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Stormy Fiscal Waters

Economic reality has finally set in at the state Capitol. While most states in recent years had to cut their budgets to cover revenue shortfalls, Louisiana's budget swelled after Hurricane Katrina. Major infusions of money from insurance settlements and federal aid produced higher sales and income tax revenues, and surging oil prices poured even more cash into the state treasury.

Now the party's over. Most insurance proceeds have been spent, and the federal spigot has slowed to a relative trickle.

State economic forecasters predict a \$341 million deficit this fiscal year and a possible \$2 billion shortfall in fiscal 2009-10 (which begins July 1, 2009). The ongoing national recession will no doubt reduce sales and corporate tax collections, but the biggest fiscal blow will come from plummeting oil and gas prices. When gasoline prices started dropping below \$2 a gallon, most Louisianans were happy — but state officials no doubt had mixed emotions. "I think legislators have been very spoiled — particularly this new group in the first year or so — because it was such a breeze," says Jim Brandt, president of the Public Affairs Research Council of Louisiana (PAR). "The state was awash in cash, almost had an embarrassment of riches. They could cut taxes; they could fund their pet projects and still have a \$1 billion surplus."

No more.

What lawmakers and Gov. Bobby Jindal didn't do when they had all that money was prepared for a future that doesn't include surpluses. Earlier this year, lawmakers repealed the so-called Stelly Plan, which increased income taxes but lowered some sales taxes in 2003. In doing so, they eliminated a fiscal safety valve. Repealing Stelly was a popular move, especially after lawmakers had just tried to give themselves a massive pay raise. Now, legislators must cut vital state services.

When Louisiana has to cut spending, the first casualties are typically higher education and health care. Those big-ticket budget items, unlike K-12 education and other priorities, are not

constitutionally protected. Louisiana's Medicaid program alone accounts for \$2 billion of the state's nearly \$30 billion budget, and Medicaid costs are projected to rise annually.

Besides reducing health care services to the poor and uninsured in a state that was recently ranked 50th in overall health outcomes, the problem with cutting Medicaid is that every \$1 the state eliminates costs Louisiana \$2 more in federal aid. That's because the state contributes only about 30 percent to the program; the federal government pays the rest. Jindal and state Health and Hospitals Secretary Alan Levine are pushing a health care overhaul — Louisiana Health First — which, among other things, would transform the state's Medicaid program from a fee-based system for services to a managed-care system run by private insurance providers. Jindal says the plan will cover more people *and* save money, but critics — including former DHH secretary David Hood, who is currently a health care policy analyst for PAR — say the plan will increase administrative costs and *reduce* the number of patients receiving care. Even without the overriding fiscal crisis, this is a hot-button issue. Meanwhile, Jindal has told public colleges to carve \$109 million from this year's budget.

On a brighter note, there is still a projected surplus of more than \$800 million from fiscal year 2007-08, which ended June 30. However, that money can only be spent on one-time uses such as reducing state debt or construction projects — not covering deficits.

State lawmakers will begin next year's belt-tightening when they go back into session on April 27. The heavy lifting regarding balancing this year's budget (i.e., eliminating the projected \$341 million deficit in the current fiscal year) falls to members of the Joint Legislative Committee on the Budget. Procedurally, the committee must formally notify Jindal of the deficit, at which time he will have 30 days to act. He can cut up to 3 percent of nondedicated funds in the discretionary budget (read: higher education and health care), but legislative sources say that translates to only \$181 million in reductions. He could make up the difference by tapping the state's "rainy day fund," but he has said he won't do that. Instead, Jindal will likely cobble together a budget-reduction package, combining cuts from nondedicated and dedicated funds. He must then ask the joint legislative committee to approve it.

As lawmakers prepare for the annual session in April, they should be looking for ways to trim future state budgets and invest last fiscal year's surplus wisely. We suggest paying down state debt, which would reduce the state's annual debt payments, save interest charges and free up money for future operating budgets. Reducing debt is not as sexy as building roads or repealing taxes, but it makes good fiscal sense. In the long run, it will help calm the kind of stormy fiscal waters that engulf Louisiana now.