Testimony and Forecast of GRF Revenues and Public Assistance Spending For the FY 2004 - FY 2005 Biennial Budget

Testimony by LSC Fiscal Staff
February 4, 2003

LEGISLATIVE SERVICE COMMISSION TESTIMONY

TABLE OF CONTENTS

Ohio Legislative Service Commission

Forecast of GRF Revenues and Public Assistance Spending For the FY 2004-FY 2005 Biennial Budget

Testimony before the House Finance and Appropriations Committee

February 4, 2003

Testimony of LSC Staff by
David Brunson, Division Chief for Education and Taxes
With assistance from other LSC Tax and Human Services Fiscal Staff

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Chairman Calvert and members of the House Finance and Appropriations Committee, we are here today to present the forecasts of the staff of the Legislative Service Commission (LSC) for fiscal years 2003, 2004, and 2005. This testimony and the other information in your packet includes forecasts for GRF revenues, for the economy, for the Medicaid program, for TANF (Temporary Assistance for Needy Families), and for the DA (Disability Assistance) program.

The estimates provided today assume current law continues throughout the next biennium. As better information on the executive's tax and human services proposals become available, we will augment these baseline forecasts with information on those proposals.

Summary

The executive has estimated a shortfall of $720 million for the current year, FY 2003. Our shortfall estimate is slightly less at $651 million. The executive shortfall is composed of a GRF revenue shortfall of $680.3 million versus our shortfall estimate of $638.4 million.

The executive's human services shortfall is $40 million in state funds versus our estimate of $13 million.

The LSC revenue estimate for FY 2004 GRF income (excluding federal) is $17,209 million ($17.209 billion). The LSC estimate is $41.9 million more than the executive's estimate. For FY 2005, the LSC estimate is $18,063 million. This is $126.7 million more than the executive's estimate.

Our baseline forecast on Medicaid expenditures is approximately $9.02 billion in FY 2004 and $9.69 billion in FY 2005. Our estimated expenditures are 1.04 percent below the Office of Budget and Management's (OBM's) baseline forecast for FY 2004 and 2.78 percent below their forecast for FY 2005. LSC's forecast is lower than the executive's forecast by the following amounts:

	State	**Federal**	**Total**
FY 2003	$ 27.0 million	$ 37.8 million	$ 64.8 million
FY 2004	$ 39.0 million	$ 55.3 million	$ 94.3 million
FY 2005	$ 111.6 million	$ 158.0 million	$ 269.6 million

Both LSC and OBM predict that Medicaid expenditures for FY 2003 will be greater than what is currently appropriated. OBM estimates that appropriations for the Medicaid program will fall $40 million short in state share in FY 2003. LSC estimates that appropriations for the Medicaid program will fall $13 million short in state share in FY 2003. The difference in estimated shortfalls is equal to the difference between both forecasts for FY 2003 (i.e., $27 million in state share). These shortfall estimates or funding differences also take into account the DA Medical program which is now part of the Medicaid line item. One of the reasons the LSC estimates are less than the OBM estimates is that our estimates of DA Medical are lower by $5.6 million in FY 2003, $6.9 million in FY 2004, and $13.2 million in FY 2005 than the OBM estimates.

Our forecast for the Disability Assistance (DA) Cash program is also lower than the OBM forecast. The LSC forecast is lower by $2.2 million in FY 2004 and by $2.9 million in FY 2005 than the OBM forecast. However, the LSC forecast is higher than the OBM forecast by $0.2 million in FY 2003.

The Economy

On its way out of what was thought to be a short and shallow recession, the economy hit a sizable soft spot, and its recovery appears to have stalled.

According to the National Bureau for Economic Research (NBER), which dates recessions in the U.S., the recession officially began in March 2001, although it is likely that the Ohio economy had already been in recession for some time. The NBER has yet to call the end of the recession. Many economists announced that it ended in March of last year, and their optimism seemed validated when the Bureau of Economic Analysis (BEA) announced that gross domestic product (GDP) grew by 3.1 percent over the third quarter of 2002 (that is, over the July through September period). That number was subsequently revised upward to 4 percent, but by then the economy had started to falter.

The third quarter GDP growth was due almost entirely to consumer spending, particularly on durable goods. Spending on residential construction also contributed to the high growth rate. At the same time consumer confidence had been falling since June -- particularly in consumers' assessment of current conditions. This indicator tends to reflect the current employment situation, and employment has been virtually flat throughout 2002. (For all of 2002 total nonfarm payroll employment declined by 181,000. This compares to a loss of 1.4 million in 2001.)

In October, the Conference Board index of consumer confidence fell by 15 percent to its lowest level since November 1993. In addition to ongoing concerns about employment, consumers in October were concerned about volatile stock markets, geopolitical uncertainty, the West coast dock strike, and the Washington area sniper attacks. These factors all acted to increase uncertainty and decrease confidence. Consumers continued to spend but at a much lower rate, and their purchases shifted away from durables to non-durable items. Indicators of business confidence also declined in the fourth quarter, leading Alan Greenspan to announce in November of last year that the economy had hit a "soft spot."

The economy remained in this soft spot throughout November and December. December unemployment remained at an eight-year high and employment fell for the third time in four months. Retail sales grew less than expected and sales excluding motor vehicles were flat.

The BEA's advance estimates of GDP growth for the fourth quarter of 2002 (released January 30, 2003) was 0.7 percent -- substantially lower than the third quarter increase of 4 percent. The chief driver of growth was defense spending by the Federal government: it increased by 11.2 percent. Personal consumption expenditures increased by only 1 percent (compared to the 4.2 percent increase in the third quarter). Investment expenditures and net exports both negatively affected GDP growth.

All evidence seems to suggest that the economy has not yet moved beyond the soft spot. Moreover, the general consensus among economists is that it is unlikely to do so until the uncertainty in the international environment -- particularly with respect to the possible war with Iraq -- is resolved, and consumer and business confidence improve.

While forecasting is always fraught with difficulties, the heightened importance of the international political situation makes economic forecasting especially difficult at this time. It basically requires the forecaster to predict not only whether there will be a war, but also to predict how long and how extensive the war will be.

The January 2003 Global Insight forecast that we have relied on for most of our revenue projections assumes a 60 percent likelihood of a short and successful war with Iraq during the first quarter of 2003. According to the forecast, the war will first have a depressing impact on both consumer confidence and GDP growth, but both will improve considerably after the first quarter. Global Insight predicts a GDP growth rate of 2.6 percent for the first quarter of 2003, increasing to 3.5 percent in the second quarter and 5.5 percent in both the third and fourth quarters, resulting in an annual average growth rate of 3.1 percent for all of 2003.

Employment is predicted to recover much more slowly, much like the "jobless recovery" following the 1990-1991 recession. The forecast assumes that employment bottomed out in the fourth quarter of 2002 and remains flat in the first quarter of 2003. Employment is expected to start growing in subsequent quarters, but it is not expected to regain its previous level (which peaked in May 2000) until the second quarter of 2005.

The slow growth of employment is attributed in part to the substantial productivity improvements of the 1990s. Tremendous technological advances resulted in economy-wide productivity gains that underscored much of the prosperity of the 1990s. Advances in productivity allowed businesses to expand output proportionately more than inputs (especially raw materials and labor), which, in turn fostered much of the increase in real incomes in the late twentieth century. These trends appear to be continuing in the new century.

The technological improvements were typically made through major capital investment projects. Since the recession of 2001, those massive capital investments have resulted in substantial excess capacity throughout the economy. As a result of the excess capacity, businesses have little incentive to invest, especially since demand is weak. Furthermore, even as demand recovers, businesses can expand production considerably without adding more workers. Ohio employment, in particular, is unlikely to increase until the GDP growth rate exceeds 4 percent. According to this forecast, that will not happen until the second half of 2003 (i.e., in FY 2004).

The reluctance of businesses to invest is further compounded by the Iraq situation and low business confidence. In any case, employment is unlikely to increase in the absence of substantial capital investment, and business can easily expand production without making that investment. Hence, employment is expected to remain flat for the first quarter and to pick up gradually after that.

Global Insight mentions several "risks" to the forecast, which could further complicate the economic recovery:

- The war against Iraq could take longer and be a lot messier.
- There could be another major terrorist attack in the U.S. or Europe.
- The stock market could take another dive.
- The "housing bubble" could burst.
- The value of the U.S. dollar could fall precipitously.
- There could be another financial crisis.

Alternatively, the following events might hasten the economic recovery:

- The situation with Iraq might be resolved without a war.
- Improvements in the international situation could cause businesses to increase investment spending more quickly.
- Europe and Japan could grow more quickly, spurring demand for American exports.

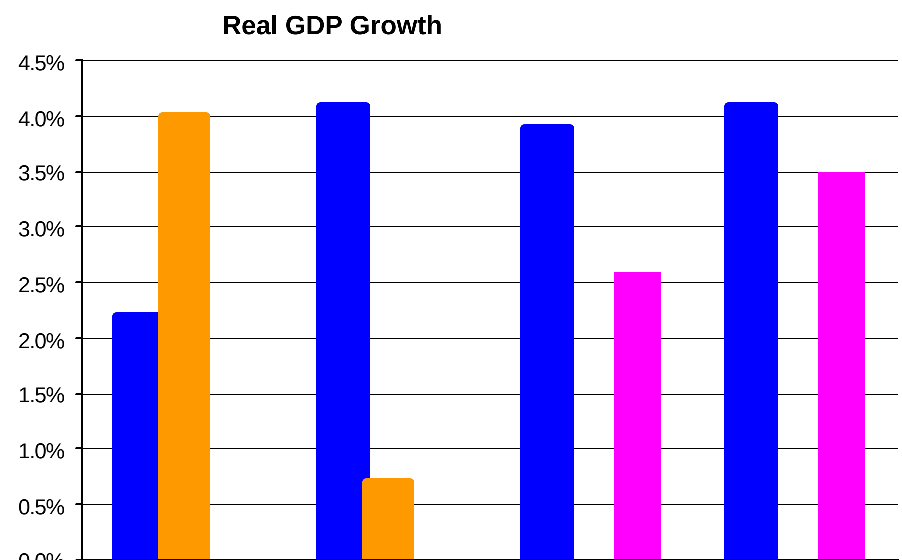
And, of course, many as yet unthought of things could happen.

After 2003, the forecast becomes much brighter. At that time both national and international economic forces will be favoring economic recovery and expansion. Global Insight projects a real GDP growth rate of 4.7 percent for 2004 -- the best growth rate since 1985. While the growth rate for 2005 is forecast at only 3.3 percent, employment should be recovering by then, so that it will at least feel better.

Revenue Estimates

Based on our current economic forecast, LSC believes that revenue estimates for the current year, FY 2003, should be reduced by $638.4 million. The economy barely expanded in the 4th quarter of calendar year (CY) 2002, and slow growth is expected for this quarter and possibly the second quarter of 2003 as well. The original estimates assumed that Ohio and the US would have fairly good growth all this fiscal year as the economy pulled out of the recession, and that employment growth would have started last quarter. Instead, employment is shrinking and employment growth is still a couple of quarters off into the future.

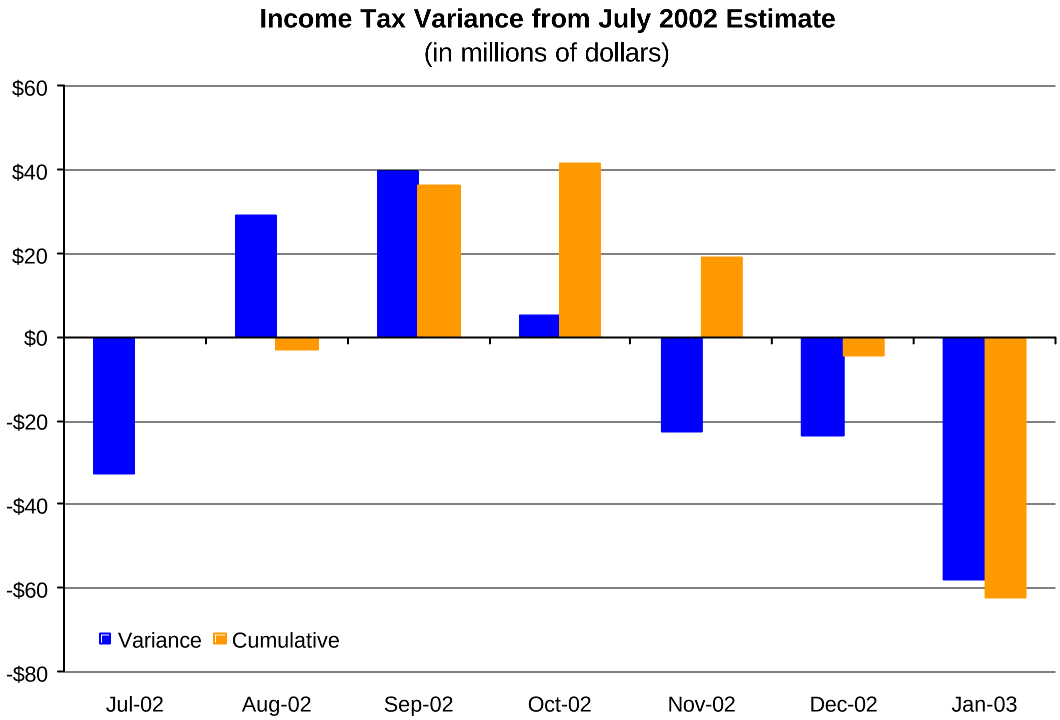
Revenues for the personal income tax and the non-auto sales tax have essentially followed national economic trends during the first seven months of FY 2003. In the first quarter, the economy expanded at a 4.0 percent rate and revenues were above estimates. However in the second quarter (the last quarter of CY 2002), the economy had an annualized growth rate of only 0.7 percent, employment decreased, unemployment increased, and state tax revenues were below estimates in October, November, and December. This same revenue trend has continued for January and a meager revenue performance is now expected for the rest of the fiscal year.



	2002-3	2002-4	2003-1	2003-2
May 2002 Forecast	2.20%	4.10%	3.90%	4.10%
Actual	4.00%	0.70%		
January 2003 Forecast			2.60%	3.50%

Source: Forecasts by Global Insight

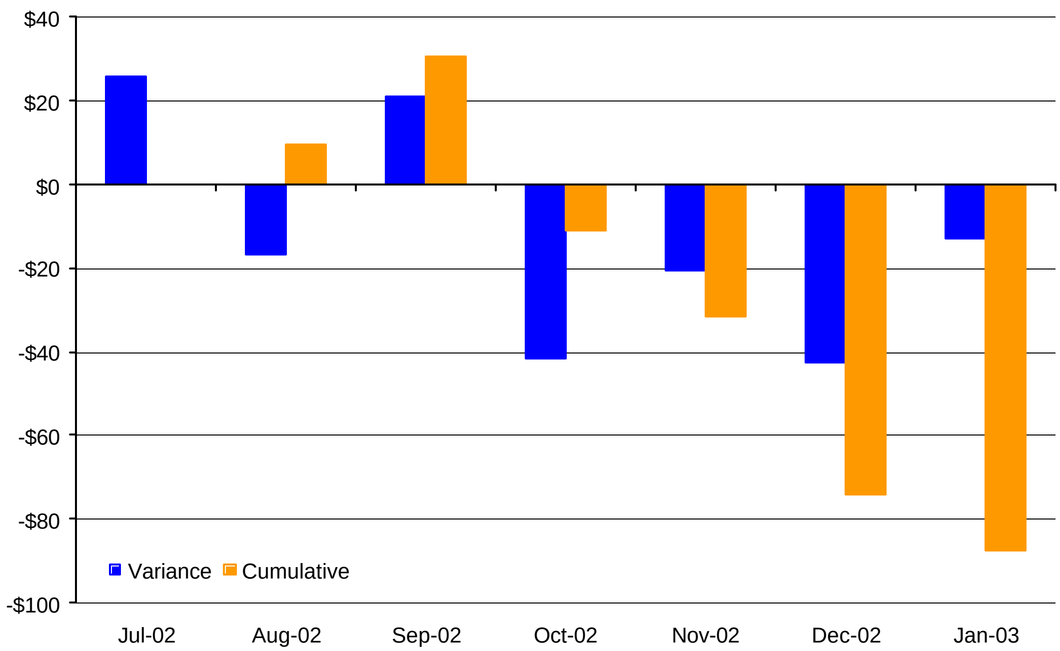
Personal income tax monthly receipts have generally followed the same pattern as the economy. August and September were positive months off-setting July. However, part of the overage during this period was higher than estimated revenue from the new tax on trusts. This overage is not expected to continue due to further changes to the tax made in the capital bill. October had a small monthly surplus followed by widening monthly shortfalls over the November, December, and January period. Clearly, receipts are not heading in a positive direction. Downward movement in employment, consumer confidence, profits, and stock prices are holding back receipts whereas the May forecast assumed improvement for these measures by year's end. For the fiscal year to date, receipts are up 3.7 percent over the same period last year. Our forecast for FY 2003 calls for 4 percent growth for the year, with about 1 percent of that growth due to the new tax on trusts.



The non-auto sales tax shows a similar revenue pattern. Two out of the first three months had positive revenue results. Then, the months of October through January all had negative tax results. The overall shortfall has grown to $87 million for the seven months.

Compared to last year, receipts are up 2.1 percent (or $64 million). However, we believe that this growth was due to the auto leasing tax change that was effective about February 2002. This tax change increased the receipts the second half of last fiscal year by about $85 million with a similar increase possible this year for each six-month period. This is why we are predicting a 1.7 percent growth rate for the year as a whole. If you take out the tax change from both this year and last year, the tax revenues would be about the same for both years.

Non-auto Sales Tax Variance from July 2002 Estimate
(in millions of dollars)

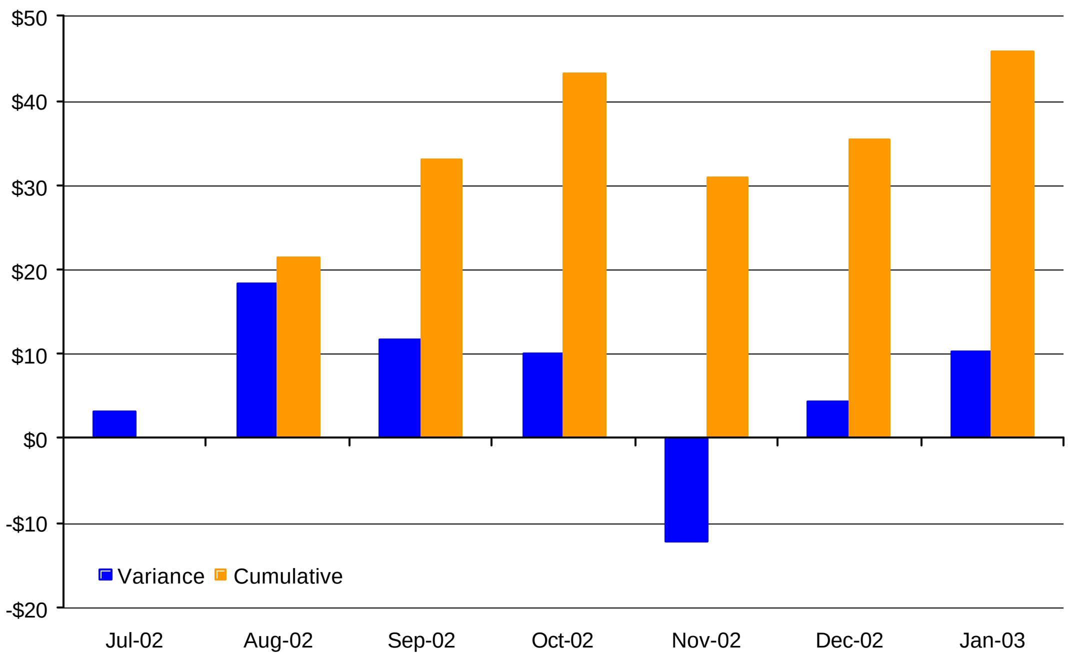


The auto sales tax has continued to perform amazingly well so far this year. The surplus revenue for this portion of the tax traces to the first four months of the year. November was a down month as the auto industry tried to reduce incentives to purchase new cars and light trucks. Vehicle sales plunged. The incentives were reinstated. It is clear that until the economy is more robust and consumer confidence is restored, this market is controlled by the level of auto maker provided incentives.

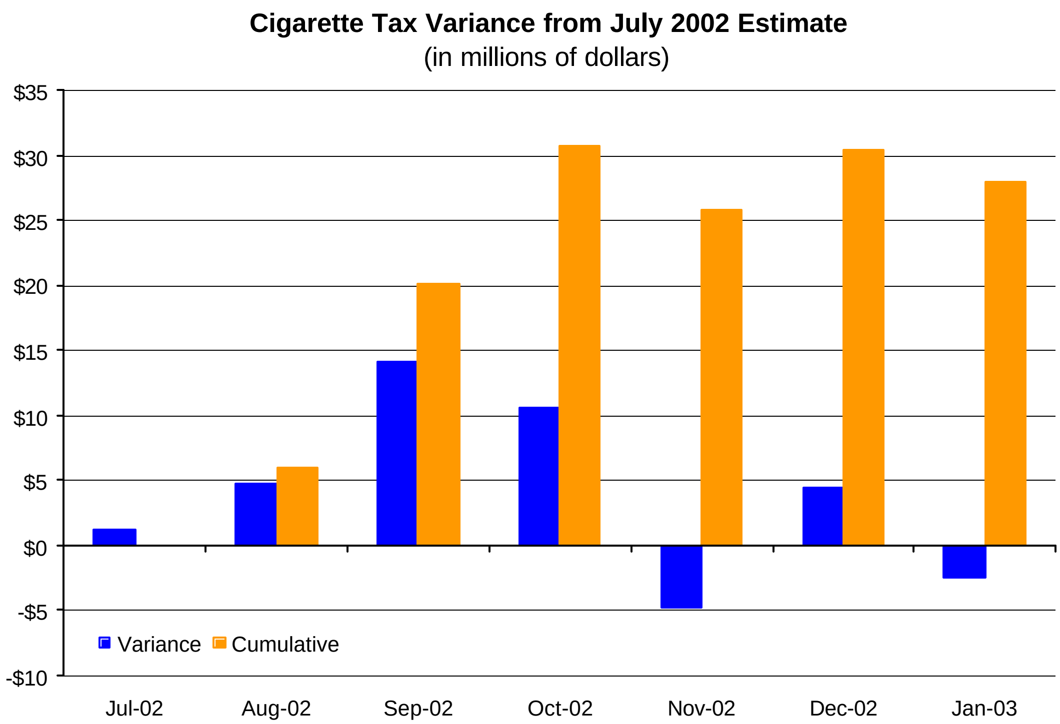
Normally the auto sales tax has one or two years of significant decline during a recession period. Because of the auto manufacturers' strategy of offering massive incentives, this decline has not occurred during this recession. We are truly in uncharted territory.

So far this year, receipts are about even with last year (0.2 percent over). We are anticipating a slight erosion in this position for a 1.5 percent decline for the year. Through January revenues are $46 million over estimate. This is estimated to erode to $9 million by year's end, since new car sales this spring are not expected to match last spring's brisk selling rates.

Auto Sales Tax Variance from July 2002 Estimate
(in millions of dollars)



As of July 1, 2002, cigarette taxes were increased from 24 cents to 55 cents per pack. Cigarette tax revenue showed small monthly surpluses for the first four months of the year and has been close to the estimate the last three months. The surpluses appear due to two factors: the floor tax brought in more revenue than expected and the fall-off in cigarette consumption was not entirely immediate. The floor tax, the tax on unsold cigarettes in inventory, was more than expected as inventories were higher than expected. This was a one-time gain. Some additional gain was due to cigarette consumption not decreasing as quickly due to the tax increase as was expected. However, this appears to be temporary, since consumption has been on target the last several months with some possibility that consumption will fall more during the second half of the year. The tax is now $28 million over estimate and we estimate the overage will slip to $20 million over estimate by year's end. We estimate that consumption will decline 6 percent this year due to the tax increase. This is in addition to the normal decline of 1½ percent per year.



Turning to the other sources of income for FY 2003, we estimate that:

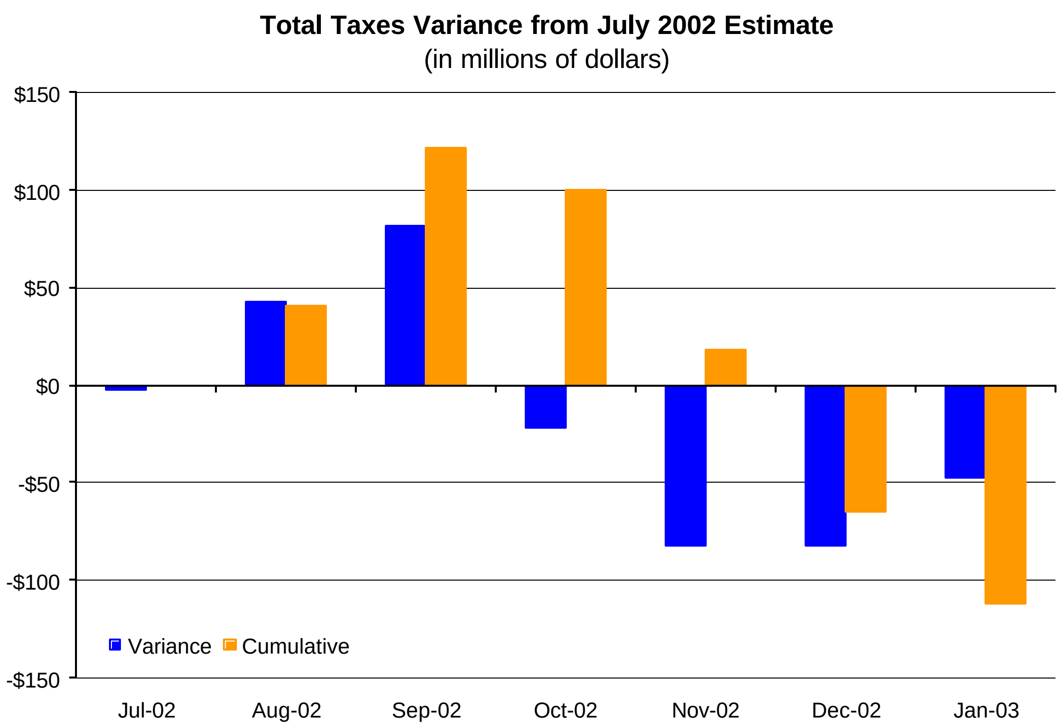
- Because economic growth stalled out in the last quarter of 2002, we have reduced the corporate franchise tax estimates for FY 2003. We now show a 3.1 percent decrease from FY 2002 due to declining corporate profits rather than the originally expected increasing profits for CY 2002. Through January, the tax is $22 million under estimate but ahead of last year's low receipt pace that was caused by very high refunds.

- The public utility tax is short by $30 million so far and we expect it to finish short by $36 million for the year.

- Foreign insurance tax revenues are estimated to be $31 million below estimate while domestic insurance tax revenues are estimated to be $7 million over estimate for the year.

- Earnings on investments estimates were lowered $52 million due to low cash balances for investments and low interest rates. Results for seven months are $36 million under estimate.

- Liquor transfers estimates were increased $10 million due to favorable results for the first seven months.



The total taxes chart for the first seven months of FY 2003 shows two things. (This chart excludes earnings on investments, liquor profits and several other categories of non-tax revenues.)

- Revenue variances, on the whole, were positive for the first three months of the year.

- By October, revenue variances had turned negative.

Tax revenues are estimated to grow 3.8 percent in FY 2004 and 5.0 percent in FY 2005. Most categories of receipts should have reasonable growth. Some exceptions are:

- The auto sales tax should have no or very slow growth both years due to the high level of sales in FY 2003 caused by the auto manufacturer incentives. Current high sales levels limit the upside revenue potential as we emerge from the recession. The normal reason for large growth for this source coming out of a recession is consumer pent-up demand. This is where consumers put off making a new purchase during a recession because of the economic uncertainty or because their income is reduced. Due to the large incentives, pent-up demand may exist for those with reduced incomes, but not for most families. In fact the danger is that auto companies are pulling sales forward from the future by the great deals, and that sales may actually decline for a period of time. As with the current year, sales levels during the biennium will be greatly affected by manufacturer decisions on incentives.

- The cigarette tax is estimated to decrease 3.8 percent in FY 2004 and 1.4 percent in FY 2005. The decrease in FY 2004 is due to the play-out of the 6 percent decline in consumption caused by the tax increase and the one-time revenue from the floor tax in FY 2003. (Essentially, due to a year long adjustment period to the higher tax, the ending consumption level in FY 2003 is below the average consumption level for the year.) The FY 2005 decline reflects the general on-going slow decline in cigarette consumption.

- The estate tax declines 24 percent in FY 2004 due to the tax changes previously enacted for that tax. Growth of 4.3 percent is estimated for FY 2005.

- The public utility excise tax is estimated to fall slightly at the rate of 0.4 percent in FY 2005 reflecting slow erosion in the regulated utility markets for local telephone service and natural gas.

- The ISTV's & IDC's category is estimated to fall to $60 million in FY 2004, since there are no BSF (Budget Stabilization Fund) moneys left to transfer and that any other transfers that might be made are subject to additional legislation and are not in place under current law for these baseline estimates.

While the executive is proposing additional law changes for both FY 2003 and the new biennium, these law changes have not been included in our estimates. We will be estimating these changes after the proposed bill containing these changes becomes available. For the three Local Government Funds we have assumed the current statutory percentage rates for deposit into those funds. The executive's proposed cap on the percentage increase going into those funds will redirect funds to the GRF from the LGFs.

Also not included in our estimates are effects from proposed federal law changes that might impact state tax revenues. One federal proposal that would affect state revenues is the exemption for stock dividends from the U.S. personal income tax. The normal workings of the tax would remove this income from FAGI (Federal Adjusted Gross Income), the starting point for income under the Ohio personal income tax. Almost all states with personal income taxes will face a decision as to what to do about this proposal should it become law. The general effect on states will be to cut state income tax revenue by about 2 to 3 percent.

Forecast of Medicaid Caseloads and Expenditures Before The House Finance and Appropriations Committee For The FYs 2004-2005 Biennial Budget

Chuck Phillips, Division Chief

February 4, 2003

Good afternoon, Mr. Chairman and Members of the House Finance and Appropriations Committee. My name is Chuck Phillips. Today I will be presenting the Legislative Service Commission's baseline forecast for Medicaid caseloads and expenditures.

Medicaid has many funded programs within the state budget including 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 line item 600-525, Health Care/Medicaid, 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 the overall medical care policies and expenditures for the state. However, expenditures for these waiver programs are capped at the level at which they are appropriated. In contrast, traditional Medicaid is an entitlement program. In other words, the state must provide federally mandated services to all those who meet the eligibility criteria. Therefore, in order to get an idea of what level of appropriations will be needed to fund the traditional Medicaid program in Ohio, we forecast the caseload and expenditures each biennium.

Caseloads

The total number of persons eligible for Medicaid grew by approximately 11 percent from 1.28 million in FY 2001 to 1.42 million in FY 2002. The total number of eligibles is estimated to reach 1.56 million in FY 2003, approximately a 10 percent increase over FY 2002. LSC forecasts that the number of persons eligible for Medicaid will continue to grow to 1.64 million in FY 2004 and 1.65 million in FY 2005, approximately a 5 percent and 1 percent increase, respectively.

Poor labor market conditions associated with the recession have been the primary driving force behind the growth in total caseload. An additional factor behind the recent growth in caseload has been the CHIP-II program expansion that began on July 1, 2000. The CHIP-II program covers uninsured children under age 19 in families with incomes between 150 percent and 200 percent of the Federal Poverty Guideline (FPG). The eligible population for CHIP-II grew by slightly over 90 percent in FY 2002, and is forecast to grow by approximately 18 percent in FY 2003, as the process of enrolling those made newly eligible under the expansion reaches its conclusion.

LSC forecasts that the overall Covered Families and Children (CFC) caseload, which includes Healthy Families, Healthy Start, CHIP-I, and CHIP-II will peak in the fourth quarter of FY 2004, and begin to drop in the second quarter of FY 2005 as the economy begins to recover.

CFC eligibles access their health care benefits through either the traditional fee-for-service system or the Medicaid managed care program. The Medicaid managed care program has three different enrollment categories: mandatory, voluntary, and preferred option. In FY 2001, the state introduced the preferred option. Under preferred option, recipients are automatically enrolled in managed care if they fail to select the traditional fee-for-service. This policy change has pushed up the HMO penetration rate from approximately 28 percent in FY 2001 to 32 percent in FY 2002. LSC's baseline forecast assumes that the take up effect of the preferred option program will diminish in FY 2003, and projects the HMO penetration rate will be approximately 35 percent for FY 2004 and FY 2005.

Growth in the Aged, Blind, and Disabled (ABD) caseload accelerated in FY 2002 and continued into the first half of FY 2003. The acceleration was driven by the disabled subcategory of the ABD category. The accelerated growth in the disabled subcategory is projected to continue through the end of FY 2003, after which the growth rate is projected to gradually return to a more typical historical rate.

Costs

Medicaid program costs are estimated separately for each of the nine major expenditure categories: long-term care (nursing facilities and Intermediate Care Facilities for the Mentally Retarded), hospitals (inpatient and outpatient), physician services, prescription drugs, health maintenance organizations (HMOs), Medicare buy-in, waiver, all other care, and DA Medical. After forecasting changes in the caseload, a cost per Medicaid recipient is projected. The cost per recipient is itself broken down into two components: the average number of claims per recipient, called the "utilization rate," and the average cost per claim submitted. The average cost per claim depends heavily on overall health care inflation -- Medicaid spending on health care services that are market driven significantly outweighs program payments to providers that are tied to fee schedules. In addition, payment rates for long-term care, inpatient hospital care, and prescription drugs are statutorily connected to market place trends. Consequently Medicaid, like any other third party payer, is very susceptible to market forces.

I will briefly highlight our forecast of costs for the three largest Medicaid expenditure categories: nursing facilities, hospitals, and prescription drugs. These three categories combined represent approximately 74 percent of total Medicaid spending in the 600-525 line item.

Payments to nursing facilities are based on cost reports. Nursing facilities annually submit cost reports to JFS, which are used to calculate facility-specific per diems for the following state fiscal year. The per diem rates are then adjusted quarterly to account for differences in each resident's needs -- known as the "case-mix adjustment." The average per diem in FY 03 for nursing facilities is projected to grow by approximately 6 percent to $152.29. The average per diem in FY 2004 and FY 2005 is projected to grow by approximately 5 percent to $159.56 and an additional 5 percent to $167.94, respectively. The rise in the per diem is fueled by heightened acuity levels, increased capital costs, and to a larger extent, elevated direct care costs. Estimated expenditures for nursing facilities are approximately $2.76 billion in FY 2004 and $2.95 billion in FY 2005.

The growth rate in spending for hospital care is projected to be approximately 10 percent from FY 2003 to FY 2004, and 8 percent from FY 2004 to FY 2005. Estimated expenditures for inpatient and outpatient hospital services are $1.97 billion in FY 2004 and $2.12 billion in FY 2005. The Ohio Administrative Code requires an annual inflationary update to inpatient rates; however, outpatient rates are based on a fee schedule that is not automatically inflated.

S.B. 261 of 124^{th} General Assembly authorizes JFS to establish a supplemental drug rebate program under which drug manufacturers may be required to provide a supplemental rebate to the state as a condition of having their products covered by Medicaid without prior approval. The bill also allows the Director of JFS to apply for a federal Medicaid waiver, if necessary, to establish the program. It is expected that this program will be implemented in the coming biennium. LSC assumes that this policy will affect the growth rates for cost-per-claim, as well as drug utilization and thus forecasts that the growth rates for cost-per-claim and utilization ratio will decelerate and hold constant for FY 2004 and FY 2005.

The combined effects of the increased utilization rates and increased costs-per-claim for the ABD population, as well as other eligibility groups, are expected to result in an increase in prescription drug spending of approximately 23 percent in FY 2003, 14 percent in FY 2004, and 13 percent in FY 2005. Estimated expenditures for prescription drug services are $1.76 billion in FY 2004 and $1.99 billion in FY 2005.

Offsetting the prescription drug services expenditures is the prescription drug rebate estimated at $372 million in FY 2004 and $430 million in FY 2005.

Medicaid Expenditures. For the upcoming biennium, LSC's baseline forecast for Medicaid expenditures is approximately $9.02 billion in FY 2004 and $9.69 billion in FY 2005. Our estimated expenditures are 1.04 percent below the Office of Budget and Management's (OBM's) baseline forecast for FY 2004 and 2.78 percent below their forecast for FY 2005. LSC's forecast is lower than the executive's forecast by the following amounts:

	State	Federal	Total
FY 2004	$ 39.0 million	$ 55.3 million	$ 94.3 million
FY 2005	$ 111.6 million	$ 158.0 million	$ 269.6 million

In FY 2004, the difference between LSC's forecast and OBM's forecast is $94.3 million, of which $39.0 million is state share. In FY 2005, the difference between the two forecasts is $269.6 million, of which $111.6 million is state share.

We have not yet met with OBM and JFS to discuss the cost management initiatives that are assumed in the Governor's Blue Book. Therefore, this is a baseline forecast assuming no policy changes. We will meet with OBM and JFS to discuss the Governor's recommended cost management initiatives and will provide an updated comparison of our expenditure estimates in the LSC Red Book.

In closing Mr. Chairman, I have simply highlighted the forecast. Included in the packet is much more detail and analysis on all the topics I have covered.

I would be happy to answer any questions the committee may have.

Summary of TANF and Disability Assistance Caseload and Expenditure Forecasts Before the House Finance and Appropriations Committee On The FY 2004-2005 Biennial Budget

Steve Mansfield, Fiscal Supervisor ***February 4, 2003***

Good afternoon, my name is Steve Mansfield. I am a fiscal supervisor at the Legislative Service Commission, and I will present the Legislative Service Commission's forecasts for the Temporary Assistance for Needy Families (TANF) and Disability Assistance (DA) caseloads and expenditures.

Under the TANF program, Ohio receives a federal block grant with flat funding from the federal government and a static "maintenance of effort" requirement for the state. Thus, unless the costs of cash assistance exceed the amount available, the caseload count no longer dictates expenditures. And since the caseload count has significantly decreased over the last several years, a large portion of the TANF expenditures provide supportive services to those transitioning off welfare or to "divert" people from reliance on government cash assistance.

The state DA program, in contrast, has recently experienced increasing caseloads and sharp cost increases. In response to these increases, the Governor has recommended an increase of funding over the FY 2003 level to $124.2 million for each year of the biennium. Since the recommended level of funding is lower than what is required to fully fund the forecast growth in the DA caseload, it will be necessary, if spending is to stay within this level, to introduce changes in the DA program and its eligibility criteria.

I will now summarize our forecasts for these two programs.

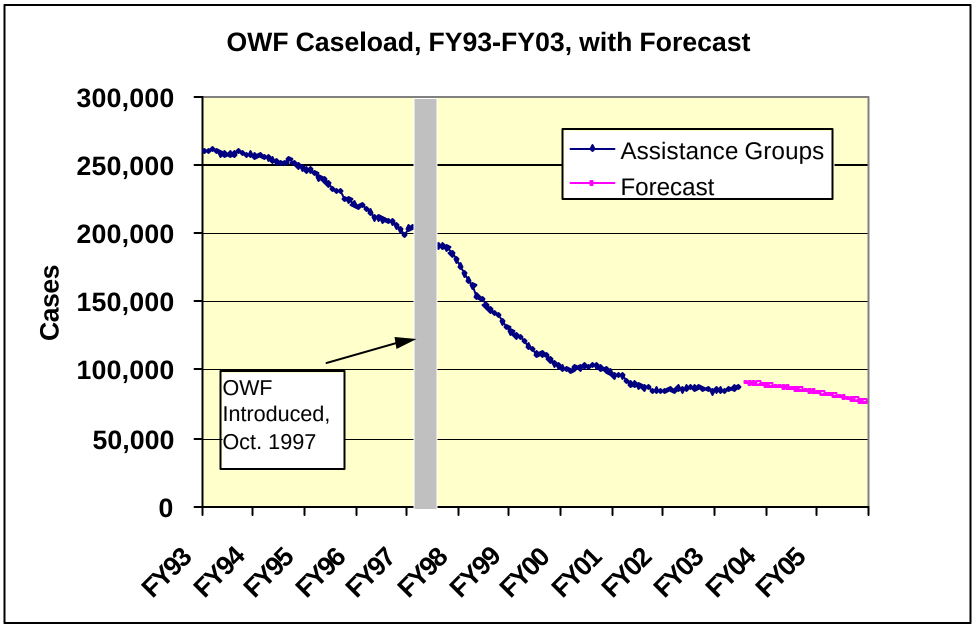
With the introduction of the federal TANF program in 1996 and Ohio's implementation of that program with the Ohio Works First (OWF) and the Prevention, Retention, and Contingency (PRC) programs in 1997, the purpose of cash assistance has changed from an entitlement program to a block grant program with temporary benefits designed to assist people as they move to the workforce. The effects of the program are seen in large numbers of recipients moving into jobs, as well as some recipients being forced off of assistance by sanctions for failure to meet program requirements and by time limits that began to be felt in October 2000.

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 the programs that TANF replaced (ADC, JOBS, and Family Emergency Assistance). However, the mandatory MOE rate can by reduced to 75 percent (or approximately $390 million) 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. Current year appropriations have allocated $401 million, or 77 percent of that level, which included a 2 percent cushion to offset any disallowances or underspending. If a state fails to meet its MOE requirement, its TANF grant for the next federal fiscal year will be reduced by the amount of the deficit, and the state will be required to increase its TANF spending by the amount of the penalty.

One of the consequences of the block grant funding arrangement is that reductions in recipient caseloads reduce the amount of "baseline" cash benefits, thus leaving more funds available for other TANF related program services or activities. If TANF grant funds go unspent in a particular year, the PRWORA legislation provides that "a State may reserve amounts paid to the State under [this legislation] for any fiscal year for the purpose of providing, without fiscal year limitation, assistance under the State program funded under [this legislation]."[1] At the end of FFY 2002 (September 30, 2002), Ohio's TANF reserve was $520.9 million, with $278.9 million reported as unliquidated obligations, and $242.0 million reported as the unobligated balance. Reserve funds are held at the federal level and are available to be spent on cash benefits.

[1] H.R. 3734, Personal Responsibility and Work Opportunity Reconciliation Act of 1996, sec. 404 (e).

TANF/OWF Forecast



As the chart detailing the trend in the OWF combined caseload indicates, the number of OWF cases (or ADC as it was known before) reached a peak in the spring of 1992 and then began a long-term decline as Ohio and the nation recovered from recession. The rate of decline was strong prior to the implementation of OWF, but the rate of decline clearly accelerated around the time of the introduction of OWF.

Over the last two years, with a stagnating economy, the caseload has stayed about the same, with only a small decline. In the coming fiscal years, however, the economy is expected to recover and the creation of jobs, particularly service sector jobs, is expected to increase. LSC believes that this will have the effect of further reducing the OWF caseload over the course of the biennium.

LSC forecasts the total number of TANF cases (or assistance groups) to decrease in FY 2004 to an average of 85,573 monthly cases. This forecast assumes an economic recovery and an expansion in service sector employment, although there are a number of significant uncertainties at the present time. The forecast decrease in the total number of TANF cases will result in approximately $10.2 million less being spent on TANF cash benefits in FY 2004 than LSC estimates for FY 2003 expenditures. The total spending on cash benefits, assuming a continuation of the current benefit levels, is forecast to be $305.2 million for FY 2004.

The decline in the number of TANF cases is expected to continue into FY 2005. The monthly average of cases is expected to decline to 79,063, representing a decrease in spending for TANF cash benefits of $26.6 million for the year. That estimate brings total spending for cash benefits, assuming current eligibility and benefit levels, to $278.6 million for FY 2005.

TANF/OWF - LSC Baseline Estimates			
	FY 2003	**FY 2004**	**FY 2005**
Average monthly cases	87,551	85,573	79,063
Total cash benefits (millions)	$316.4	$305.2	$278.6

The TANF cash benefits are paid from line items 600-410, TANF State, 600-658, Child Support Collections, and 600-689, TANF Block Grant. The executive has recommended FY 2004 total funding for the combination of these three line items at $1,018.1 million. The total recommended funding level for these three line items in FY 2005 is $1,017.5 million.

Funding cash benefits for FY 2004 at the forecast level of $305.2 million, and at $278.6 million for FY 2005, leaves $712.9 million in FY 2004 and $738.9 million in FY 2005 from these three line items for employment services, work activities, PRC services, transitional services, direct payments from TANF federal funds for child day care (in addition to receiving funds directly from the TANF federal block grant, child care receives funding from other sources), and other allowable activities.

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 15,400 recipients. An additional 5,000 or so individuals currently receive medical benefits only. The DA cash and medical recipient caseloads both exhibited a steady decline until the Fall of 1999. Since then, however, the cash assistance caseload has been increasing steadily. In January 2001 the medical caseload also began to increase and, along with an increase in medical inflation, has added quickly to the cost of the program. LSC forecasts that these trends will continue at the same pace that has been exhibited since these upturns.

Disability Assistance LSC Baseline Forecast	FY 2003	FY 2004	FY 2005
Average monthly cash recipients	15,393	17,442	19,247
Average monthly medical recipients	20,628	24,321	28,262
(millions $)			
DA Cash	$23.0	$26.1	$29.4
DA Medical	$90.1	$109.0	$134.9
DA Total -- LSC Forecast	**$113.1**	**$135.1**	**$164.3**
Recommended by Gov. -- DA Cash		$22.8	$22.8
Recommended by Gov. -- DA Medical		$101.4	$101.4
DA Total--Recommended by Gov.		**$124.2**	**$124.2**

If current eligibility criteria stay the same, LSC anticipates the FY 2004 average number of monthly recipients of DA cash benefits to be 17,442, which represents an increase of 13.3 percent over the FY 2003 estimate. If cash benefit levels stay the same, benefits for the year will total $26.1 million, constituting an increase of 13.5 percent over the FY 2003 estimate for cash benefits. Total cash benefits for the DA program in FY 2005 are forecast to be $29.4 million, representing a 12.6 percent increase from FY 2004. This reflects an expected increase in FY 2005 to about 19,250 average monthly recipients of DA cash.

If current eligibility criteria stay the same, the DA medical recipient caseload and expenditures are expected to continue its recent increases. Overall expenditures to serve DA medical recipients are anticipated to increase in FY 2004 to $109.0 million, representing a 21.0 percent increase over the FY 2003 estimate. LSC anticipates total medical spending to increase to $134.9 million in FY 2005, which represents a 23.8 percent increase. In addition to the effects of continued caseload growth, the calculation of DA expenditures includes the effects of inflation in medical costs. Historically, medical costs in the DA program constitute about 70 percent of total DA expenses.

Combined DA cash benefits and DA medical benefits are estimated to total $135.1 million for FY 2004 and $164.3 for FY 2005. This assumes current eligibility and benefit levels. OBM estimates the combined total for DA to be $118.4 million in FY 2003, $144.2 million in FY 2004, and $180.4 million in FY 2005.

Estimated FY 2003 GRF Revenue Shortfall - State Sources Only

GRF Amounts by Source (dollar amounts in millions)

REVENUE SOURCE	OBM July 2002 Estimates	OBM Jan 2003 Estimates	difference from July 2002 OBM estimates	LSC Jan 2003 Estimates	difference from July 2002 OBM estimates
Auto Sales & Use	$905.0	$905.0	$0.0	$914.0	$9.0
Non-Auto Sales & Use	$5,385.0	$5,172.0	-$213.0	$5,197.0	-$188.0
Total Sales & Use	$6,290.0	$6,077.0	-$213.0	$6,111.0	-$179.0
Personal Income	$7,863.0	$7,501.0	-$362.0	$7,599.0	-$264.0
Corporate Franchise	$774.3	$725.0	-$49.3	$690.0	-$84.3
Public Utility	$265.0	$240.0	-$25.0	$228.7	-$36.3
Kilowatt-Hour	$335.0	$335.0	$0.0	$339.5	$4.5
Foreign Insurance	$225.0	$225.0	$0.0	$194.1	-$30.9
Domestic Insurance	$155.0	$155.0	$0.0	$161.6	$6.6
Business & Property	$56.9	$56.9	$0.0	$49.0	-$7.9
Cigarette	$568.2	$583.2	$15.0	$585.0	$16.8
Alcoholic Beverage	$58.0	$58.0	$0.0	$56.3	-$1.7
Liquor Gallonage	$30.0	$30.0	$0.0	$29.7	-$0.3
Estate	$91.0	$95.0	$4.0	$91.0	$0.0
Total Taxes	**$16,711.4**	**$16,081.1**	**-$630.3**	**$16,134.9**	**-$576.5**
Earnings on Investment	$85.0	$50.0	-$35.0	$33.1	-$51.9
Licenses and fees	$33.0	$33.0	$0.0	$28.0	-$5.0
Other Income	$746.5	$125.8	-$620.7	$125.8	-$620.7
ISTV's & IDC's	$0.0	$605.7	$605.7	$605.7	$605.7
Total Non-Tax Receipts	**$864.5**	**$814.5**	**-$50.0**	**$792.6**	**-$71.9**
Liquor Transfers	$105.0	$105.0	$0.0	$115.0	$10.0
Transfers In - Other	$248.5	$235.2	-$13.3	$235.2	-$13.3
Transfers In - Temporary	$0.0	$13.3	$13.3	$13.3	$13.3
Total Transfers In	**$353.5**	**$353.5**	**$0.0**	**$363.5**	**$10.0**
Total Sources Excluding Federal	**$17,929.4**	**$17,249.1**	**-$680.3**	**$17,291.0**	**-$638.4**

2/3/2003

LSC and Baseline OBM GRF Revenue Forecasts Compared - State Sources Only

GRF Amounts by Source (dollar amounts in millions)

	FY 2003			FY 2004			FY 2005		
REVENUE SOURCE	OBM	LSC	Difference	OBM	LSC	Difference	OBM	LSC	Difference
Auto Sales & Use	$905.0	$914.0	$9.0	$920.0	$912.4	-$7.6	$920.0	$922.0	$2.0
Non-Auto Sales & Use	$5,172.0	$5,197.0	$25.0	$5,410.0	$5,381.5	-$28.5	$5,680.0	$5,628.3	-$51.7
Total Sales & Use	$6,077.0	$6,111.0	$34.0	$6,330.0	$6,293.9	-$36.1	$6,600.0	$6,550.3	-$49.7
Personal Income	$7,501.0	$7,599.0	$98.0	$7,834.0	$7,987.1	$153.1	$8,262.0	$8,467.9	$205.9
Corporate Franchise	$725.0	$690.0	-$35.0	$770.0	$742.1	-$27.9	$837.0	$821.5	-$15.5
Public Utility	$240.0	$228.7	-$11.3	$250.0	$239.3	-$10.7	$262.5	$238.3	-$24.2
Kilowatt-Hour	$335.0	$339.5	$4.5	$345.0	$347.3	$2.3	$355.0	$354.8	-$0.2
Foreign Insurance	$225.0	$194.1	-$30.9	$230.0	$203.7	-$26.3	$230.0	$211.9	-$18.1
Domestic Insurance	$155.0	$161.6	$6.6	$165.0	$170.7	$5.7	$175.0	$178.3	$3.3
Business & Property	$56.9	$49.0	-$7.9	$0.0	$50.9	$50.9	$0.0	$52.8	$52.8
Cigarette	$583.2	$585.0	$1.8	$554.8	$563.0	$8.2	$551.2	$555.0	$3.8
Alcoholic Beverage	$58.0	$56.3	-$1.7	$60.0	$56.7	-$3.3	$60.0	$57.4	-$2.6
Liquor Gallonage	$30.0	$29.7	-$0.3	$30.0	$29.9	-$0.1	$31.0	$30.2	-$0.8
Estate	$95.0	$91.0	-$4.0	$105.0	$69.0	-$36.0	$105.0	$72.0	-$33.0
Total Taxes	**$16,081.1**	**$16,134.9**	**$53.8**	**$16,673.8**	**$16,753.6**	**$79.8**	**$17,468.7**	**$17,590.4**	**$121.7**
Earnings on Investment	$50.0	$33.1	-$16.9	$60.0	$49.0	-$11.0	$75.0	$62.0	-$13.0
Licenses and fees	$33.0	$28.0	-$5.0	$35.0	$28.0	-$7.0	$35.0	$28.0	-$7.0
Other Income	$125.8	$125.8	$0.0	$98.0	$98.0	$0.0	$98.0	$98.0	$0.0
ISTV's & IDC's	$605.7	$605.7	$0.0	$60.0	$60.0	$0.0	$60.0	$60.0	$0.0
Total Non-Tax Receipts	**$814.5**	**$792.6**	**-$21.9**	**$253.0**	**$235.0**	**-$18.0**	**$268.0**	**$248.0**	**-$20.0**
Liquor Transfers	$105.0	$115.0	$10.0	$105.0	$118.0	$13.0	$97.0	$122.0	$25.0
Transfers In - Other	$235.2	$235.2	$0.0	$102.5	$102.5	$0.0	$102.5	$102.5	$0.0
Transfers In - Temporary	$13.3	$13.3	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Total Transfers In	**$353.5**	**$363.5**	**$10.0**	**$207.5**	**$220.5**	**$13.0**	**$199.5**	**$224.5**	**$25.0**
Total Sources Excluding Federal	**$17,249.1**	**$17,291.0**	**$41.9**	**$17,134.3**	**$17,209.1**	**$74.8**	**$17,936.2**	**$18,062.9**	**$126.7**

2/3/2003

LSC and Baseline OBM GRF Revenue Forecasts Compared - State Sources Only

Growth Rates

	FY 2003		FY 2004		FY 2005	
REVENUE SOURCE	OBM	LSC	OBM	LSC	OBM	LSC
Auto Sales & Use	-2.4%	-1.5%	1.7%	-0.2%	0.0%	1.1%
Non-Auto Sales & Use	1.2%	1.7%	4.6%	3.6%	5.0%	4.6%
Total Sales & Use	0.6%	1.2%	4.2%	3.0%	4.3%	4.1%
Personal Income	2.7%	4.0%	4.4%	5.1%	5.5%	6.0%
Corporate Franchise	1.8%	-3.1%	6.2%	7.6%	8.7%	10.7%
Public Utility	-7.7%	-12.1%	4.2%	4.6%	5.0%	-0.4%
Kilowatt-Hour	3.6%	5.0%	3.0%	2.3%	2.9%	2.2%
Foreign Insurance	5.0%	-9.4%	2.2%	4.9%	0.0%	4.0%
Domestic Insurance	17.1%	22.0%	6.5%	5.6%	6.1%	4.5%
Business & Property	704.3%	592.6%	-100.0%	3.9%	0.0%	3.7%
Cigarette	107.3%	108.0%	-4.9%	-3.8%	-0.6%	-1.4%
Alcoholic Beverage	4.1%	1.0%	3.4%	0.7%	0.0%	1.2%
Liquor Gallonage	2.3%	1.3%	0.0%	0.7%	3.3%	1.0%
Estate	-18.3%	-21.7%	10.5%	-24.2%	0.0%	4.3%
Total Taxes	3.9%	4.3%	3.7%	3.8%	4.8%	5.0%
Earnings on Investment	-36.7%	-58.1%	20.0%	48.0%	25.0%	26.5%
Licenses and fees	6.1%	-10.0%	6.1%	0.0%	0.0%	0.0%
Other Income	-87.5%	-87.5%	-22.1%	-22.1%	0.0%	0.0%
ISTV's & IDC's	0.0%	0.0%	-90.1%	-90.1%	0.0%	0.0%
Total Non-Tax Receipts	-27.2%	-29.1%	-68.9%	-70.4%	5.9%	5.5%
Liquor Transfers	-6.3%	2.7%	0.0%	2.6%	-7.6%	3.4%
Transfers In - Other	-32.5%	-32.5%	-56.4%	-56.4%	0.0%	0.0%
Transfers In - Temporary	-72.5%	-72.5%	0.0%	0.0%	0.0%	0.0%
Total Transfers In	-30.5%	-28.5%	-41.3%	-39.3%	-3.9%	1.8%
Total Sources Excluding Federal	0.9%	1.1%	-0.7%	-0.5%	4.7%	5.0%

Economic Outlook

The national economy began the new year in a "soft spot."

The modest economic recovery stalled in October. In its November 6 meeting, the Federal Open Market Committee (FOMC), acting for the first time in almost a year, reduced its target federal funds rate by 50 basis points to 1.25 percent. The committee noted that although greater productivity growth was supporting economic activity, "incoming economic data have tended to confirm that greater uncertainty, in part attributable to heightened geopolitical risks, is currently inhibiting spending, production, and employment." In testimony before the Joint Economic Committee on November 13, Fed Chairman Alan Greenspan noted, "the evidence has accumulated that the economy has hit a soft spot." In its December 10 meeting, the FOMC left the target federal funds rate at 1.25 percent. The committee noted that economic activity was supported by accommodative monetary policy and productivity growth, but that "the limited number of incoming economic indicators since the November meeting, taken together, are not inconsistent with the economy working its way through its current soft spot." The January 15 Federal Reserve "Beige Book" reported "subdued growth in economic activity from mid-November through early January, with little change in overall conditions relative to the last survey period." Districts reported "sluggish" growth and "soft" or "subdued" economic activity.

Real gross domestic product (GDP) grew at an annual rate of 0.7 percent in the final quarter of 2002. This followed 4.0 percent growth in the third quarter and continued the irregular pattern of growth during the recovery. This pattern is influenced by the volatility of auto sales (due to dealer incentives). Exhibit 1 presents real GDP growth on both a quarter-to-quarter annualized basis (QA) and a year-over-year basis (Y-o-Y). The erratic nature of the recovery is evident in the ups and downs of the QA series during 2002. The year-over-year series shows that the recovery is real, but modest. The Chicago Fed National Activity Index indicates that the economy is growing below trend.[2]

[2] The Chicago Fed National Activity Index, produced by the Federal Reserve Bank of Chicago, is a weighted average of 85 indicators of national economic activity. It is constructed so that a value of 0 indicates the economy is expanding at its historical trend rate of growth. Values less than 0 indicate below-trend growth and values greater than 0 indicate above-trend growth.

Exhibit 2 presents another picture of the soft state of the economy. The GDP gap is defined as the percentage difference between actual GDP and potential GDP.[3] Also presented are the growth rates of actual GDP and potential GDP. In the late 1990s, the GDP gap was positive, meaning that the economy was producing above its "maximum sustainable level." This suggests that comparing the present situation to the late 1990s may not be a fair comparison. The recession shows up not as the shrinking of the positive gap or even as a negative gap. The recession shows up as a large negative GDP gap and an actual growth rate substantially less than the potential growth rate. The modest recovery is evident by positive actual growth. However, a recovery in which the economy grows slower than its potential does not feel like a recovery. A major reason for this is that the economy is not growing fast enough to generate new employment.

The soft spot is also evident in the Conference Board's index of coincident economic indicators. The coincident index, which describes where the economy is, was flat during the last quarter of 2002. Exhibit 3 shows the performance of the coincident index since January 1999. The index bottomed out in November 2001, suggesting that the recovery may have started then. The index slowly rose throughout 2002 until pausing in September. The four variables used in constructing the index (industrial production, real manufacturing and trade sales, real personal income less transfer payments, and nonagricultural employment) are the same variables used by the National Bureau of Economic Research (NBER) to date the business cycle. The performance of each of these variables is presented in Exhibit 4. Compared to March 2001, industrial production (IP) is down by 2.2 percent and nonagricultural employment (Emp) is down by 1.3 percent. Real personal income less transfers (Income) is up 0.9 percent and real manufacturing and trade sales are up 2.0 percent. The indicators suggest an economy that has stopped falling but is struggling to move forward.

The Conference Board's index of leading economic indicators, which describes where the economy is going, improved throughout the last quarter of 2002.[4] In December, eight of the ten variables used to calculate the leading index were up and two were down. Although the index often gives false signals, it generally turns down before a recession and up before an expansion. In its January 23 news release of the December index, the Conference Board noted "the leading index has improved for three straight months, suggesting a stronger economic recovery in the first half of 2003."

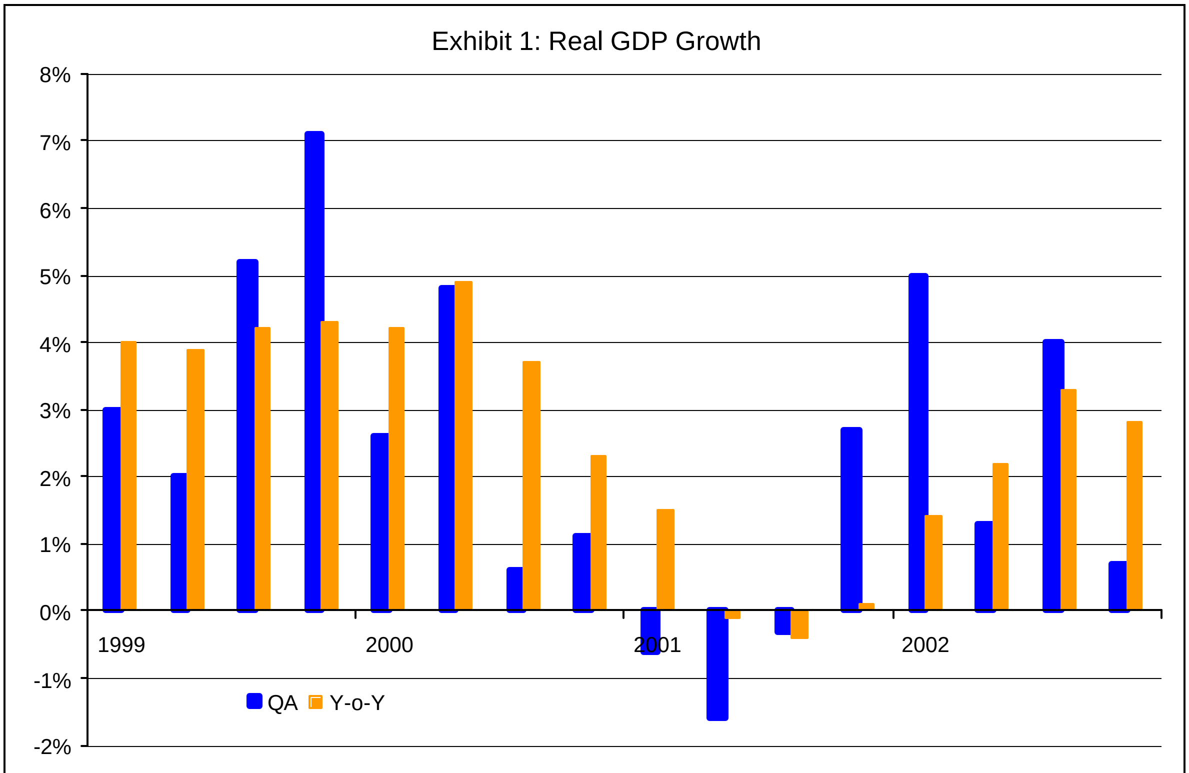
[3] Potential GDP is an estimate of an economy's maximum sustainable level of output. It is not the maximum level of output that can be produced, but is instead the level of GDP attainable when the economy is operating at a high rate of resource use. If actual output rises above its potential level, then constraints on capacity begin to bind and inflationary pressures build; if output falls below potential, then resources are lying idle and inflationary pressures abate.

[4] The leading index is a weighted average of 10 economic variables (average manufacturing workweek, jobless claims, new orders for consumer goods, new orders for capital goods, vendor performance, building permits, stock prices, money supply, interest rate spread, and consumer confidence) designed to predict near-term economic conditions.

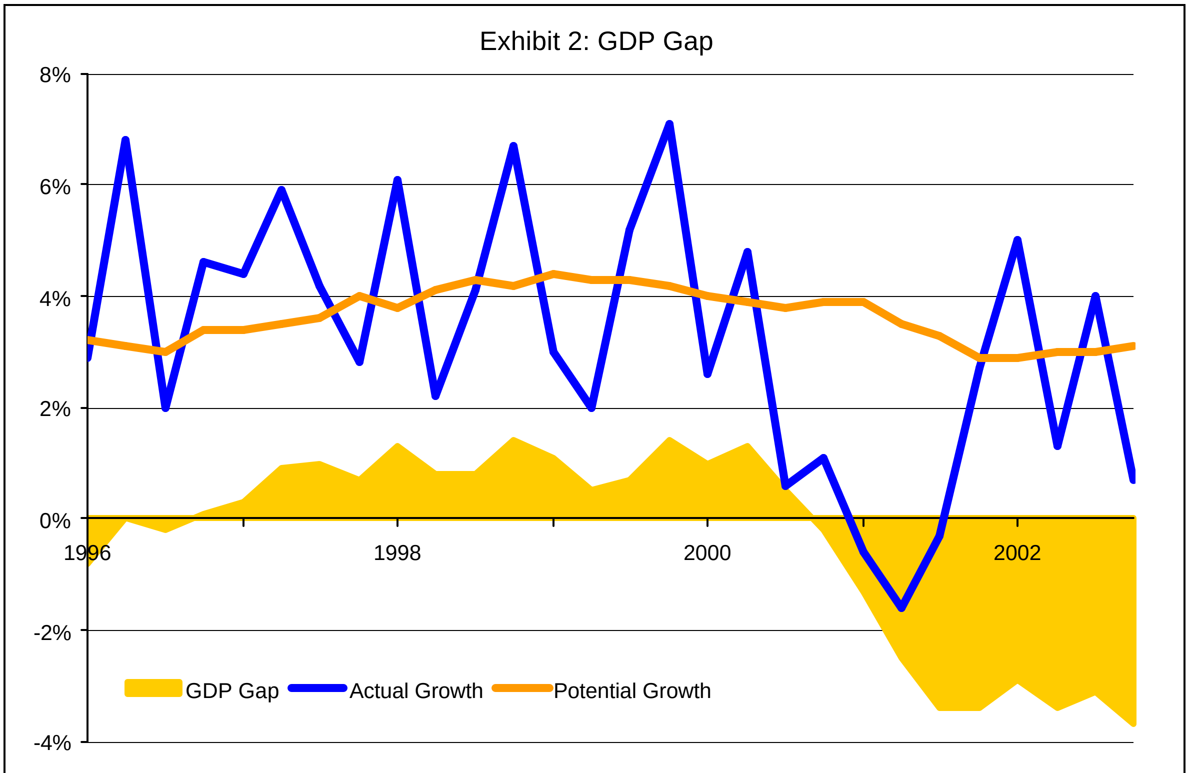
In its January 29 meeting, the FOMC again left the target federal funds rate at 1.25 percent. The committee noted that "oil price premiums and other aspects of geopolitical uncertainty have reportedly fostered continued restraint on spending and hiring by businesses" but "that as those risks lift, as most analysts expect, the accommodative stance of monetary policy, coupled with ongoing growth in productivity, will provide support to an improving economic climate over time."

As is generally the case around turning points in economic cycles, indicators are mixed. The housing market, helped by low mortgage rates, is healthy. Personal income continues to grow. Retail sales are strong, but not outstanding. Purchasing managers indices indicate increases in new orders, which should lead to increased production. Consumer confidence is down. Of course, it has been down for a while, but consumers have continued to spend. One worry is that low consumer confidence will finally lead to lower consumer spending. Industrial production has been flat since summer and capacity utilization is low. The employment situation has been dreary, with output growth insufficient to generate employment growth.

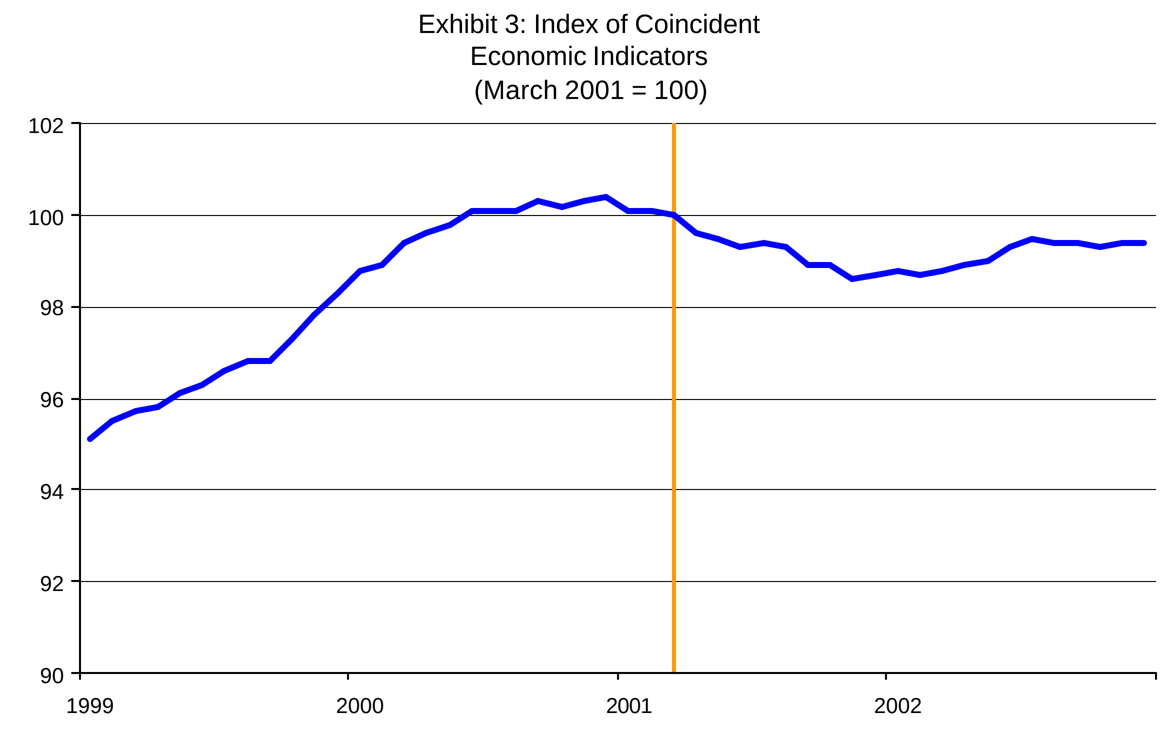
Although the economy began the year in a soft spot, it is not expected to remain there. The economy is forecasted to grow at a faster pace in 2003, but the forecast is subject to a number of risks. The Global Insight January forecast lists the following negative risks: the United States goes to war with Iraq; there is another major terrorist attack; the stock market takes another dive; the housing "bubble" bursts; the U.S. dollar crashes; and there is another financial crisis. One or more these could significantly undermine the economy's nascent recovery. Global Insight also notes two positive risks are: capital spending takes off; and Europe and Japan grow strongly. If either of these were to occur, the economic recovery could be a lot stronger than called for by the baseline forecast.



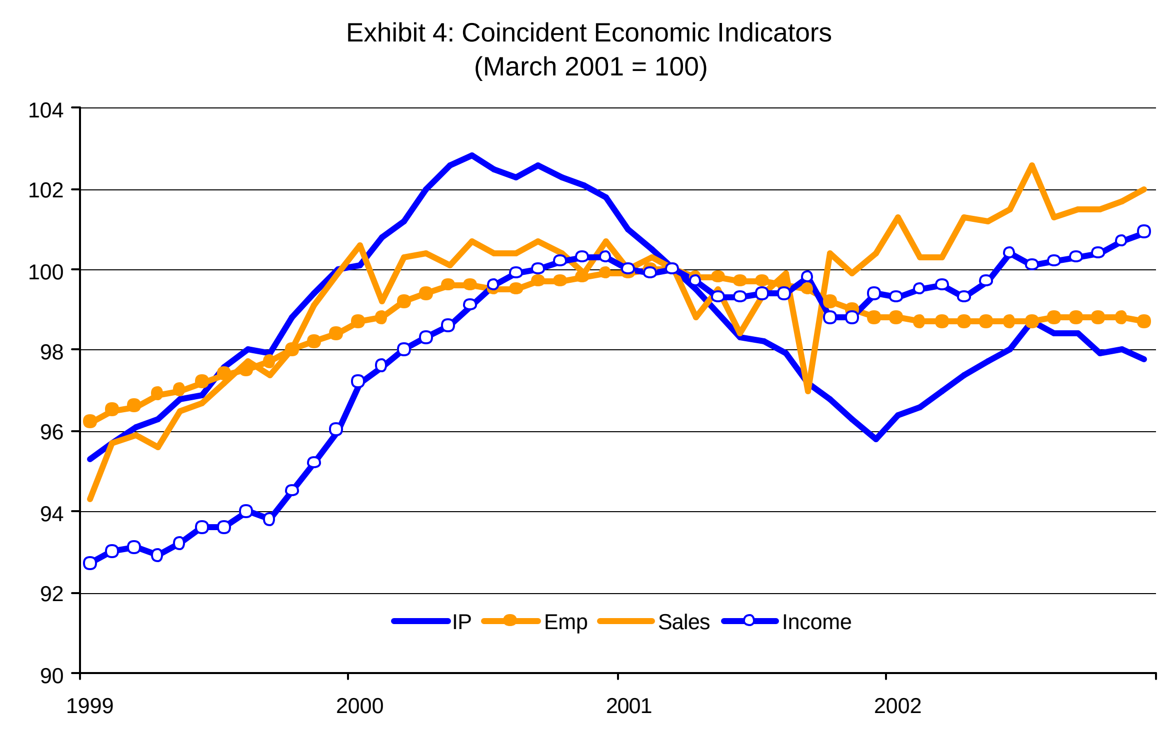
Source: U.S. Bureau of Economic Analysis



Source: U.S. Bureau of Economic Analysis, Global Insight, and LSC calculations



Source: NBER and LSC calculations



Source: NBER and LSC calculations

Economic Forecasts

The following tables contain forecasts from Global Insight and the Governor's Economic Advisory Council (GEAC). The Global Insight forecasts are from the January 2003 release (based on a model run in December 2002). The GEAC forecasts are from the November 2002 meeting. Global Insight presents its forecasts on both an annual (calendar year) and quarterly basis. The GEAC forecast is on a calendar year basis. The accompanying charts are based on actual values and the Global Insight quarterly forecasts.

Gross Domestic Product

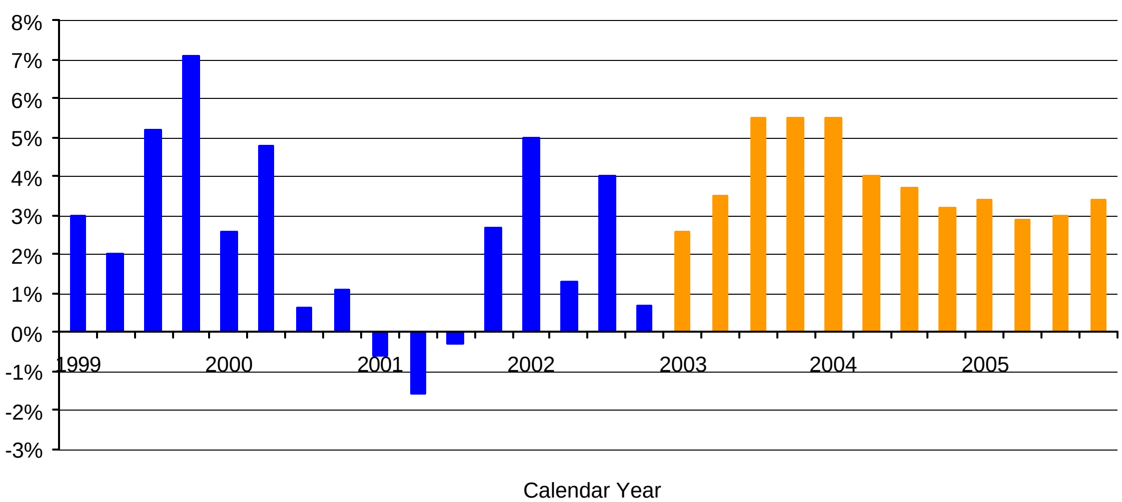
The most recent Global Insight forecast expects U.S. gross domestic product (GDP) to increase by 3.1 percent. Growth will be lower in the first quarter, but will pick up in the remainder of the year. Global Insight's forecast assumes that a war with Iraq starts in late January and lasts four to six weeks. Slower growth in consumer spending is offset by increased federal government spending, growth in business equipment spending, and a slower rate of decline in nonresidential construction. State and local government purchases are expected to fall in the first half of the year but increase slightly in the second half as revenues increase due to economic growth. In 2004, global economic recovery helps push U.S. growth to 4.7 percent, its highest rate since 1985.

Table 1 Real GDP Growth

	2003				2004				2005			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Global Insight	2.6	3.5	5.5	5.5	5.5	4.0	3.7	3.2	3.4	2.9	3.0	3.4
Global Insight	3.1				4.7				3.3			
GEAC	2.8				3.6				3.5			

Chart 1 depicts growth in real (inflation adjusted) gross domestic product from the first quarter of 1999 through the fourth quarter of 2002 along with the Global Insight forecast for growth starting with the first quarter of 2003.

Chart 1: Real GDP Growth



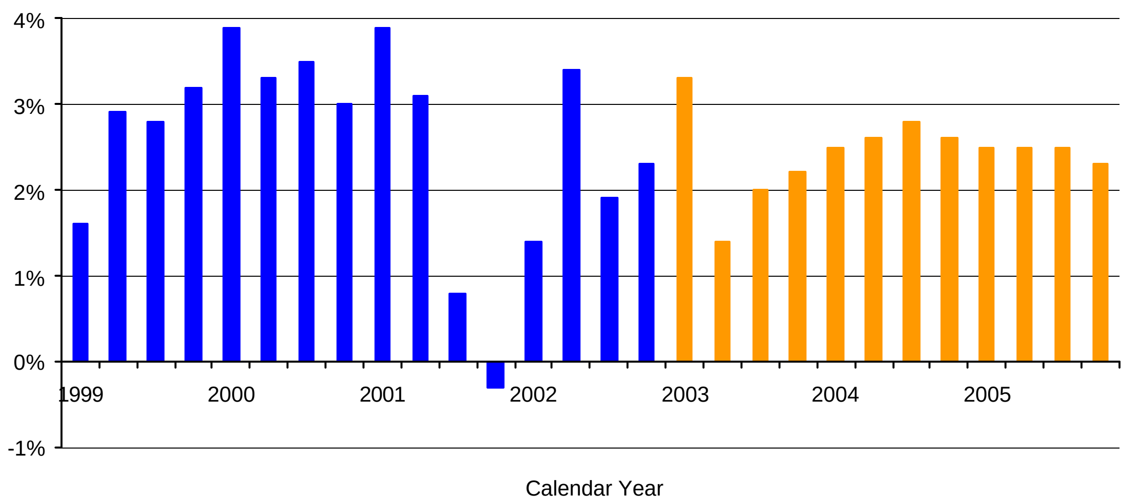
Inflation

Table 2 and Chart 2 contain information on inflation measured by changes in the Consumer Price Index (CPI). CPI inflation averaged 2.5 percent from the first quarter of 1999 through the last quarter of 2002. Inflation is not a major concern for policy makers. The forecasted jump in the first quarter of 2003 is due to an increase in oil prices. The increase in oil prices is due to the assumed war in Iraq and the assumption that output from Venezuela remains down. Oil prices are assumed to fall quickly upon successful completion of the war.

Table 2 CPI Inflation

	2003				2004				2005			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Global Insight	3.3	1.4	2.0	2.2	2.5	2.6	2.8	2.6	2.5	2.5	2.5	2.3
Global Insight		2.3				2.4				2.6		
GEAC		2.0				2.3				2.5		

Chart 2: CPI Inflation



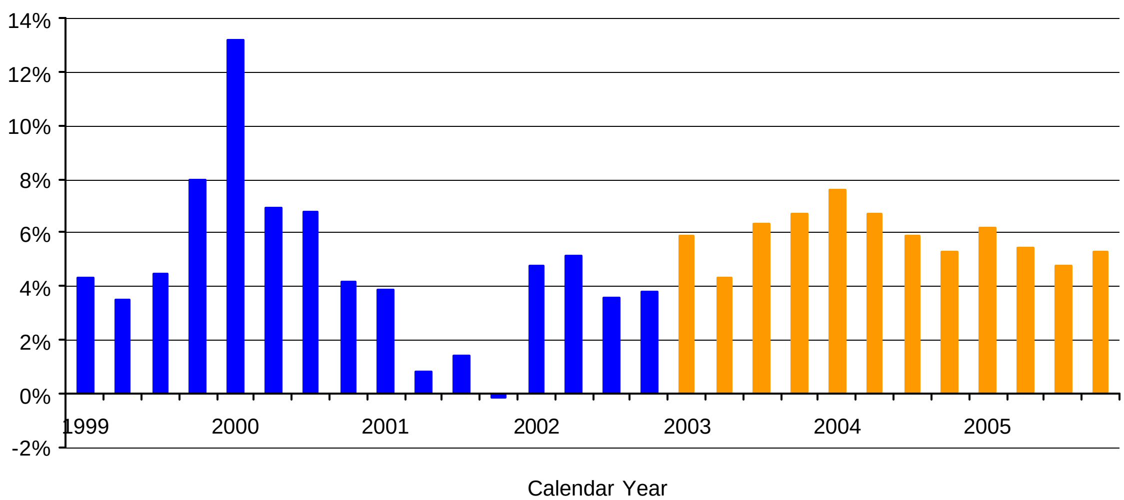
U.S. Income

Table 3 and Chart 3 contain information on growth in U.S. personal income. Personal income growth averaged 4.7 percent from the first quarter of 1999 through the last quarter of 2002.

Table 3 **U.S. Personal Income Growth**

	2003				2004				2005			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Global Insight	5.9	4.3	6.3	6.7	7.6	6.7	5.9	5.3	6.2	5.4	4.8	5.3
Global Insight		5.0				6.5				5.6		
GEAC		4.2				5.5				5.4		

Chart 3: U.S. Personal Income Growth



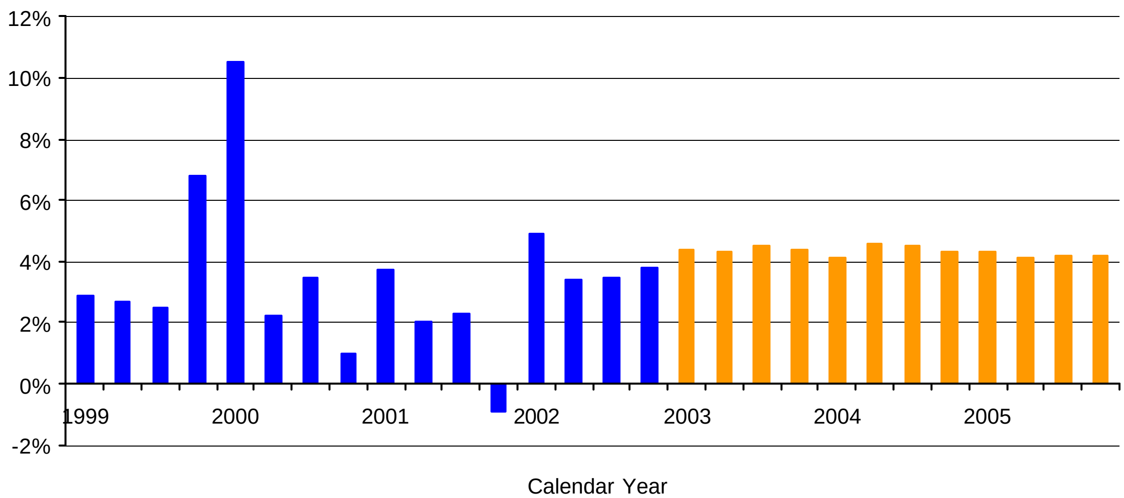
Ohio Income

Table 4 and Chart 4 contain information on growth in Ohio personal income. Personal income growth averaged 3.8 percent from the first quarter of 1999 through the last quarter of 2002.

Table 4 Ohio Personal Income Growth

	2003				2004				2005			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Global Insight	4.4	4.3	4.5	4.4	4.1	4.6	4.5	4.3	4.3	4.1	4.2	4.2
Global Insight	4.1				4.4				4.3			
GEAC	3.8				5.0				4.8			

Chart 4: Ohio Personal Income Growth



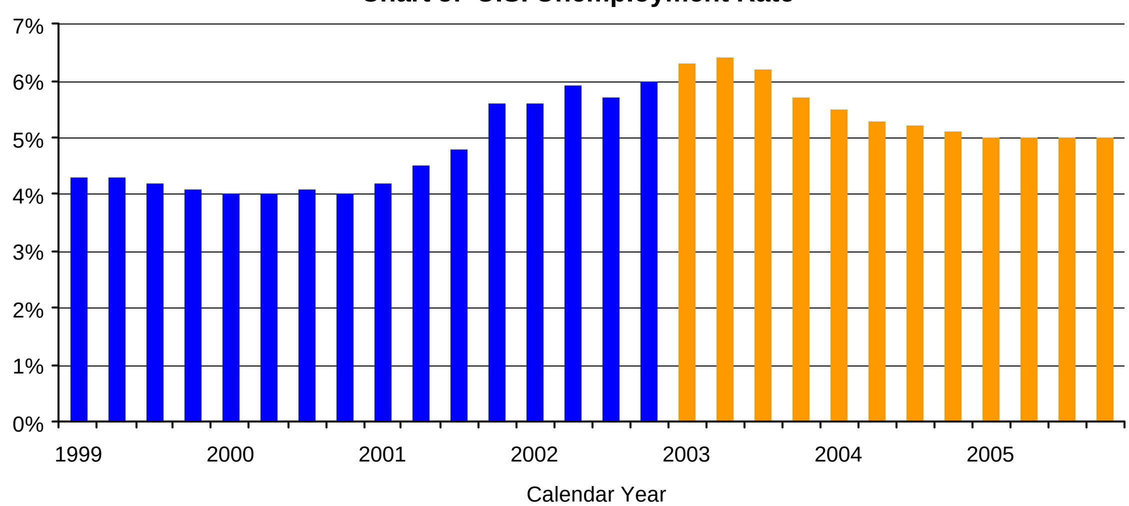
U.S. Unemployment Rate

Table 5 and Chart 5 contain information on the U.S. unemployment rate. The unemployment rate averaged 4.7 percent from the first quarter of 1999 through the last quarter of 2002. The rate is forecasted to rise in the first half of 2003 before falling as economic growth increases.

Table 5 U.S. Unemployment Rate

	2003				2004				2005			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Global Insight	6.3	6.4	6.2	5.7	5.5	5.3	5.2	5.1	5.0	5.0	5.0	5.0
Global Insight	6.2				5.3				5.0			
GEAC	5.8				5.4				5.0			

Chart 5: U.S. Unemployment Rate



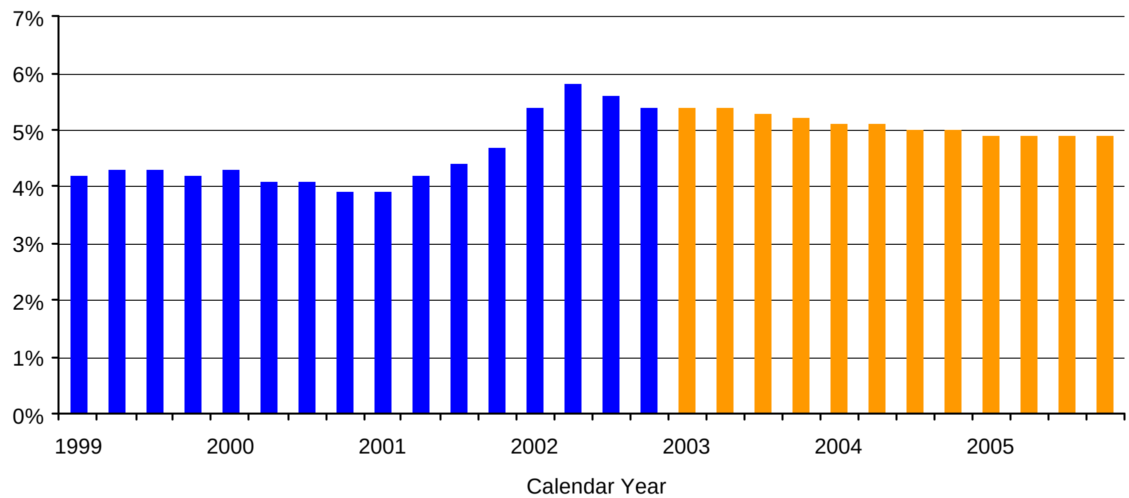
Ohio Unemployment Rate

Table 6 and Chart 6 contain information on the Ohio unemployment rate. The unemployment rate averaged 4.6 percent from the first quarter of 1999 through the last quarter of 2002. The rate is forecasted to fall throughout the year.

Table 6 Ohio Unemployment Rate

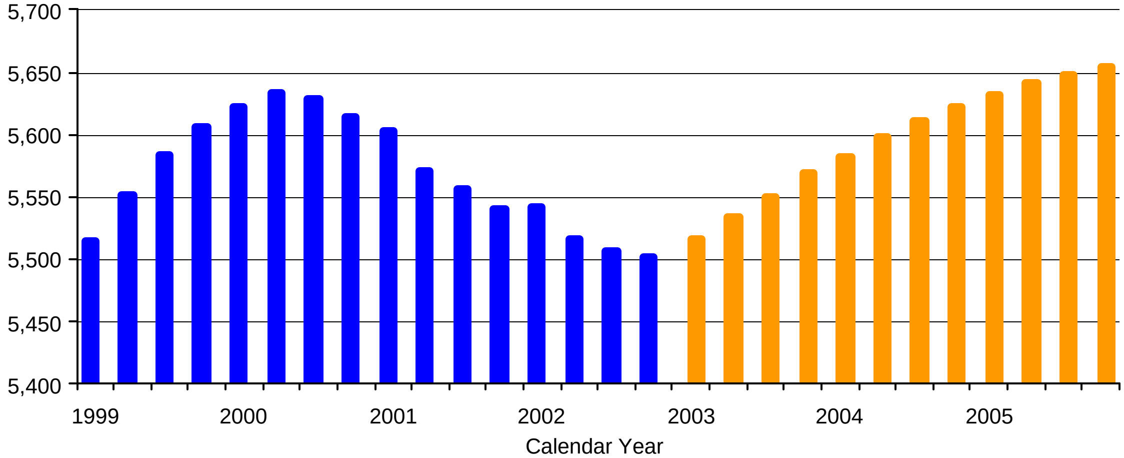
	2003				2004				2005			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Global Insight	5.4	5.4	5.3	5.2	5.1	5.1	5.0	5.0	4.9	4.9	4.9	4.9
Global Insight	5.3				5.0				4.9			
GEAC	5.6				5.3				4.9			

Chart 6: Ohio Unemployment Rate



However, the unemployment rate does not provide a full picture of the employment situation. Chart 7 presents the actual and forecasted level of establishment employment in Ohio. Employment peaked in the second quarter of 2000 and is forecasted to have bottomed out in the fourth quarter of 2002 at a level 132.4 thousand below the peak. Global Insight forecasts Ohio employment to increase throughout the forecast period, but it will not reach its earlier peak until the second quarter of 2005.

Chart 7: Ohio Establishment Employment
(in thousands, seasonally adjusted)



Tax Revenues

LSC expects lagging tax revenue growth for the remainder of FY 2003 with an acceleration in growth for FY 2004-2005. This pattern of revenue growth is dependent on the pattern of economic growth. The most recent economic forecast we have is for economic growth to pick up during the second half of 2003. The table below summarizes our tax revenue forecasts and provides information on revenue growth.

GRF Tax Revenues

Estimate for FY 2003, Forecast for FY 2004-2005

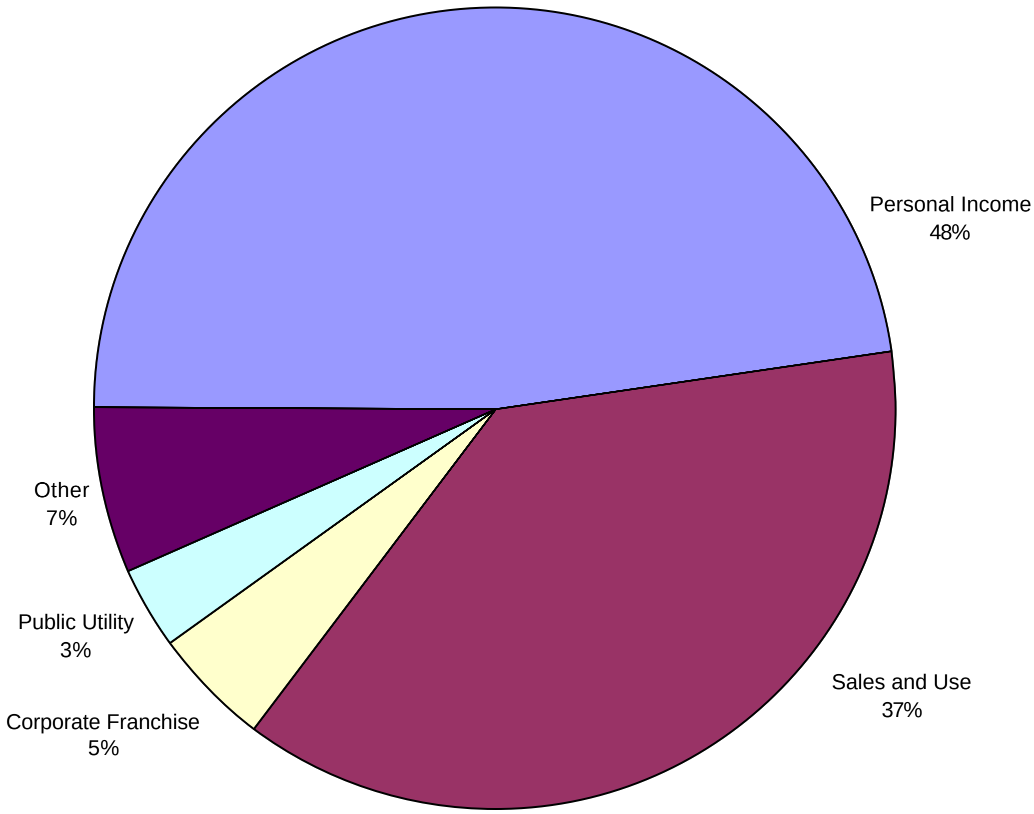
Dollar amounts in millions

Tax	2003	2004	2005	2003	2004	2005
Auto Sales	$914.0	$912.4	$922.0	-1.5%	-0.2%	1.1%
Non-Auto Sales & Use	$5,197.0	$5,381.5	$5,628.3	1.7%	3.6%	4.6%
Total Sales	$6,111.0	$6,293.9	$6,550.3	1.2%	3.0%	4.1%
Personal Income	$7,599.0	$7,987.1	$8,467.9	4.0%	5.1%	6.0%
Corporate Franchise	$690.0	$742.1	$821.5	-3.1%	7.6%	10.7%
Public Utility	$228.7	$239.3	$238.3	-12.1%	4.6%	-0.4%
Kilowatt Hour Excise	$339.5	$347.3	$354.8	5.0%	2.3%	2.2%
Total Major Taxes	**$14,968.2**	**$15,609.7**	**$16,432.8**	**2.3%**	**4.3%**	**5.3%**
Foreign Insurance	$194.1	$203.7	$211.9	-9.4%	4.9%	4.0%
Domestic Insurance	$161.6	$170.7	$178.3	22.0%	5.6%	4.5%
Business & Property	$49.0	$50.9	$52.8	592.6%	3.9%	3.7%
Cigarette	$585.0	$563.0	$555.0	108.0%	-4.3%	-1.4%
Alcoholic Beverage	$56.3	$56.7	$57.4	1.0%	0.7%	1.2%
Liquor Gallonage	$29.7	$29.9	$30.2	1.3%	0.7%	1.0%
Estate	$91.0	$69.0	$72.0	-21.7%	-24.2%	4.3%
Total Other Taxes	**$1,166.7**	**$1,143.9**	**$1,157.6**	**39.5%**	**-2.2%**	**1.2%**
Total Taxes	**$16,134.9**	**$16,753.6**	**$17,590.4**	**4.3%**	**3.8%**	**5.0%**

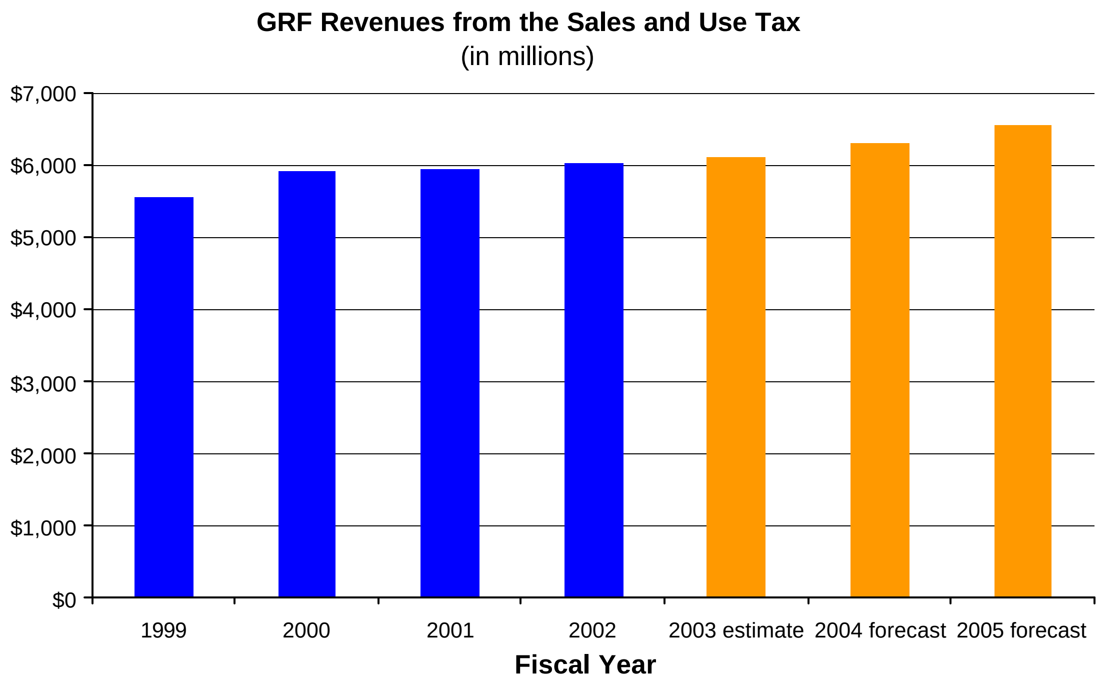
The "major taxes" are expected to account for over 90 percent of GRF tax revenues. The largest source is the personal income tax, which is forecasted to account for 48 percent of GRF tax revenues in the upcoming biennium. The sales tax is forecasted to account for 37 percent, the corporate franchise tax 5 percent, and public utilities taxes (the public utility excise tax and the kilowatt-hour tax) 3 percent. Because of the recent increase, the cigarette tax is expected to account for 3 percent of GRF tax revenues during the next biennium. The chart below presents the distribution of GRF tax revenues by source for the upcoming biennium.

GRF Tax Revenues by Source

FY 2004-2005



Sales and Use Tax



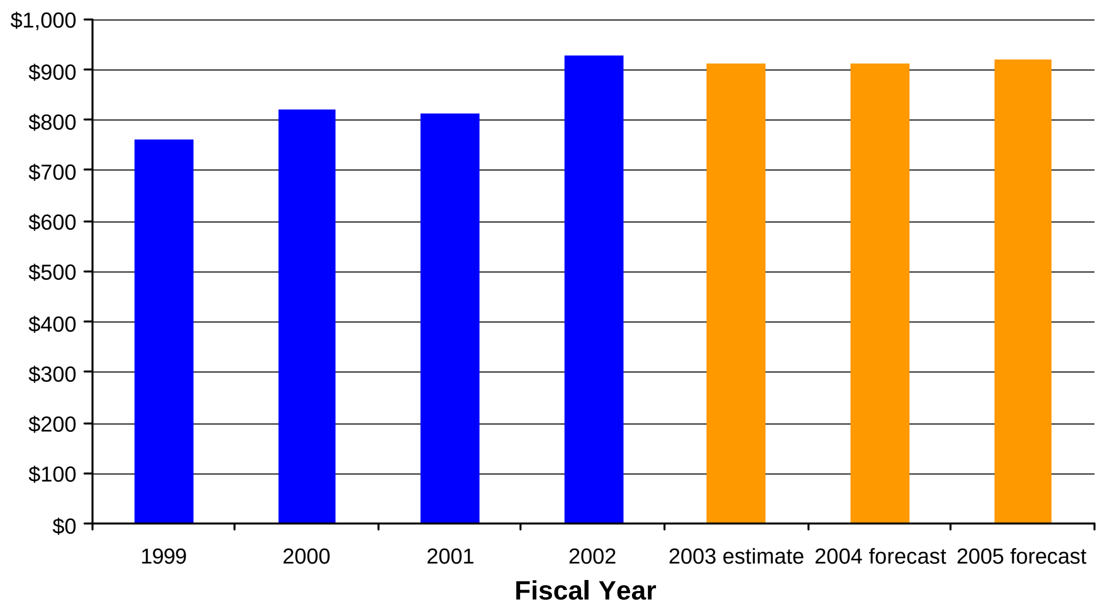
	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Sales and Use Tax	$5,545.3	$5,913.7	$5,935.6	$6,038.0	$6,111.0	$6,293.9	$6,550.3
growth	5.3%	6.6%	0.4%	1.7%	1.2%	3.0%	4.1%

The state sales and use tax is levied at a rate of 5 percent on retail sales of tangible personal property, rental of some tangible personal property, and selected services. Major exemptions include: food for human consumption off the premises where sold; newspapers and magazine subscriptions sent by second class mail; motor fuel (taxed separately); packaging and packaging equipment; prescription drugs and medical supplies; property used primarily in manufacturing or used directly in mining or agriculture; and credit for trade-ins on new motor vehicles.

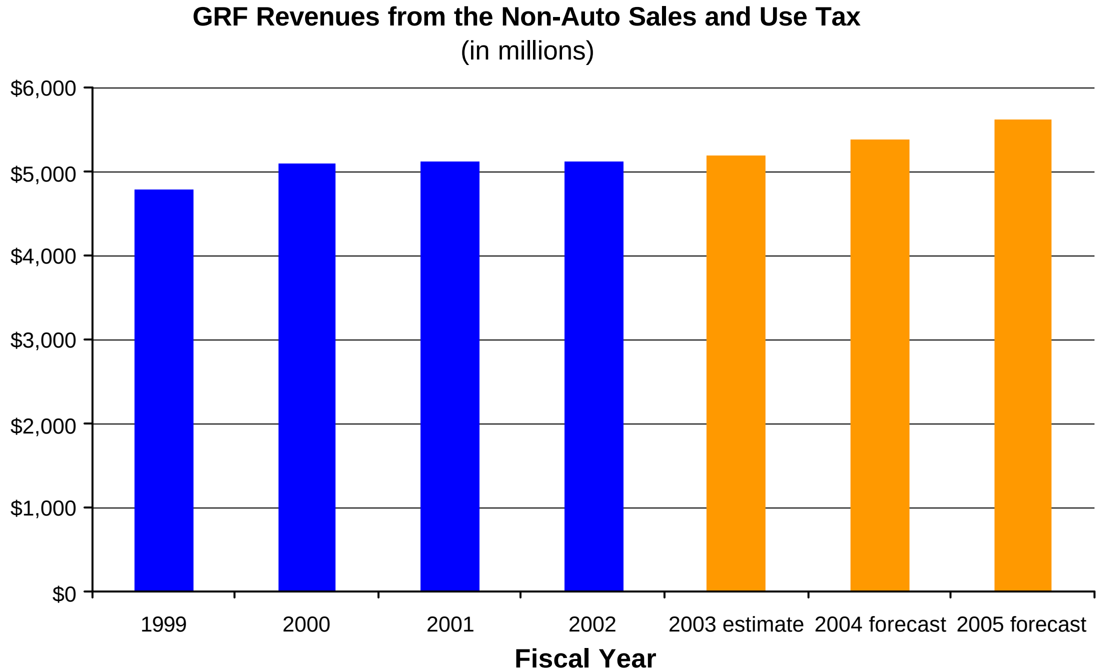
The revenue collected is disposed of as follows: 95.2 percent to the General Revenue Fund, 4.2 percent to the Local Government Fund, and 0.6 percent to the Local Government Revenue Assistance Fund. For forecasting purposes, the tax is separated into two parts: Auto and Non-Auto. Auto includes revenue collected from the sale or use of automobiles and trucks. Non-auto includes all other sales and use tax collections. Auto taxes arising from auto leases are paid immediately at the lease signing and mostly recorded under the non-auto tax, instead of the auto tax. The level of auto sales has become dependent on the level of incentives provided by manufacturers and dealers. The incentives have also changed the way consumers decide whether to purchase or lease their vehicles. As the share of vehicles leased and manufacturers' incentives have varied over the years, the auto tax has become more volatile. Also, those changes have affected the non-auto sales tax because taxes arising from leases are recorded under the non-auto sales tax.

The forecast for the sales and use tax revenue is based primarily on expected growth in Ohio personal income. Total sales and use tax receipts have stagnated in the last two fiscal years. The non-auto sales and use tax portion has shown little or no growth, while auto tax revenues have increased. The forecast shows a growth in tax receipts from the non-auto sales and use tax. The forecast for non-auto sales and use tax is based on a regression of non-auto sales tax revenue against Ohio personal income, housing starts and manufacturing employment. The results were adjusted for the negative impact on non-auto sales and use tax revenues of the growth in retail e-commerce sales. The forecast for auto sales tax is based on a regression of auto sales tax revenues against expected consumer spending on purchased and leased vehicles.

GRF Revenues from the Auto Sales Tax
(in millions)

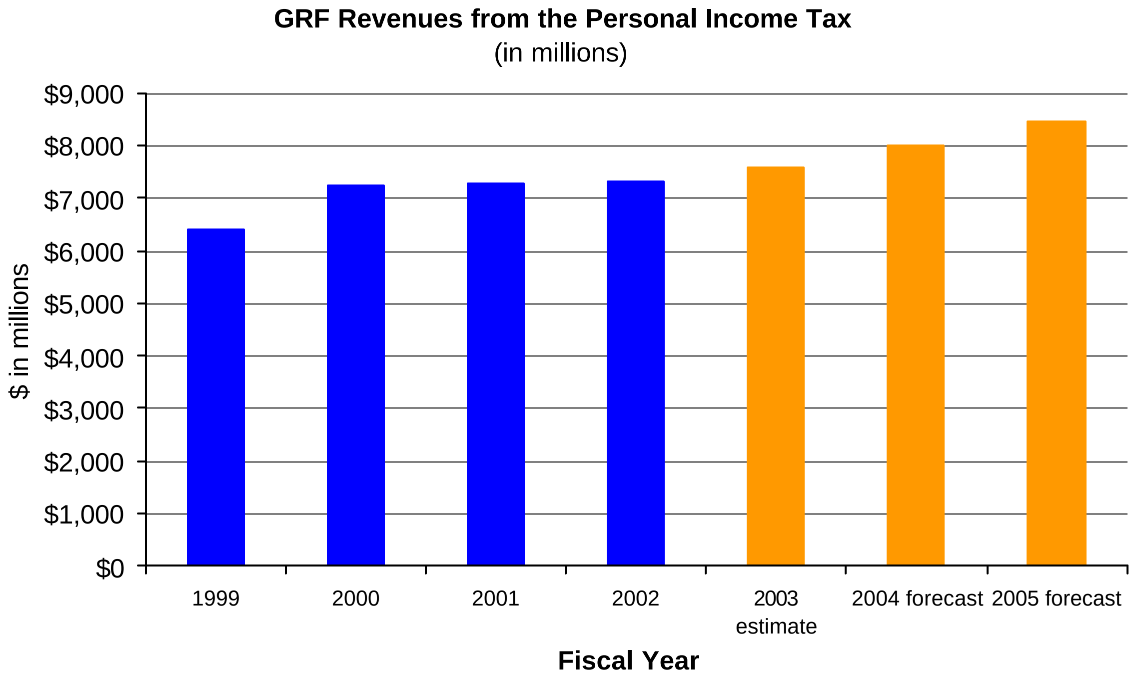


	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Auto Sales Tax	$760.4	$821.7	$811.5	$927.5	$914.0	$912.4	$922.0
growth	5.2%	8.1%	-1.2%	14.3%	-1.5%	-0.2%	1.1%



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Non-Auto Sales & Use Tax	$4,784.9	$5,092.0	$5,124.1	$5,110.4	$5,197.0	$5,381.5	$5,628.3
growth	5.3%	6.4%	0.6%	-0.3%	1.7%	3.6%	4.6%

Personal Income Tax



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Personal Income Tax	$6,416.8	$7,232.0	$7,263.4	$7,304.1	$7,599.0	$7,987.1	$8,467.9
growth	3.3%	12.7%	0.4%	0.6%	4.0%	5.1%	6.0%

The Personal Income Tax is levied on Ohio taxable income (the amount reported as federal adjusted gross income (FAGI) to the U.S. Internal Revenue Service plus or minus adjustments). After these adjustments are made, a taxpayer's tax liability before credits is obtained by applying Ohio's graduated tax rates to the taxpayer's Ohio taxable income. Certain credits may be subtracted from this amount to arrive at the taxpayer's final tax liability.

Major additions to FAGI in the determination of Ohio adjusted gross income include: state and local bond interest (except Ohio governments), federal bond interest exempt from federal tax but subject to state tax, and accumulation distribution from a complex trust. Major subtractions include: federal bond interest, disability and survivors' benefits included in FAGI, compensation earned in Ohio by residents of reciprocity states, social security and railroad retirement benefits included in FAGI, and state and municipal tax refunds.

Ohio taxable income is obtained by subtracting personal exemptions from Ohio adjusted gross income. Taxpayers may claim an exemption for the taxpayer, the taxpayer's spouse (if filing a joint return), dependent children, and others to whom the taxpayer provides support and claims on the taxpayer's federal return. For tax year 2002, the personal and dependent exemption is $1,200. This amount is indexed for inflation and is expected to increase each year.

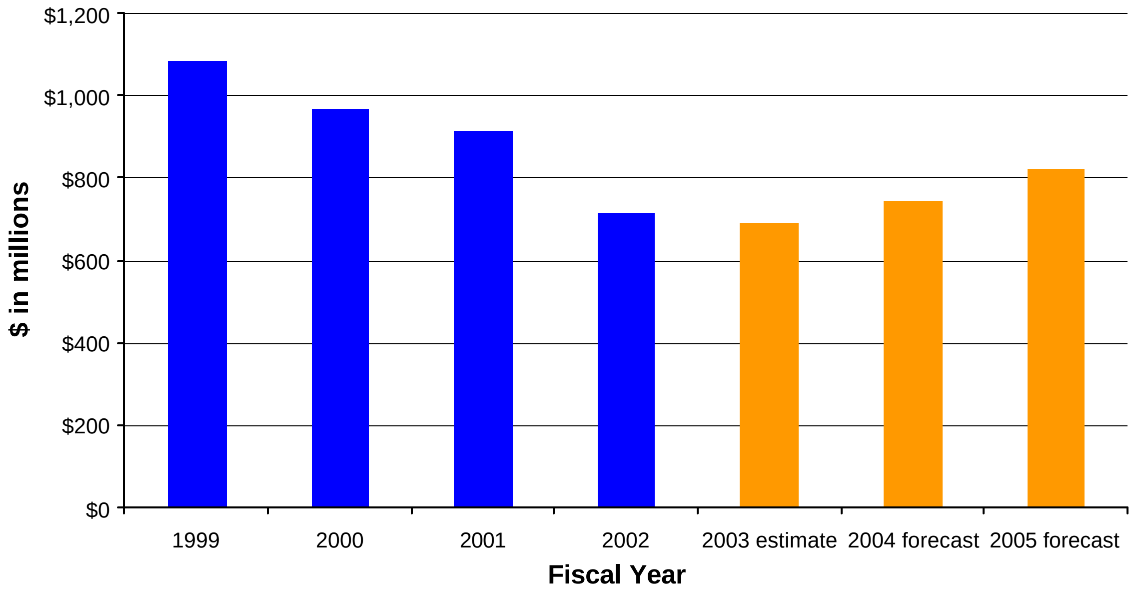
The taxpayer's tax liability before credits is obtained by applying graduated rates to the taxpayer's Ohio taxable income. Ohio's statutory tax rates range from 0.743 percent on the first $5,000 of Ohio taxable income to 7.5 percent on Ohio taxable income in excess of $200,000. For tax years 1996-2000, these rates were reduced by rate cuts paid for out of the Income Tax Reduction Fund (ITRF). The ITRF tax rebate mechanism is structured to give unanticipated surpluses back to taxpayers. If there is no surplus, there is no rate reduction.

Major credits available to taxpayers include: the personal exemption credit of $20 per exemption, the senior citizen credit of $50 per return, the retirement income credit, the child and dependent care credit, various business credits, the displaced worker training credit, the political contribution credit, the adoption credit, and the joint filer credit for two working spouses (graduated based on income with a maximum credit of $650).
Statutorily, the revenue collected is disposed of as follows: 89.5 percent to the General Revenue Fund, 4.2 percent to the Local Government Fund, 0.6 percent to the Local Government Revenue Assistance Fund, and 5.7 percent to the Library and Local Government Support Fund. The FY 2002-2003 biennial budget bill temporarily froze distributions to the three local government funds at their FY 2001 levels.

The estimated revenue for FY 2003 is a revision of the OBM July 2002 estimates. The revision assumed that the trend for the last calendar quarter of 2002 would persist for the final two quarters of FY 2003. For FY 2004 and FY 2005, the estimate for FY 2003 was grown based on the results of a model of revenue collections. The model works with the four components of the tax collections as reported in Table 44 of the Department of Taxation's Annual Report. The components are: employer withholding (partial-weekly, monthly, quarterly, and annual returns), individual taxpayer (quarterly estimated payments and annual returns), other collections (Attorney General collections, assessments, and bad checks), and refunds. The data was organized on a fiscal year basis. Withholding was assumed to be a function of Ohio wage and salary income. The individual taxpayer component was assumed to be a function of the S&P 500 index (used to represent U.S. stock markets), and combined Ohio rent, interest, dividend, and proprietors' income. Other collections were assumed to be a function of the same variables as for the individual taxpayer component plus a trend variable. Refunds were assumed to be a function of gross collections (employer withholding + individual taxpayer + other collections), the value of the personal and dependent exemption, and the ITRF percentage rate cut. Forecasted values of the explanatory variables were taken from the Global Insight January 2003 release.

The revenue data used for estimation did not include the new tax on trusts. (S.B. 261 of the 124th General Assembly included income from trusts in the personal income tax base for tax years 2002 through 2005.) An estimate of the revenue from the tax on trusts was added separately. The local funds freeze was assumed to expire, so the forecasted GRF amounts reported are 89.5 percent of gross collections minus refunds.

Corporate Franchise Tax

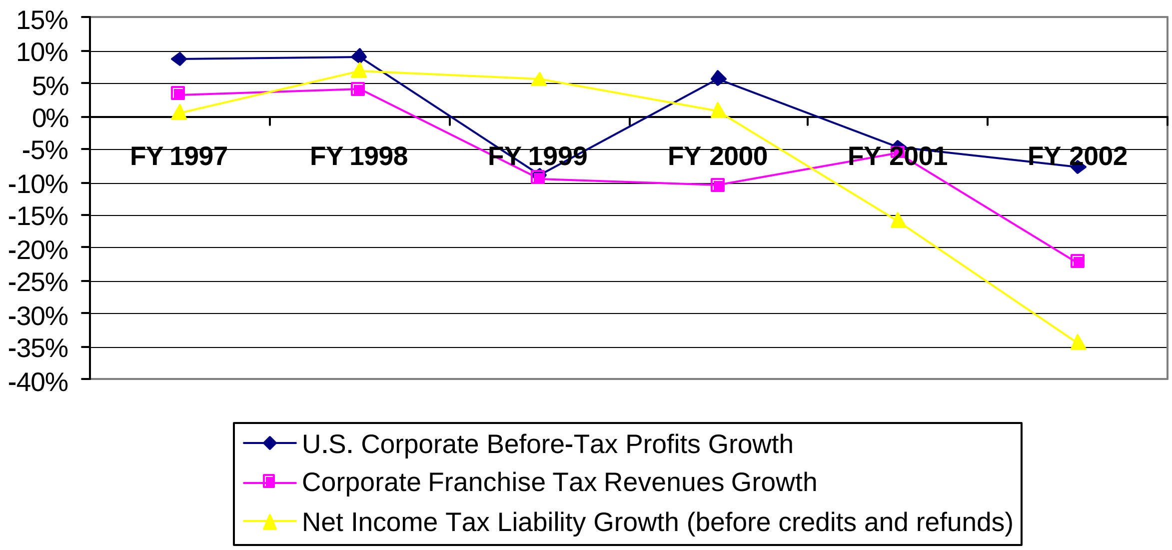


	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Corporate Franchise	$1,084.1	$969.4	$915.3	$712.3	$690.0	$742.1	$821.5
growth	-9.4%	-10.6%	-5.6%	-22.2%	-3.1%	7.6%	10.7%

The franchise tax has two bases: the net worth base (generally determined as net book value of assets minus the net carrying value of liability) and the net income base (generally, the Ohio portion of the federal taxable income with exclusions and additions as required by statute). Differing tax rates apply to each tax base. The corporate taxpayer calculates its Ohio tax liability under the two bases and pays the higher of the two tax liabilities. H.B. 215 (FY 1998-1999 Operating Budget) decreased the net worth tax rate from 5.82 mills to 4 mills and capped the net worth tax liability at $150,000 for each corporation, effective in FY 1999. The full impact of those net worth tax changes have decreased the cushioning effect of the net worth tax base on franchise tax revenues in an environment of lower corporate net income and profits. In addition, more and more new firms are taking advantage of alternative forms of business organization (such as limited liability company), which are not generally subject to the corporate franchise tax. Instead, this net business income is taxed under the personal income tax as a pass-through entity, which has helped contribute to increased volatility in that tax.

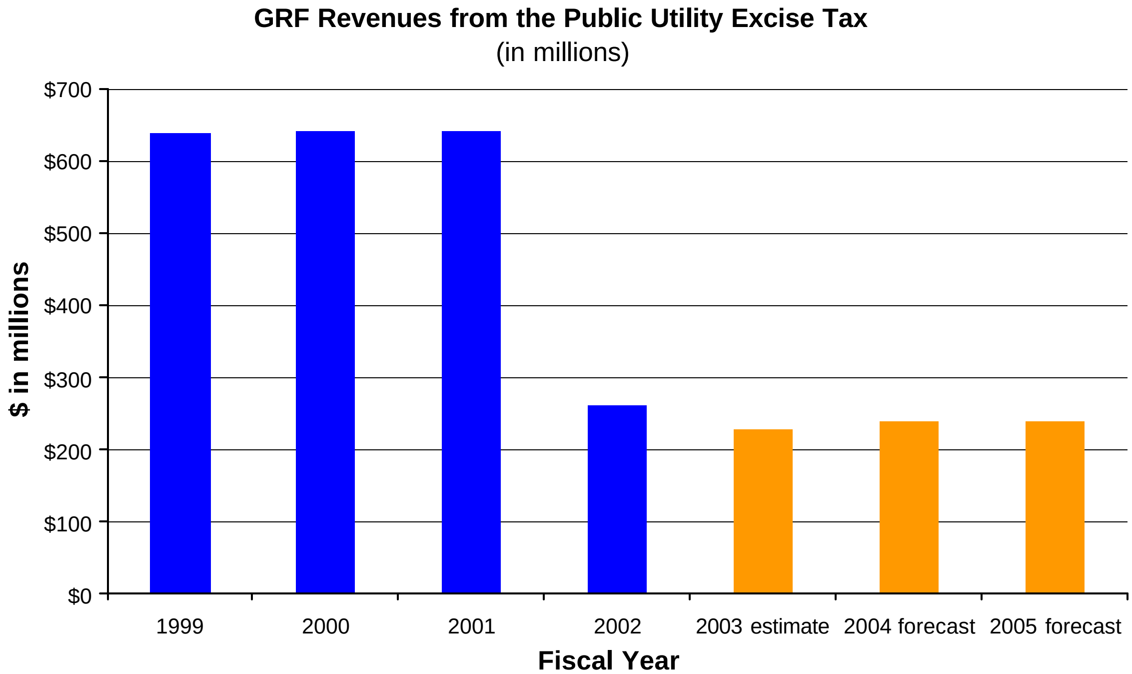
LSC derives its forecasts of baseline corporate franchise tax (CFT) revenues from projections of U.S. corporate profits. Translating a corporate profits forecast into a franchise tax forecast is not straightforward because of the dual base of the franchise tax (net worth or net income), the fact that corporations often have taxable years that do not coincide with calendar years, and corporations' decisions on the timing and use of statutory tax credits. In the past, the net worth tax base kept revenues from falling as sharply as profits in recessions or downturns. During the current downturn, it has had less of a cushioning effect. The cap on net worth tax liability of $150,000 shifted many of the corporations to the net income basis (which is not capped). This caused franchise tax revenues to decline greatly as corporate profits fell and the net income tax liability fell. Regardless of a firm's net worth, its net worth liability would at most be the cap amount.

Growth in corporate franchise tax revenues and corporate profits



An analysis of tax revenues in the last few years shows that the elasticity of the corporate franchise tax revenues with respect to U.S. corporate profits has increased. The graph also suggests that this elasticity is asymmetrical. During a period of economic growth, the growth in corporation franchise tax revenues is slower than the growth in U.S. corporate profits. During a downturn, the decline in Ohio franchise tax revenues would be larger than the decline in U.S. before-tax profits. Forecasted corporate franchise tax revenues are based on the profit forecast and elasticity estimates for the next two years. LSC expects a negative growth in franchise tax revenues in FY 2003. U.S. before-tax profits are forecasted to grow 12.6 percent in 2003 and 17.8 percent in 2004. Ohio franchise tax revenues are expected to grow at the rates of 7.6 percent in FY 2004 and 10.7 percent in FY 2005.

Public Utility Excise Tax



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Public Utility	$637.6	$642.1	$640.5	$260.1	$228.7	$239.3	$238.3
growth	-5.3%	0.7%	-0.2%	-59.4%	-12.1%	4.6%	-0.4%

The public utility excise tax -- also known as the gross receipts tax -- is a tax on the intrastate revenues of public utilities. The tax is levied on local telephone companies, natural gas utilities, pipeline companies, heating companies, waterworks, and water transportation companies. All companies subject to the tax pay a tax of 4.75 percent of gross receipts except pipeline companies, who pay a tax of 6.75 percent of gross receipts. Historically the largest single contribution to the tax came from electric companies, but they were removed from the tax by S.B. 3 of the 123rd G.A., which accounts for the sharp drop in tax receipts shown in the graph above for FY 2002. The tax receipts lost because of dropping electric companies from this tax were intended to be replaced by corporate franchise tax payments and by payments to the newly created kilowatt-hour tax, which was created by S.B. 3. Thus, receipts under the kilowatt-hour tax are somewhat less than the amount historically paid by electric companies under this tax.

In FY 2002 natural gas companies accounted for 55.1 percent of the receipts under the tax, local telephone companies accounted for 39.8 percent of the receipts, and electric utilities accounted for 4.0 percent of the tax with their last payment in November of 2001. During FY 2003 electric companies received refunds worth $11.6 million through December under the tax. A Department of Taxation official reports that it is expected that electric companies have now received all the refunds they are due under the tax, so the forecast assumes no receipts from or refunds to electric utilities after December 2002. Because all other utility companies accounted for under 1.5 percent of receipts in FY 2002, the discussion that follows will be restricted to the assumptions underlying the forecast for the receipts from natural gas companies and from local telephone companies.

Natural Gas Utilities

Natural gas utilities paid $143.3 million under the tax in FY 2002. The tax is paid by utilities, not marketers. Non-utility companies that sell gas on a retail basis under the Choice Program do not pay the tax, but they are supposed to collect sales tax on their sales. Most industrial customers are in practice exempt from the sales tax due to the exemption for direct use in manufacturing. Participation in the Choice Program has grown gradually: as of December 2002, 40.1 percent of residential customers statewide were enrolled in a Choice Program compared with 39.0 percent in February 2002. Similarly, 39.6 percent of commercial customers were enrolled in a Choice Program in December 2002, up from 38.6 percent in February 2002. In both cases, the share of natural gas customers still subject to the tax (i.e., those not enrolled in a Choice Program) in December was 98.3 percent of the share subject to the tax in February. This trend is projected to continue, with the percentage of households subject to the tax in FY 2004 being 98.3 percent of the percentage subject to the tax in FY 2003, and similarly in FY 2005. While we believe that enrollment increases in Choice Programs are the most likely outcome over the next two years, unexpected news could swing customers away from them, or accelerate the recent enrollment trend, in a dramatic fashion. That would change receipts for this tax, but it should be balanced by changes in sales tax receipts in the opposite direction.

Even more than the effects of enrollment in a Choice Program, the receipts from the tax depend on changes in the market price of natural gas and the volume of gas used. Forecasts of these changes are taken from the Global Insight (formerly DRI-WEFA) economic forecast for the U.S. published in January 2003. The following table presents the Global Insight forecasts of natural gas usage and price changes nationwide between the first quarter of the preceding calendar year to the first quarter of the year shown in the table:

DRI-WEFA forecast of changes in U.S. natural gas prices, volumes used		
Year	**Price**	**Volume**
2003	12.9%	5.8%
2004	-4.2%	2.8%
2005	0.9%	1.3%

The relatively high growth in both price and volumes from the first quarter of (CY) 2002 to the first quarter of 2003 is due to unusually cold winter temperatures in most of the country east of the Rocky Mountains. The effects of this relatively cold weather will continue to be felt in FY 2004, and customers who are on a budget plan will likely have to pay an increased amount toward the end of the budget plan period, which shows up in tax receipts received by the state in August.

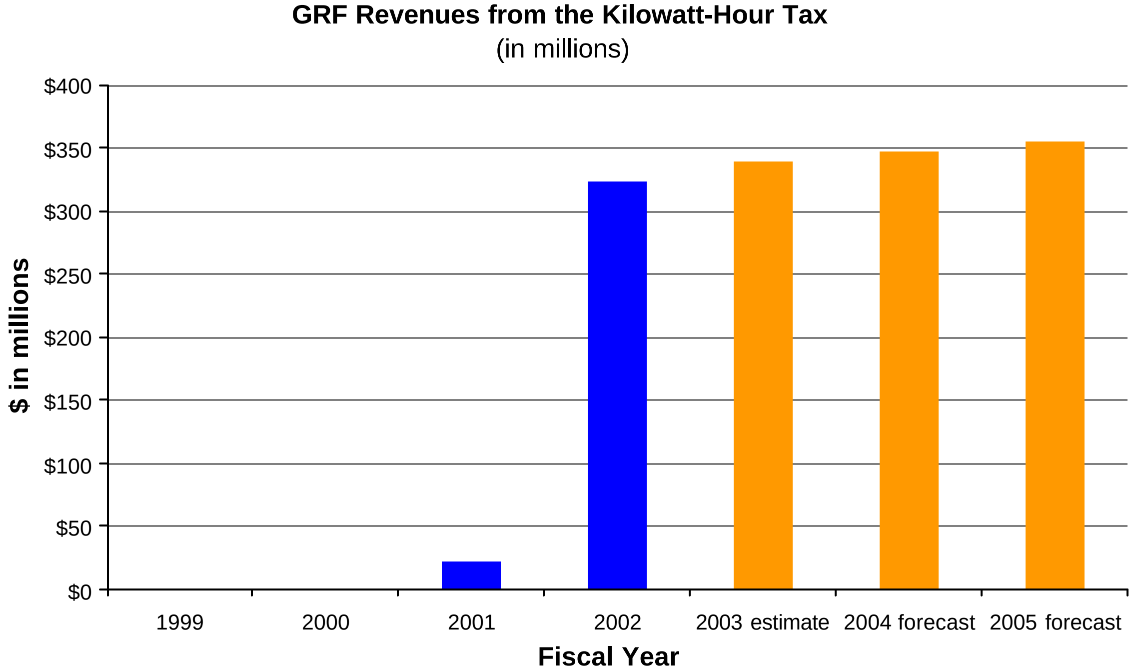
The natural gas forecast applies the Choice Program adjustment factor described above along with the growth rates in the table to arrive at a forecast of $127.8 million in FY 2003, $128.8 million in FY 2004, and $129.4 million in FY 2005.

Local Telephone Companies

Local telephone companies paid $103.4 million under the tax in FY 2002. The tax applies to local companies like SBC/Ameritech and Cincinnati Bell, but not to cellular or long-distance companies. It also does not apply to emerging companies that offer local telephone services using network resources that belong to a local telephone company, who are referred to in the industry as competitive local exchange carriers. Sales by these carriers, wireless companies, and long-distance companies are taxed under the sales tax.

The amount paid by local telephone companies has fallen for two straight fiscal years going into FY 2003, but data on receipts through the first half of this fiscal year indicate that receipts will grow to a projected $108.6 million this year. This projected increase is based heavily on a reduction in refunds to utilities in November 2002 compared with November 2001. This reduction seems to be due to telephone utilities losing less market share to competitors who are not subject to the tax than was expected when advance tax payments were made. Nevertheless, data from the Federal Communications Commission indicate that local telephone companies lost market share for analog business lines in both 2000 and 2001, while they lost market share for residential lines in 2001. Therefore tax receipts from local telephone companies are projected to resume their former downward trend after FY 2003, falling by 1.5 percent per year. This yields a forecast of $107.0 million in FY 2004 and $105.3 million in FY 2005.

Kilowatt-Hour Tax



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Kilowatt Hour Excise Tax	no tax	no tax	$22.8	$323.3	$339.5	$347.3	$354.8
growth	na	na	na	1317.8%	5.0%	2.3%	2.2%

The kilowatt-hour tax was created in S.B. 3 of the 123rd G.A., and revenues from the tax began to be received in May 2001. The tax is levied on distribution companies, which remain regulated, and which include the tax in the rates that they charge for distributing electricity. The tax rate depends on the volume of electricity used by the customer. There are three distinct marginal tax rates, $.00465 per kilowatt-hour (kWh) for the first 2,000 kilowatt-hours consumed in a month, $.00419 per kWh for the next 13,000 kilowatt-hours consumed, and $.00363 per kWh for all kWhs consumed over 15,000. Very large users, those that use over 45 million kWhs per year, have the option of self-assessing, which enables them to pay a still-lower rate of $.00075 per kWh (up to the first 504 million kWhs consumed) plus 4 percent of the price.

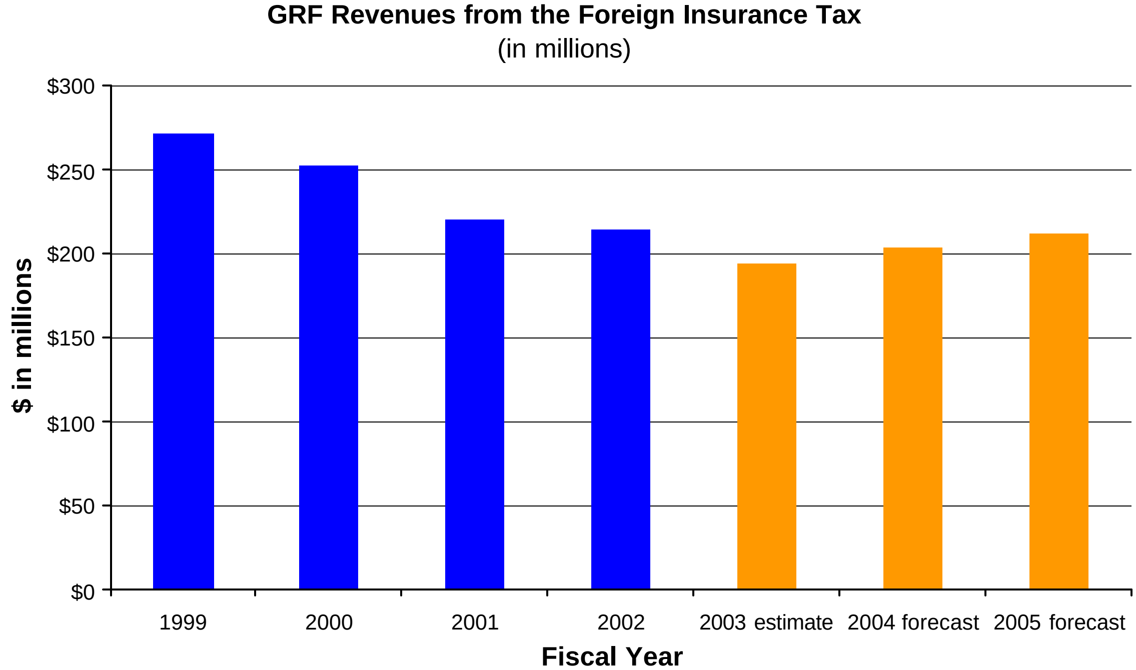
Because of the relative newness of the tax there is little historical data on revenues to use in forecasting future revenues. In addition, data on electricity usage from the Energy Information Administration (EIA) within the U.S. Department of Energy are provided by customer classes -- residential, commercial, and industrial -- that do not correspond precisely to the classifications used to determine the tax rate as described above. On the other hand, the tax base is one that grows fairly steadily and is not directly affected by possibly volatile swings in prices, a factor that is helpful for forecasting.

The revenue for FY 2003 through December has grown by 5.1 percent over the corresponding period in FY 2002. This growth rate is essentially assumed to hold for the remainder of the fiscal year due to the colder than average temperatures experienced through January, with a very slight drop in the growth rate in the spring. Thus revenue for fiscal year 2003 is forecast to grow by 5.0 percent over the FY 2002 figures.

The forecast for FY 2004 and 2005 begins by estimating the share of the tax paid by residential, commercial, and industrial customers. The estimate assumes that residential customers pay the highest tax rate, commercial customers pay the middle rate, and industrial customers pay the lowest tax rate. Under this assumption, their respective shares of revenue paid work out to 33.7 percent, 28.2 percent, and 38.1 percent. This may overestimate the share paid by industrial customers, since some industrial customers pay based on the lower self-assessors' rate. To the extent that it does so, revenues will be underestimated, since the growth rate assumed for industrial usage is the lowest of the three categories.

The most recent data available from the EIA report that residential consumer usage grew by 2.3 percent per year, on average, from 1990 to 1999. The comparable data for commercial users was 2.9 percent and for industrial users it was 0.7 percent. The historical growth rate for industrial users was falling during the second half of the 1990s when growth in manufacturing was slowing significantly; the average growth rate from 1990 to 1994 was 1.5 percent. Because the period 1990 through 1994 was a period of slow recovery from a recession, just as the FY 2004 and 2005 period is forecast to be, the growth rate assumed for industrial users for the biennium is 1.5 percent per year. The growth rates used in the forecast for residential and commercial users start with the respective average rates for 1990 through 1999. For the FY 2004 forecast, these averages are adjusted for weather and business cycle factors using the Global Insight (formerly DRI-WEFA) forecast of national growth in demand for electricity; for FY 2005 the averages are not adjusted, implicitly assuming normal weather patterns and average economic growth. The overall growth rates for revenue forecast using this method are 2.3 percent in FY 2004 and 2.2 percent in FY 2005.

Foreign Insurance Tax



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Foreign Insurance	$271.6	$252.3	$220.6	$214.3	$194.1	$203.7	$211.9
growth	-3.3%	-7.1%	-12.6%	-2.8%	-9.4%	4.9%	4.0%

As with the domestic insurance tax, the new tax structure created in Am. Sub. H.B. 215 of the 122nd G.A. is in place for the first time in FY 2003, after a five-year phase-in schedule. The new tax structure is the same as the tax structure for the domestic insurance tax: in FY 2003, foreign insurance companies that are health insuring corporations (HICs) will pay a tax of 1.0 percent of premiums, while other foreign insurance companies will pay a tax of 1.4 percent of premiums.

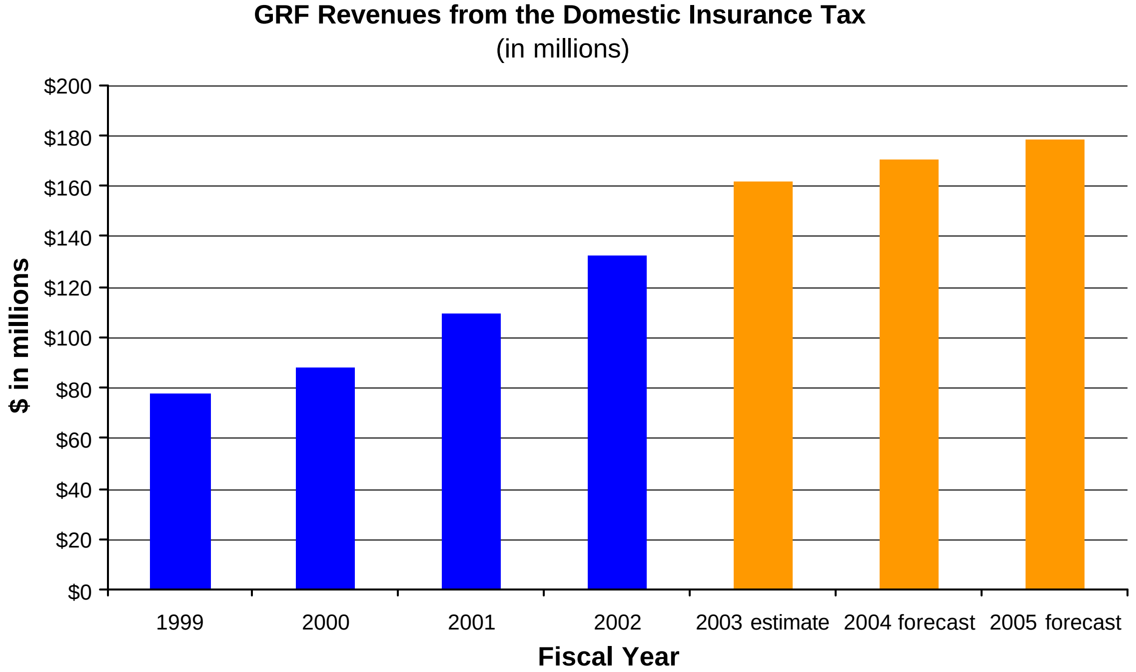
The recent decreases in revenues from this tax are primarily due to the phase-in to the new tax structure. In FY 2002, foreign insurance companies paid a tax of 1.62 percent of premiums, so that the new rate of 1.4 percent of premiums represents a straightforward decrease in the tax rate. This decrease is partially offset by an increase in the retaliatory tax that some foreign insurance companies pay. This retaliatory tax rate applies instead of the normal 1.4 percent rate for any insurance company headquartered in a state that levies a tax rate on Ohio insurance companies higher than the 1.4 percent that Ohio otherwise imposes on foreign insurance companies. Since Ohio has recently been lowering the tax rate applied to foreign insurance companies, more of those companies wind up paying the tax at the retaliatory rate. The retaliatory portion of this tax certified to the Treasurer of State increased from $72.4 million in FY 2001 to 112.5 million in FY 2002. This approximately $40 million increase in the retaliatory tax went a long way toward offsetting the reduction in the normal tax rate.

The forecast is based on separate growth rates for different types of insurance companies. In FY 2002, 51.4 percent of the revenue certified by the Department of Insurance to the Treasurer of State for collection was assessed on fire and casualty insurance companies, 45.9 percent was assessed on life insurance companies, and 0.4 percent was assessed on HICs; the remainder was assessed on other insurance companies. These shares are significantly different from the comparable shares for domestic insurance companies, which are described in the section on the domestic insurance tax.
Premiums collected by insurance companies are projected to grow at rates close to their average growth rate in recent years, with some adjustments that appear to be warranted due to considerations described below. The adjustments are described in the section on the domestic insurance tax. Tax revenues are assessed on premiums collected during a calendar year, so that FY 2003 revenues are based on CY 2002 premiums, FY 2004 revenues are based on calendar year 2003 premiums, etc.

Premiums collected by HICs are projected to grow by 9.2 percent in calendar year 2002, and by 6.6 percent in both calendar years 2003 and 2004. Premiums collected by fire and casualty insurers are projected to grow by 9.0 percent in CY 2002, by 5.5 percent in CY 2003, and by 3.9 percent in calendar year 2004. Premiums collected by life insurance companies are projected to grow by 0 percent in calendar year 2002, by 4.3 percent in 2003, and by 4.2 percent in 2004.

As with the domestic insurance tax, the revenue collected from this tax is deposited into the General Revenue Fund.

Domestic Insurance Tax



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Domestic Insurance	$77.5	$88.2	$109.3	$132.4	$161.6	$170.7	$178.3
growth	22.7%	13.7%	24.0%	21.2%	22.0%	5.6%	4.5%

The new tax structure created in Am. Sub. H.B. 215 of the 122nd G.A. is in place for the first time in fiscal year 2003, after a five-year phase-in schedule. In FY 2003, domestic insurance companies that are health insuring corporations (HICs) will pay a tax of 1.0 percent of premiums, while other domestic insurance companies will pay a tax of 1.4 percent of premiums.

The recent growth in revenues from this tax is primarily due to the phase-in to the new tax structure. In FY 2002, domestic HICs paid a tax of 0.8 percent of premiums, so that the new rate of 1.0 percent of premiums represents a straightforward increase in the tax rate. Other domestic insurance companies paid their FY 2002 tax based on a weighted average of the new formula described above and the formula that was in place prior to H.B. 215. Under the weighted average formula that applied in FY 2002, companies paid 80 percent of the tax calculated using the new formula of 1.4 percent of premiums, plus 20 percent of the tax calculated using the old formula. Under the old formula, insurance companies paid the lesser of 2.5 percent of premiums or 0.6 percent of capital and surplus. Even though the tax rate imposed on premiums was higher under the previous formula, for many companies the tax of 0.6 percent of capital and surplus was the lesser of the two calculations. The not-so-straightforward result has been that as the previous formula has been phased-out over the last five years, many companies have been submitting larger tax payments to Ohio under the tax. Ohio companies that operate in other states may have realized a fall in their overall tax burden, however, as the higher rates paid to Ohio may have reduced their tax payments to some other states under the retaliatory tax many states, including Ohio, impose. The retaliatory tax is described in the foreign insurance tax section.

The forecast is based on separate growth rates for different types of insurance companies. In FY 2002, 68.5 percent of the revenue certified by the Department of Insurance to the Treasurer of State for collection was assessed on fire and casualty insurance companies, 11.6 percent was assessed on life insurance companies, and 19.8 percent was assessed on HICs; the remainder was assessed on other insurance companies. An analysis of company-level data provided by the Department of Insurance led to an estimate that the transition from the old formula to the new formula in FY 2003 would increase taxes paid by fire and casualty insurers by 11.3 percent and taxes paid by life companies by 1.9 percent. For HICs, the adjustment would be 25 percent, the percentage increase from a 0.8 percent tax rate to a 1.0 percent tax rate.

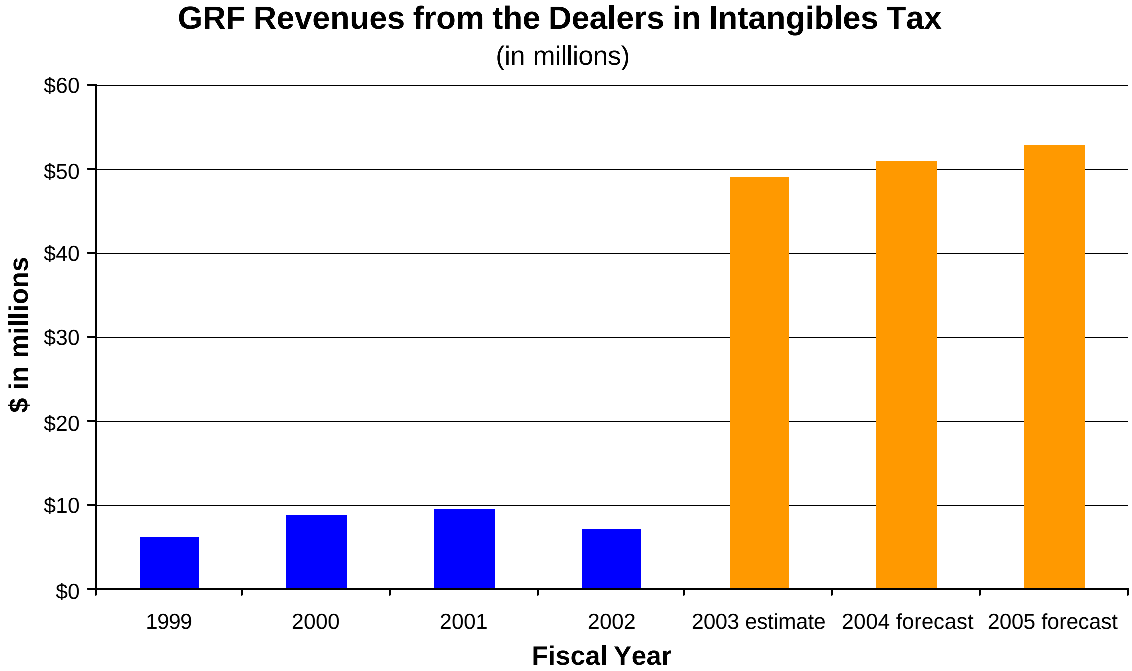
Premiums collected by insurance companies are projected to grow at rates close to their average growth rate in recent years, with some adjustments that appear to be warranted due to considerations described below. Tax revenues are assessed on premiums collected during a calendar year, so that FY r 2003 revenues are based on calendar year 2002 premiums, FY 2004 revenues are based on calendar year 2003 premiums, etc.
Premiums collected by HICs are projected to grow by 9.2 percent in CY 2002, and by 6.6 percent in both CY 2003 and 2004. The 9.2 percent rate is the rate of growth in premiums collected during the first half of calendar year 2002 compared with premiums collected during the first half of CY 2001 according to Department of Insurance data. The 6.6 percent growth rate is the average rate of growth in premiums between 1997 and 2001.

Premiums collected by fire and casualty insurers are projected to grow by 9.0 percent in CY 2002, by 5.5 percent in CY 2003, and by 3.9 percent in CY 2004. The growth rate assumed for 2002 is high by historical measures, but is consistent with media reports of large increases in property and casualty premiums nationwide. An article in the September 30, 2002 issue of *National Underwriter* reported that premiums increased by 12 percent nationwide from the first half of 2001 to the first half of 2002. The growth rate projected for 2003 is the average growth rate between 1991 and 2001, according to Department of Insurance data. The growth rate for 2004 is projected to moderate further because the period 1991 through 2001 had two years, 1995 and 2001, with growth rates that seemed unusually high by historical standards.

Premiums collected by life insurance companies are projected to grow by zero percent in CY 2002, by 4.3 percent in 2003, and by 4.2 percent in 2004. The average growth in premiums between 1991 and 2000 was between 4.2 percent and 4.3 percent, and this average is used to project the growth for 2003 and 2004. The lack of growth projected for 2002 is due to the after-effect of a very high rate of growth in 2001. Life insurance premiums grew by over 37 percent in 2001; the next-highest rate of growth since 1991 was less than 22 percent, in 1993. In only one other year, 1999, did the growth exceed 10 percent. The rate of growth was actually negative in both years that followed a year with double-digit growth (1994 and 2000). This is also possible for 2002.

The revenue collected from insurance taxes is deposited into the General Revenue Fund. An additional 0.75 percent tax is levied on the gross premium receipts derived from fire insurance and that portion of the gross premium for other coverage that is reasonably allocable to fire insurance. Revenue from this tax is deposited into the Fire Marshall's Fund. The amount certified to the Treasurer of State to go to the Fire Marshall's Fund for FY 2002 was $6.5 million.

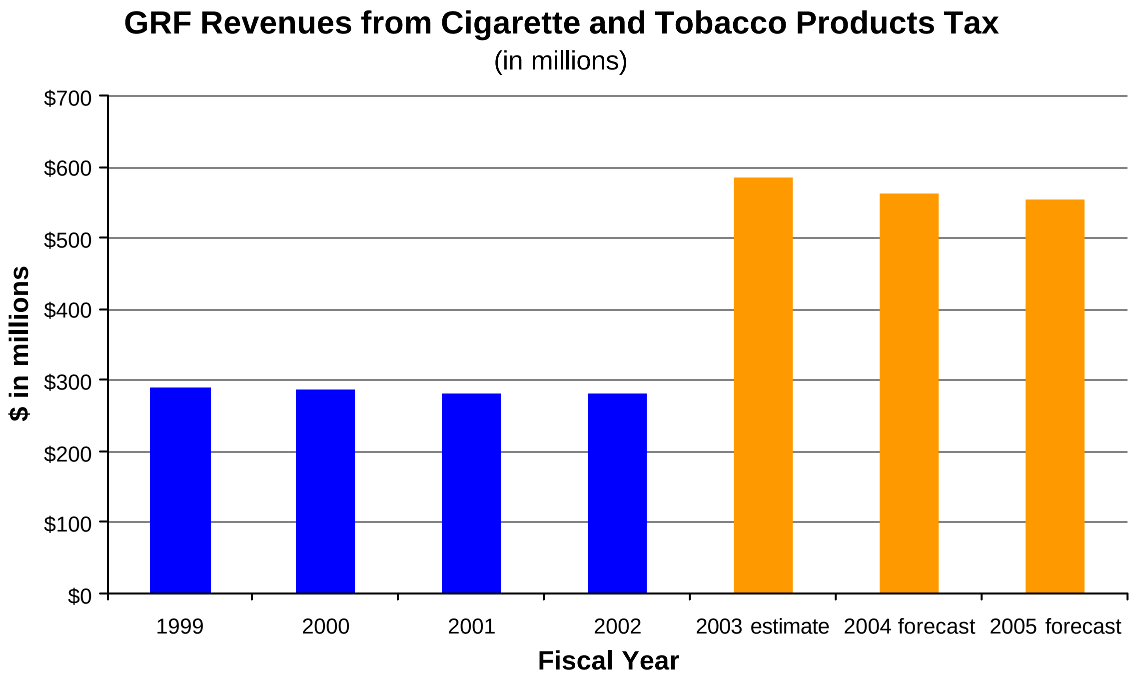
Business and Property (Dealers in Intangibles Tax)



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Dealers in Intangibles Tax	$6.2	$8.7	$9.5	$7.1	$49.0	$50.9	$52.8
Growth	-3.1%	40.3%	9.2%	-25.3%	590.1%	3.9%	3.7%

Ohio law provides for the taxation of shares and capital employed by dealers in intangibles. The tax, which is known as the Dealers in Intangibles Tax, is imposed on businesses (excluding financial institution and insurance companies) engaged in lending money, buying and selling notes, mortgages and other evidences of indebtedness, and firms buying and selling securities. The tax rate is 8 mills of the values of shares or capital employed by the taxpayer. A share of the revenue under this tax, 3 mills, is deposited in the General Revenue Fund. The remainder, 5 mills, is distributed to the counties. Am. H.B. 405 tightened the eligibility requirements for dealers under this tax and expanded the tax base. This change increased revenues under this tax in FY 2003. The forecast for FY 2004 and FY 2005 is based on historical revenue growth rates for this tax.

Cigarette and Tobacco Products Tax



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Cigarette	$290.6	$287.7	$282.5	$281.3	$585.0	$563.0	$555.0
growth	-2.0%	-1.0%	-1.8%	-0.4%	108.0%	-3.8%	-1.4%

The cigarette and other tobacco products tax is levied on cigarettes, cigars, chewing tobacco, snuff, smoking tobacco, and other tobacco products. Cigarettes are taxed at a rate of 55 cents per package of 20 cigarettes. Other tobacco products are taxed at 17 percent of their wholesale price.

Revenue collected from the tax is deposited into the General Revenue Fund. Prior to FY 2003, cigarette and other tobacco tax receipts declined as tobacco consumers quit or looked for sources of non-taxed cigarettes. Revenues from taxed cigarettes were generally 91 to 93 percent of the cigarette and other tobacco products tax take. Other tobacco products provided between 7 and 9 percent of the tax receipts. Trends for the two tax bases are not always similar. In the last three years prior to FY 2001, cigarette tax receipts declined slowly each year while tax revenues from other tobacco products increased.[5]

[5] A plausible explanation is that huge cigarette price increases led some smokers to favor the consumption of other tobacco products instead of purchasing cigarettes. Cigarette prices grew 9.8%, 30.9%, 11.2%, and 7.8% in 1998, 1999, 2000, and 2001, respectively. Other tobacco products prices grew 3.4%, 7.6%, 7.1% and 3.4% during the same years. More recently, some smokers may have switched

However, in FY 2001, growth in cigarette tax receipts was flat, while other tobacco products tax receipts plunged by about 24 percent. In FY 2002, receipts from both tax sources declined slightly. For FY 2003, Am. Sub. S.B 261 increased cigarette taxes from 24 cents per pack to 55 cents per pack of 20 cigarettes and left unchanged the tax rate on other tobacco products. Due to the tax increase on cigarettes, the tax base of other tobacco products will become a much smaller share of the cigarette and other tobacco products tax.

The forecast for the cigarette and tobacco products tax is primarily based on trends in consumption of both cigarettes and other tobacco products. S.B. 261 increased cigarette prices by an amount at least equal to the increase in tax. This price increase will gradually decrease monthly consumption of taxed cigarettes by at least 6 percent by the end of FY 2003.[6] FY 2003 revenues include one-time revenue of about $13.2 million from the "floor" tax, a tax on cigarette inventories that paid tax at the old rate but were not yet sold. It is expected that smokers will continue to make further adjustments to their consumption of taxed cigarettes during FY 2004. Some consumers will switch to other tobacco products whose tax rate was left unchanged by S.B. 261. This will increase tax revenues from this source of the tax base. The long-term annual decline in cigarette consumption, which has been about 1.5 percent, is expected to continue. Additional factors, such as increases in cigarette prices and increases in the share of non-taxed cigarettes (smuggling and Internet purchases), may create an even steeper decline in consumption of taxed cigarettes in future years.

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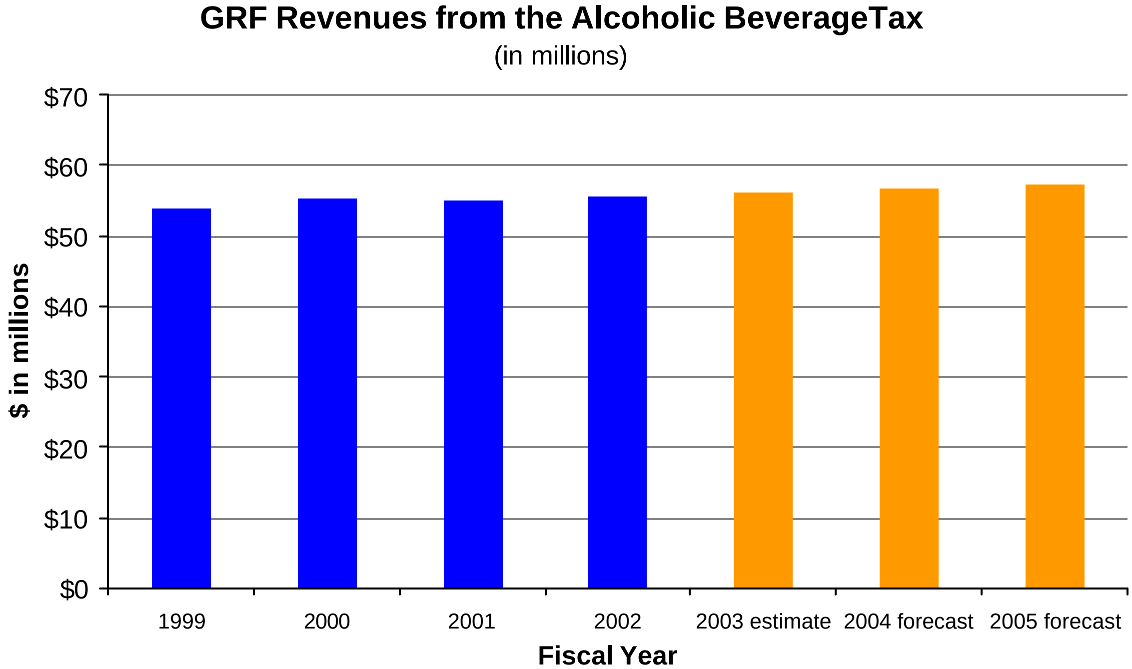
back to more affordable "generic cigarettes" which cost less than name brand cigarettes, looked for cheaper cigarettes in neighboring states, and purchased through mail-order catalog or Internet sites at lower cost.

[6] The average weighted price includes both generic and premium cigarettes. The price elasticity of demand for cigarettes is assumed to be at -0.6, i.e. a 10 percent price increase results in a 6 percent decrease in consumption. Accepted ranges of price elasticity of demand for cigarettes are between -0.4 and -0.6.

Alcoholic Beverage Tax

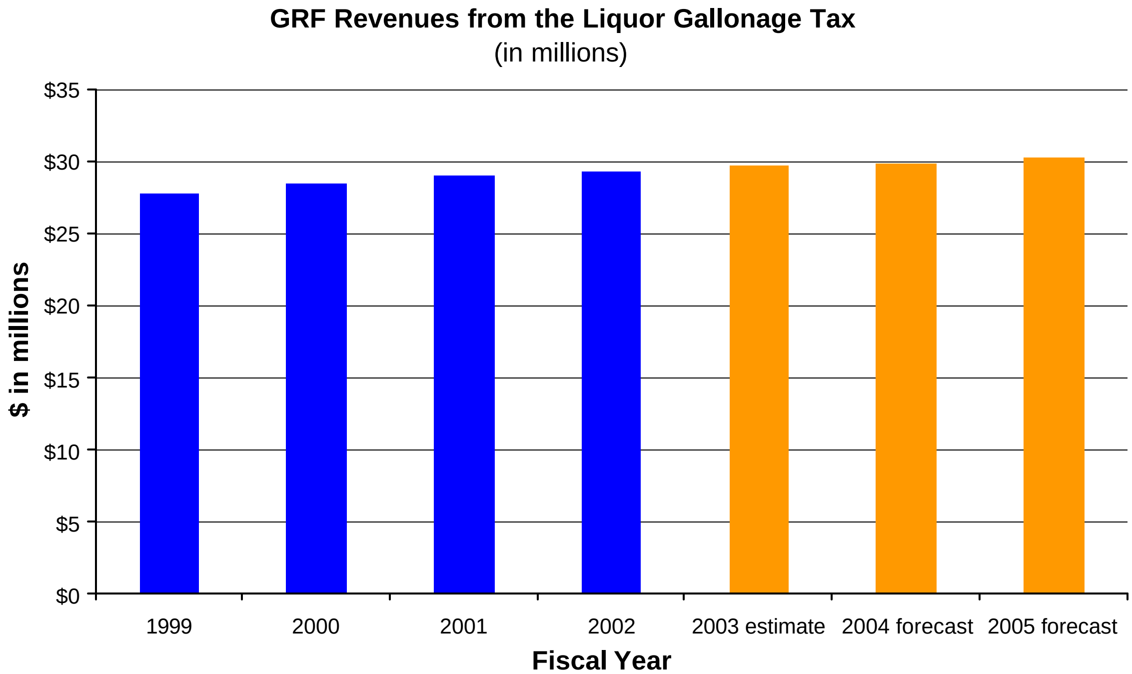


	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Alcoholic Beverage	$53.8	$55.3	$55.0	$55.7	$56.3	$56.7	$57.4
growth	2.6%	2.8%	-0.4%	1.3%	1.0%	0.7%	1.2%

The alcoholic beverage tax applies to sales of beer, malt beverages, wine, and mixed alcoholic beverages. The tax is based on a per-container rate depending on the type of beverage sold. Beer is taxed at varying rates that are equivalent to 0.14 cents per ounce (about 10 cents for a six-pack of 12 oz containers). Wine less than 14 percent alcohol by volume is taxed at 32 cents per gallon (about 5.4 cents for a standard 750 ml[7] bottle). Wine between 14 percent and 21 percent alcohol by volume is taxed at $1.00 per gallon (or 17.0 cents for a standard 750 ml bottle). Mixed beverages are taxed $1.20 per gallon (or 20.4 cents for a standard 750 ml bottle). Major exemptions to the tax are sacramental wine, sales to the federal government, and sales in interstate commerce. Revenue is deposited in the General Revenue Fund with two exceptions. One percent of the tax is deposited in the Beverage Tax Administration Fund and five cents per gallon of wine is deposited into the Ohio Grape Industries Special Account. The forecast for the alcoholic beverage tax revenue is based on trend analysis of the contribution of each alcoholic beverage to the tax base in the last few years.

[7] This is a three-fourths liter bottle.

Liquor Gallonage Tax

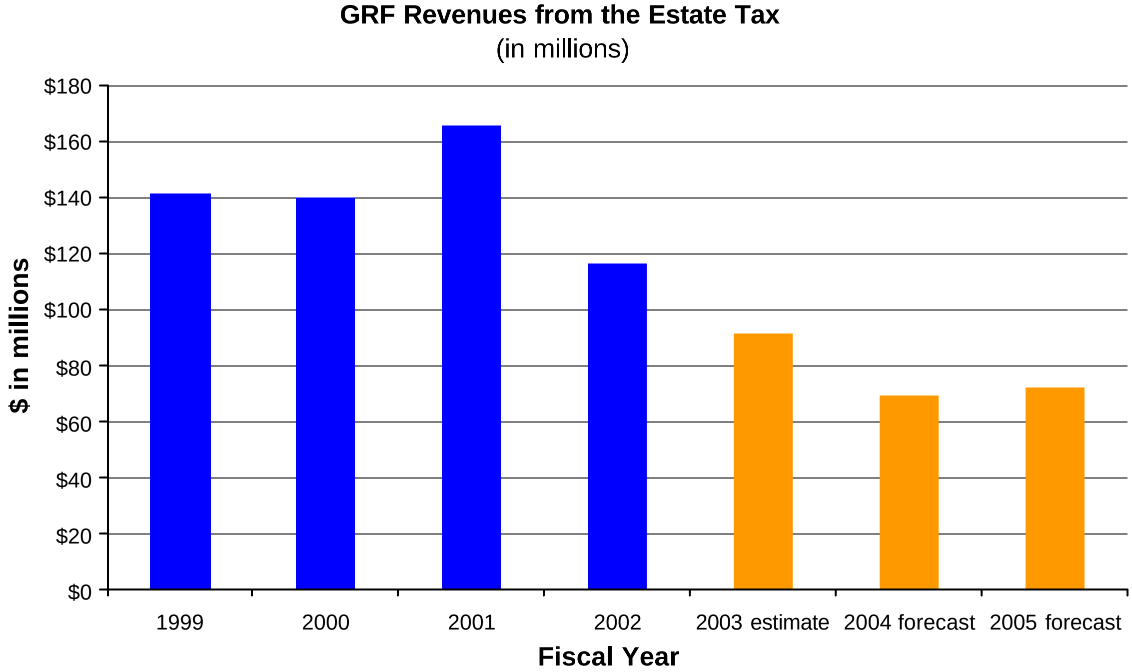


	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Liquor Gallonage	$27.6	$28.5	$29.0	$29.3	$29.7	$29.9	$30.2
growth	1.2%	3.1%	1.8%	1.1%	1.3%	0.7%	1.0%

The Liquor Gallonage Tax is levied at the rate of $3.38 per gallon of spirituous liquor. This is the equivalent of 57.6 cents per standard 750 ml bottle. Revenue from this tax is deposited into the General Revenue Fund.

Important determinants of alcohol consumption slowly change over time. Specifically, the demographic shift to an older population may account for the long-term decline in per capita consumption, since alcohol consumption typically falls as a person ages. However, the relative importance of disposable income as a determinant of demand for liquor may have increased, explaining the small year-over-year increases in tax receipts. The forecast of liquor gallonage tax is based on trend analysis of wholesale and retail gallonage sales of liquor in Ohio.

Estate Tax



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Estate	$141.5	$140.0	$166.0	$116.3	$91.0	$69.0	$72.0
growth	23.2%	-1.1%	18.6%	-30.0%	-21.7%	-24.2%	4.3%

The forecast for the Estate Tax is based on historical trend analysis. Estate Tax revenues are estimated to decrease from $91 million to $69 million in FY 2004. In FY 2005, estate tax revenues are estimated to increase by 4 percent to $72 million.

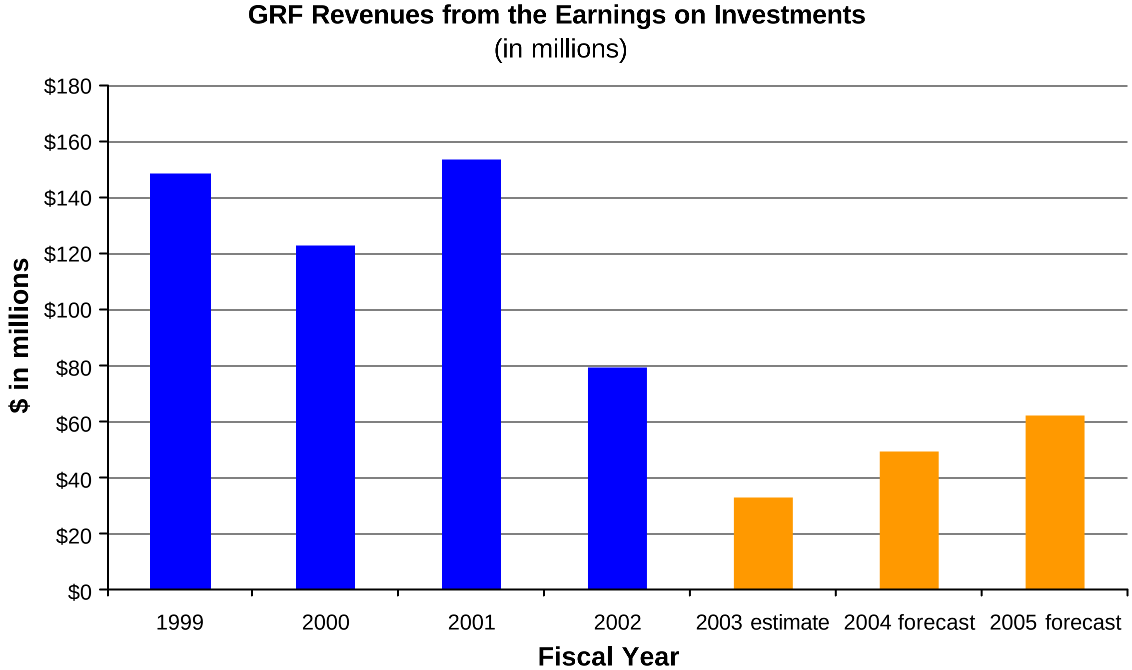
Estate tax is one of the more volatile state revenue sources as the estate of a very wealthy individual can account for 10 percent or more of the total state estate tax revenues. Estate Tax return is filed within nine months of a person's date of death. The municipal corporation or township of origin receives 80 percent of the revenue and the General Revenue Fund (GRF) receives the remaining 20 percent, less cost of local administration for estates with dates of death from January 1, 2002. The tax is progressive with rates ranging from 2 percent of the taxable estate to 7 percent of the value of the taxable estate over $675,000.

The estate tax is assessed upon the total assets owned by a decedent (either solely or in conjunction with another person) who was a resident of Ohio at time of death. The tax due is based on the net value of the decedent's estate. This net value is based on the gross value minus the debts and administration expenses of the estate. The gross value is made up of all assets, such as real estate, bank accounts, stocks, bonds, etc. The debts and administration expenses are made up of funeral costs, attorney and executor fees, outstanding bills in the name of the decedent, etc. Ohio also allows an unlimited marital deduction that allows property to pass from one spouse to another without taxation for dates of death on and after July 1, 1993. This can result in no estate tax on property passing to a surviving spouse.

Senate Bill 108 of 123rd General Assembly (effective September 29, 2000), reduced Ohio's death taxes by 36 percent for estates valued under $675,000, which is the current federal exemption figure. It also increases the size of estates exempted from paying any death taxes from $200,000 net taxable value to $338,000. That provision affects about 12 percent of estates. (figure from S.B. 108).

In the next biennium, Ohio estate tax revenue is also affected by the federal estate tax repealed under HR 1836 -- The Economic Growth and Tax Relief Reconciliation Act 2001. Ohio levied an estate tax but has no inheritance tax. Federal estate taxes are assessed on the net worth of an individual at death. No tax is levied for the first $675,000 of the estate, but beyond that threshold taxes are assessed at a rate ranging from 37 percent to 55 percent. The unified estate and gift tax rates decreases and the exemption from the estate increases each year until it is completely repealed in 2010.

Earnings on Investments



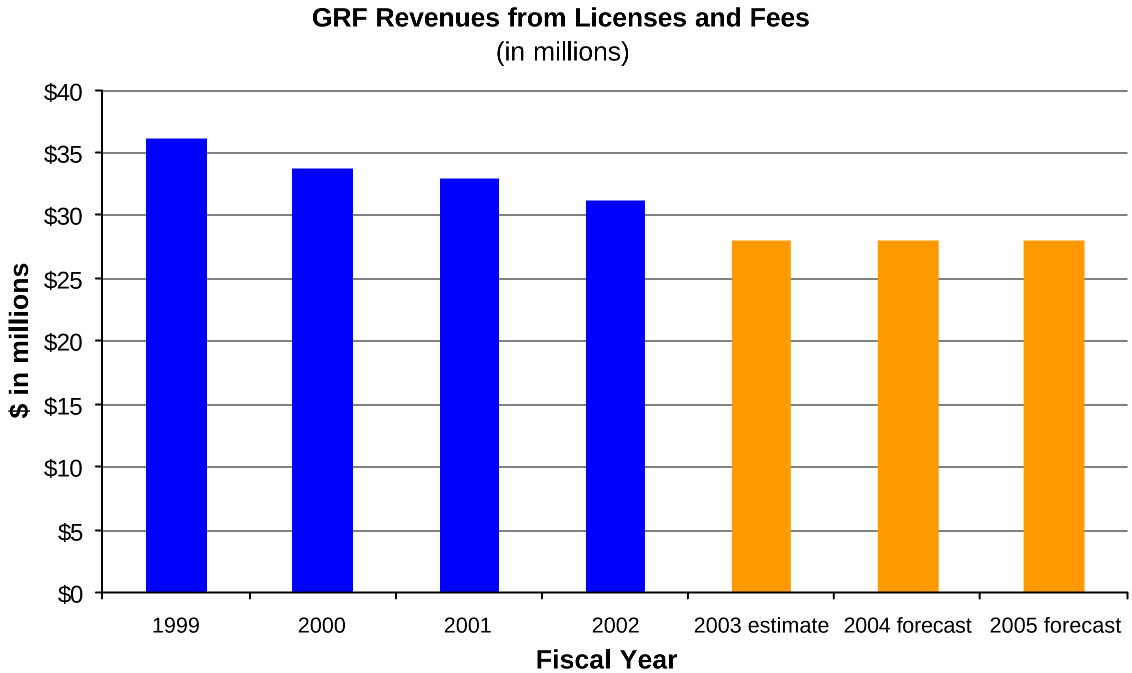
	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Earnings on Investments	$148.4	$122.5	$153.3	$79.0	$33.1	$49.0	$62.0
growth	15.0%	-17.5%	25.1%	-48.5%	-58.1%	48.0%	26.5%

In FY 2003, earnings on investments are estimated to decline from $79 million to $33.1 million because of very low fund balances and interest rates. Earnings are expected to rebound somewhat in both FY 2004 and FY 2005 as interest rates increase and budget balances recover. In FY 2004, earnings on investments are estimated to increase from $33.1 million to $49 million. In FY 2005, earnings on investments are estimated to increase by twenty-eight percent to $62 million.

In forecasting the state's investment earnings, information on historical data trends and economic conditions were used in formulating assumptions. The calculations made were based on the average of state funds that will be available for investment including the Budget Stabilization Fund balance multiplied by the average short-term and medium-term interest rates.

The Treasurer of State is responsible for managing the state's portfolio and investing state funds. State funds are invested in a diversified portfolio with a mixture of short-term and medium term debt investments. All earnings on investments from state funds are credited to GRF unless stated otherwise in the Ohio Revised Code.

Licenses and Fees



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Licenses and Fees	$36.1	$33.7	$32.9	$31.1	$28.0	$28.0	$28.0
growth	-0.6%	-6.6%	-2.4%	-5.5%	-10.0%	0.0%	0.0%

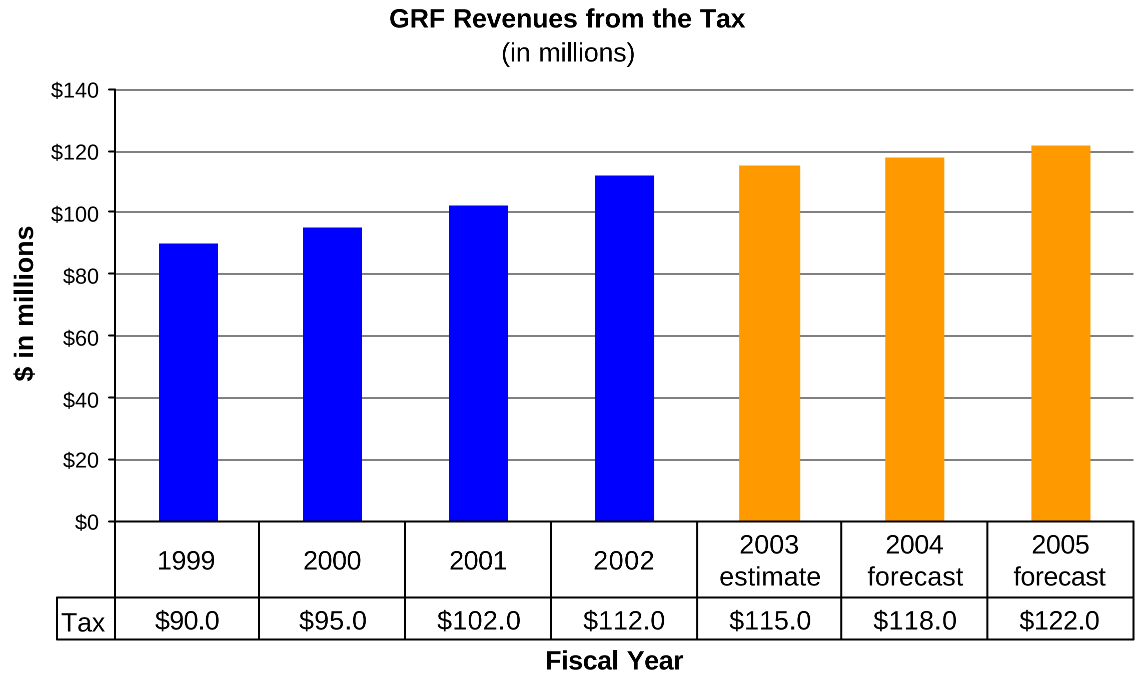
The General Revenue Fund benefits from a number of licenses and fees that are either completely or partially deposited into the GRF. LSC estimates licenses and fees will annually generate $28.0 million of revenue for the GRF in fiscal years 2003 - 2005.

The two largest contributors of license and fee revenue have traditionally been the license fees deposited by the Department of Insurance and liquor permits deposited by the Department of Commerce. Motor vehicle licenses, fees and license revenues deposited by the Environmental Protection Agency, and various business licenses also contribute revenues to the GRF.

Revenue generated by licenses and fees has been steadily declining over the years. Several factors have contributed to this decline. A decline in license fees paid to the Department of Insurance account for part of the decline. Another contributor is the trend away from depositing these moneys into the GRF. Many licenses and fees that were once completely or partially deposited into the GRF are now being deposited into various State Special Revenue funds. In fact, in FY 2003 the bingo licensing fee paid to the Office of the Attorney General and a plan approval fee for water treatment facilities paid to the

Environmental Protection Agency will no longer be deposited into the GRF. Instead, the fees will be deposited into SSR funds. As a result of these changes, the GRF will loose approximately $400,000 annually.

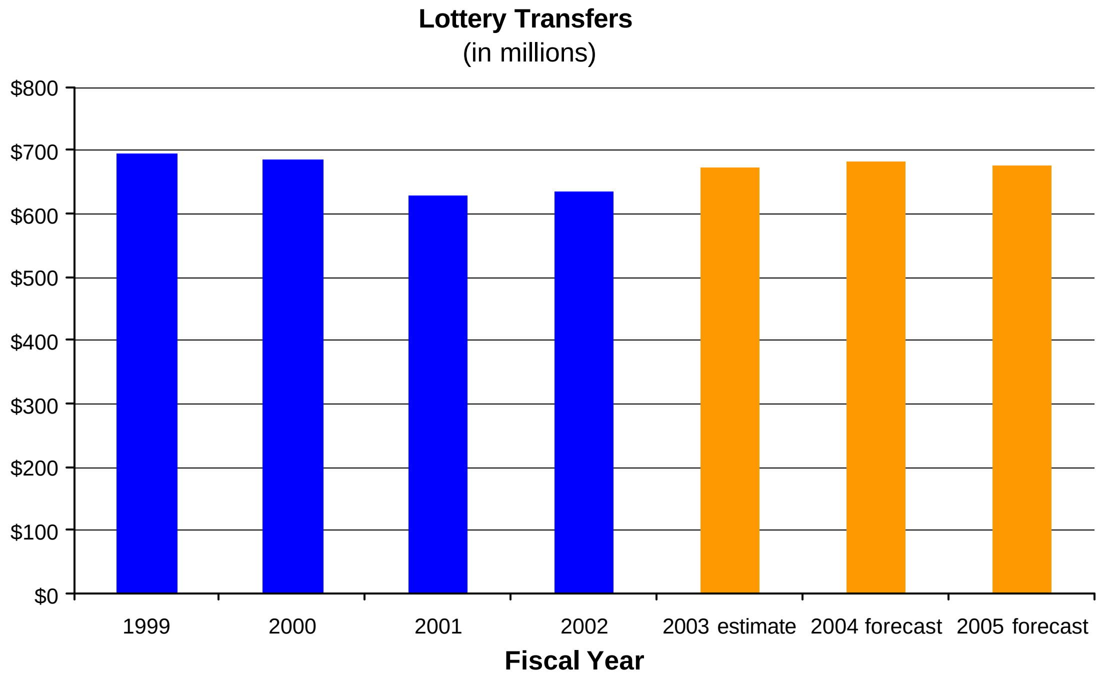
Liquor Transfers



	1999	2000	2001	2002	2003 estimate	2004 forecast	2005 forecast
Tax	$90.0	$95.0	$102.0	$112.0	$115.0	$118.0	$122.0

The Division of Liquor Control within the Ohio Department of Commerce is responsible for regulating the sale of spirituous liquor within the state. Revenue from the sale of spirituous liquor is applied first to paying the operating expenses of the division, then to paying the debt service on industrial development bonds. Revenue exceeding the need for these two purposes is transferred to the General Revenue Fund. LSC projects that these transfers will grow by slightly under 3 percent in FYs 2003 and 2004. This growth is forecast to accelerate slightly in FY 2005.

Lottery Transfers



	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimate	FY 2004 Forecast	FY 2005 Forecast
Operating Profits	$671.3	$661.0	$604.1	$610.1	$637.7	$648.2	$641.0
growth	-3.4%	-1.5%	-8.6%	1.0%	4.5%	1.6%	-1.1%
Unclaimed Prizes	$25.0	$25.0	$25.0	$25.0	$35.0	$35.0	$35.0
growth	-12.9%	0.0%	0.0%	0.0%	40.0%	0.0%	0.0%
Total	$696.3	$686.0	$629.1	$635.1	$672.7	$683.2	$676.0
growth	-3.8%	-1.5%	-8.3%	1.0%	5.9%	1.6%	-1.1%

The Ohio Lottery Commission operates to create profits to be transferred to the Lottery Profits Education Fund (LPEF) for use in programs benefiting primary, secondary, vocational, and special education in Ohio. The amount transferred comes largely from operating profits with occasional transfers made from the Unclaimed Prize Fund. This forecast assumes that transfers from operations would be about 29.8 percent of ticket sales[8] and transfers from the Unclaimed Prize Fund would remain at $35.0 million per year.[9]

After a peak of $2.31 billion in sales in FY 1996, Lottery sales declined steadily to $1.92 billion in FY 2001. Changes to Buckeye 5, the entry into Mega Millions and an improvement in Instant ticket sales increased ticket sales to $1.98 billion in FY 2002. An increase in ticket sales is expected during the next biennium, primarily from sales of Mega Millions. The forecast assumes that Ohio Lottery will change the mix of Instant games and increase their payout and sales. The improvement in Instant ticket sales and Mega Millions sales are expected to stabilize lottery ticket sales at approximately $2.1 billion for the next few years. Although incomes continue to grow and attitudes towards gaming remain generally favorable, increased competition in the gaming market (in regular and riverboat casinos, racetracks video lottery terminals, primarily from neighboring states), and Internet gaming may limit any significant future increase in lottery ticket sales. The table below presents a recent history of lottery sales, an estimate of sales for FY 2003, and forecasts of sales for FYs 2004 and 2005.

Lottery Sales: Recent History and Forecast *(in millions)*							
Fiscal Year	1999	2000	2001	2002	2003	2004	2005
Ticket Sales	$2,144.7	$2,150.4	$1,922.0	$1,982.5	$2,084.5	$2,118.7	$2,095.3

Ticket sales were estimated on a trend basis for each on-line game and for Instant games. The forecast assumes no significant change in the current mix of games and no substantial increases in advertisement expenditures.

[8] This is the percentage of ticket sales transferred from operations in the first half of FY 2003 (December 2002). Am. Sub. H.B. 94 removed a provision of law requiring that at least 30 percent of ticket sales be transferred to the Lottery Profit Education Fund and also changed the manner in which the Ohio Lottery transfers profits to LPEF. A target amount for such transfers will be determined for each biennium during the legislative budget process. Thus, actual transfer percentage is likely to be different than the percentage used in this forecast.

[9] These transfers from non-operating sources, such as transfers from Unclaimed Prize Funds, may or may not occur.

Temporary Assistance to Needy Families

Overview

The Temporary Assistance for Needy Families (TANF) program was created by the federal government in the Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA) of 1996. TANF is now in the process of being reauthorized, and at this time it is not known whether there will be programmatic changes. Congress is expected to act on reauthorization in the next few months. The purposes of the program as it now exists are to:

- Provide assistance to needy families so that children may be cared for in their own home or in the homes of relatives.
- End the dependence of needy parents on government benefits by promoting job preparation, work, and marriage.
- Prevent and reduce the incidence of out-of-wedlock pregnancies and establish annual numerical goals for preventing and reducing the incidence of these pregnancies.
- Encourage the formation and maintenance of two-parent families.

To accomplish these goals Ohio has developed and implemented two main programs that provide time limited cash assistance to needy families with children and also provide a new array of services that furnish parents with work training and other supports to help them attain permanent self-sufficiency. Ohio's two main programs that are administered by the Department of Job and Family Services (JFS) are the Ohio Works First (OWF) program and the Prevention, Retention, and Contingency (PRC) program. In addition, Ohio also operates some specific programs in which TANF eligible individuals receive services (TANF funds may fully or partially fund these programs). These include the Head Start program in the Department of Education, the TANF Family Planning program in the Department of Health, the TANF Housing Program in the Department of Development, the AdoptOhio program in the Department of Job and Family Services, and the Substance Abuse, Treatment and Mentoring program in the Department of Alcohol and Drug Addiction Services.

TANF

The PRWORA eliminated the Aid to Families with Dependent Children program (or AFDC; in Ohio this was called Aid to Dependent Children or ADC), the Job Opportunity and Basic Skills (JOBS) program, and the Family Emergency Assistance (FEA) program. Congress replaced these programs with the TANF program. Prior to TANF, under the AFDC program, the federal government provided states with open-ended matching funds for cash welfare payments to all families who qualified. Cash benefits were an "entitlement" and had no time limit. Under an entitlement, qualified recipients have a "right" to receive benefits and appropriations must be provided in case of a shortfall. In the old AFDC program the federal government reimbursed states for welfare spending between 50 and 80 percent -- depending on per capita income. In Ohio this reimbursement averaged approximately 60 percent over the decade prior to PRWORA.

The focus of public assistance has now shifted from "entitlement" to temporary assistance that encourages self-sufficiency by requiring recipients to work or participate in a developmental activity. PRWORA established a five-year maximum lifetime limit on a family's receipt of federally funded cash benefits. The TANF program requires that states impose stricter work requirements on recipients than under AFDC, and eliminated all but a few of the exemptions from participation in work for adult welfare recipients. The PRWORA prescribes little in the way of eligibility requirements, while being very prescriptive in the amount of work activity required of adult TANF recipients. Exercising the flexibility that PRWORA allows, OWF further limits receipt of cash benefits to three years, with a possible hardship extension of two years, if a minimum of two years has passed since the last receipt of benefits.

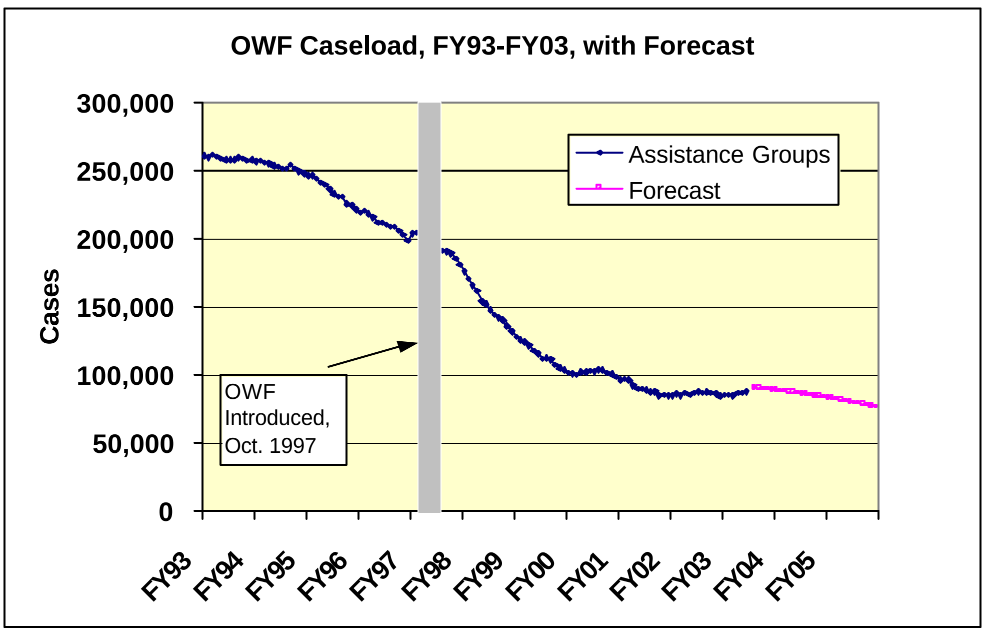
While Congress has not yet passed legislation re-authorizing the TANF program, we are likely to see a continuation of federal funding for the TANF program at the current level of $16.5 billion. The President's proposal for reauthorization of the TANF program continued funding at the current level, and the reauthorization bill that passed the U.S. House of Representatives last year also continued funding at that level.

Ohio's annual TANF block grant award of approximately $728 million is based on the amount of federal funds expended in federal fiscal year (FFY) 1994 for the three eliminated programs (AFDC, JOBS, and FEA). Ohio is required to meet a minimum maintenance of effort (MOE) requirement of 80 percent of what it spent in FFY 1994 on the three eliminated programs (80 percent of that amount is approximately $417 million), through FFY 2002. The MOE can be lowered to 75 percent ($390.8 million) if the state meets its participation requirement. Ohio currently meets the participation rate requirements and has been meeting the MOE at a 77 percent level, leaving a small cushion for underspending or disallowances in an audit. If the state fails to meet the MOE, its TANF grant for the next federal fiscal year will be reduced by the amount of the deficit, and the state will be required to increase its TANF spending by an amount equal to the penalty.

One of the consequences of the block grant funding arrangement is that reductions in recipient case loads reduce the amount of "baseline" cash benefits, thus leaving more funds available for other TANF related program services or activities. If TANF grant funds go unspent in a particular year, the PRWORA legislation provides that "a State may reserve amounts paid to the State under [this legislation] for any fiscal year for the purpose of providing, without fiscal year limitation, assistance under the State program funded under [this legislation]."[10] At the end of FFY 2002 (September 30, 2002), Ohio's TANF reserve was $520.9 million, with $278.9 million reported as unliquidated obligations, and $242.0 million as the unobligated balance. These figures do not include funds that have been transferred to the Social Services Block Grant and the Child Care Development Fund, but which had not yet been spent as of that date. Reserve funds are held at the federal level and are available to be spent on cash benefits.

Another significant aspect of Ohio's welfare reform is that it "devolves" significant authority to counties to implement their own program of services without Ohio Administrative Code rules, but within the parameters of all applicable state and federal laws and regulations. Counties can design their own services in human service functions, including TANF, PRC, day care, transportation services for low-income workers, child support, children services, and employment and training activities. Each county is also given various options to consolidate their funding, or maintain as separate the eight different allocation streams from the federal government. All 88 of the counties have opted for the full consolidation of their funding.

<u>TANF/OWF Forecast</u>



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[10] H.R. 3734, Personal Responsibility and Work Opportunity Reconciliation Act of 1996, sec. 404 (e).

As the chart detailing the trend in the OWF combined caseload indicates, the number of OWF (or ADC as it was known) cases reached a peak in the spring of 1992 and then began a long-term decline as Ohio and the nation recovered from recession. The rate of decline was strong prior to the implementation of OWF, but the rate of decline clearly accelerated around the time of the introduction of OWF.

As the caseload has declined since 1992, and especially after the introduction of OWF, there have been several important changes in the demographic composition of OWF. One of the most significant developments in the changing demographics of TANF recipients in Ohio is the increase in the number of "child only" cases. These cases occur when adults in the household are ineligible for TANF benefits or they are recipients in other programs such as supplemental security income (SSI). Recent data indicates that in Ohio the relationship of non-recipient adults in the households where "child only" cases occur is most often that of the catch-all category of "other relative," followed by grandparent, natural or foster parent, sibling, non-relatives, and step parents.[11] Such cases are exempt from time limits and work requirements. The number of "child only" cases in November 2002 was approximately 39,000 -- fully 46 percent of the caseload. Because the children in these cases remain eligible until age 18 and they are not subject to adult participation requirements, they form a stable core of the OWF caseload.

LSC expects the total number of TANF cases (or assistance groups) to decrease in FY 2004 to an average of 85,573 monthly cases from a FY 2003 average of 87,551. This forecast assumes an economic recovery and an expansion in service sector employment, although there are a number of significant uncertainties at the present time. The forecast decrease in the total number of TANF cases will result in approximately $10.2 million less being spent on TANF cash benefits in FY 2004 than LSC estimates for FY 2003 expenditures. The total spending on cash benefits, assuming current benefit levels, is forecast to be $305.2 million for FY 2004.

[11] U.S. Department of Health and Human Services, Administration for Children and Families, Office of Planning, Research and Evaluation, "Characteristics and Financial Circumstances of AFDC Recipients" FY 1996, Table 33.

The decline in the number of TANF cases is expected to continue into FY 2005. The monthly average of cases is expected to decline to 79,063, representing a decrease in spending for TANF cash benefits of $26.6 million for the year. That estimate brings total spending for cash benefits, assuming current eligibility and benefit levels, to $278.6 million for FY 2005.

TANF TANF/OWF - LSC Baseline Estimates			
	FY 2003	**FY 2004**	**FY 2005**
Average monthly cases	87,551	85,573	79,063
Total cash benefits (millions)	$316.4	$305.2	$278.6

The TANF cash benefits are paid from line items 600-410, TANF State, 600-658, Child Support Collections, and 600-689, TANF Block Grant. The executive has recommended FY 2004 total funding for the combination of these three line items at $1,018.1 million. The total recommended funding level for these three line items in FY 2005 is $1,017.5 million.[12]

Funding cash benefits for FY 2004 at the forecast level of $305.2 million, and at $278.6 million for FY 2005, leaves $712.9 million in FY 2004 and $738.9 million in FY 2005 from these three line items for employment services, work activities, PRC services, transitional services, direct payments from TANF federal funds for child day care (in addition to receiving funds directly from the TANF federal block grant, child care receives funding from other sources), and other allowable activities.

Methodology

The forecasts of TANF recipients and families are done using econometric models. These models are based on a multiple-regression analysis of the relationship between the TANF caseload and explanatory factors that predict TANF participation. These models decompose past data trends and discern the interaction of policy changes with the recipient count. The TANF forecast is based on forecasts of these explanatory factors under the assumption that the historical relationships in the model will continue into the future.

[12] Approximately $17.0 in FY 2004 and $17.6 million in FY 2005 from administrative line items and $28.5 million from counties in each year will be included in the state's total MOE. The executive has also recommended an earmark for a portion of the state's TANF MOE of $45.4 million in each year, out of line item 600-413, Day Care Match/MOE for use, along with other non-TANF funds, to provide child day care.

The total cash benefits for a fiscal year are developed by calculating the moving average value of the cost per recipient, projecting this into the future, and then multiplying the forecast cost per recipient in each quarter by the forecast of TANF recipients. This forecast assumes the continuation of current eligibility requirements and benefit levels.

Disability Assistance

The Disability Assistance (DA) program is a state- and county-funded effort to provide cash and/or medical assistance to persons not eligible for public assistance programs that are supported in whole or in part by federal funds, for example OWF or Supplemental Security Income. Eligibility criteria for DA are established by the state.

The DA program has two distinct components: DA cash assistance and DA medical assistance. There is no time limit for receipt of DA benefits; assistance is provided on an ongoing basis as long as all eligibility requirements are met.

Three recent pieces of legislation have had a direct effect on the DA program. These are Am. H.B. 249 and Sub. H.B. 167 of the 121st General Assembly and Am. Sub. H.B. 408 of the 122nd General Assembly. Am. H.B. 249 eliminated cash eligibility for people who had previously qualified solely because of a medication dependency. Emancipated minors also became eligible for DA benefits under H.B. 249. Sub. H.B. 167 and Am. Sub. H.B. 408 affected the DA program by easing certain qualifications for OWF. Under these two acts, the work history requirement and the 100-hour work rule for two-parent families have been eliminated, thus making it easier for DA recipients with children to meet qualifications for OWF.

In the wake of this legislation and the implementation of OWF, the DA cash and medical recipient caseloads both exhibited a steady decline until the Fall of 1999. Since then, however, the cash assistance caseload has been increasing steadily. In January 2001 the medical caseload also began to increase and, along with an increase in medical inflation, has added quickly to the cost of the program. LSC forecasts that these trends will continue at the same pace that has been exhibited since these upturns.

Disability Assistance LSC Baseline Forecast			
	FY 2003	**FY 2004**	**FY 2005**
Average monthly cash recipients	15,393	17,442	19,247
Average monthly medical recipients	20,628	24,321	28,262
(millions $)			
DA Cash	$23.0	$26.1	$29.4
DA Medical	$90.1	$109.0	$134.9
DA Total -- LSC Forecast	**$113.1**	**$135.1**	**$164.3**
Recommended by Gov. -- DA Cash		$22.8	$22.8
Recommended by Gov. -- DA Medical		$101.4	$101.4
DA Total--Recommended by Gov.		**$124.2**	**$124.2**

If current eligibility criteria stay the same, LSC anticipates the FY 2004 average number of monthly recipients of DA cash benefits to be 17,442, which represents an increase of 13.3 percent from the level LBO estimates for FY 2003. If cash benefit levels stay the same, benefits for the year will total $26.1 million, constituting an increase of 13.5 percent over the FY 2003 estimate for cash benefits. Total cash benefits for the DA program in FY 2005 are forecast to be $29.4 million, representing a 12.6 percent increase from FY 2004. This reflects an expected increase in FY 2005 to about 19,250 average monthly recipients of DA cash.

If current eligibility criteria stay the same, the DA medical recipient caseload is expected to continue its recent increases. Overall expenditures to serve DA medical recipients are anticipated to increase in FY 2004 to $109.0 million, representing a 21.0 percent increase over the FY 2003 estimate. If current eligibility criteria stay the same, DA medical expenditures will continue to increase. LSC anticipates total medical spending to increase to $134.9 million in FY 2005, which represents a 23.8 percent increase. In addition to the effects of continued caseload growth, the calculation of DA expenditures includes the effects of inflation in medical costs. Historically, medical costs in the DA program constitute about 70 percent of total DA expenses.

Combined DA cash benefits and DA medical benefits are estimated to total $113.1 million for FY 2003, $135.1 million for FY 2004, and $164.3 million for FY 2005. This assumes current eligibility and benefit levels. OBM estimates the combined total for

DA to be $118.4 million in FY 2003, $144.2 million in FY 2004, and $180.4 million in FY 2005.

The Governor has recommended an increase of funding over the FY 2003 level to $124.2 million for each year of the biennium. Since this level of funding is lower than what is required to fully fund the forecast growth in the DA caseload, it will be necessary, if funding is to stay within those levels, to introduce changes in the DA program and its eligibility criteria.

Methodology

The forecast of DA cash recipients is based solely on a quantitative model that analyzes past trends in the DA cash recipient time series during the time period since implementation of October 1, 2000. This model takes the DA cash recipient time series and identifies patterns in the data. These patterns are assumed to continue into the future.

Total cash benefits payable are then determined by forecasting average benefits per month per recipient. Average benefits are forecast using a linear regression model. Multiplying the average cash benefits and the number of monthly recipients produces the total monthly benefit for DA cash. Summing the monthly benefits each fiscal year yields the yearly total DA cash benefit forecast.

The forecast of DA medical recipients is based solely on a quantitative model that analyzes past trends in the time series during the time period since October 2000. These trends are assumed to continue into the future.

To determine the baseline total spending, the DA cash benefit forecast and the DA medical forecast are simply added together.

Public Assistance Expenditures
Health Care/Medicaid

Overview

The Office of Ohio Health Plans in the Department of Job and Family Services (JFS) operates several state and federally funded programs providing health care coverage to certain low-income and medically vulnerable people of all ages: Medicaid, the State Children's Health Insurance Program (SCHIP, created by the Social Security Act as Title XXI), the Hospital Care Assurance Program (HCAP, also created by the Social Security Act as Title XXI), and the state Disability Assistance Medical program (DA).

Medicaid, the largest health program in Ohio, was created by the Social Security Act as Title XIX, and became law in 1965. Medicaid is an entitlement program and is a state-federal partnership, which jointly funds the provision of adequate medical care to eligible needy persons. In this partnership, the federal government establishes broad national guidelines, and each state determines its own eligibility requirements, determines the scope of services, sets payment rates for services, and administers its program.

SCHIP allows Ohio to provide health care coverage to children who were not previously eligible for Medicaid and whose family income is below 200 percent of the federal poverty guideline (FPG). Through HCAP, hospitals are reimbursed for some of their costs of providing medical care to persons below 100 percent of FPG. The DA Medical program is state and county funded and provides limited medical coverage to persons who are not eligible for a federally funded program.

In Ohio, Medicaid and SCHIP provided health care coverage to about 1.4 million Ohioans every month in FY 2002. These programs apply to people in the following four distinct insurance markets: children in families with incomes at or below 200 percent of FPG; pregnant women with incomes at or below 150 percent of FPG; parents at or below 100 percent of the FPG; and low-income elderly and persons with disabilities of all ages, commonly referred to as Aged, Blind, and Disabled (ABD). Many consumers with disabilities have medical needs so extensive that commercial plans would deem them "uninsurable." Even though Medicare provides coverage for most of Ohio's elderly population, many of these individuals are "dually eligible," and Medicaid supplements their Medicare benefits by providing Medicaid coverage for services such as prescription medications and long-term care. Medicaid also provides assistance with Medicare premiums, co-payments, and deductibles to certain low-income seniors.

Although other state agencies provide Medicaid services, the vast majority of Medicaid spending occurs within the budget of JFS. Recognized by the federal government as Ohio's single Medicaid agency, JFS provides long-term care and basic medical services with state and federal moneys through GRF line item 600-525, Health Care/Medicaid. Beginning in FY 2003, the 600-525 line item is not only used to fund Medicaid, but also SCHIP, and DA Medical.[13] In addition to the funding from the GRF, several provider tax programs and other special revenues are used to pay for Medicaid services.[14]

The federal financial share of Ohio's Medicaid program changes every federal fiscal year. In accordance with federal law, the federal government shares in the states' cost of Medicaid at a matching rate known as the FMAP (Federal Medical Assistance Percentage). The FMAP is calculated for each state based upon the state's per capita income in recent years relative to the entire nation. The general description of how this cost-sharing mechanism works has traditionally been as follows: for every one dollar Ohio spends on Medicaid, the federal government gives Ohio 60 cents. However, while the majority of the spending in line item 600-525, Health Care/Medicaid, is matched at the FMAP, a few items, primarily contracts, are matched at 50 percent, and all family planning services receive a 90 percent match. In addition, about 15 percent of Medicare buy-in premiums receive no federal match. Lastly, the State Children's Health Insurance Plan (SCHIP) is matched at an enhanced FMAP of about 70 percent.

Forecast Summary

The total number of persons eligible for Medicaid grew by 11.19 percent from 1,276,967 in FY 2001 to 1,419,856 in FY 2002. LSC forecasts that the total number of eligibles will reach 1,559,487 in FY 2003, a 9.83 percent increase over FY 2002. Furthermore, LSC projects the number of persons eligible for Medicaid will grow to 1,637,550 in FY 2004 and 1,650,731 in FY 2005, a 5.01 percent and a 0.80 percent increase, respectively.

Spending within the 525 line item can generally be placed into one of nine major categories: long-term care (nursing facilities, or NFs, and Intermediate Care Facilities for the Mentally Retarded, or ICFs/MR), hospitals (inpatient and outpatient), physician services, prescription drugs, health maintenance organizations (HMOs), Medicare buy-in, waiver, all other care, and DA Medical.

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[13] Prior to FY 2003, spending for part II of SCHIP is funded through line item 600-426, and spending for DA medical is funded through line item 600-511.

[14] Provider tax programs refer to assessments on hospitals, as well as bed taxes on nursing facilities and intermediate care facilities for the mentally retarded. The programs serve as a mechanism by which to draw additional federal matching funds.

Other special revenues include funds for the Disproportionate Share Hospital (DSH) offset, drug rebates, and the franchise fees.

LSC projects an increase in health care expenditures in FY 2004 of 16.64 percent or $1,287 million in combined state and federal GRF dollars, with a state share increase of $512 million. For FY 2005, LSC projects total health care expenditures will go up by another 7.42 percent, or $669 million in combined state and federal GRF dollars, with a state share increase of $278 million.

Eligibility

While individuals can become eligible for Medicaid programs that are funded out of the 525 line item by meeting any one of many sets of eligibility criteria, all of these various eligibility groups can be categorized into seven major types: Aged, Blind, and Disabled (ABD); Qualified Medicare Beneficiaries (QMBs); Specified Low-Income Medicare Beneficiaries (SLMBs); Healthy Families (HF); Healthy Start (HS); Children in families with incomes at or below 150 percent of the FPG known as CHIP-I; and Children in families with incomes between 150 percent and 200 percent of the FPG known as CHIP-II. Generally, Healthy Families, Healthy Start, CHIP-I, and CHIP-II are grouped as Covered Families and Children (CFC). Each of these groups will be discussed briefly in turn.

ABD. The ABD eligibility group is loosely based on the Supplemental Security Income (SSI) program. Although SSI eligibility generally leads to Medicaid eligibility in most states, Ohio and 11 other states exercise what is known as the “spend-down” option. In other words, Ohio has opted to use a more restrictive income test than that incorporated in the eligibility guidelines of the SSI program (100 percent of the FPG); 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 FPG, they “spend-down” to Medicaid eligibility for the month. This allows individuals who have expensive medical needs, but who may have incomes over the SSI level, to receive Medicaid coverage for the remainder of the month.

The ABD eligibility group is the most costly of the seven groups. Not only do ABD eligibles generate more costly acute care services than the other groups, almost all of the Medicaid long-term care recipients come from the ABD eligibility group.
The number of ABD eligibles increased rapidly in the early 1990s as the result of a dramatic increase in the number of children applying under the disability definition for the SSI program. This was followed by a decline in this population as the result of a change in federal law.[15] However, the Balanced Budget Act of 1997 reversed this more restrictive

[15] During 1996, federal legislation was passed that eliminated SSI eligibility for individuals whose alcohol and drug addiction is a material factor that contributes to their disabilities. Later that same year, the Personal Responsibility and Work Opportunity Act of 1996 tightened eligibility among children by making the disability definition more restrictive.

definition, making these children once again eligible for Medicaid. Despite these earlier changes, growth over the next biennium is expected to be slow.

QMBs and SLMBs. The following two eligibility groups, Qualified Medicare Beneficiaries (QMBs) and Specified Low-income Medicare Beneficiaries (SLMBs), are created by a federal mandate that states' Medicaid programs must "buy-in" to Medicare coverage for certain individuals. QMBs have incomes below 100 percent of the FPG, and Medicaid must pay for their Medicare premiums, copayments, and deductibles.[16] For SLMBs, Medicaid covers the Medicare Part B premiums only for those with incomes between 100–120 percent of FPG. Premiums for both of these eligibility groups (and for Medicare-eligible ABD eligibles for whom the state chooses to buy-in to Medicare)[17] are reflected in the Medicare buy-in service category. The copayments and deductibles of QMBs are reflected in the appropriate service categories, which Medicare covers.

Healthy Start. Children up to age 19 and pregnant women, whose families' incomes are below 150 percent of the FPG, are Medicaid eligible through the Healthy Start program.

Healthy Families. Apart from Healthy Start eligibles, Medicaid provides health care to other families and children. Prior to the enactment of the federal Personal Responsibility and Work Opportunity Act of 1996, which created the TANF program (implemented in Ohio as Ohio Works First) to provide income maintenance services to low-income families, recipients of Aid to Dependent Children (ADC) were automatically eligible for Medicaid. Although TANF severs the link between cash assistance and Medicaid eligibility, a provision of the law requires states to provide Medicaid coverage to families who meet guidelines for ADC eligibility as they were on July 16, 1996. In fact, federal law mandates that eligibility for a state's Medicaid program cannot be more restrictive than the ADC guidelines that existed in each state on July 16, 1996. "Ohio has designed OWF and made the allowable modifications to the July 1996 ADC plan in order to meet Ohio's goal that all OWF cash assistance recipients also automatically receive Medicaid. In addition, in some instances where OWF is more restrictive than the July 1996 ADC rules, individuals who will not be eligible to receive cash will be eligible for Medicaid under the Low-Income Families group which uses the July 1996 ADC policy."[18] These Low-Income Families, who

[16] Because many individuals who are initially eligible for Medicaid through the QMB program "spend-down" to ABD eligibility during the month, the reported QMB population is understated. The QMB grouping in the eligibility table refers only to those QMB individuals who do not spend-down to ABD eligibility.

[17] Under Medicare, eligibility is not limited to age alone. Eligibility is also based on work history (individual's payroll deductions while they were working, similar to Social Security qualifications). Ohio's Medicaid program buys-into Medicare for Medicaid eligibles who do not have the necessary work history for example, to qualify for Medicare, and purchases Medicare hospital coverage.

[18] Source: Ohio Medicaid Report, December 1998, Ohio Department of Human Services.

would have previously received cash assistance, continue to grow as a subset of an eligibility group referred to as Healthy Families.

In addition to individuals who meet eligibility guidelines for 1996 ADC cash assistance, Medicaid eligibility is given to individuals who no longer meet ADC eligibility guidelines due to increased income, but previously received OWF cash assistance. Transitional Medicaid eligibles receive an additional six months of health care coverage that can be extended for an additional six months if monthly income is less than or equal to 185 percent of the FPG. 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 and are referred to as Extended Medicaid. As a subset of Extended Medicaid, coverage is provided to individuals eligible for Title IV-E foster care and other miscellaneous groups.

CHIP-I. The Balanced Budget Act of 1997 added a sixth eligibility group to the Medicaid population that Ohio funds out of the 525 line item. The Act created the State Children's Health Insurance Program (CHIP), Title XXI of the Social Security Act, giving states another option to initiate or expand health care to uninsured low-income children. The program affords states increased flexibility in designing and implementing CHIP programs and provides states a higher federal matching payment than under the regular Medicaid program. Prior to the passage of the Federal Balanced Budget Act of 1997, which included CHIP, Ohio included in its biennial budget a children's health insurance expansion for children up to the age of 19 in families at or below 150 percent of the FPG. Combining the state's initiative with the federal CHIP opportunity, Ohio submitted a CHIP State Plan to the Center for Medicare and Medicaid (CMS, formerly known as the Health Care Financing Administration, or HCFA) to implement a Medicaid expansion under CHIP. CMS approved Ohio's CHIP State Plan on March 23, 1998 – making Ohio the fifth state approved to draw down CHIP funding. Ohio implemented its children's health insurance plan (CHIP-I) by expanding Healthy Start, to include Medicaid coverage for low-income children up to age 19, in families at or below 150 percent of the FPG.

CHIP-II. Am. Sub. H.B. 283 of the 123rd General Assembly, the main budget act, appropriated funds for the Children's Health Insurance Plan II (CHIP-II) under Title XXI, for uninsured children under age 19 in families with incomes between 150 percent and 200 percent of the FPG. CHIP-II commenced on July 1, 2000.

Caseloads Forecast

Total Caseload. The total number of persons eligible for Medicaid grew by 11.19 percent from 1,276,967 in FY 2001 to 1,419,856 in FY 2002. The total number of eligibles is estimated to reach 1,559,487 in FY 2003, a 9.83 percent increase over FY 2002. LSC forecasts that the number of persons eligible for Medicaid will continue to grow to

1,637,550 in FY 2004 and 1,650,731 in FY 2005, a 5.01 percent and a 0.80 percent increase, respectively.

The last time the Medicaid program was expanded was in July 2000. At that time, JFS implemented two expansions. First, coverage was extended to parents with enrolled children for families with incomes at or below 100 percent of the FPG under the Healthy Families program. Second, JFS rolled out CHIP-II, expanding Healthy Start eligibility to uninsured children from families with incomes between 150 percent and 200 percent of the FPG. No program expansions were implemented during the FYs 2002-2003 biennium. The forecast assumes that no program expansions will be implemented during the coming biennium.

Poor labor market conditions associated with the recession (which has not been declared to have ended as of this writing) have been the primary driving force behind the growth in total caseload. An additional factor behind the recent growth in caseload has been the CHIP-II program expansion. The eligible population for CHIP-II grew by slightly over 90 percent in FY 2002, and is forecast to grow by an additional 17.99 percent in FY 2003 as the process of enrolling those made newly eligible under the expansion reaches its conclusion.

Covered Families and Children. LSC forecasts that the overall CFC caseload will peak in the fourth quarter of FY 2004, and begin to drop in the second quarter of FY 2005 as the economy begins to recover. This forecast is based on a statistical model of the relationship between the Healthy Families caseload and the unemployment rate. Forecasts of future unemployment rates used for the caseload forecast are taken from the January 2003 economic forecast by Global Insight (formerly DRI-WEFA).

Aged, Blind, and Disabled. Growth in the ABD caseload accelerated in FY 2002, and this acceleration continued into the first half of FY 2003. This acceleration was driven by the disabled subcategory of the ABD category. The accelerated growth in the disabled subcategory is projected to continue through the end of FY 2003, after which the growth rate is projected to gradually return to a more typical historical rate. The Aged subcategory is projected to increase at average historical rates, with a slight adjustment for the growth in the overall Ohio population over the age of 65.

HMO Penetration. Although Ohio has contracted with HMOs since the late 1970s to provide care for certain Medicaid eligibles, the use of capitated rates was not given major emphasis in Ohio's program until the state received an 1115 demonstration waiver in January 1995. As one initiative of the federally approved OhioCare proposal, the state was given the freedom to require mandatory HMO enrollment by CFC Medicaid eligibles. Ohio Medicaid's experience with mandatory enrollment on a large scale began in 1996, with the implementation of the waiver. However, despite a concerted effort to attract new plans, the program (as in the other areas of the country) has been plagued by limited interest and other

obstacles. Counties with mandatory enrollment have dropped from a high of ten (Butler, Cuyahoga, Franklin, Hamilton, Lorain, Lucas, Montgomery, Stark, Summit, and Wood) to four (Cuyahoga, Lorain, Lucas, and Summit).
CFC eligibles access their health care benefits through either the traditional fee-for-service system or the Medicaid managed care program. The Medicaid managed care program has three different enrollment categories: mandatory, voluntary, and preferred option. In FY 2001, the state introduced the preferred option. Under preferred option, recipients are automatically enrolled in managed care if they fail to select the traditional fee-for-service option. This policy has pushed up the HMO penetration rate[19] from 27.97 percent in FY 2001 to 32.44 percent in FY 2002.

LSC's baseline forecast assumes that the take up effect of the preferred option program will diminish in FY 2003, and the HMO penetration rate will be approximately 35 percent for FY 2004 and FY 2005. In other words, about 35 percent of all Covered Family and Children consumers are expected to be enrolled in a Medicaid HMO during the next biennium.

Medicaid Program Cost Forecast

Medicaid program costs are estimated separately for each of the nine major expenditure categories described in the Forecast Summary section. After forecasting changes in the caseload, a cost per Medicaid recipient is projected. The cost per recipient is itself broken down into two components: the average number of claims per recipient, called the "utilization rate," and the average cost per claim submitted. The average cost per claim depends heavily on overall health care inflation -- Medicaid spending on health care services that are market driven significantly outweighs program payments to providers that are tied to fee schedules. In addition, payment rates for long-term care, inpatient hospital care, and prescription drugs are statutorily connected to market place trends. Consequently, Medicaid, like any other third party payer, is very susceptible to market forces.

Most measures of price inflation in the health care sector of the U.S. economy showed that inflation decelerated in 2002. Among the measures showing this are the Producer Price Index for Health Services, the price deflator for Personal Consumption Expenditures on Medical Care (PCE-MC), and the price deflator derived for the National Income and Product Accounts medical care component. Nevertheless, some components of the Consumer Price Index (CPI) indicate that some categories of care experienced an acceleration in inflation during 2002, and Global Insight is forecasting an acceleration in inflation in the overall health sector in 2003 and 2004.

[19] Penetration is the number of managed care eligible divided by total Covered Family and Children eligibles.

Generally speaking, the forecast of average cost per claim in each category of care under Medicaid starts with historical data on costs per claim. To project whether increases in costs per claim would accelerate or decelerate, LSC used the Global Insight forecast of inflation, as measured by the price deflator for PCE-MC, as a baseline. This baseline was then adjusted separately for each category of care. For those categories for which there is a corresponding subcomponent of the CPI, that subcomponent is used to make the adjustment. Some of the subcategories of care that are lumped under the All Other Care component of Medicaid spending do not have a corresponding subcomponent of the CPI, and in those cases the assumption regarding inflation was based on the PCE-MC with no adjustments. The prescription drug spending category received special treatment. The above method yielded a deceleration in health inflation in 2005. A separate Global Insight forecast of the price deflator for PCE on drugs indicated an acceleration of inflation in 2005. Due to the conflicting results from these two approaches, inflation for the prescription drug category was projected to continue at the same rate in FY 2005 as was projected for FY 2004.

Historical relationships between the number of eligibles in each eligibility group and the number of claims they generate in each category of service allow for the calculation of utilization rates. By applying forecasts of utilization rates to forecasts of the number of eligibles, an estimated number of claims can be calculated.
Due to the delayed submissions of claims by providers and delays in processing payments, claims are not always paid in the same quarter in which services are given to Medicaid eligibles. In fact, it is generally the case that providers are not completely reimbursed for all of the services they give to Medicaid eligibles until well over a year following the date of service. Thus, it is necessary to make the distinction between the date of service and the date of payment.

Because disbursements from the 525 line item reflect the payment of claims and not the provision of services, it is necessary to incorporate the appropriate payment lags when estimating spending from the 525 line item. In short, forecasting Medicaid spending involves the estimation of the number of Medicaid eligibles in each month. Then it is necessary to estimate the demand each eligibility group will have for each major category of service. The next step is to estimate the relevant cost-per-claim. Taken together these estimates can be used to predict the cost of services in a given period (in this case, quarterly). However, disbursement estimates reflect the payment of claims -- so it is necessary to apply the appropriate payment lags before the estimates are complete.

Nursing Facilities. Expenditures for nursing facilities' services were $2.46 billion and represented approximately 35 percent of expenditures from line item 525 in FY 2002.
Payments to nursing facilities are based on cost reports. Nursing facilities annually submit cost reports to JFS, which are used to calculate facility-specific per diems for the following state fiscal year. In other words, each fiscal year's per diem rates are based on cost reports from the preceding calendar year. The per diem rates are then adjusted

quarterly to account for differences in each resident's needs -- known as the "case-mix adjustment."

The FYs 2002-2003 biennial budget act established a maximum mean total per diem rate applicable to nursing facilities in FY 2002 and FY 2003. For FY 2002, the mean total per diem rate for all nursing facilities in the state, weighted by Medicaid days and calculated as of July 1, 2001, is not to exceed $143.92. For FY 2003, the mean total per diem rate for all nursing facilities in the state, weighted by Medicaid days and calculated as of July 1, 2002, is not to exceed $152.66, plus any difference between $143.92 and the mean total per diem rate for all nursing facilities in the state for FY 2002, weighted by Medicaid days and calculated as of July 1, 2001, under the law governing the calculation of Medicaid reimbursement rates.

LSC also offers the following more general observation on some of the important dynamics surrounding nursing facilities and their costs of care. In this country, for various reasons related to demography, lifestyles, the physical environment, medical care, and so forth, people are living longer and the size of the aging population is growing. As a result, there is a larger pool of people that might require the more intensive level and more costly form of care associated with a nursing facility stay and for longer periods of time as well. To aid in constraining the acceleration of nursing facility care costs associated with such a trend is the development of less-costly alternative forms of care, programs like PASSPORT, which allow some people with a nursing home level of care to live in the community. From the perspective of nursing facilities, this means that the medical conditions of those people occupying their beds these days are generally more acute than was previously the case. This rise in acuity level alone would increase the nursing facility's cost of doing business and the state's per diem has grown to reflect that reality.

In summary, the rise in the state's per diem is fueled by heightened acuity levels, increased capital costs, and to a larger extent, elevated direct care costs. The average per diem in FY 2002 increased by 8.37 percent from FY 2001 levels of $132.31 to $143.38. The average per diem in FY 2003 is projected to grow by 6.22 percent to $152.29. The average per diem in FY 2004 and FY 2005 is projected to grow by 4.78 percent to $159.56 and 5.25 percent to $167.94, respectively. Estimated expenditures for Nursing Home Services are $2.76 billion in FY 2004 and $2.95 billion in FY 2005.

Inpatient and Outpatient Hospital Services. Expenditures for Inpatient and Outpatient Hospital Services were $1.55 billion and represented approximately 22 percent of expenditures from the 525 line item in FY 2002.

The Ohio Administrative Code requires an annual inflationary update to inpatient rates; however, outpatient rates are based on a fee schedule that is not automatically inflated. Health economists are predicting increased health care inflation in the coming years. In addition, demand for more and expanded health care services continues to push up the costs. The growth rate in spending for hospital care is projected to be 9.70 percent from FY 2003 to FY 2004, and 7.85 percent from FY 2004 to FY 2005. Estimated expenditures for Inpatient and Outpatient Hospital Services are $1.97 billion in FY 2004 and $2.12 billion in FY 2005.

Physician Services. The cost estimates for Physician Services reflect the historical costs of providing medical care. The growth rate in spending is projected to be 12.95 percent from FY 2002 to FY 2003, 9.74 percent from FY 2003 to FY 2004, and 6.88 percent from FY 2004 to FY 2005. Estimated expenditures for Physician Services are $582.6 million in FY 2004 and $622.6 million in FY 2005.

Prescription Drugs. Expenditures for Prescription Drug Services were $1.24 billion and represented approximately 17.5 percent of expenditures from the 525 line item in FY 2002. Offsetting the prescription drug services expenditures was the prescription drug rebate of $258.5 million in FY 2002.
S.B. 261 of 124th General Assembly authorizes JFS to establish a supplemental drug rebate program under which drug manufacturers may be required to provide a supplemental rebate to the state as a condition of having their products covered by Medicaid without prior approval. The bill also allows the Director of JFS to apply for a federal Medicaid waiver, if necessary, to establish the program. It is expected that this program will be implemented in the coming biennium. LSC assumes that this policy will affect the growth of cost-per-claim, as well as drug utilization, and thus forecasts that the growth rates for cost-per-claim and utilization ratio will decelerate and hold constant for FY 2004 and FY 2005. Estimated expenditures for Prescription Drug Services are $1.76 billion in FY 2004 and $1.99 billion in FY 2005. Offsetting the prescription drug services expenditures is the prescription drug rebate estimated at $371.8 million in FY 2004 and $430.3 million in FY 2005.

The prescription drug utilization rate for ABD eligibles is expected to increase by 5.29 percent in FY 2003, 3.96 percent in FY 2004 and FY 2005. LSC estimates that the prescription drug cost-per-claim for the ABD population will increase by 6.37 percent over FY 2003. Note that the increase in the prescription drug cost-per-claim is not entirely due to inflationary factors -- it also may be due to an increased number of drugs per claim and a shift to higher cost drugs within each claim. The increases in cost-per-claim are expected to continue in FY 2004 and FY 2005, increasing by 5.59 percent each year.

The combined effects of the increased utilization rates and increased costs-per-claim for the ABD population, as well as other eligibility groups, are expected to result in an increase in prescription drug spending of 23.44 percent in FY 2003, 14.47 percent in FY 2004, and 12.98 percent in FY 2005.

Health Care Spending (ALI 600-525 Only)
Table 1

Service Category	FY 2002	FY 2003		FY 2004		FY 2005	
	Actual	Estimated	% Change	Estimated	% Change	Estimated	% Change
Long Term Care	$2,878,316,825	$3,023,192,682	5.03%	$3,196,882,543	5.75%	$3,403,753,579	6.47%
Nursing Facilities	$2,461,762,040	$2,594,029,881	5.37%	$2,756,788,734	6.27%	$2,950,871,715	7.04%
ICF/MRs	$416,554,785	$429,162,801	3.03%	$440,093,809	2.55%	$452,881,864	2.91%
Hospitals	$1,554,044,390	$1,795,104,002	15.51%	$1,969,250,314	9.70%	$2,123,763,924	7.85%
Inpatient	$1,099,011,540	$1,262,894,378	14.91%	$1,380,190,293	9.29%	$1,483,992,231	7.52%
Outpatient	$455,032,850	$532,209,624	16.96%	$589,060,021	10.68%	$639,771,693	8.61%
Physicians	$469,970,680	$530,853,727	12.95%	$582,552,534	9.74%	$622,620,895	6.88%
Prescription Drugs	$1,244,229,690	$1,535,835,042	23.44%	$1,758,091,686	14.47%	$1,986,332,347	12.98%
HMO	$597,202,743	$738,505,804	23.66%	$847,102,898	14.70%	$897,725,969	5.98%
Medicare Buy-In	$133,386,397	$151,071,008	13.26%	$161,595,642	6.97%	$172,718,896	6.88%
Waiver	$162,482,168	$183,394,398	12.87%	$221,645,685	20.86%	$248,613,924	12.17%
All Other Care	$662,893,933	$777,901,354	17.35%	$879,958,142	13.12%	$960,030,703	9.10%
CHIP-II	$47,900,786						
DA Medical	$67,868,259	$90,100,000	32.76%	$109,000,000	20.98%	$134,900,000	23.76%
Claims FY04 53rd Week				$92,000,000			
Total	**$7,818,295,871**	**$8,825,958,017**	**12.89%**	**$9,818,079,444**	**11.24%**	**$10,550,460,237**	**7.46%**
Other Revenue Offset	$691,685,505	$1,089,540,009		$794,207,562		$857,429,318	
Total Net GRF Expenditures	**$7,126,610,366**	**$7,736,418,008**	**8.56%**	**$9,023,871,882**	**16.64%**	**$9,693,030,919**	**7.42%**
Federal Share	$4,200,424,150	$4,515,241,231		$5,290,034,376		$5,680,676,907	
State Share	$2,926,186,216	$3,221,176,777		$3,733,837,506		$4,012,354,011	

Note:

1. This table only includes health care spending through Department of Job and Family Services' 600-525 line item. It includes spending for Medicaid, CHIP-I, CHIP-II, and DA Medical.
2. The forecast is the LSC baseline forecast, which assumes no change in the state health care policies and program for the upcoming biennium.
3. "Other Revenue Offset" includes revenue from drug rebates, franchise fees, DSH payments, and Budget Stabilization Fund. Expenditures of CHIP-II and DA Medical are included in the Other Revenue Offset for FY 2002 since CHIP-II was funded through line item 600-426 and DA Medical was funded through line item 600-511 prior to FY 2003.
4. The growth rate for FY 2003 for Hospitals, Physicians, Prescription Drugs, HMO, and All Other Care includes the growth of CHIP-II spending.
5. "All Other Care" includes services such as dental care, home health care, and other practitioners, and includes various contracts.
6. The FMAP rate used here is a blended FMAP.

Health Care Spending
Table 2

Fiscal Year	ALI 600-525 Total	% Change	Financial Participation State	% Change	Federal	% Change
1991	$3,304,346,333	17.92%	$1,350,486,346	17.66%	$1,953,859,987	18.10%
1992	$3,941,073,001	19.27%	$1,661,556,377	23.03%	$2,279,516,624	16.67%
1993	$4,149,379,774	5.29%	$1,686,307,940	1.49%	$2,463,071,834	8.05%
1994	$4,521,872,195	8.98%	$1,779,356,709	5.52%	$2,742,515,486	11.35%
1995	$4,585,549,544	1.41%	$1,791,624,838	0.69%	$2,793,924,706	1.87%
1996	$4,941,254,040	7.76%	$1,971,066,236	10.02%	$2,970,187,804	6.31%
1997	$4,897,184,802	-0.89%	$1,987,767,311	0.85%	$2,909,417,491	-2.05%
1998	$5,056,299,328	3.25%	$2,107,465,560	6.02%	$2,948,833,768	1.35%
1999	$5,229,514,139	3.43%	$2,214,699,238	5.09%	$3,014,814,901	2.24%
2000	$5,525,569,750	5.66%	$2,294,216,560	3.59%	$3,231,353,190	7.18%
2001	$6,481,731,098	17.30%	$2,657,509,750	15.84%	$3,824,221,348	18.35%
2002	$7,126,610,366	9.95%	$2,926,186,216	10.11%	$4,200,424,150	9.84%
2003*	$7,736,418,008	8.56%	$3,221,176,777	10.08%	$4,515,241,231	7.49%
2004*	$9,023,871,882	16.64%	$3,733,837,506	15.92%	$5,290,034,376	17.16%
2005*	$9,693,030,918	7.42%	$4,012,354,011	7.46%	$5,680,676,907	7.38%

* LSC baseline estimates

Note:

1. This table only includes health care spending through the Department of Job and Family Services' 600-525 line item. Beginning in FY 2003, it includes spending for CHIP-II, and DA Medical.
2. The LSC baseline forecast assumes no change in the state health care policies and program for the upcoming biennium.

Medicaid Caseload by Eligibility Group
Table 3

	ABD&CFC		ABD							
Fiscal	Total		Total ABD		ABD (no QMB)		QMB		SLMB	
Year	mo. avg.	% change	mo. avg.	% change	mo. avg.	% change	mo. avg.	% change	mo. avg.	% change
1991	1,108,464		232,629		228,955		3,674			
1992	1,232,398	11.18%	255,971	10.03%	246,369	7.61%	9,602	161.38%		
1993	1,270,110	3.06%	280,162	9.45%	263,676	7.02%	16,067	67.32%	420	
1994	1,294,972	1.96%	313,240	11.81%	286,655	8.71%	20,191	25.67%	6,395	
1995	1,284,005	-0.85%	345,304	10.24%	309,576	8.00%	22,773	12.79%	12,955	102.58%
1996	1,228,262	-4.34%	366,783	6.22%	321,978	4.01%	22,736	-0.16%	22,069	70.35%
1997	1,166,169	-5.06%	370,047	0.89%	323,023	0.32%	23,791	4.64%	23,233	5.27%
1998	1,107,999	-4.99%	365,493	-1.23%	315,884	-2.21%	23,683	-0.46%	25,925	11.59%
1999	1,095,716	-1.11%	373,158	2.10%	314,855	-0.33%	23,538	-0.61%	34,764	34.09%
2000	1,109,202	1.23%	372,357	-0.21%	318,720	1.23%	23,635	0.41%	30,002	-13.70%
2001	1,276,967	15.12%	376,886	1.22%	323,150	1.39%	22,451	-5.01%	31,284	4.28%
2002	1,419,856	11.19%	383,846	1.85%	327,427	1.32%	20,800	-7.35%	35,619	13.86%
2003*	1,559,487	9.83%	404,035	5.26%	342,955	4.74%	22,138	6.43%	38,942	9.33%
2004*	1,637,550	5.01%	421,222	4.25%	358,636	4.57%	22,775	2.88%	39,810	2.23%
2005*	1,650,731	0.80%	434,715	3.20%	370,959	3.44%	23,048	1.20%	40,708	2.25%

	CFC									
Fiscal	Total		Healthy Families		Healthy Start		CHIP-I / HS Exp		CHIPII	
Year	mo. avg.	% change	mo. avg.	% change	mo. avg.	% change	mo. avg.	% change	mo. avg.	% change
1991	875,835		828,828		47,007					
1992	976,427	11.49%	894,261	7.89%	82,166	74.80%				
1993	989,948	1.38%	880,786	-1.51%	109,162	32.86%				
1994	981,732	-0.83%	858,069	-2.58%	123,663	13.28%				
1995	938,701	-4.38%	808,875	-5.73%	129,826	4.98%				
1996	861,479	-8.23%	721,950	-10.75%	139,529	7.47%				
1997	796,122	-7.59%	662,403	-8.25%	133,719	-4.16%				
1998	742,506	-6.73%	580,827	-12.32%	137,912	3.14%	23,767			
1999	722,558	-2.69%	500,840	-13.77%	169,210	22.69%	52,509	120.93%		
2000	736,846	1.98%	481,064	-3.95%	185,127	9.41%	70,655	34.56%		
2001	900,081	22.15%	657,175	36.61%	141,385	-23.63%	81,310	15.08%	20,210	
2002	1,036,010	15.10%	774,752	17.89%	130,898	-7.42%	91,897	13.02%	38,464	90.32%
2003*	1,155,452	11.53%	863,707	11.48%	143,126	9.34%	103,235	12.34%	45,385	17.99%
2004*	1,216,328	5.27%	906,511	4.96%	151,280	5.70%	109,721	6.28%	48,816	7.56%
2005*	1,216,016	-0.03%	906,935	0.05%	151,010	-0.18%	109,441	-0.25%	48,630	-0.38%

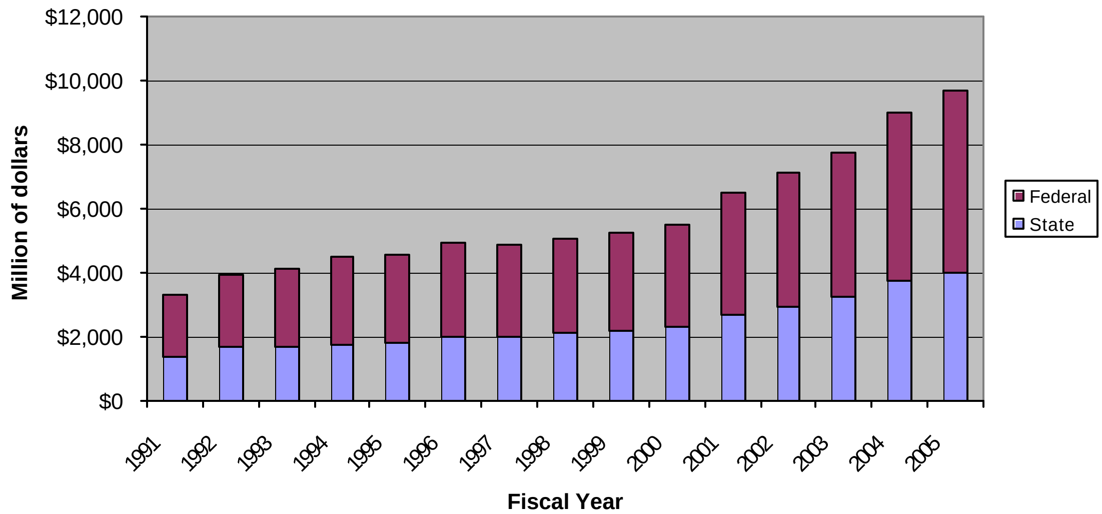
* LSC baseline estimates

Medicaid Caseload for Covered Families and Children (CFC):
Fee-for-Service vs HMO
Table 4

Fiscal Year	Total CFC mo. avg.	Total CFC % change	FFS mo. avg.	FFS % change	HMO mo. avg.	HMO % change	Penetration Rate (=HMO/CFC)
1991	875,835		750,006		125,829		14.37%
1992	976,427	11.49%	842,914	12.39%	133,513	6.11%	13.67%
1993	989,948	1.38%	841,939	-0.12%	148,009	10.86%	14.95%
1994	981,732	-0.83%	812,600	-3.48%	169,133	14.27%	17.23%
1995	938,701	-4.38%	748,172	-7.93%	190,528	12.65%	20.30%
1996	861,479	-8.23%	607,327	-18.83%	254,153	33.39%	29.50%
1997	796,122	-7.59%	464,883	-23.45%	331,239	30.33%	41.61%
1998	742,506	-6.73%	411,458	-11.49%	331,048	-0.06%	44.59%
1999	722,558	-2.69%	465,809	13.21%	256,750	-22.44%	35.53%
2000	736,846	1.98%	483,743	3.85%	253,103	-1.42%	34.35%
2001	900,081	22.15%	648,350	34.03%	251,731	-0.54%	27.97%
2002	1,036,010	15.10%	699,979	7.96%	336,031	33.49%	32.44%
2003*	1,155,452	11.53%	757,613	8.23%	397,839	18.39%	34.43%
2004*	1,216,328	5.27%	790,213	4.30%	426,115	7.11%	35.03%
2005*	1,216,016	-0.03%	780,831	-1.19%	435,185	2.13%	35.79%

* LSC baseline estimates

Health Care (600-525 Only) Spending History
Chart 1



Medicaid Eligibility - Monthly Averages
Chart 2