now making up nearly 30 percent of the total caseload. Also of interest is the fact that the decline in caseloads accelerated following the implementation of Ohio Works First, but that decline was not due to persons leaving the caseload, but rather to fewer people applying for OWF benefits. The exit rate actually slowed in the year after implementation of OWF. Other observations would include the fact that there are only about 80,000 adults currently receiving OWF cash benefits, and around 35 percent, or 28,000, of those are employed, albeit in low wage or part time positions. Clearly, welfare is not the same as it once was.

Disability Assistance

Disability Assistance (DA) is a wholly state and county funded program which provides cash and medical assistance to persons not eligible for TANF or SSI. Ohio has divided that program into two components – DA Cash, and DA Medical. There are no time limits, and all those receiving cash benefits also receive medical benefits—currently about 10,000 recipients. An additional 3,000 individuals currently receive medical benefits only. DA spending has been declining over the last several years due to declining caseloads. LBO expects that decline in cash recipients to slow in FY 2000, but still to come down 6.9 percent from FY 1999 levels. DA medical recipients will also decrease at about same rate. However, due to the escalating costs of prescription drugs, (which historically composes about 62 percent of DA medical costs), total DA expenditures are forecast to decrease only slightly. Total DA costs for FY 2000 will decrease by $1.8 million from $54.1 million to $52.3 million.

The rate of decline in DA cash and medical expenditures is expected to slow even further in FY 2001. This is due to nearly steady caseloads and a somewhat higher inflation rate for prescription drugs. Costs should go from $52.3 million in FY 2000 to $52 million in FY 2001.

Clearly, the picture we have painted is somewhat reassuring in terms of increasing costs for the upcoming biennium, but I would caution you that so many things have changed, and are changing, that it is increasingly difficult to forecast with a high level of confidence. We do not know how high medical inflation will go, we are uncertain whether managed care can exert continued downward cost pressure, and we can not foretell how time limits will ultimately play out in welfare reform. Having said that, I believe that these estimates are based on sound economic principles and forecasting models, and that the dangers are in the subsequent biennia. I will be happy to answer any questions, and Ogbe Aideyman and Steve Mansfield, who actually did the hard work and number crunching, are here as well. ❑

Summary of Medicaid Eligibility in Ohio

Eligibility Category	Basic Eligibility Requirements	Caseloads and Share of Total Caseloads (Average Monthly Eligibles) FY 1998	FY 1999	FY 2000	FY 2001
OWF Cash Recipients	Eligible for OWF cash assistance. -Countable income at or below 34% of FPL.	397,555 35.90%	305,154 28.84%	266,219 26.07%	214,567 21.79%
Low-Income Families	Meet the TANF regulations in effect in July 1996, or eligible for OWF assistance but do not receive cash assistance due to any of the following: sanctions, and time limits.	183,272 16.55%	200,007 18.90%	191,113 18.71%	193,061 19.61%
Transitional Medicaid	Additional 12 months of health care coverage is given to individuals who no longer meet "ADC" eligibility guidelines due to increased income, but previously received OWF cash assistance.				
Extended Medicaid	Families whose incomes exceed ADC guidelines due to the collection, or increased collection, of child or spousal support payments receive Medicaid coverage for four months. In addition, individuals eligible for Title IV-E foster care and other miscellaneous groups receive coverage under this category.				
Healthy Start (HS)	Healthy Start Program is a two-part Medicaid program that (i) covers children birth through 6 years whose family income is at or below 133 percent of FPL and children 7 through 15 (as at October 1, 1998) whose family income is at or below 100 percent of FPL. Part (ii) covers low-income pregnant women who do not otherwise qualify for Medicaid, with family incomes up to 133 percent of FPL.	137,951 12.46%	149,244 14.10%	146,797 14.37%	148,998 15.13%
Aged, Blind and Disabled (ABD)	The ABD eligibility group is loosely based on the Supplemental Security Income (SSI) program. However, once individuals who do not meet the initial ABD income test spend an amount on medical care such that their income after medical expenses is at or below the more restrictive ABD income level of about 63 percent of the FPL, they "spend-down" to Medicaid eligibility.	339,567 30.67%	341,245 32.25%	343,465 33.63%	343,889 34.92%
Qualified Medicare Beneficiaries (QMBs)	Eligibility for Medicare Part A coverage. Income is at or below 100% of FPL	23,683 2.14%	24,048 2.27%	24,576 2.41%	24,975 2.54%
Specified Low-Income Medicare Beneficiaries SLMB	Eligibility for Medicare Part A coverage. Income is between 100 - 120% of FPL	23,233 2.10%	23,233 2.20%	23,233 2.27%	23,233 2.36%
Additional Low-Income Medicare Beneficiaries (ALMB) or Qualifying Individuals QI-1 & QI-2	Eligibility for Medicare Part A coverage & not otherwise eligible for Medicaid. For QI-1 - income is between 120 - 135% of FPL; QI-2 income is between 135 - 175% of FPL	2,693 New Program - Not reasonable for comparison	15,165	25,913	36,029
Children's Health Insurance Program	Kids up to age 19 in families with incomes at or below 150% of FPL	13,506 New Program - Not reasonable for comparison	81,888	130,638	134,439
	Total Caseload without (CHIP & ALMB)	1,107,323	1,058,096	1,021,316	984,752