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TOPICS OF LEGISLATIVE INTEREST

January/February 2008

Federal Expenditures in Michigan

By Gary S. Olson, Director

Each fiscal year, the Federal government allocates a significant portion of the overall Federal budget to expenditures that have a direct impact on the states. The United States Bureau of the Census annually reports on these Federal expenditures to the states in its report entitled, *"Consolidated Federal Funds Report"*. The most recent Consolidated Federal Funds Report is for fiscal year (FY) 2005.

The Census Bureau report covers five broad categories of Federal expenditures received by states. These categories are: retirement and disability payments to individuals, other direct payments to individuals, Federal salaries and wages, procurement, and grants to state and local governments. Retirement and disability payments include such large Federal programs as Social Security payments and pension payments to retired Federal employees. Other direct payments to individuals include the Medicare program, food stamps, and unemployment compensation payments. Federal salaries and wages measure the amount spent in each state on the base salary and overtime costs of Federal employees located within the state. Procurement is the amount spent in each state for direct purchases by the Federal government of either goods or services. Grants to state and local government are direct Federal aid programs and include such programs as Federal transportation aid, job training aid, education spending, and the Medicaid program.

Historically, Michigan's share of Federal expenditures has lagged behind the amount of most other states. As measured on a per-capita basis, in FY 2005 total Federal expenditures in Michigan equaled $6,414. The national average for all states on a per-capita basis was $7,706. Table 1 provides a summary of Federal expenditures in Michigan during FY 2005. Michigan's total per-capita expenditures ranked 43rd among the states. The only two broad categories of Federal expenditures in which Michigan was close to the national average were the categories of retirement and disability payments to individuals and other direct payments to individuals. Michigan ranked 28th and 24th on a per-capita basis for these types of Federal expenditures. Michigan's rank was 49th among the states in Federal salaries and wages, 40th among the states in procurement, and 39th among the states in grants to state and local governments.

Table 1

Distribution of Federal Funds
Fiscal Year 2005
(Millions of Dollars)

	National Amount	Michigan Amount	Mich. as % of Nat'l Total	National Per Capita	Michigan Per Capita	Mich. Rank
Retirement & Disability Payments to Individuals	$702,758	$24,369	3.5%	$2,348	$2,413	28
Other Direct Payments to Individuals	499,928	17,533	3.5%	1,676	1,736	24
Federal Salaries and Wages	231,511	3,722	1.6%	781	368	49
Procurement	380,984	5,849	1.5%	1,285	579	40
Grants to State & Local Governments	469,579	13,313	2.8%	1,584	1,318	39
Total	**$2,284,760**	**$64,786**	**2.8%**	**$7,706**	**$6,414**	**43**
Resident Population	296,507,061	10,100,833	3.4%			

Source: United States Bureau of Census, Federal Expenditures by State for Fiscal Year

An analysis of the Census Bureau data leads to the conclusion that the citizens of Michigan are receiving much less than their fair share of Federal expenditures if the expenditures were simply distributed on a per-capita basis. Table 2 provides a summary of the actual amount of Federal expenditures received in Michigan for the period FY 1985 through FY 2005 versus the amount that Michigan would have received if Federal expenditures had equaled Michigan's percentage of the total United States population. In FY 2005, this Federal funding shortfall equaled $13.0 billion.

Table 2

Michigan's Federal Funding Shortfall (Millions of Dollars)

Fiscal Year	Actual Federal Expenditures in Michigan	Federal Expenditures in Michigan on a Per-Capita Basis	Michigan's Expenditure Shortfall
1985	$22,384	$29,844	$(7,460.8)
1986	23,342	31,398	(8,055.5)
1987	23,283	31,814	(8,530.4)
1988	23,887	33,207	(9,320.3)
1989	26,109	34,735	(8,625.3)
1990	29,433	37,438	(8,005.6)
1991	31,968	41,292	(9,323.4)
1992	36,137	44,998	(8,860.3)
1993	37,238	46,845	(9,607.2)
1994	39,485	49,021	(9,536.4)
1995	39,569	49,055	(9,486.5)
1996	39,633	50,062	(10,429.2)
1997	40,651	51,441	(10,789.7)
1998	41,917	53,905	(11,988.6)
1999	44,128	55,355	(11,227.5)
2000	46,851	58,242	(11,390.9)
2001	51,722	62,986	(11,264.3)
2002	55,910	67,566	(11,656.2)
2003	57,870	71,455	(13,584.8)
2004	60,488	74,460	(13,971.8)
2005	64,786	77,833	(13,046.8)

Source: United States Bureau of the Census, Senate Fiscal Agency calculations

The $13.0 billion shortfall in FY 2005 represents a decline from Michigan's Federal funding shortfall in FY 2004 of $14.0 billion. Michigan moved from a per-capita ranking of 46th among the states in FY 2004 to 43rd in FY 2005. This movement up for Michigan in the national per-capita rankings can be attributed to Michigan's recent economic problems compared with those of other states. The economic situation in Michigan has led to increased payments in such programs as unemployment compensation and Medicaid. Spending on these programs tends to increase in a state experiencing severe economic problems, such as Michigan.

The Federal funding shortfall in Michigan can be attributed to two major factors. First is that Michigan has a smaller proportion of Federal employees compared with other states. The second is the lack of major defense facilities or major defense contractors within Michigan. This accounts for Michigan's ranking of 49th among the states in per-capita Federal procurement.

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Update on Michigan Department of Corrections Spending Pressures
By Lindsay Hollander, Fiscal Analyst

The Michigan Legislature is currently considering the Governor's budget recommendation for fiscal year (FY) 2008-09. Changes in the appropriation for the Michigan Department of Corrections (MDOC) are dependent on various spending pressures, such as the prison and camp population, staffing costs, and health care costs. This analysis includes year-to-date (YTD) appropriation and population information from FY 2001-02 to FY 2006-07. Additionally, the article discusses employee-related economic increases up to the current fiscal year, FY 2007-08.

Appropriation and Prisoner Population

During the course of the analysis period, the Michigan Department of Corrections' YTD General Fund/General Purpose (GF/GP) appropriation grew every year. As displayed in Table 1, this is in contrast to the prison population, but somewhat consistent with other expenditures. The Gross appropriation decreased in FY 2002-03 from its FY 2001-02 amount, but then grew at an increasing rate until FY 2006-07. It did not grow as rapidly as the GF/GP appropriation grew, which may be because the MDOC appropriation has become increasing reliant on GF/GP revenue as a funding source. In FY 2001-02, GF/GP funding was 94.8% of the Gross appropriation, and that proportion grew almost every year since, with GF/GP funds accounting for 95.8% of the Gross appropriation in FY 2006-07.

Table 1

Five-Year Appropriation, Population, and Full-Time Equated (FTE) Position History

Fiscal Year	Change in Prison & Camp Population	Change in Avg. Cost/ Prisoner	Change in FTE Positions	Change in Gross Approp.	Change in GF/GP Approp.	Change in Prisoner Health Care Approp.[1]	Health Care as a % of Gross Approp.[1]
2002-03	(1.0)%	(2.4)%	(2.90)%	(0.06)%	0.02%	4.97%	9.27%
2003-04	(1.7)	3.8	(2.82)	1.11	0.59	3.65	9.50
2004-05	1.6	4.0	(2.97)	3.70	4.95	4.95	9.61
2005-06	4.0	6.7	(1.38)	6.59	6.94	12.85	10.18
2006-07	(2.0)	1.0	1.56	3.61	3.64	18.87	11.68

[1] Includes Health Care Administration, Hospital & Specialty Care Services, Vaccination Program, Hepatitis C Testing & Treatment, and all Clinical Complexes. Does not include Consent Decrees.

Source: Michigan Department of Corrections; Annual Appropriation Acts

The prison and camp population fluctuated between FY 2001-02 and FY 2006-07. Table 2 lists the number and percentage of prisoners by security level for that period. The table shows that the number of Level I (lowest security level) prisoners generally rose, while Level IV and V prisoners decreased. The cost of care for a prisoner in a higher security level is higher on average than for a lower security level prisoner. Despite this, the approximate average cost per prisoner rose almost every year. Changes in average cost per prisoner positively correlate with changes in GF/GP appropriations, due to the fact that typically 84.0% to 87.0% of the GF/GP appropriation is spent on prisoner costs. The only other measure with a higher average annual percentage change than GF/GP and the annual cost per prisoner is the health care appropriation.

The health care appropriation rose every year, with an additional $58.1 million allocated during the past two years. In order to fund care for the population, the health care appropriation supports hundreds of nurses, physicians, and mid-level positions, as well as treatment and specialty care costs. Currently, a third of the prison population is in chronic care clinics, meaning those prisoners have a chronic condition that necessitates seeing a doctor at least twice per year. It makes sense that the health care appropriation has grown along with the average cost per prisoner, because after prison and camp staffing and operations, health care is the largest portion of the average cost per prisoner. Health care, which is supported almost exclusively by GF/GP dollars, is one component of the increasing appropriations for the MDOC.

Table 2

Michigan Prison Population History by Security Level

Fiscal Year	Total Population	Level I	Level II	Level IV	Level V	Other[1)]
2001-02	49,478	17,390	18,956	5,445	1,964	5,723
2002-03	49,002	17,139	19,344	5,143	1,930	5,446
2003-04	48,185	17,595	18,613	5,370	1,764	4,843
2004-05	48,970	18,560	18,616	4,722	1,757	5,315
2005-06	50,946	20,320	18,617	4,582	1,436	5,991
2006-07	49,928	20,451	18,260	4,475	1,422	5,362
		% Total	**% Total**	**% Total**	**% Total**	**% Total**
2001-02	49,478	35.15%	38.31%	11.00%	3.97%	11.57%
2002-03	49,002	34.98	39.48	10.50	3.94	11.11
2003-04	48,185	36.52	38.63	11.14	3.66	10.05
2004-05	48,970	37.90	38.02	9.64	3.59	10.85
2005-06	50,946	39.89	36.54	8.99	2.82	11.76
2006-07	49,928	40.39	36.54	8.96	2.85	10.73

[1)] Other includes segregation, Level V reception, youthful offenders, various mental health units, etc.

Source: Michigan Department of Corrections Client Census Reports

Employee Costs

Employee costs also have a major impact on the MDOC appropriation. Approximately 70.0% of the Department's budget is spent on staffing costs. Interestingly, the number of full-time equated positions (FTEs) has gone down every year during the period. Measures such as the human resources optimization, which have cut costs and FTEs for individual departments, could be one explanation for this decrease. If FTEs are cut more than costs are reduced, then the number of FTEs will not grow with the appropriation. Another reason for this reduction may be that employee costs are rising. For FY 2002-03 through FY 2007-08, Table 3 shows appropriated economic increases as enacted, but excludes any unfunded economic increases. After peaking in FY 2004-05, funded employee-related economic increases actually decreased both in total amount, and as a percentage of the total appropriation, in the following two years. In FY 2007-08, these economic increases have risen dramatically, but this is primarily due to an executive order one-time reduction in the retirement contribution in FY 2006-07 that had to be restored in the FY 2007-08 appropriation. Otherwise, the funded employee-related economic increases in FY 2007-08 would have been lower as a percentage of the enacted appropriation than in FY 2006-07.

The MDOC budget was reduced in other areas since FY 2004-05 in order to fund economic increases displayed in Table 3. For example, in FY 2003-04, the MDOC abolished 80 FTE management positions in order to fund the previous year's retirement shortfall. In FY 2002-03 and 2003-04, appropriations for economic increases were either entirely or partially unfunded. In FY 2007-08, Southern Michigan Correctional Facility and Camp Manistique closed in order to fund increases. Regardless of what is funded in the appropriation, the MDOC is responsible for paying any contractual increases in employee salaries and benefits. If they are not funded, the MDOC must make reductions elsewhere, which results in actual employee costs' taking up an even greater proportion of the full appropriation. Table 4 shows how employee-related expenditures as a percentage of the appropriation increased significantly beginning in FY 2004-05, when the staffing cost increase was more than double the total appropriation increase. This proportion did drop in FY 2006-07, partially a result of the retirement rate reduction. Without that reduction, the 1.7% drop would have been a 0.9% decrease.

Table 3

History of Funded Employee-Related Economic Increases

Fiscal Year	Salary	Insurance	Retirement	Other	Total Employee Economics	% of Enacted Gross Appropriation	Total Appropriation Increase
2002-03	$17,876,300	$ 0	$2,331,800	$(7,217,100)[a]	$12,991,000	0.76%	$17,854,300
2003-04[b]		0	0	28,595,600[c]	28,595,600	1.66	37,450,369
2004-05	61,617,600	21,209,900	68,827,200	(46,342,500)[d]	105,312,200	5.90	80,352,719
2005-06	10,590,700	22,831,700	18,362,900	46,342,500[d]	98,127,800	5.28	91,198,600
2006-07	36,328,100	13,633,100	32,057,900	0	82,019,100	4.23	70,315,100
2007-08	42,283,700	16,714,900	24,356,500	64,865,600[e]	148,220,700	7.13	124,646,100

[a] This eliminated a lump sum salary payment that had been part of the contract during FY 2000-01 and FY 2001-02.
[b] Salary, insurance, and retirement increases were unfunded this year, but totaled $81.2 million.
[c] Restored FY 2002-03 shortfall in retirement.
[d] This reduction and subsequent increase of the same amount mark the start and end of employee concessions such as furlough days and banked leave time.
[e] Executive Order 2007-3 reduced the rate departments had to pay into the retirement fund, resulting in a $64,865,600 reduction in FY 2006-07. In FY 2007-08, this funding was restored. If this is not included, economic increases as a percentage of the enacted Gross appropriation would be 4.01% and would total $83,355,100.

Source: Office of State Budget

Table 4

Employee-Related Expenditures			
Fiscal Year	Employee-Related Expenditures	YTD Appropriation	Percent of YTD Appropriation
2002-03	$1,172,840,833	$1,687,056,800	69.5%
2003-04	1,172,211,289	1,705,829,900	68.7
2004-05	1,302,251,756	1,768,907,800	73.6
2005-06	1,384,836,314	1,885,554,200	73.4
2006-07	1,399,894,911	1,953,623,000	71.7

Source: Michigan Administrative Information Network

Another component of employee costs is realized in the form of overtime. In general, staff working more than eight hours per day, or more than 80 hours biweekly, must be paid one and a half times their salary for those additional hours. Table 5 shows that the amount the MDOC paid in regular overtime for correctional facility staff rose between FY 2002-03 and FY 2006-07. Not only did the amount spent increase during every year shown in Table 5, but it took up an increasing proportion of the Gross appropriation. For the current fiscal year, the MDOC is trying to alleviate this issue by hiring more correctional officers. Once new officers are trained, the MDOC will save money by paying a new officer full-time salary with benefits, rather than paying 80 hours biweekly of overtime to existing employees. The cost of benefits is usually lower than 50.0% of employee salaries.

Table 5

Funds Spent on Regular Overtime Pay (not Holiday)					
	2002-03	2003-04	2004-05	2005-06	2006-07
Regular Overtime	$31,512,145	$36,241,923	$52,456,794	$58,618,526	$71,018,988
Percent Change	N/A	15.01%	44.74%	11.75%	21.15%
% of YTD Gross Appropriation	1.87%	2.12%	2.97%	3.13%	3.64%

Source: Michigan Administrative Information Network

Facilities

One way the MDOC cuts costs is to close facilities. This is especially effective if a facility is inefficient or underused. Throughout the past few years, the State often has closed housing units within facilities, but in FY 2001-02, FY 2004-05, and FY 2007-08, several entire facilities were closed. Table 6 shows that among them, six prisons and five camps were closed, with inmates moving to open beds elsewhere in the MDOC system or to parole. The net loss for prisons is actually four because the MDOC opened Bellamy Creek Correctional Facility in 2001 and reopened Michigan Reformatory in 2007. In FY 2006-07, the MDOC closed Camp Brighton, and opened a new women's camp, Camp Valley, at the Huron Valley Technical Rule Violator (TRV) Center, as well as a second women's camp, Camp White Lake, at the site of the former Gilman Technical Rule Violator Center. A new community re-entry center opened at Camp Tuscola in November 2006, and in 2008, Grand Rapids Corrections Center beds will be replaced by an expansion of the Lake County Center.

Table 6

Facility Closures				
FY 2001-02	**FY 2004-05**	**FY 2005-06**	**FY 2006-07**	**FY 2007-08**
Camp Waterloo	Western Wayne Correctional Facility	Michigan Youth Correctional Facility	Camp Brighton	Southern Michigan Correctional Facility
Adrian Corrections Center	Kalamazoo Corrections Center			Camp Manistique
Muskegon Corrections Center	Benton Harbor Corrections Center			Riverside Correctional Facility
Jackson Maximum Facility[1)]	Gilman Technical Rule Violator Center			Grand Rapids Corrections Center
Michigan Reformatory[1)]	Camp Sauble[1)]			
Camp Pellston[1)]	Camp Tuscola[1)]			
Pontiac Corrections Center[1)]	Saginaw Corrections Center[1)]			
[1)] Closed via Executive Order				

Source: Annual Appropriation Acts; Executive Orders

Conclusion

When the history of the MDOC appropriation is reviewed, it is apparent that the cost of staffing the Department has risen. Whether funded or not, many of these costs have crowded out various programs and positions. While operational efficiencies have been identified, programs such as the technical rule violator pilot drug treatment program, and education in Level V facilities, have been eliminated or reduced, hundreds of positions have been abolished, and several facilities have closed. In a department that is based on supervising and providing care for prisoners, parolees, and probationers, a certain staffing level per offender is required for public safety. Major reductions in staffing costs are possible only if enough staff are retained to reduce overtime costs, the number of offenders supervised by the MDOC is reduced so fewer FTEs will be required, and contracts are renegotiated in order to cut staffing costs.

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Prescriptions for Cost-Containment: Michigan's Efforts to Manage Pharmaceutical Expenditures
Matthew Grabowski, Fiscal Analyst

Between fiscal year (FY) 1998-99 and FY 2006-07, total Medicaid expenditures in Michigan increased by approximately 82.1%. Simultaneously, Michigan's Medicaid enrollment expanded to reach a current caseload of just over 1.5 million individuals; this represents an increase of nearly 50.0% in less than a decade. Also, despite State efforts to constrain spending, Senate Fiscal Agency projections suggest that total Medicaid expenditures in FY 2007-08 will exceed $9.0 billion for the first time. Table 1 provides a brief summary of Medicaid expenditures in Michigan between FY 1998-99 and the current fiscal year.

Table 1

Michigan Medicaid Program Spending and Caseloads (Millions of Dollars)

Fiscal Year	Medicaid Total Spending	Percentage Change	Medicaid Caseload (actual)	Percentage Change
1998-99	$4,797.3		$1,068,158	
1999-00	4,970.6	3.61%	1,066,131	(0.19)%
2000-01	5,518.1	11.01	1,117,594	4.83
2001-02	5,890.9	6.76	1,211,816	8.43
2002-03	6,478.4	9.97	1,296,374	6.98
2003-04	7,022.6	8.40	1,374,206	6.00
2004-05	7,624.3	8.57	1,437,983	4.64
2005-06	7,977.9	4.64	1,475,741	2.63
2006-07	8,734.8	9.49	1,536,000	4.08
2007-08 Estimated	9,268.0	6.10	1,581,000	2.93
Chge from FY '98-99 to FY '07-08	4,470.7		512,842	
Percentage Change	93.19%		48.01%	

One line item in the Medicaid budget that has not necessarily followed the prevailing pattern is the pharmaceutical services line. Over the past several years, pharmaceutical expenditures under Michigan's fee-for-service program have not kept pace with increases in aggregate Medicaid spending. Because the enactment of Medicare Part D effectively shifted responsibility for the prescription drug costs of many of the highest-need patients away from Medicaid, states have been challenged to develop cost-containment strategies aimed at various other subsets of the Medicaid population. Through a variety of strategic initiatives, which are discussed below, Michigan has realized significant progress in its efforts to restrain General Fund/General Purpose (GF/GP) spending on prescription drugs. Before the adoption of these initiatives, Medicaid pharmaceutical expenditures had been increasing at rates in excess of 10.0% per year. In contrast, prescription drug expenditures in FY 2006-07 were only about 0.6% higher than in FY 2005-06, as shown in Table 2.

Table 2

Michigan Medicaid Program Pharmaceutical Fee-for-Service Spending (Millions of Dollars)			
Fiscal Year	**Pharmaceutical Spending**	**Percentage Change**	**Pharmaceutical Spending as % of Medicaid Total**
1998-99	$264.9		5.52%
1999-00	320.1	20.84%	6.44
2000-01	465.5	45.42	8.44
2001-02	552.2	18.63	9.37
2002-03	616.1	11.57	9.51
2003-04	641.5	4.12	9.14
2004-05	648.5	1.09	8.51
2005-06[a)]	655.1	1.02	8.21
2006-07[a)]	658.8	0.56	7.54
2007-08[a,b)]	680.1	3.23	7.30

[a)] Includes Medicare Part D expenditures. [b)] Estimated using FY 2007-08 Executive current services base.

Michigan's Preferred Drug List and the Michigan Multi-State Pooling Agreement

Since 2002, the Michigan Medicaid program has employed a preferred drug list, known as the Michigan Preferred Product List (MPPL), for two principal purposes, both of which are aimed at cost-containment. First, an enumerated listing of "preferred" products allows the State to negotiate supplemental rebates from pharmaceutical manufacturers in exchange for the inclusion of specific drugs in the MPPL. Second, the MPPL has been used to encourage the use of generic drugs in cases in which affordable alternatives to higher-cost drugs exist. Michigan's preferred drug list is periodically reviewed and updated by the 11-member Pharmacy and Therapeutics Committee, which includes both pharmacists and physicians who have served Medicaid-eligible patients. In 2004, about 70.0% of all drugs prescribed to Medicaid recipients in Michigan were included in the preferred drug list.

In 2003, Michigan and Vermont jointly launched the Michigan Multi-State Pooling Agreement (MMSPA), also known as the National Medicaid Pooling Initiative (NMPI), in an effort to obtain additional discounts from pharmaceutical manufacturers via the establishment of a multistate market. In the nearly five years since, Alaska, Hawaii, Nevada, New Hampshire, Minnesota, and Montana have received authorization from the Centers for Medicare and Medicaid Services to join the project. Michigan achieved approximately $8.0 million in savings in 2004 as a result of pooled purchasing, according to the Kaiser Family Foundation. Numerous other states have established similar alliances in an effort to reinforce their ability to negotiate fair prices and supplemental rebates from suppliers of prescription drugs.

Data collected by the Department of Community Health (DCH) provide sufficient evidence to indicate that Michigan has generated considerable savings as a result of these reforms. During FY 2006-07, Michigan collected over $18.0 million in supplemental prescription drug rebates; this equates to an 11.0% increase in total rebates to the State Medicaid program. In addition, a report prepared by the U.S. Department of Health and Human Services in 2004 determined that 55.0% of all drugs prescribed to Medicaid recipients in Michigan were generics, and that Michigan had achieved a generic substitution rate of 90.0%. For each of these indicators, Michigan ranked above the national average.

Pharmacy Quality Improvement Project

The Pharmacy Quality Improvement Project (PQIP), first implemented in 2005, seeks to ensure that physicians prescribe drugs to mental health patients in accordance with evidence-based treatment guidelines. In other words, PQIP monitors the prescribing practices of Medicaid-participating physicians to create greater uniformity regarding which drugs are prescribed and their dosages. The program was designed to approximate existing prescription monitoring programs in other states that reportedly had improved treatment outcomes and reduced pharmaceutical expenditures. One such program in Missouri achieved a 98.0% reduction in the number of patients receiving prescriptions for the same medication from multiple doctors in its first year of operation.

According to a brief prepared by the DCH in February 2007, PQIP has been an effective tool for limiting prescription drug redundancy. The brief refers to an impact analysis comparing the prescribing habits of about 600 physicians both before (May 2005) and after (January 2006) a PQIP intervention; the analysis indicated a 22.0% reduction in pharmaceutical claims and a 21.0% decline in costs. Through this initial evaluation, the DCH determined that the program produced cost savings of approximately $1.7 million during the six-month intervention period. In light of the program's strong early performance, PQIP has received two year-long extensions. Additionally, a work group within the DCH Mental Health Advisory Committee meets quarterly to provide project oversight and performance assessments. In February 2006, opiates were added to the catalogue of drugs monitored by PQIP, suggesting that future expansions of the program may be possible.

Medicaid Managed Care

Before the mandated shifts to managed care occurred between FY 1997-98 and 1999-2000, Michigan's Medicaid program reimbursed health care providers primarily through fee-for-service arrangements. In the past decade, however, more than 60.0% of all Medicaid recipients have been enrolled in an approved health maintenance organizations (HMO) plan. This striking transition toward a managed care model in Michigan coincided with a national trend during the 1990s in which Medicaid managed care increased nearly tenfold.

Generally speaking, Michigan and other states adopting managed care methodologies were spurred on by early predictions of cost-containment and the desire for greater operational stability. Whether and to what extent these benefits have been realized remain somewhat ambiguous. A study conducted by the Rockefeller Institute of Government at SUNY-Albany claims that Michigan achieved savings of about $120.0 million in 1998 as a result of managed care implementations. It should be noted, however, that any initial savings associated with managed care may not reflect actual program performance. According to a nationwide analysis published by the Urban Institute in 2003, "managed care did not translate into dramatically slower growth in program costs per beneficiary. . . [s]tudies that focus on long-term cost savings are needed to assess the extent to which initial savings may have eroded."

Managed care providers have not been as effective as Michigan's fee-for-service program in limiting the growth of prescription drug expenditures. While HMOs offering prescription drug coverage to Medicaid recipients have developed their own tailored drug formularies, they have not benefited from participation in the fee-for-service preferred drug list or the multistate pooling agreements. As Table 3 indicates, spending by HMOs on prescription drugs increased by nearly $69.0 million between 2005 and 2007. Also, despite the fact that HMOs were subject to increasing caseloads during this period, the rising cost of prescription drugs was the primary impetus for this striking growth in spending. The experience of HMOs in Michigan between 2005 and 2007 lends additional support to the hypothesis that cost-containment measures aimed at the fee-for-service population have been successful in limiting State spending on prescription drugs.

Table 3

Prescription Drug Expenditures by HMOs: FY 2005-2007

	2005	**2006**	**2007[a)]**
Community Choice Michigan	$17,985,642	$19,861,387	$21,043,345
Great Lakes Health Plan	32,494,879	41,681,414	53,359,936
Health Plan of Michigan	30,526,409	34,090,247	42,320,477
HealthPlus Partners	24,349,911	22,306,136	23,301,223
M-Caid (Now Blue-Caid)	5,173,693	4,805,333	5,412,916
McLaren Health Plan	17,257,440	19,674,945	22,448,173
Midwest Health Plan	18,178,662	18,391,623	21,075,132
Molina Healthcare of Michigan	47,638,163	70,302,334	70,399,812
OmniCare Health Plan	18,832,159	18,117,385	19,027,939
Physicians Health Plan of Mid-Michigan-Family Care	6,138,809	6,061,360	5,642,301
Priority Health Government Programs	14,790,437	16,608,186	16,642,961
Total Health Care	13,865,018	13,001,169	14,328,340
Upper Peninsula Health Plan	9,447,188	9,953,822	10,574,507
Total	**$256,678,410**	**$294,855,341**	**$325,577,062**
Percent Change		**14.9%**	**10.4%**

[a)] Projected

Medicare Part D

Pursuant to the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (MMA), the Medicare Part D prescription drug program became operative on January 1, 2006. The program offers Medicare recipients the option of enrolling in a variety of tailored plans that subsidize the cost of prescription drugs. In addition, the MMA dictates that individuals who are dually-eligible for Medicare and Medicaid be automatically enrolled in Medicare Part D. As of 2002, these "dual-eligibles" (primarily low-income senior citizens and disabled persons) represented 14.0% of the Medicaid population but were the beneficiaries of 40.0% of all Medicaid spending nationwide. Approximately 190,000 dual-eligibles living in Michigan are currently enrolled in a Medicare Part D prescription plan.

While the Medicare program has assumed oversight of the prescription drug needs of many Medicaid recipients, the State has not been released from its fiscal responsibility for these individuals. A mechanism commonly referred to as the "clawback" requires Michigan to reimburse the Federal government through monthly payments designed to approximate the amount that the State would have spent on prescription drug coverage under Medicaid absent the prescription drug benefit enacted by the MMA. As reported in Table 4, these payments totaled about $127.0 million in FY 2005-06 and about $178.0 million in FY 2006-07. In addition to the effect of the clawback payments, Michigan is forced to account for the loss of revenue that would have resulted from the Federal contribution to Medicaid had the Medicare prescription drug benefit not been enacted. The total costs of the foregone revenue and the clawback payments also are reflected in Table 4.

Table 4

Medicare Part D Expenditures (millions of dollars)		
Fiscal Year	**GF/GP Clawback**	**Total Expenditures**
2005-06	$127.5	$288.5
2006-07	177.8	407.6
2007-08	178.2	425.4

Despite predictions that the costs associated with Medicare Part D would outweigh any savings realized by the State in the form of reduced Medicaid pharmaceutical expenditures, total costs have remained relatively stable. As shown in Table 5, the growth rate in prescription drug expenditures has been between 4.0% and 5.0% since the enactment of the Medicare prescription drug benefit. When compared with the large escalations in pharmaceutical expenditures in Michigan between 2000 and 2005, these year-to-year increases appear quite restrained.

Table 5

Total Prescription Drug Spending on Medicaid Recipients			
	FY 2004-05	**FY 2005-06**	**FY 2006-07**
Fee-for-Service Expenditures	$648,522,000	$366,611,500	$251,197,400
HMO Expenditures	$256,678,410	$294,855,341	$325,577,062
Medicare Part D	0	$288,537,400	$407,611,200
Total Pharmaceutical Expenditures	**$905,200,410**	**$950,004,241**	**$984,385,662**
% Change (Year-to-Year)		4.9%	4.1%

Conclusion

During the first half of this decade, the growth in Medicaid enrollments and expenditures in Michigan contributed to the State's emerging budgetary constraints. Through the application of innovative cost-containment initiatives, such as the MPPL, MMSPA, and PQIP, the State has achieved modest success in limiting the growth of Medicaid prescription drug expenditures. While the implementation of the Medicare prescription drug benefit may have limited Michigan's ability to expand existing strategies for cost-containment, it does not appear to have overshadowed the constructive effects of these strategies.

State Notes

TOPICS OF LEGISLATIVE INTEREST

January/February 2008

Civil Service Commission, Collective Bargaining, and Compensation Plans for Fiscal Years 2008-09, 2009-10, and 2010-11

By Joe Carrasco, Jr., Fiscal Analyst

On December 19, 2007, the Civil Service Commission approved new three-year collective bargaining agreements with nine of the 10 State employee bargaining units represented by five State employee unions. The newly approved agreements do not include the Michigan State Police Troopers Association (MSPTA) because bargaining for the next three-year contract for fiscal year (FY) 2008-09 through FY 2010-11 will not begin until the spring of 2008.

Over 70.0% of the total State classified work force is represented by unions eligible to bargain collectively on behalf of State employees. Employees not eligible for exclusive union representation include those in supervisory, managerial, and confidential positions as well as employees in business/administration services. These nonexclusively represented employees (NEREs) have their terms and conditions of employment determined through a process administered by the Civil Service Employee Relations Board. The Employee Relations Board serves as a Coordinated Compensation Panel that recommends a Coordinated Compensation Plan for NEREs to the Civil Service Commission. The Coordinated Compensation Plan and the collective bargaining agreements are subject to review, modification, and approval by the Civil Service Commission.

The following provides an overview of the collective bargaining process and the recently approved collective bargaining agreements that will be in effect for fiscal years 2008-09, 2009-10, and 2010-11.

The Process

Article XI, Section 5 of the Michigan Constitution of 1963 establishes the classified State Civil Service and the State Civil Service Commission (CSC), and provides for a process to increase the rates of compensation for State employees. Ultimately, the CSC has authority over rates of compensation and conditions of employment, including the authority to make modifications to previously agreed-upon collective bargaining agreements. The CSC created the collective bargaining process for certain State employees based on the premise that the Michigan Constitution does not prohibit collective bargaining as long as the collective bargaining agreements are subject to review, modification, and approval by the Commission (*Patrick, et al.* v *Michigan Corrections Organization, et al.*, United States District Court, Western District of Michigan, 2000). Chapter 6 of Civil Service Commission Rules provides for the collective bargaining process. The rules clearly describe the plenary nature of the CSC's constitutional authority over all conditions of employment. Rule 6-3 states:

> *The ability of eligible employees to elect an exclusive representative and engage in collective bargaining is a privilege granted by the civil service commission under its exclusive constitutional authority. However, the commission cannot delegate its constitutional responsibilities to the collective bargaining parties and the privilege to engage in collective bargaining remains subject to the commission's sovereign authority and the rules of the commission.*

Under CSC Rule 6-3.1(c), the Civil Service Commission retains the authority to modify the agreement without the approval of the parties at any time during the term of the collective bargaining agreement.

Article XI, Section 5 of the Michigan Constitution also states that increases in the rates of compensation authorized by the CSC require prior notice to the Governor, who then transmits the increases to the Legislature as part of the budget. Within 60 calendar days following the transmission, the Legislature, by a two-thirds vote of the members elected to and serving in each house, may reject or reduce increases in rates of compensation authorized by the CSC. Reductions made by the Legislature must apply uniformly to all classes of employees and cannot adjust pay differentials already established by the Commission. Rates of compensation also cannot be reduced below those in effect at the time the increases were transmitted to the Legislature.

Impasse Panel and Resolution

According to CSC Rule 6-9, State employee contracts are negotiated on behalf of the employer by the State Employer. The State Personnel Director is responsible for establishing a time frame for primary negotiations as well as impasse resolution that is in line with the legislative budget cycle and provisions within the Constitution that govern the timing of wage increases for State classified employees. If agreement cannot be reached in the collective bargaining process by the date set by the State Personnel Director, the matter may be referred to the impasse panel for resolution. The Civil Service Commission may refer unresolved matters to the impasse panel if the parties have not voluntarily reached agreement or requested impasse panel assistance before the expiration of an existing collective bargaining agreement. Rule 6-9.4 states:

> *If either party files a timely request for impasse panel assistance, the parties are eligible for impasse panel assistance. If neither party files a timely application, the parties are ineligible for impasse panel assistance, except as provided in rule 6-9.3. If the parties are ineligible for impasse panel assistance, the state personnel director may require the use of mediation, advisory arbitration, or fact-finding provided in the regulations. If the civil service commission approves increases in the rates of compensation too late to be included in the governor's budget, the increases must be submitted under the waiver of notice provisions of article 11, section 5, of the constitution.*

If an impasse resolution is sought, the State Personnel Director then notifies the Employee Relations Board and the board appoints the members of the impasse panel. The impasse panel must act in accordance with civil service rules and regulations and make a recommendation to the Civil Service Commission by the date set by the State Personnel Director. The final step is the review and action of the CSC pursuant to Rule 6-10. Specifically, CSC Rule 6-10.1 reads as follows:

> *It is the policy of the civil service commission to encourage agreement between the parties. However, the commission retains the final authority to approve, modify, or reject, in whole or in part, all primary and secondary collective bargaining*

agreements, impasse panel recommendations, and coordinated compensation recommendations submitted to the commission. Therefore, if the parties reach a proposed collective bargxaining agreement, the parties shall submit a copy of the proposed agreement to the commission for review. If the parties are at impasse, the impasse panel shall submit its recommendations for impasse resolution to the commission. The commission shall review each proposed agreement, impasse panel recommendation, and coordinated compensation recommendation. The commission shall approve, modify, or reject, in whole or in part, each agreement and recommendation.

Collective Bargaining Agreements for FYs 2008-09, 2009-10, and 2010-11

On December 17, 2007, the Civil Service Commission approved collective bargaining agreements for the next three fiscal years (2008-09, 2009-10, and 2010-11) for employees exclusively represented by the American Federation of State, County, and Municipal Employees (AFSCME), the Michigan State Employees Association (MSEA), the Michigan Corrections Organization (MCO), the United Automobile, Aerospace, and Agricultural Implement Workers of America (UAW), and the State Employees International Union (SEIU) Local 517M. The agreements include hourly rate increases as follows:

October 1, 2008 - 0%
October 1, 2009 - 1%
October 1, 2010 - 3%

Because State employees will not receive an adjustment to their hourly wages in FY 2008-09, the net savings compared with the cost of wage increases built into the FY 2007-08 budget amount to $91.6 million. (For FY 2007-08, State employees received a 2.0% increase on October 1, 2007, and will receive an additional 2.0% increase in April 2008.) Based on the FY 2007-08 costs built into the budget, and assuming that the work force will be generally the same, it is estimated that the costs of the wage increases scheduled for FY 2009-10 will be in the neighborhood of $25.0 million while the estimated cost of the anticipated wage increase for FY 2010-11 is approximately $75.0 million. The exact costs will depend on the actual work force and the statewide payroll at the time.

Health Care Benefit Changes

Along with rates of compensation and conditions of employment, health care benefits also are negotiated in the collective bargaining process. The newly approved collective bargaining agreements for FYs 2008-09, 2009-10, and 2010-11 make some significant changes to the premium and co-pay amounts paid by State employees. Regardless of the health care plan chosen by an employee, the amount of the annual premium that he or she must pay will be higher over the next three-year period than it was in the previous contracts for all plans. The employee's portion of the premium is deducted from his or her biweekly earnings.

Employees choosing to enroll in the State Health Plan PPO (preferred provider organization) will now be required to pay 10.0% of the annual premium, compared with 5.0% in the previous contracts. Those enrolling in a health maintenance organization (HMO) plan previously did not pay any portion of the premium; instead, the State paid 100% of the annual premium. Under the new contracts, employees choosing an HMO plan will pay 5.0% of the annual premium. The State's portion of the annual premium payment for those choosing an HMO plan will be capped at the amount the State pays for employees enrolled in the State Health Plan PPO, meaning that any portion above that capped amount will be paid by the employee. Thus, in some instances, depending on the HMO plan chosen, employees selecting an HMO plan will pay more than 5.0% of the annual premium. (It must be noted that based on FY 2007-08 estimates, the annual premium for an HMO plan is on average about $1,000 less per employee than the annual premium for the State Health Plan PPO; thus, the cost to the State is about $500 more on average per employee choosing the State Health Plan PPO.) As shown in Table 1, these changes in the amount of the annual premiums that the State will pay on behalf of State employees will result in savings to the State of an estimated $32.8 million in FY 2008-09.

In addition, Civil Service employees also receive dental and vision care benefits. The collective bargaining agreements approved on December 17, 2007, made no changes to the current amounts of premiums paid by the employee. As currently required, for the next three fiscal years employees will have to pay 5.0% of the dental care premium while the State will continue to pay 100% of the vision care premium for all employees. The difference in the annual premiums between the two is about $1,000 (dental being higher).

Table 1

Estimated FY 2008-09 Savings From Changes to State Employee Health Care Premiums, Deductibles, and Co-Pays (millions of dollars)

Item	Estimated Savings From Changes for Active State Employees	Estimated Savings From Changes for State Retirees
Health Care Premiums	$32.8	$10.2
Deductibles	5.6	4.6
Co-pays	16.9	32.3
Total	**$55.3**	**$47.1**

Source: Office of the State Employer

The new collective bargaining agreements for FYs 2008-09, 2009-10, and 2010-11 also make significant changes to the deductible and prescription and office visit co-pay amounts that are paid by State employees. The deductible for members under the State Health Plan PPO will increase from $200 per member ($400 per family) to $300 per member ($600 per family) for in-network services, while the deductible for out-of-network services will increase from $500 per member ($1,000 per family) to $600 per member ($1,200 per family). The out-of-pocket maximums remain the same as under the current contract ($1,000 for individuals and $2,000 per family for in-network; $2,000 for individuals and $4,000 per family for out-of-network).

While the current prescription drug plan is maintained, the co-pay amounts are increased under the new collective bargaining agreements. The co-pay for generic drugs increases from $7 to $10 while the co-pay for brand name drugs increases from $15 to $20. Also, the co-pay for nonpreferred brand name drugs increases from $30 to $40. Finally, the co-pays for office visits and emergency services are increased for in-network services. The office visit co-pay increases from $10 per visit to $15 per visit, while emergency visits are still covered at 100%; however, if an individual is *not* admitted to the hospital, there will be a $50 co-pay per emergency room visit. As shown in Table 1 above, the total savings from these changes in deductibles and co-pays for FY 2008-09 are estimated at $22.5 million.

Retired State employees are required to pay the same annual premiums for health care benefits that active Civil Service employees pay. As stated in MCL 38.20d, health care premiums for defined benefit plan retirees are to be paid in the same proportion as for active State employees. Members of the defined contribution plan are required to pay the portion of their premiums as laid out in MCL 38.68, which establishes a 10-year vesting requirement with employer contributions equal to 3.0% per year of service up to a maximum of 90.0%. Thus, as required by statute, all of the health care changes negotiated for active State employees will be extended to State retirees, resulting in savings in FY 2008-09 of an estimated $47.1 million, as seen in Table 1.

Conclusion

Nearly 40,000 State Civil Service employees are represented by a union and thus are represented in the collective bargaining process. The contracts for the next three fiscal years (FYs 2008-09, 2009-10, and 2010-11) have been negotiated and approved by the Civil Service Commission. The agreed-upon contracts will provide no increase to base salary in FY 2008-09, but will provide a 1.0% and 3.0% increase in FY 2009-10 and FY 2010-11, respectively. The decline in available State revenue over the last several years along with rising health care costs for active employees and retirees have put severe constraints on the budgets of all State departments and agencies. Difficult decisions have been made and State employees have made concessions in the past to help balance the State's budget. (For more detail on these concessions, please see the May/June 2007 State Notes article, "A Brief History of State Employee Wage Increases and Concessions: FY 1997-98 through FY 2006-07".) The contracts for the next three years will require State employees and retirees to pay a larger portion of their health care premiums, higher deductibles, and increased co-pays for prescription drugs and doctor office visits. The resulting savings to the State are estimated to total $102.4 million in FY 2008-09 alone.

Article XI, Section 5 of the Michigan Constitution allows the Legislature 60 days from the date of the Governor's transmission of any increases in State employee wages, by a two-thirds vote of the members elected and serving in each house, to reject or reduce increases in rates of compensation authorized by the CSC. Therefore, the currently agreed-upon contracts that provide for a 1.0% increase in wages in FY 2009-10 and a 3.0% increase in wages in FY 2010-11 could be reduced or eliminated by action of the Legislature if the Legislature acts within 60 days of the Governor's transmission of those wage increases in the upcoming Executive budget recommendations for FY 2009-10 and FY 2010-11. Also, it is important to note that the ultimate authority regarding these contracts lies with the Civil Service Commission. As stated in CSC Rule 6-3.1(c), "Notwithstanding that the civil service commission previously approved the provisions of a collective bargaining agreement, the commission retains the authority, during the term of a collective bargaining agreement, to modify the agreement without the approval of the parties…".

State Notes

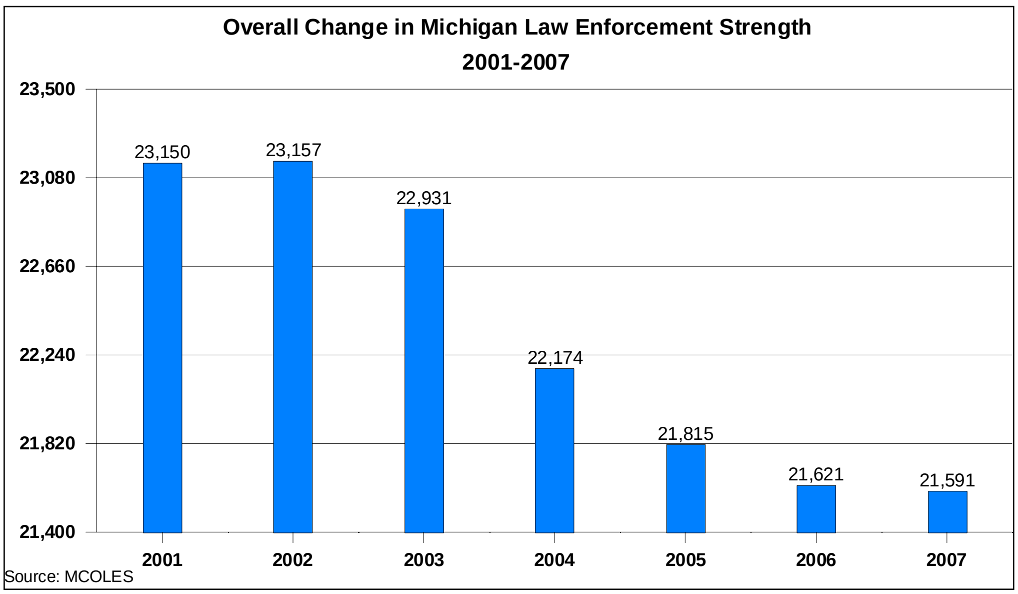
TOPICS OF LEGISLATIVE INTEREST

January/February 2008

Decline in Statewide Law Enforcement Strength
By Bruce R. Baker, Fiscal Analyst

As a result of a State economy that has seen employment decline for seven consecutive years and the consequent spending priorities set by local and State government, the number of licensed law enforcement officers has declined by 1,566 positions in the State since 2001. This information (Figure 1) comes from the Michigan Commission on Law Enforcement Standards (MCOLES), which has tracked the employment of licensed law enforcement officers among Michigan's 609 law enforcement agencies.

Figure 1



The overall loss of approximately 7.0% of police officer positions in the last seven years generally reflects a dramatic decrease in numbers within law enforcement agencies of the largest and smallest sizes, and less dramatic losses in certain types of agencies such as those representing county sheriffs, townships, and villages.

Changes in Agency Strength by Size

Large law enforcement agencies, defined here as those that employ over 100 officers, have experienced an overall reduction in officer strength of 15.0% since 2001. These agencies include police departments in Ann Arbor, Battle Creek, Clinton Township, Dearborn, Detroit, Farmington Hills, Flint, Grand Rapids, Kalamazoo, Lansing, Livonia, Southfield, Sterling Heights, Troy, Warren, and Westland, as well as the Michigan State Police. Among them, only Clinton Township, Dearborn, Farmington Hills, Sterling Heights, Troy, and Westland have managed either to maintain their strength, or, in the case of Farmington Hills and Sterling Heights, to increase their officer strength slightly.

The greatest loss of officers, in terms of numbers, has come from the State's two largest agencies. The City of Detroit's with a loss of 923 police officers since 2001 (Figure 2) represents a decrease of 23.0% in personnel of the city's police department. The other largest agency, the Michigan State Police, has lost 362 licensed police officers going back to 2001 (Figure 3), representing a decrease of 17.0%. In terms of patrol officers, or those Michigan State Troopers assigned to general police duties at posts around the State, the numbers have fallen from a historic high of 1,344 in 2000 to 1,036 in 2007 (Figure 4), a 23.0% loss. As of February 2008, the number of troopers assigned to post has fallen to 1,022.

Figure 2

Figure 3

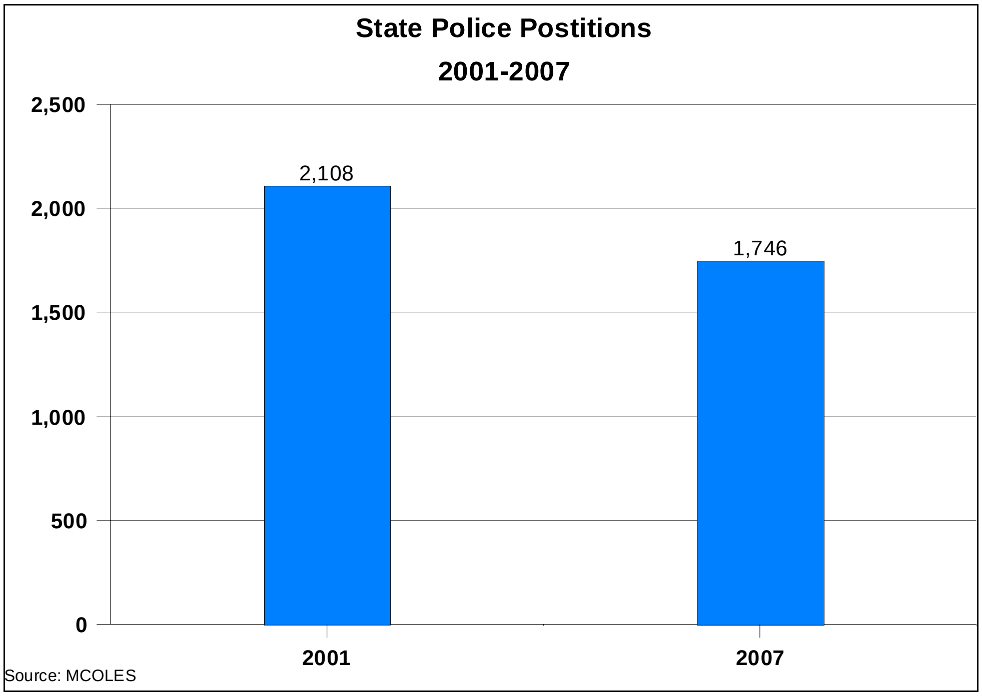
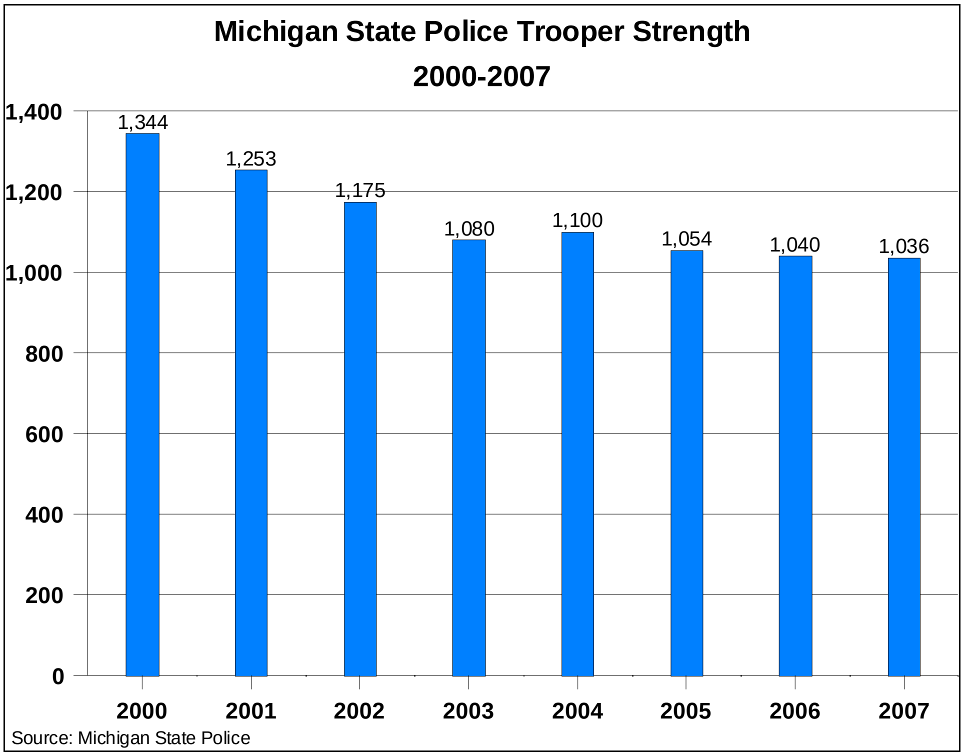


Figure 4



A recent survey of law enforcement personnel by MCOLES reveals that the very smallest of agencies, with perhaps fewer funding options, have been hit hard with officer losses. According to the survey, the 88 agencies that employ fewer than four officers have seen an overall 45.0% reduction in strength since 2001. Among those, 18 are reported to have disbanded operations and other units have increasingly relied upon part-time employment of officers to provide service.

Changes in Agency Strength by Type

While the Michigan State Police and the City of Detroit suffered the biggest losses of law enforcement officers in terms of numbers, many city police agencies also have seen a considerable decline in officers since 2001. Overall, city police agencies in the State have seen a decline of 11.0% during this time period. Many city law enforcement agencies, some of which are listed in Table 1, have been especially hard hit.

Table 1

City Law Enforcement Agencies - Percent of Licensed Officers Lost 2001-2007	
Bay City	16%
Detroit	23%
Grand Rapids	13%
Inkster	19%
Lincoln Park	18%
Livonia	11%
Pontiac	39%
River Rouge	30%
Romulus	15%
Saginaw	20%
Wyoming	13%

Source: Michigan Commission on Law Enforcement Standards

Among county sheriff departments, overall numbers of licensed law enforcement officers have remained approximately stable since 2001, though this statement may be somewhat misleading due to the growing trend in certain counties to license county jail workers as law enforcement officers and the fact that some counties have increased numbers to support other local agencies that have experienced a decline in officers during this period.

While some county sheriff departments experienced gains in officers, 25 of the State's 83 counties, or 30.0%, lost officers since 2001, with Saginaw County experiencing the greatest loss with an 18.0% decline. Other sheriff departments sustaining losses since 2001 include those in Arenac, Bay, Cass, Chippewa, Eaton, Gladwin, Gogebic, Grand Traverse, Gratiot, Ingham, Jackson, Kalkaska, Lapeer, Lenawee, Manistee, Marquette, Mason, Mecosta, Newaygo, Ontonagon, Sanilac, Schoolcraft, St. Clair, and St. Joseph Counties.

In addition to the county sheriff departments, those agencies representing townships and villages also have maintained overall strength since 2001, though 33 of 109 township agencies and 35 of 126 village agencies experienced law enforcement position losses.

Conclusion

It cannot be predicted at this time when or if the revenue of various levels of government will be directed to a greater degree than it is currently for the purpose of hiring additional licensed law enforcement personnel At the State level, however, the Governor has recently proposed a new trooper school for the Michigan State Police in her budget recommendations for fiscal year 2008-09. The school is planned to graduate a minimum of 80 troopers in early 2009, to be added to the pool of troopers assigned to posts around the State.