

Bulletin

May 29, 2002

The Commonwealth's Fiscal Crisis: Opportunity for Important Spending Reforms

While the current fiscal crisis will require tough choices among the state's priorities and some painful reductions, it also provides a singular opportunity to curb longstanding spending abuses and eliminate inefficiencies -- both large and small -- that have been tolerated in the recent, more prosperous times. In the present financially urgent situation, the state's leaders can and should tackle reforms that would normally be avoided because of their political difficulties. And when programs are being cut, state officials bear a special responsibility to target programs that use tax dollars poorly. To do otherwise undercuts confidence in government at a time when our citizens are being asked to shoulder an additional tax burden of more than \$1 billion.

The purpose of this report is to highlight several opportunities for reform, including eliminating wasteful or inequitable spending, improving program management, and relieving unnecessary cost burdens on cities and towns as well as state government. Although not nearly enough to solve a gap between annual revenues and expenditures that now exceeds \$2 billion, the opportunities for savings from such reforms are significant

and would help to ease the state's fiscal problems while making better use of taxpayers' dollars.

With its recently adopted 2003 budget¹ the House has taken an enormous step forward in dealing with the state's multiyear fiscal problems. The House leadership and individual members deserve particular credit for their balanced approach, which includes difficult but necessary spending cuts, a responsible revenue package, and the careful use of reserves. At the same time, however, it must be acknowledged that much more remains to be done to rein in abuse and improve the management of state programs. The final House budget restored some problematic spending that had been trimmed by the Ways and Means Committee and shielded away from other structural reforms. The Foundation certainly hopes that the Senate will take greater advantage of the opportunity for spending reform in its version of the 2003 budget, especially given the recent news of a further \$200-400 million drop in 2002 revenues that is not addressed in the House's budget.

¹ An MTF analysis of the House budget will be released shortly.

Curb spending abuses and inequities

Quinn Bill Eliminate or reform salary supplements paid to local police under Massachusetts' unique "Quinn bill," which reimburses cities and towns for 50 percent of the cost of pay raises, ranging from 10 to 25 percent, for officers earning college and graduate degrees.

Over the years, numerous media reports have exposed the many abuses under this program, including the wholesale awarding of questionable degrees by substandard educational institutions for the sole purpose of qualifying for additional pay. In part because of the recent decision of the City of Boston to begin participating in the program, state costs have risen dramatically in the last few years, from just under \$18 million in 1998 to an expected \$41.5 million in 2003, with an equal amount spent by cities and towns.

Clearly, the educational standards for earning pay raises under the program should be tightened to eliminate obvious abuses. While the House deserves credit for including this reform in its 2003 budget, lawmakers did not take the further step of dealing with the program's overly generous benefit structure and instead restored full funding of the program. Converting the benefit to a fixed annual dollar amount -- or reducing the benefit percentage -- would preserve the program's intended incentive effect while constraining the growth in costs for both the state and local governments. Such a change could save the state \$3-5 million in fiscal 2003, with substantial further savings in future years.

Police Details Abolish the requirement that traffic, utility and other construction details be staffed by police rather than civilian flaggers, which are commonly used in other states. This provision costs state and local governments and private companies over \$100 million a year.

Reducing the required use of state police at public construction projects would produce significant annual savings -- \$12 to \$16 million -- in the state's capital budget and approximately \$1 million in the operating budget.

Extraordinary Early Retirement Repeal the provision of state pension law that provides a generous early pension to state employees, regardless of age, who "involuntarily" leave their jobs after 20 years. These employees would otherwise be eligible for regular retirement benefits when they reach age 55.

As recently reported in *Commonwealth* magazine, this provision has been widely abused, resulting in the award of sizeable pensions to employees younger than 55 who in fact voluntarily left their position, often for a lucrative job in the private sector. The annual savings from repealing this provision are likely to be significant.

Education Local Aid Reform the Chapter 70 education aid formula to eliminate the inequitable distribution of school aid, while ensuring that the neediest districts have the resources to maintain school spending at adequate levels. Under the 1993 reform law, the state has more than tripled annual assistance to local schools to a total of over \$3 billion in fiscal 2002, with the lion's share of the new state funds going to districts with insufficient local resources to meet the law's standard for adequate school spending.

While the school aid formula has worked well in targeting aid dollars to needy districts, the mechanism for providing state assistance to better-off districts has worked poorly. Not only has this approach preserved disparities that predate the 1993 reform law, it has actually made those disparities worse. The state has disproportionately subsidized communities whose support for schools falls short of the law's standard of local effort and has largely

failed to adjust aid levels to reflect enrollment changes, including rapid enrollment growth and declining numbers of students.

Both the administration and the Taxpayers Foundation have recommended needs-based reforms to the distribution formula that would tie the annual aid allocation -- and the required local contribution to schools -- to current measures of community wealth and income. Implementing such reforms could save the state \$100-200 million in 2003, with a significant portion of those costs shifted to communities that would be required to contribute more to their schools under the reforms' standard for local tax effort.

While the reversal of the 10 percent cut in Chapter 70 funding proposed by Ways and Means is good news for local schools, the House's freezing of each district's 2003 aid allotment and required local contribution at the 2002 level is highly problematic. If this proposal is enacted, over 100 districts would be unable to meet the standard for adequate school spending required by the education reform law, undercutting the funding progress of the last nine years and making the state vulnerable to litigation. We urge the Senate to rectify this lapse. Ensuring adequate funding for the affected districts would cost an additional \$90 million using the current aid formula, an amount that could be offset by savings if the formula was reformed along the lines suggested here.

Restructure programs to improve management and establish stronger incentives for cost containment

Court personnel and administration

Eliminate unnecessary patronage positions authorized by the Legislature and centralize management of court personnel.

While the courts have struggled to deal with \$40 million of budget cuts in 2002, they

have been burdened with an influx of legislatively-mandated new hires to fill positions not even requested by court administrators. A recent report by Pioneer Institute documented that over 400 such positions were added by lawmakers between 1998 and 2001. Eliminating these unneeded positions would save approximately \$20 million in fiscal 2003.

At the same time, greater centralization of court administration would enable the judiciary to reallocate personnel and resources to the courts with the heaviest caseloads and reduce unnecessary staffing in less busy courts. Regrettably, the Legislature's recent actions have largely gone in the opposite direction. Last fall, for example, lawmakers stripped judges of the power to hire probation officers and assistant clerks in their own courts. More recently, a member of the House leadership proposed a budget amendment, ultimately withdrawn, which would have eliminated judges' authority to hire any court personnel.

Medicaid Convert the senior pharmacy program started up last year from a broad-based, state-funded program for all seniors to a more focused program for low- and moderate-income seniors and qualified disabled individuals. With this change, which was proposed by the Governor and adopted in the House budget, the program would become eligible for 50 percent federal reimbursement.

While any serious effort to address the state's structural budget gap must take Medicaid into account, how to tackle this vast and increasingly expensive program -- except at the margins -- is very much an open question.

On the one hand, the current double-digit rate of growth in annual Medicaid spending, driven in large part by the national trend in health care costs, places enormous pressure on the rest of the budget, and the significant

expansions in eligibility and benefits in the last five years have added further to that pressure. At the same time, however, the state has failed to reimburse health care providers for the full costs of the services they provide, exacerbating the already fragile financial condition of the state's health care system.

Against this backdrop, there are few realistic opportunities for substantial savings in the short term, except through benefit or eligibility reductions. The House's action to rescind the recent expansion of eligibility to the long-term unemployed is an example of such a reduction. However, given the sheer size and complexity of the program, and its deep interconnections with the entire health care system, identifying and realizing major systemic savings is likely to require years of effort.

While the modification of the senior pharmacy program suggested here is much less sweeping, it would save approximately 50 million of state tax dollars annually and eliminate an open-ended entitlement which has the potential for enormous cost growth in future years.

Sentencing guidelines reform Restrain the growth in corrections spending by adopting the Massachusetts Sentencing Commission's proposed guidelines.

With over \$1.5 billion devoted to the criminal justice system and the state's prisons filled beyond capacity, the Legislature should seize the opportunity to adopt the Commission's sentencing guidelines, which set priorities for the type of crimes that warrant imprisonment and provide less-costly alternatives to incarceration for first time and non-violent offenders.

Unfortunately, the sentencing guidelines approved by the House earlier this year would be a step in the opposite direction, actually causing a significant increase in

corrections spending by requiring longer prison sentences and limiting the use of alternatives to incarceration. The Foundation urges the Senate to adopt the Sentencing Commission's guidelines, which would enable the Commonwealth to gain greater control over the allocation of resources for corrections.

Workers' compensation for local public safety personnel Tighten the state's "injured on duty" statute for local police and firefighters, which compensates individuals who are temporarily unable to perform their duties because of on-the-job injuries.

This expensive and too-often-abused system would benefit greatly from the kind of management reforms applied so successfully to the workers' compensation system in the early 1990s. These reforms include the greater use of independent medical evaluations, speedier decisions on claims, and more emphasis on injury prevention.

A more comprehensive reform would also limit the amount of compensation available under the statute to 60 percent of pay, the percentage available to all other employees under the state's workers' compensation law. Injured police and firefighters currently are eligible to receive 100 percent of pay, tax free, while on leave as a result of injuries on duty, a compensation structure which creates a powerful incentive for some individuals to remain out of work longer

than is justified. Over time, the local savings from such reforms would be substantial.

State Facilities Continue the process of evaluating the need for state-operated facilities and, where cost-effective and appropriate alternatives are available or can be developed, take steps to consolidate or close outdated, duplicative and overly expensive facilities.

At a time when the demand for human services, particularly for mental health and

mental retardation, exceeds the capacity of the programs funded by the Commonwealth, the state cannot afford to maintain overly expensive, aging facilities when less costly alternatives exist. This is especially true in the current fiscal environment.

The House is to be commended for appropriating \$3.6 million in its 2003 budget for the one-time costs associated with closing Medfield State Hospital and transferring the roughly 100 patients remaining in that facility to community residential placements. When completed, that change will free up approximately \$5 million for other pressing client care needs. Careful review of other facilities, including those operated by the departments of mental retardation and public health, is needed to determine where additional savings can be achieved.

Capital Assets Streamline disposal of state property by giving the state's property management agency greater authority to sell or lease surplus property without time-consuming legislative approval.

Savings would result from reduced maintenance and security costs and increased revenue would be received from property sales and leases. The state could realize several million dollars annually from these reforms. In order to fully achieve them, local barriers to the property disposal process would also need to be addressed.

Construction Reform Implement the recommendations of Construction Reform Task Force proposed in 1998 and filed as legislation by the administration the following year.

- Allow quality and schedule to be factored into contract procurement as alternatives to the Commonwealth's one-size-fits-all low-bid construction procurement process, which often results in cost overruns, overly lengthy

construction times and projects of inferior quality.

- Authorize state agencies and authorities to consider alternatives to the traditional design-bid-build contracting process, such as design-build, build-operate-transfer, turnkey, and construction manager-at-risk. These approaches can save time and costs by integrating the design and construction processes and reducing administrative requirements, as well as improve quality by shifting the risk of higher maintenance costs to the builder.
- Increase the dollar threshold for filed sub-bids, the requirement for separate bids on subcontracts for specific types of work. Filed sub-bids, unique to Massachusetts, add millions of dollars to the cost of state construction.

State savings from these reforms would accrue primarily in the capital budget, and would be substantial in the long term. Since municipal construction is governed by the same restrictive requirements, local governments would also be able to realize significant savings as a result of the reforms.

Contracting for services Repeal the Pacheco anti-privatization law which raises almost insurmountable obstacles to achieving public savings through competitive contracting for the delivery of services. Since its passage in 1993, the law has stymied efforts by state agencies and authorities to save tens -- and perhaps hundreds -- of millions of taxpayer dollars by privatizing services now delivered by public employees.

Program cuts and other measures

Employee health costs Increase state employees' share of health premium costs from 15 percent to 25 percent, a percentage more in line with the norm in private

industry. Like employers across the country, the Commonwealth is facing extraordinary increases in annual health care costs, with the added burden of a multi-billion dollar structural deficit between revenues and spending. In these circumstances, a modest increase in the portion paid by workers is an equitable means of sharing the burgeoning cost of health insurance. This change would save the state approximately \$50 million in fiscal 2003.

The House Ways and Means budget for 2003 included a constructive proposal to increase the share for current state employees from 15 percent to 20 percent and for newly hired employees to 30 percent, an initiative which was dropped in the final House budget. The Ways and Means recommendation is a reasonable alternative to an increase to 25 percent for all employees, and we urge the Senate to adopt this recommendation in its version of the 2003 budget.

Emergency Salary Savings Consider a variety of measures to achieve temporary savings in state personnel accounts, including a freeze on salaries and recurring temporary furloughs.

In the event of further declines in revenues that threaten the state's ability to sustain the most critical services, lawmakers should consider instituting a one- or two-year freeze on employee salary levels, despite previously negotiated collective bargaining agreements providing for annual raises and additional benefits.

While public employee unions are likely to oppose any savings measures specifically targeted to state workers, a salary freeze might be viewed as preferable to further layoffs. Such a freeze might save several hundred million dollars over a period of years.

Alternatively, a system of "rolling furloughs" -- in effect, staggered one-day layoffs for all state employees -- could be put in place, with substantially reduced savings: A one day per month furlough program would save roughly \$10 million per year.

School construction Use unallocated dollars under the state's \$1.2 billion bond cap to help fund local school building projects.

These funds would be used in lieu of the state share of local borrowing for school construction and reduce by approximately \$6 million the amount that would need to be appropriated annually for "initial payments" on approved projects starting in fiscal 2003.

Since the \$70 million that is available would otherwise be used for other capital needs, this proposal gives priority under the bond cap to school building costs which would ordinarily be funded in the operating budget.