



Bulletin

March 13, 2015

Governor's FY 2016 Budget Proposal Includes Savings, Risks

Governor Baker's first budget was released last week amid a range of unique circumstances, including addressing a \$1 billion mid-year FY 2015 budget deficit. Even with that deficit closed, the FY 2016 budget has been hampered by a large structural gap that is the result of \$1.2 billion in one-time funds used in FY 2015 and \$1.5 billion in spending growth for non-discretionary accounts. That \$2.7 billion total shortfall is offset by tax revenue growth of \$872 million, leaving a \$1.8 billion deficit.^{1,2}

The resulting FY 2016 budget totals \$38.1 billion, a \$1.1 billion or three percent increase from projected 2015 spending, and closes the budget gap through actions on both sides of the ledger.³ The proposal level funds most discretionary accounts and reduces projected spending by \$1.2 billion. On the revenue side, while there are no tax or fee increases, the budget does rely on more than \$600 million from one-time sources. In both cases, there will be consequences for FY 2017.

There are remarkably few policy recommendations in this budget—it includes less than 50 outside sections—but it relies on two tax changes, offered through separate legislation. The administration proposes phasing in a more generous earned income tax credit (EITC) over three years and funding this by repealing the film tax credit. Such a move would provide additional tax benefits to low- and moderate-income residents while eliminating a program that, according to the Department of Revenue's analyses, largely benefits non-Massachusetts residents. Similarly, the Governor introduced separate legislation to implement an Early Retirement Incentive Program (ERIP) as a method for reducing state headcount, which the administration estimates would produce \$178 million in annual savings.

In short, this is a transition budget that combines structural cost reductions through management and administrative changes with short-term fixes that push many of the toughest decisions into FY 2017.

Expenses

As in previous years, the 2016 budget has the same challenge of controlling Medicaid cost growth, which was projected to rise by \$1.9 billion or 16 percent. The Governor's budget reduces spending growth to 5.6 percent, saving the state \$645 million through re-determining eligibility of Medicaid enrollees, holding certain provider rates steady, and negotiating reduced charges for certain drugs. In addition, the budget postpones \$116 million in FY 2016 MassHealth spending until FY 2017 through "cash management." While this is not a spending cut per se, it is a long-used practice and will provide short-term relief, however the costs will come due in the FY 2017 budget. Even with these steps, the \$820 million increase in MassHealth spending consumes approximately 75 percent of the total \$1.1 billion growth in the FY 16 budget.

The budget addresses health care cost growth in other programs as well. It proposes to lower costs for subsidized health coverage by \$93 million by reducing the caseload at the Connector. The Governor's budget also would

¹ The FY 16 consensus revenue benchmark of \$25.48 billion is \$1.172 billion more than FY 15, \$300 million of which derives from capital gains tax revenues that under current law must be deposited into the Stabilization Fund leaving \$872 million in net new tax revenues for the 2016 budget.

² The Foundation estimated a \$1.5 billion budget gap for FY 2016. In its estimate, the MTF did not include \$100 million for additional GIC spending and \$170 million in one-time revenues from cash management.

³ The \$38.1 billion figure does not include \$3.8 billion in pre-budget transfers for pensions, the Workforce Training Fund, and dedicated sales tax revenues to the MBTA and the MA School Building Authority.

change health insurance plan design and align the premium contributions of employees hired before 2003 with those hired since then by raising their premium share from 20 percent to 25 percent. These changes would reduce projected Group Insurance Commission (GIC) spending by \$125 million.

However, there are risks to some of the Governor’s budget proposals. For example, savings from the ERIP would be largely eroded if the Legislature expands the plan beyond the executive branch to include the judicial branch and educational entities which are likely to replace those accepting the ERIP with new hires.

Table 1 –FY 2016 Proposed Reductions (in \$ millions)

Spending Reductions	FY 15 Projected	FY 16 Projected	H1 Proposed Spending	H1 Proposed Reductions	Change FY 15 vs. FY 16
MassHealth (gross)	13,838	16,027	14,737	1,290	9.3%
Net Savings				645	
Group Insurance Commission	1,683	1,823	1,698	125	7.4%
OPEB Level Fund	85	115	85	30	35.5%
Debt Service	2,219	2,262	2,252	10	0.5%
Revised Connector Caseload				93	
Early Retirement				178	
Other				125	
Total Spending Savings				1,206	

Revenues

While the Baker budget proposes no new taxes, it does include \$600 million of one-time sources of funding (Table 2). Although half of what was used to balance the FY 2015 budget, this is still a heavy reliance on non-recurring revenues that adds to the structural problems in FY 2017.

For the second year, the state will suspend its required transfer of capital gains tax revenues in excess of the statutory cap to the stabilization fund, and instead use the \$300 million for the operating budget. In addition, the budget proposal uses \$100 million in one-time corporate tax settlements in excess of \$10 million. While that figure is less than the \$260 million annual average over the past five years, the state previously committed the full amount of such settlements to the Stabilization Fund.

These moves are problematic because the state should seek to rebuild the Stabilization Fund balance – which has dropped by \$500 million to \$1.1 billion since FY 2012 during an economic recovery – and because erosion could impact the state’s credit rating.

Table 2 – One-Time Revenues in FY 2016 Budget (in \$ millions)

One-Time Revenues	
Capital Gains Tax Revenues in Excess of \$1.087 Billion Cap	300
Tax Amnesty	100
Courthouse Sale	30
MassHealth Cash Management	116
FAS 109	46
FEMA - Reimbursement	17
FMAP Maximization	10
Total One-Time Revenues	619

The Governor’s budget proposal now moves to the House, which will release its own version of the budget in April.

Massachusetts Taxpayers Foundation - Fiscal 2016 Budget Summary

	FY 11 Final	FY 12 Final	FY 13 Final	FY 14 Final	FY 15 GAA	FY 15 Projected	FY 16 H1
Health Care	12,182	12,102	12,599	13,615	14,735	15,042	15,884
MassHealth	10,239	10,435	10,874	12,121	13,602	13,838	14,737
Connector	867	823	905	600	268	268	229
Trust Funds ¹	886	581	580	661	622	701	654
Other Health Care	190	262	240	232	242	235	264
Local Government Support	5,490	5,640	5,765	5,919	6,080	6,018	6,146
Chapter 70 Education Aid	4,014	4,108	4,186	4,303	4,404	4,401	4,506
Other K-12 Education Aid	501	517	571	602	633	581	572
Unrestricted Local Aid	925	927	927	948	973	973	1,007
Other Local Aid	50	89	81	67	70	63	61
Other Education	1,597	1,440	1,490	1,612	1,714	1,705	1,706
Early Education	515	507	499	524	550	544	545
Higher Education	1,082	933	990	1,088	1,164	1,161	1,162
Human Services	4,803	4,957	5,095	5,404	5,610	5,626	5,757
Developmental Services	1,358	1,402	1,441	1,553	1,720	1,715	1,825
Family Services	879	902	911	977	1,025	1,059	1,117
Cash Assistance	782	787	786	794	743	716	718
Mental Health	614	651	659	708	736	714	728
Public Health	491	517	522	560	590	585	534
Housing Support	320	337	406	420	379	422	403
Senior Support	247	240	240	253	272	271	282
Veteran Services	112	121	130	140	145	143	150
Public Safety	2,300	2,351	2,430	2,523	2,563	2,593	2,628
Corrections	543	569	579	591	602	605	609
Sheriffs	492	505	529	542	553	560	584
Judiciary	776	761	794	828	824	859	847
Police	270	285	293	310	319	308	323
District Attorneys	93	99	102	103	108	108	108
Attorney General	38	40	40	43	44	44	44
Other Public Protection	87	93	93	106	113	109	112
Transportation	1,197	1,143	1,191	1,423	1,573	1,583	1,631
MassDOT	195	180	162	272	416	440	409
Regional Transit	15	15	19	68	40	40	40
Registry	7	9	9	9	9	9	10
MBTA	927	939	947	1,074	1,108	1,094	1,172
Sales Tax Revenues	767	779	787	799	811	971	985
Discretionary Assistance	160	160	160	275	297	123	187
Economic Development	303	366	362	414	399	335	376
Business and Labor	104	144	163	194	163	109	140
Environment and Energy	199	223	199	220	236	227	236
Employee Benefits	3,014	3,170	3,207	3,445	3,793	3,981	4,187
GIC ²	1,175	1,278	1,240	1,395	1,496	1,683	1,698
State Retiree Benefits (OPEB)	397	414	415	420	505	505	518
Pensions	1,442	1,478	1,552	1,630	1,793	1,793	1,972
Capital Support	1,937	2,253	2,362	2,429	2,498	2,498	2,529
Debt Service	1,678	1,970	2,068	2,125	2,219	2,219	2,252
Contract Assistance	259	283	294	304	279	279	278
MA School Building Authority	644	678	669	729	772	772	804
Other/General Government	477	560	568	710	630	620	437
Total (Including Pre-Budget Transfers)	33,945	34,660	35,738	38,222	40,366	40,773	42,086

¹ Includes the Medical Assistance Trust Fund and the Delivery System Transformation Initiatives Trust Fund

² Includes health care costs for municipalities and authorities that reimburse the state