



## Legislative Fiscal Bureau

One East Main, Suite 301 • Madison, WI 53703 • (608) 266-3847 • Fax: (608) 267-6873

March 12, 2008

TO: Members  
Wisconsin Legislature

FROM: Bob Lang, Director

SUBJECT: March 2008 Special Session Assembly Bill LRB 4268/1

On March 10, 2008, the Governor indicated that he would transmit March 2008 Special Session Assembly Bill LRB 4268/1 to the Assembly for introduction.

The bill makes various adjustments to the state's 2007-09 budget (2007 Act 20) to eliminate the projected deficit in the state's general fund. On February 13, 2008, this office estimated that without gubernatorial and legislative action, the state would end the 2007-09 biennium with a deficit of \$652 million. At that time, the administration took two actions to reduce that estimated deficit by \$236 million to \$416 million. First, the administration indicated that it would require state agencies to lapse an additional \$111 million (above the \$200 million requirement under Act 20) and second, short-term general obligation borrowing that would otherwise be paid off in 2007-08 and 2008-09 would be rolled over. This latter action reduces debt service payments by \$125 million for the biennium. The Special Session Bill addresses the remaining \$416 million general fund deficit.

Following this introduction is a 2007-09 general fund condition statement and an identification of the effect of the provisions of the bill on the projected deficit. After these tables is a summary of each of the provisions of the Special Session Bill. For each item of the bill, a summary of the provision and fiscal effect, if any, is shown. In addition, the summary identifies the section(s) of the bill where each item is located. Following each summary is a discussion of the item.

BL/sas

# March 2008 Special Session Assembly Bill LRB 4268/1

## 2007-09 General Fund Condition Statement

	<u>2007-08</u>	<u>2008-09</u>
<b>Revenues</b>		
Opening Balance, July 1	\$66,288,000	\$65,139,800
Estimated Taxes	12,868,300,000	13,277,500,000
Departmental Revenues		
Tribal Gaming Revenues	96,731,600	46,250,700
Other	<u>534,103,700</u>	<u>651,275,900</u>
Total Available	\$13,565,423,300	\$14,040,166,400
<b>Appropriations and Reserves</b>		
Gross Appropriations	\$13,705,810,400	\$14,082,815,100
Compensation Reserves	62,759,600	156,617,900
Less Lapses	<u>-268,286,500</u>	<u>-264,286,400</u>
Net Appropriations	\$13,500,283,500	\$13,975,146,600
<b>Balances</b>		
Gross Balance	\$65,139,800	\$65,019,800
Less Required Statutory Balance	<u>-65,000,000</u>	<u>-65,000,000</u>
Net Balance, June 30	\$139,800	\$19,800*

\*In addition, \$36.6 million is estimated to be in the budget stabilization fund on June 30, 2009.

## General Fund Effect on the Projected 2007-09 Deficit (In Millions)

	<u>Item</u>	<u>Net Balance</u>
February 13, 2008, Projection		-\$652.3
Administrative Action		
Rollover Short-Term Borrowing	\$125.4	-526.9
Lapses Under s. 16.50(2)	111.0	-415.9
Special Session Assembly Bill 1		
Additional Lapses	219.4	-196.5
Hospital Assessment	125.0	-71.5
Permanent Endowment Fund to Medical Assistance	30.0	-41.5
Transfer from Budget Stabilization Fund to General Fund	21.7	-19.8
Universal Service Fund for Library Aid	11.3	-8.5
Real Estate Investment Trusts	6.0	-2.5
Transfer REAL ID Reserve to the General Fund	5.0	2.5
Supplements to Rural Hospitals and IMDs	-2.5	0.0

# Summary of Provisions

## 1. DOA SECRETARY AUTHORITY TO LAPSE OR TRANSFER FUNDS TO THE GENERAL FUND

Change to Current Law	
GPR-REV	\$330,400,000
Less Previous	
Action	<u>- 111,000,000</u>
Net Change	\$219,400,000

### Summary of Provision

Require the Secretary of the Department of Administration (DOA) to lapse or transfer \$330,400,000 biennially to the general fund from the unencumbered balances of appropriations of executive branch state agencies, other than sum sufficient appropriations and federal appropriations, during each of the 2007-09 and 2009-11 fiscal biennia. This \$330,400,000 lapse or transfer requirement would be in addition to the similar \$200,000,000 biennial lapse or transfer requirement under 2007 Act 20. These moneys would be treated as revenue (GPR-Earned) to the general fund.

Specify that the DOA Secretary could not lapse or transfer moneys if the lapse or transfer would: (a) violate a condition imposed by the federal government on the expenditure of the moneys; or (b) violate the federal or state constitution. In addition, specify that no more than \$293,000,000 could be lapsed or transferred in the 2007-09 biennium from appropriations to the Department of Transportation under this provision and the requirement under Act 20.

[Bill Section: 9201(2)]

### Discussion

In a memorandum dated February 12, 2008, the Secretary of Administration identified additional agency appropriation lapses or transfers, over and above the \$200 million biennial lapse or transfer requirement under Act 20. The memorandum indicated that this administrative action would increase the general fund balance by \$111 million compared with Act 20. This \$111 million savings amount was incorporated into the revenue estimate memorandum by this office dated February 13, 2008, which projected a closing balance for the general fund of -\$416 million on June 30, 2009.

The administration indicates that the proposed \$330.4 million lapse would replace the administrative action outlined in the February 12 memorandum, so the net benefit to the general fund would be \$219.4 million.

**2. TRANSPORTATION FUNDING CHANGES AND TRANSFERS**

**Summary of Provision**

Authorize \$190,000,000 in general fund-supported, general obligation bonds for state highway rehabilitation, major highway development, and southeast Wisconsin freeway rehabilitation projects.

Make adjustments to the funding for highway improvement programs, as shown in the following table:

Change to Current Law	
SEG-REV	- \$5,005,100
SEG-Transfer	\$243,000,000
SEG	- \$333,967,500
FED	76,967,500
SEG-S	67,000,000
BR	<u>190,000,000</u>
Total	\$0

	Act 20 Funding		Special Session Bill Change to Act 20	
	2007-08	2008-09	2007-08	2008-09
State Highway Rehabilitation				
SEG	\$320,131,900	\$343,859,900	-\$125,500,000	-\$80,000,000
FED	348,454,300	345,747,300	58,000,000	0
GPR-Supported Gen. Ob. Bonds	<u>0</u>	<u>0</u>	<u>67,500,000</u>	<u>80,000,000</u>
Total	\$668,586,200	\$689,607,200	\$0	\$0
Major Highway Development				
SEG	\$69,700,000	\$76,368,700	-\$59,000,000	-\$18,967,500
FED	78,975,000	78,975,000	10,967,500	0
SEG-S (Trans. Rev. Bonds)	<u>165,738,300</u>	<u>167,395,600</u>	<u>48,032,500</u>	<u>18,967,500</u>
Total	\$314,413,300	\$322,739,300	\$0	\$0
Southeast WI Freeway Rehabilitation				
SEG	\$64,256,500	\$87,658,400	-\$30,500,000	-\$20,000,000
FED	72,493,500	80,091,600	8,000,000	0
SEG-Supported Gen. Ob. Bonds	30,600,000	59,600,000	0	0
GPR-Supported Gen. Ob. Bonds	<u>0</u>	<u>0</u>	<u>22,500,000</u>	<u>20,000,000</u>
Total	\$167,350,000	\$227,350,000	\$0	\$0
Highway Program Totals				
SEG	\$454,088,400	\$507,887,000	-\$215,000,000	-\$118,967,500
FED	499,922,800	504,813,900	76,967,500	0
SEG-S (Trans. Rev. Bonds)	165,738,300	167,395,600	48,032,500	18,967,500
SEG-Supported Gen. Ob. Bonds	30,600,000	59,600,000	0	0
GPR-Supported Gen. Ob. Bonds	<u>0</u>	<u>0</u>	<u>90,000,000</u>	<u>100,000,000</u>
Grand Total	\$1,150,349,500	\$1,239,696,500	\$0	\$0

Specify that the adjustments to SEG appropriations shall not affect the 2008-09 appropriation base for the purposes of the preparation of the 2009-11 biennial budget. Decrease estimated transportation fund revenue by \$5,005,100 in 2008-09 to reflect additional revenue bond debt service payments associated with the increase in the use of bonds in the major highway development program.

Specify that not more than \$293,000,000 may be lapsed or transferred to the general fund in the 2007-09 biennium from the Department of Transportation appropriations under the

combination of a provision of Act 20 that requires total lapses and transfers to the general fund of \$200,000,000 from executive branch state agencies and a provision of the bill that would require lapses and transfers to the general fund totaling \$330,400,000 during the 2007-09 biennium. Since, according to the administration, DOT is expected to lapse or transfer \$50,000,000 under the Act 20 provision, this item would increase the potential lapse or transfer from DOT by \$243,000,000.

[Bill Sections: 1, 4, 7, 8, 49 thru 51, 9148(2),(3)&(4), 9201(2), and 9248(2),(3)&(4)]

## **Discussion**

### *Impacts on Highway Program Funding and Transportation Fund Balance*

This provision would make several changes to funding for state highway improvement programs, but the changes would have no net impact on the total funding level for the programs (usable appropriations would increase by \$45.0 million, as described in the next section). Instead, additional general obligation bonds, federal highway aid, and transportation revenue bonds would be used to offset reductions in each program's SEG appropriation. To summarize the impacts:

- \$190,000,000 in general fund-supported, general obligation bonds would be authorized for highway improvement programs.
- The federal funds appropriations for state highway programs would be increased by a total of \$76,967,500. This is the amount that the state received in federal fiscal year 2008 above the level assumed in Act 20.
- The SEG-S (transportation revenue bond) appropriation for major highway development would be increased by a total of \$67,000,000. This increase would use bonds authorized by Act 20 that would otherwise be used in the 2009-11 biennium.
- The total increase in revenues for highway programs from these three sources would be \$333,967,500.
- Highway improvement SEG appropriations would be reduced by a total of \$333,967,500, resulting in no net change to total funding levels for these programs.
- A total of \$293,000,000 could be transferred from the transportation fund to the general fund. Of this amount, \$288,000,000 would come as the result of highway program appropriation reductions and \$5,000,000 would come from lapses of other DOT appropriations.
- The use of additional transportation revenue bonds in the major highway development program would increase revenue bond debt service by \$5,005,100.
- The impact on the 2007-09 transportation fund balance of the above provisions is a net increase of \$40,962,400, since highway program appropriations would be decreased by more than the amount transferred to the general fund. The additional reduction would be used

to eliminate a projected transportation fund deficit. DOA estimates that the current fund balance under provisions of Act 20 is -\$40,367,900. Therefore, the estimated balance of the fund under the bill would be \$594,500.

The following table summarizes the funding changes under this item, expressed in terms of their impact on the transportation fund balance.

**Impact on Transportation Fund Balance**

	<u>2007-08</u>	<u>2008-09</u>	<u>Biennial Total</u>
<b>Additions to Balance</b>			
Highway Program SEG Appropriation Reduction	\$215,000,000	\$118,967,500	\$333,967,500
Lapse from Other DOT Appropriations	<u>2,500,000</u>	<u>2,500,000</u>	<u>5,000,000</u>
Total SEG Reduction	\$217,500,000	\$121,467,500	\$338,967,500
<b>Subtractions from Balance</b>			
Transfer to the General Fund	-\$177,500,000	-\$115,500,000	-\$293,000,000
Additional Revenue Bond Debt Service	<u>0</u>	<u>-5,005,100</u>	<u>-5,005,100</u>
Total of Transfers and Revenue Reduction	-\$177,500,000	-\$120,505,100	-\$298,005,100
Net Change to Transportation Fund Balance	\$40,000,000	\$962,400	\$40,962,400
Projected Act 20 Biennium-Ending Deficit			-\$40,367,900
Estimated Transportation Fund Balance under Bill			\$594,500

*Impacts on Highway Program Funding Relative to Act 20*

Under Act 20, the Secretary of the Department of Administration is required to lapse a total of \$200.0 million in the 2007-09 biennium from appropriations in executive branch agencies to the general fund. Under the initial plan for 2007-08, \$25.0 million would have been lapsed from DOT appropriations, including \$22.5 million from highway program appropriations and \$2.5 million from other appropriations. If this plan were used for both years of the biennium, DOT would be responsible for \$50.0 million of the \$200.0 million lapse (\$45.0 million from highway programs and \$5.0 million from other appropriations). In contrast to this scenario, funding for highway improvement programs under the bill would not be negatively affected, although other DOT appropriations would continue to be required to lapse \$5.0 million over the biennium. Therefore, although the bill does not change total appropriations for the highway programs, it would increase usable appropriations by \$45.0 million over the biennium.

*Impacts on Potential Transportation Program Funding*

Although the bill would not subject highway improvement program funding to a \$45.0 million reduction, as under provisions of Act 20 as determined by DOA, it would hold these programs harmless through the use of additional federal highway aid and transportation revenue bonds. In the absence of any lapse requirement, the additional \$77.0 million in federal

funds could be used to effectively eliminate the projected transportation fund deficit and increase transportation program spending by about \$33.6 million in 2007-08. Instead, the federal fund increases are used to offset additional SEG reductions that are used, in turn, to increase the transfer to the general fund. Similarly, the use of \$67.0 million in additional transportation revenue bonds increases future transportation debt service payments, but is used, in effect, to increase the transfer to the general fund instead of providing a net increase in highway program spending. In total, revenues from these two sources total \$144.0 million, but \$103.0 million of this amount would be used to assist the general fund.

*Comparison to Transfers from the Transportation Fund in the Past Two Biennia*

The transfer of transportation fund revenues to the general fund under the bill would be similar to provisions contained in the prior two biennial budgets. As with the provisions under the bill, some, but not all, of the amounts transferred or used for general fund purposes would be replaced by general fund-supported, general obligation bonds. The following table shows the amount of transportation fund revenues used for general fund purposes in the last two biennia, the amount replaced with general fund-supported bonds, and the net loss to the transportation fund. In addition, the debt service on the bonds issued in the 2003-05 biennium was initially paid from the transportation fund, which effectively adds to the loss to the fund. Below these amounts are the comparable figures as proposed under the bill. The total proposed use of transportation fund revenues for general fund purposes shown in the table for 2007-09 includes \$293.0 million (a \$243.0 million increase over the anticipated use under Act 20), which is the maximum transfer under this item, plus an additional \$5.0 million from a lapse of funds set aside by Act 20 for the implementation of the federal Real ID Act, which is summarized separately below.

**Past and Proposed Use of Transportation Fund Revenues for General Fund Purposes (\$ in Millions)**

<b>2003-05 and 2005-07 Biennia</b>	<u>2003-05</u>	<u>2005-07</u>	4-Year <u>Total</u>
Use of Transportation Revenues for General Fund	\$675.0	\$427.0	\$1,102.0
Less GPR-Supported Bonds	-565.5	-250.0	-815.5
Plus Trans. Fund Debt Service	<u>43.9</u>	<u>0.0</u>	<u>43.9</u>
Total	\$153.4	\$177.0	\$330.4
<b>Special Session Bill Proposal</b>	<u>Proposed 2007-09</u>	<u>6-Year Total</u>	
Use of Transportation Revenues for General Fund	\$298.0	\$1,400.0	
Less GPR-Supported Bonds	-190.0	-1,005.5	
Plus Trans. Fund Debt Service	<u>0.0</u>	<u>43.9</u>	
Total	\$108.0	\$438.4	

*Impacts on Transportation Fund and General Fund Debt Service*

The bill would increase the use of both transportation fund-supported and general fund-supported bonds. As noted, the use of transportation fund-supported bonds would increase by \$67.0 million. Annual debt service payments on this amount could be expected to be about \$5.2 million for 20 years (initially \$5.0 million in 2008-09, according to DOA estimates).

A total of \$190 million in general fund-supported, general obligation bonds would be issued to replace SEG funds in the highway improvement programs. Annual general fund debt service payments on this amount could be expected to be about \$20.5 million. Initially, the Department of Administration estimates that debt service on these bonds will be \$1.2 million in 2008-09, although this will depend largely on the timing of issuance. No additional GPR debt service is reflected in DOA's general fund condition statement submitted with the bill.

The \$20.5 million in GPR debt service would be added to approximately \$90.5 million being paid annually on replacement bonds issued in the prior two biennia. Since a portion of these bonds have had 10-year maturity dates, debt service on outstanding bonds will be reduced by about half as the first of these bonds begin to be retired in 2014-15 and then will fall to \$24.5 million in 2016-17 as all of the 10-year bonds are retired.

*Other Issues*

Although the bill would limit the transfer from the transportation fund to the general fund to \$293.0 million in the 2007-09 biennium, no such limit would be created for the 2009-11 biennium. Total lapses and transfers from executive branch agencies in that biennium under Act 20 and the bill would be \$530,400,000.

While the bill would specify that the adjustments made to the highway program SEG appropriations in 2008-09 would not impact the 2008-09 base for the purposes of the preparation of the 2009-11 budget, the increase made to the transportation revenue bond appropriation would have an ongoing effect under the bill. The Department of Administration indicates that it was not intended that the increase in the revenue bond expenditure be ongoing.

**3. TRANSFER FUNDING FOR FEDERAL REAL ID ACT IMPLEMENTATION TO GENERAL FUND**

**Summary of Provision**

Prohibit the Joint Committee on Finance from providing an appropriation supplement to DOT for the implementation of the federal Real ID Act that does not leave at least \$5,000,000 in the Committee's appropriation from funds placed in the appropriation by Act 20 for that purpose. (Although the bill does not explicitly require the unused amount to lapse, it would presume that it does.) Require the

Change to Current Law	
GPR-REV	\$5,000,000
SEG-Lapse	\$5,000,000
SEG-Transfer	\$5,000,000

Secretary of the Department of Administration to transfer \$5,000,000 in 2007-08 from the transportation fund to the general fund.

[Bill Sections: 9148(1) and 9248(1)]

**Discussion**

Act 20 provided \$9,805,300 SEG in 2007-08 and \$12,184,000 SEG in 2008-09 (transportation fund) for the implementation of changes needed to comply with the federal Real ID Act. At the time of passage, the federal Department of Homeland Security had not published final rules identifying the specific implementation requirements, so the implementation costs were unknown. Consequently, the funding was placed in the Joint Committee on Finance's supplemental appropriation and the Department was given authority to submit one or more requests to the Committee to transfer the funding to the Department's appropriation for the Division of Motor Vehicles once more information was available on the cost to implement the requirements. If the actual costs were determined to be less than the amount of funding set aside for implementation, the Committee was given the authority to transfer the excess funding to any DOT SEG appropriation.

The final rules were released on January 11, 2008, outlining the specific implementation requirements. Under the rules, states are allowed to request a extension to the original May 11, 2008, deadline (to December 31, 2009), something that most states, including Wisconsin, have requested and been granted. Because of the delay in implementation allowed by the extension, the implementation costs in 2007-08 are expected to be less than the amount of funding set aside in the Committee's appropriation. The bill would effectively lapse \$5,000,000 in 2007-08 from the Joint Committee on Finance SEG appropriation and transfer that amount to the general fund. This would leave \$4,805,300 SEG in 2007-08 available for Real ID Act implementation. The funding set aside for implementation in 2008-09 would not be affected. If additional funds are needed in the next biennium due to the delayed implementation, DOT could request them in the Department's 2009-11 budget request.

The transfer under this item is not included in the \$293,000,000 limit on transfers under the previous item. Consequently, the total transfer from the transportation fund to the general fund under the bill could be as high as \$298,000,000.

**4. HOSPITAL ASSESSMENT, RATE INCREASE, AND MA BENEFITS FUNDING CHANGE**

**Summary of Provision**

Provide \$338,381,100 (-\$60,000,000 GPR, \$194,848,300 FED, and \$203,532,800 SEG) in 2007-08 and \$362,217,400 (-\$62,500,000 GPR, \$213,490,900 FED, -\$1,500,000 PR and \$212,726,500 SEG in 2008-09) to reflect the net fiscal effect of: (a) creating an assessment on hospitals' gross patient revenue; (b) allocating a portion of the SEG revenue from the assessment to support

Change to Current Law	
SEG-REV	\$416,259,300
PR-REV	- 1,500,000
GPR	-\$122,500,000
FED	408,339,200
PR	- 1,500,000
SEG	<u>416,259,300</u>
Total	\$700,598,500

the state's share of the costs of increasing reimbursement for inpatient and outpatient services hospitals provide to medical assistance (MA) and BadgerCare Plus recipients; (c) allocating the balance of the SEG revenue from the assessment to replace GPR funds currently budgeted to support MA and BadgerCare Plus benefits in the 2007-09 biennium; and (d) increasing GPR-funded reimbursement to rural hospitals and psychiatric hospitals. Authorize the Department of Health and Family Services (DHFS) to assess hospitals up to \$203,532,800 SEG in 2007-08 and \$212,726,500 SEG in 2008-09 for these purposes. Estimate a reduction of revenue from the current hospital assessment by \$1,500,000 PR in 2008-09.

*Assessment.* DHFS would assess all hospitals, other than critical access hospitals (CAHs) and institutions for mental diseases (IMDs), that conduct business in the state, an annual amount, based on each hospital's gross patient revenue. Each hospital would be required to pay the total 2007-08 assessment by June 1, 2008, and, for 2008-09, hospitals would make quarterly payments by September 1, 2008, December 1, 2008, March 1, 2009, and June 1, 2009. All revenue from the assessment would be deposited to a segregated fund, the hospital assessment fund, which would be created in the bill.

At the discretion of DHFS, a hospital that is unable to make a timely payment by the statutory dates could be allowed to make a delayed payment. A determination by DHFS that a hospital may not make a delayed payment would be final and would not be subject to an administrative review under Chapter 227 of the statutes.

The amount of each hospital's assessment would be based on the information that is currently provided to DHFS under Chapter 153 of the statutes, or would be based on any other source that is approved in the MA state plan.

DHFS would be required to verify the amount of each hospital's gross patient revenue and determine the amount of the assessment owed by each hospital based on a uniform rate that is applicable to total gross patient revenue that DHFS estimates will yield the amounts that would be budgeted for increases in hospital reimbursement under the new appropriation and to replace GPR funding currently budgeted for MA and BadgerCare Plus benefits costs.

DHFS would levy, enforce, and collect the assessments and develop and distribute forms necessary for these purposes. If DHFS determined that any portion of the revenue needed to provide MA payment increases for inpatient and outpatient hospital services as fee for service or through health maintenance organizations (HMOs) is not eligible for federal MA matching funds, DHFS would be required to refund the amount of the revenue to hospitals in proportion to each hospital's payment of the assessment.

*Repeal Current Hospital Assessment.* The bill would repeal the current hospital assessment administered by DHFS, the appropriation supported by the assessment, and all related statutory references to the assessment. Currently, DHFS is required to annually assess hospitals a total of \$1.5 million. Revenue from the assessment is credited to a program revenue (PR) appropriation that supports MA and BadgerCare Plus benefits costs. However, DHFS has already collected and expended this revenue from hospitals in 2007-08. Consequently, these provisions would first

affect revenue and expenditures in 2008-09, although this is not specified in the bill. A reduction of \$1,500,000 in state-funded MA benefits would reduce estimated federal matching funds by approximately \$2,153,200 FED in 2008-09.

*Use of the Assessment Revenues.* DHFS would be authorized to assess hospitals a total of \$203,532,800 in 2007-08 and \$212,726,500 in 2008-09 to: (a) fund the state's share of the costs to increase reimbursement to hospitals for inpatient and outpatient services they provide to MA and BadgerCare Plus recipients (\$145,032,800 SEG in 2007-08 and \$147,726,500 SEG in 2008-09); and (b) increase funding for MA and BadgerCare Plus benefits by \$58,500,000 SEG in 2007-08 and \$65,000,000 SEG in 2008-09 and reduce GPR funding by a corresponding amount. The amounts identified under (b) would be initially deposited to the hospital assessment fund, but transferred to the MA trust fund for this purpose.

Funding for hospital rate increases would be provided under a biennial SEG appropriation that would be created in the bill. The appropriation would fund: (a) increases in inpatient and outpatient hospital reimbursement provided on a fee-for-service basis; and (b) increases in capitation payments to HMOs, which pay hospitals for services their MA and BadgerCare Plus enrollees receive. The Joint Committee on Finance would be prohibited from transferring moneys from any of these three appropriations to other appropriations under its current authority under s. 13.101 of the statutes.

*Rate Adjustment for Rural Hospitals.* The bill would provide \$3,044,300 (\$1,250,000 GPR and \$1,794,300 FED) in 2008-09 to increase reimbursement for rural hospitals. Under the current MA state plan for inpatient hospital services, certain rural hospitals qualify for an upward adjustment to their rates if they meet certain criteria. The administration's intent is to both increase the number of rural hospitals that would qualify for the adjustment, and increase the amount of the adjustment.

*Rate Adjustment for Institutions for Mental Diseases (IMDs).* The bill would provide \$3,044,300 (\$1,250,000 GPR and \$1,794,300 FED) in 2008-09 to increase reimbursement for institutions for mental diseases, which are defined under federal law as facilities established and maintained primarily for the care and treatment of individuals with mental diseases. These facilities would be exempt from the hospital assessment.

*Statutory Change Relating to the Rural Hospital Adjustment.* Beginning in 2007-08, the bill would increase, from \$2,256,000 to \$5,256,000 (all funds), the maximum amount DHFS could provide annually to support supplemental funds (in the form of adjustments to payment rates) to rural hospitals that, as determined by DHFS, have a high utilization of inpatient services by patients whose care is provided from governmental sources. In addition, the bill would delete references to CAHs as hospitals that are eligible for these supplemental payments. (The MA program currently reimburses hospitals that are certified as CAHs for their reasonable costs for both inpatient and outpatient services. Consequently, these hospitals do not currently receive supplemental rural hospital payments.)

*HMO Payments to Hospitals.* The bill would direct DHFS to develop a methodology for calculating rate increases for inpatient and outpatient hospital services in connection with the hospital assessment. The methodology would incorporate encounter data provided by HMOs and information that DHFS uses to calculate the capitated rates that DHFS pays HMOs for providing services to MA recipients. DHFS would be required to publicly disclose the methodology, and review the methodology every 12 months.

DHFS would be directed to require HMOs to do all of the following, as a term of the contracts DHFS makes with the HMOs:

1. Make monthly prospective payments, calculated using the methodology described above, to hospitals that serve MA recipients who are enrolled in the HMO.
2. Calculate the amounts that result from applying the rate increases that are derived using the methodology described above, for services for MA recipients for which hospitals submit claims to the HMO;
3. Within 90 days after the end of each six-month period, compare the amounts that the HMO paid under (1) for the six-month period with the amounts calculated under (2) for services provided during the same period and, if the amount under (2) exceeds the amount of the payments under (1), pay hospitals the difference within 90 days.

If the total payments that a HMO made to the hospital under (1) for a six-month period exceed the amount calculated under (2) for services provided during that same period, hospitals would be required to pay the HMO the difference within 90 days after the comparison is completed.

If DHFS determines that an HMO has not complied with payment condition as described above, DHFS would be directed to require the HMO to comply with the condition within 15 days after DHFS' determination. DHFS could terminate a contract with an HMO for failure to comply with the conditions described above. DHFS would be required to audit HMOs to determine whether they have complied with these conditions.

If an HMO and hospital cannot resolve the amount the HMO owes a hospital, or the amount a hospital owes an HMO, and either the HMO or the hospital, within six months after the end of the time period to which the disputed amounts relates, requests that DHFS determine the amount owed, DHFS would be required to determine the amount within 90 days after the request is made. The HMO or hospital would be, upon request, entitled to a contested case hearing under Chapter 227 on the DHFS determination.

*Report to the Joint Committee on Finance.* By December 31, 2008, and by December 31, 2009, DHFS would be required to report to the Joint Committee on Finance all of the following information for the previous state fiscal year: (a) the total amount of assessments collected; (b) the total amount of assessments collected from each hospital; (c) the total amounts DHFS determines were paid to HMOs for increased MA payments to hospitals under the provisions of the bill; (d) the total amount of payments made to each hospital by HMOs; (e) the total amount of MA

payments made to each hospital and the portion of the MA capitated payments made to HMOs for inpatient and outpatient hospital services from GPR appropriations; (f) the total amounts, including the amounts specified under (c), that DHFS determines were paid to HMOs for MA payments to hospitals; and (g) the results of any audits conducted by DHFS regarding payments by HMOs to hospitals, and any actions taken by DHFS as a result of these audits.

*Supplemental Funding for Hospitals Participating in the Relief Block Grant Program.* The bill would modify a provision in current law that requires DHFS to provide supplemental payments to hospitals that enter into a contract to provide health care services funded under the relief block grant program. Under the bill, DHFS would be permitted, but not required, to provide supplemental payments for this purpose.

*Effective Date and Sunset Provisions.* All of the provisions would take effect on the bill's general effective date. However, the provisions that authorize DHFS to assess hospitals would not apply after December 31, 2009. Consequently, legislation would be required to continue the assessment in the 2009-11 biennium. Without this legislation, there would be insufficient funds to maintain the rate increases that would be provided to hospitals under the bill. Further, since the provision would replace \$65 million of base GPR funds for MA and BadgerCare Plus benefits with SEG revenue from the assessment, the effect of sunseting the new hospital assessment and repealing the current assessment would be to increase GPR funding commitments in the 2009-11 biennium by \$66.5 million per year to offset the loss of hospital assessment revenue to support MA and BadgerCare Plus benefits costs.

*Fiscal Effect.* The bill would authorize DHFS to collect \$203,532,800 in 2007-08 and \$212,726,500 in 2008-09 in assessment revenue from hospitals. DHFS would use this revenue to: (a) fund the state's share of the costs to increase reimbursement to hospitals for inpatient and outpatient services they provide to MA and BadgerCare Plus recipients (\$145,032,800 SEG in 2007-08 and \$147,726,500 SEG in 2008-09; and (b) transfer \$58,500,000 SEG in 2007-08 and \$65,000,000 SEG from the hospital assessment fund to the MA trust fund to support MA and BadgerCare Plus benefits costs to replace base GPR funding for the program.

Because the bill would increase the state's share of MA payments to hospitals by \$145,032,800 SEG in 2007-08 and \$150,226,500 (\$147,726,500 SEG and \$2,500,000 GPR) in 2008-09, this funding would be matched with additional federal MA matching funds totaling \$196,884,600 FED in 2007-08 (based on an estimated matching rate of 57.5825% in 2007-08) and \$215,644,100 in 2008-09 (based on an estimated matching rate of 58.94% in 2008-09).

In 2007-08, hospitals would pay increased assessments totaling \$203,532,800, but MA payments to hospitals would increase by an estimated \$341,917,400, resulting in a net increase in revenues to hospitals of \$138,384,600.

In 2008-09, hospitals would pay \$212,726,500 under the new assessment, but would no longer pay \$1,500,000 under the current assessment, for a net increase in assessments totaling \$211,226,500. MA payments to hospitals would increase by an estimated \$365,870,600, resulting in a net increase in revenue to hospitals of \$154,644,100.

However, this net increase in funding available for hospitals would have distributional effects -- not all hospitals would receive more in increased MA reimbursement than they would pay in assessments.

The following tables summarize the funding and revenue changes relating to this proposal.

### Summary of Fiscal Effect of Hospital Assessment and Rate Increase Proposal

#### State Fiscal Year 2007-08

	MA Benefits (GPR)	Hospital Revenue (SEG)	Current Assessment (PR)	MA Matching Funds (FED)	Total (All Funds)
<b>Changes in Payments to Hospitals</b>					
General Hospital Rate Increase	\$0	\$145,032,800	\$0	\$196,884,600	\$341,917,400
Supplements for Rural Hospitals	0	0	0	0	0
Supplements for IMDs	0	0	0	0	0
Subtotal	0	\$145,032,800	\$0	\$196,884,600	\$341,917,400
<b>MA Base Funding Changes</b>					
Transfer SEG Funding to MA Trust Fund	-\$60,000,000	\$58,500,000	\$0	-\$2,036,300	-\$3,536,300
<b>Total Fiscal Effect on State Budget</b>	-\$60,000,000	\$203,532,800	\$0	\$194,848,300	\$338,381,100
<b>Effect on Hospitals</b>					
Net Change in Hospital Assessments		\$203,532,800			
Aggregate Rate Increase for Hospitals (All Funds)		\$341,917,400			
Net (Aggregate) Gain for Hospitals		\$138,384,600			

#### State Fiscal Year 2008-09

	MA Benefits (GPR)	Hospital Revenue (SEG)	Current Assessment (PR)	MA Matching Funds (FED)	Total (All Funds)
<b>Changes in Payments to Hospitals</b>					
General Hospital Rate Increase	\$0	\$147,726,500	\$0	\$212,055,500	\$359,782,000
Supplements for Rural Hospitals	1,250,000	0	0	1,794,300	3,044,300
Supplements for IMDs	1,250,000	0	0	1,794,300	3,044,300
Subtotal	\$2,500,000	\$147,726,500	\$0	\$215,644,100	\$365,870,600
<b>MA Base Funding Changes</b>					
Transfer SEG Funding to MA Trust Fund	-\$65,000,000	\$65,000,000	\$0	\$0	\$0
Repeal Current PR Assessment	0	0	-1,500,000	-2,153,200	-3,653,200
<b>Total Fiscal Effect on State Budget</b>	-\$62,500,000	\$212,726,500	-\$1,500,000	\$213,490,900	\$362,217,400
<b>Effect on Hospitals</b>					
Hospital Total Assessment (New Assessment)		\$212,726,500			
Elimination of Current Assessment		<u>-1,500,000</u>			
Net Change in Hospital Assessments		\$211,226,500			
Aggregate Rate Increase for Hospitals (All Funds)		\$365,870,600			
Net (Aggregate) Gain for Hospitals		\$154,644,100			

[Bill Sections: 2, 3, 5, 6, 9, 11 thru 36, 52, and 9221(1),(2)&(3)]

## Discussion

*Hospital Reimbursement.* The state's MA program pays hospitals for inpatient and outpatient services they provide to MA and BadgerCare Plus recipients. DHFS pays hospitals on a fee-for-service basis directly for inpatient and outpatient services they provide to recipients who are not enrolled in managed care organizations. DHFS pays HMOs monthly capitation payments for each MA and BadgerCare Plus recipient enrolled in the HMO. HMOs use revenue from the capitation payments to pay providers, including hospitals, for services they render to their enrollees.

Under MA and BadgerCare, hospitals are not fully reimbursed for their costs of providing care to MA and BadgerCare recipients, nor are they reimbursed at rates equal to their "usual and customary charges."

Most inpatient services are reimbursed under the diagnosis related groups (DRG) system. Under this method, DHFS annually calculates, for each hospital, a hospital-specific DRG cost-based payment rate, using hospital cost data, adjusted to ensure compliance with the MA budget. For each inpatient stay, this rate is multiplied by a DRG weight, which is intended to reflect the relative resource consumption of each type of inpatient stay, to determine the hospital's reimbursement for the stay. A cost outlier payment is made when the cost of providing a service exceeds a pre-determined "trimpoint." Each inpatient hospital claim is tested to determine whether the claim qualifies for a cost outlier payment.

The DRG includes all covered services except professional services provided at the hospital, including physicians, dentists, anesthesia assistants, pharmacy, specialized medical vehicle transportation and durable medical equipment and supplies for non-hospital use. The certified provider bills these services separately.

Each hospital receives a single, predetermined rate for each outpatient visit the hospital provides. The rate is not based on the services a patient receives, or the conditions that resulted in the hospital visit. Instead, the outpatient rate per visit is based on a hospital's outpatient cost per visit, as documented in an audited cost report, which is inflated to the current fiscal year and adjusted to reflect the amount of funding available and other limits on outpatient hospital payments.

If the Governor's proposal were enacted, DHFS would increase each hospital's DRG cost-based payment rate and continue to pay hospitals the product of the rate and the DRG weight for most inpatient services. In addition, DHFS would increase each hospital's outpatient rates. The effect of these changes would vary by hospital, depending on number and type of inpatient stays each hospital receives. The administration has contracted with a consultant to model and estimate the effects of these changes for each hospital. However, this analysis is not yet completed.

*Provider Taxes.* Federal MA rules have been established to limit states' ability to tax health care providers. In general, if a state wishes to implement a health care-related tax for the purpose

of providing a source of state funding for MA payments, it must ensure that the tax is broad-based and applied uniformly to classes of providers. States may not pay back providers, dollar for dollar, the assessments that they pay the state. Under federal law, the provider tax must create "winners" and "losers."

If a provider tax does not meet the standards established in rule for being "broad-based" or "uniformly imposed," a state may seek a waiver from these requirements. However, if a state applies for such a waiver, it must demonstrate that the net effect of the tax and associated expenditures is redistributive in nature, and the amount of the tax is not directly correlated with MA payments. Wisconsin currently has two provider taxes -- the nursing home bed assessment and the hospital assessment.

*MA State Plan Amendment.* Prior to the enactment of 2007 Wisconsin Act 20, the state submitted a state plan for MA inpatient hospital reimbursement to the U.S. Department of Health and Human Services, Centers for Medicare and Medicaid Services (CMS) that assumed that the Governor's 2007-09 biennial budget hospital assessment proposal would be enacted. CMS approved the state plan. Following the enactment of the budget, DHFS submitted an amended plan that, if approved, would have the effect of paying hospitals the same inpatient rates as the rates that were in effect during the 2006-07 fiscal year. CMS has not yet approved this revised plan. However, the plan will be approved unless CMS requests additional information from the state by March 20, 2008. If this bill is enacted, it will be necessary for DHFS to withdraw the amended state plan so that the current state plan, which anticipated a hospital assessment and rate increase, would take effect for fiscal year 2007-08.

*Cost to Continue and Effect on Structural Deficit.* The bill would reduce state funding for MA and BadgerCare benefits by \$66,500,000 (\$65,000,000 GPR and \$1,500,000 PR) in 2008-09, but terminate the hospital assessment after the 2008-09 fiscal year. Consequently, unless the hospital assessment is continued in the 2009-11 biennium, the bill would increase the GPR structural deficit by \$133 million in the 2009-11 biennium.

## 5. REAL ESTATE INVESTMENT TRUSTS

<b>Change to Current Law</b>
GPR-REV \$6,000,000

### Summary of Provision

Modify the method of calculating net income for real estate investment trusts (REITs) to specify that the dividends paid deduction otherwise allowed by federal law in computing the net income of an REIT that is subject to federal income tax would be required to be added back to income in computing the state income and franchise tax, unless the REIT was a qualified REIT.

"Qualified REIT" would be defined to mean an REIT, except an REIT: (a) of which more than 50% of the voting power or value of the beneficial interests or shares are owned or controlled, directly or indirectly, by a single entity that is subject to federal Internal Revenue Code (IRC) provisions governing corporate distributions and adjustments (including distributions, liquidations, organizations and reorganizations, carryovers, and treatment of certain

interests as stock or indebtedness); (b) that is not exempt from taxation under state law; and (c) that is not an REIT subsidiary or a qualified real estate trust subsidiary as defined under the IRC.

State definitions of REIT, regulated investment company (RIC), and real estate mortgage investment conduit (REMIC) would be referenced to the IRC. Statutory provisions that are currently used to update references to the IRC for REITs, RICs, and REMICs would be deleted. The Department of Revenue indicates that the current updating provisions are not necessary because federal provisions related to REITs, RICs, and REMICs are included whenever state law is referenced to the IRC for corporations. Specific provisions defining income for REITs, RICs, and REMICs through references to the appropriate sections of the IRC would be adopted. These definitions would be automatically updated whenever state corporate income and franchise tax references were updated by the Legislature. Also, statutory provisions would specify the state treatment of differences between depreciation or adjusted basis for federal and state income tax purposes.

These provisions would first apply to tax years beginning on or after July 1, 2008, and would increase income and franchise tax revenues by an estimated \$6.0 million in 2008-09, and annually thereafter.

[Bill Sections: 37 thru 48 and 9341(1)]

### **Discussion**

An REIT is an organization or corporation that is designed to act as an investment agent for its shareholders to enable small investors to pool resources together to make real estate investments that they might not otherwise be able to individually. A corporation, association, or trust must meet the following ownership and purpose requirements in order to qualify as an REIT:

- a. Beneficial ownership in the organization must be held by at least 100 persons for at least 335 days during the 12-month tax year.
- b. The beneficial ownership must be evidenced by transferable shares or certificates of beneficial interest.
- c. The organization's management must be in the hands of one or more trustees or directors, with the trustees generally holding legal title to the organization's property and having exclusive authority over management.
- d. The organization must possess all other necessary attributes that would, except for its treatment as an REIT, cause it to be taxed as a corporation.
- e. Five or fewer individuals may not directly or indirectly own more than 50% of the value of the organization's stock during the last six months of the organization's tax year.

- f. The organization cannot be a financial institution or an insurance company.
- g. The organization must distribute at least 90% of its taxable income for the tax year to its shareholders.
- h. The organization must elect to be treated as an REIT.

An REIT must also meet the following income and investment requirements:

a. At least 95% of the REIT's gross income must be from dividends, interest, rents from real property (including rents from interests in real property), net gains from the sale or other disposition of stock, securities, real property, and interests in mortgages on real property, abatements and refunds of taxes on real property (including foreclosure property involuntarily acquired), and gain from the sale of a real estate asset that is not a prohibited transaction.

b. At least 75% of the REIT's gross income must be derived from real property. Included within this 75% category are rents from real property, interest on obligations secured by mortgages on real property, net gain from the sale of real property and interests in mortgages on real property, dividends and other distributions from, and net gain on sale or other disposition of transferable shares in, other REITs, abatements and refunds of taxes on real property, and gain from the sale of a real estate asset that is not a prohibited transaction.

At the close of each quarter of the tax year, REITs must meet two tests regarding their assets: (a) 75% of the value of total assets must be represented by real estate assets, cash and cash items, or government securities; and (b) not more than 25% of the value of the REIT's assets may be represented by securities other than those described in the 75% test, and the entire amount of securities of any one issuer may not exceed 5% of the value of the total assets of the REIT or 10% of the voting securities of the issuer.

As noted, to qualify as an REIT, an organization is required to distribute to its shareholders at least 90% of its taxable income each tax year. If this threshold is met, the REIT is only taxed on the undistributed portion of its income at corporate income tax rates. To the extent the income is paid out as an ordinary dividend, the REIT may claim a dividends paid deduction for the amount of the dividend distribution. Under federal law, the REIT shareholder is not permitted to claim a dividends received deduction for the dividend, and the dividend distribution is taxed at the shareholder level. The REIT is a pass-through entity and the shareholder pays the tax on the REIT income when received as a dividend.

There is no distribution threshold for the net capital gains of an REIT. But any distribution of capital gains to shareholders must be paid out of the organization's net capital gains for that year. No deduction is provided for capital gains distributions, and any undistributed capital gains are subject to taxation at the REIT level.

The bill's modifications are designed to address two general types of business practices where REITs have been used to avoid state taxation. One type of practice generally involves large multi-state retailers that transfer ownership of the retailer's real property to a related REIT. The REIT charges the retailer rent for use of the property, which reduces the retailer's taxable income and state tax liability. Due to the ownership of property in the state, the REIT is subject to state income taxes. However, the REIT typically distributes the rental payments as dividends to an affiliate or holding company that is located in a state that allows a dividends received deduction for REIT distributions, has no state corporate income tax, or that allows combined reporting. The REIT would not pay taxes on the rental income because it may claim a dividends paid deduction for the distributions of rental income to the affiliate or holding company. The affiliate or holding company also would not pay taxes on the distribution because it could: (a) claim a dividends received deduction for the rental payments distribution; (b) is located in a state, such as Delaware, that imposes no state income tax on this type of income; or (c) is located in a state that allows or requires combined reporting, which requires all intercompany transfers, such as dividend payments, to be eliminated in calculating taxable income.

A second similar practice generally involves multi-state banks. In this case, the bank transfers its mortgages or mortgage-backed securities to a related out-of-state REIT. As a result, the bank would shift its mortgage-related income to the REIT. If the REIT has no nexus with the bank's state, interest on the mortgages and related securities cannot be taxed by that state. In such cases, the REIT may be located in a state which imposes no state income tax on the REIT, and the interest income is not taxed. If the REIT is subject to taxation by the bank's state or the state in which it operates, it can distribute the interest income as a dividend to an affiliate or holding company and claim a dividends paid deduction for that interest dividend. In turn, the affiliate or holding company would not pay taxes on the interest dividend for the reasons described in the preceding paragraph.

It should be noted that the inherent nature of an REIT is that it is a pass-through entity and generally not subject to taxation. When used as designed, an REIT is intended to result in income being taxed only once at the shareholder level. Moreover, most publicly-traded REITs are established for investment purposes, and not as vehicles for tax avoidance.

Similar provisions were included in the version of the 2007-09 biennial budget bill passed by the Senate last summer (2007 SB 40). However, the Senate provisions would have applied to regulated investment companies (RICs, or mutual funds) in addition to REITs. Identical provisions, which would have applied to REITs but not RICs, were included in the Governor's October, 2007, special session biennial budget bill. Neither provision was included in the final version of the biennial budget bill (Act 20).

## 6. TOBACCO SECURITIZATION

Change to Current Law	
SEG-REV	\$30,000,000
GPR	- \$30,000,000

### Summary of Provision

Increase the transfer from the permanent endowment fund to the medical assistance (MA) trust fund by \$15 million annually (from \$50 million annually under Act 20 to \$65 million annually) associated with additional tobacco bond proceeds from a tobacco securitization transaction to be carried out by the Badger Tobacco Asset Corporation (BTASC).

Reduce funding for MA and BadgerCare Plus benefits by \$15 million GPR annually to reflect the availability of the transferred revenues to support MA and BadgerCare benefits costs in the 2007-09 biennium. (Although the bill would not increase MA benefits funding by \$15 million SEG in each year from the MA trust fund to permit DHFS to expend these funds, the administration indicates that this change would be needed to meet the Governor's intent.)

[Bill Sections: 10 and 9221(4)]

### Discussion

According to the Department of Administration (DOA), \$15 million in additional annual revenues to the permanent endowment fund would be generated by BTASC carrying out another tobacco securitization transaction, which would be different than the securitization transaction envisioned during legislative deliberations on 2007 Act 20. Under Act 20, \$50 million annually is to be transferred from the permanent endowment fund to the medical assistance trust fund associated with a securitization transaction that DOA identified at that time.

Under 2001 Act 16 (the 2001-03 budget), the DOA Secretary was authorized to securitize the state's rights to its tobacco settlement payments. Using this authority, the DOA Secretary assigned the rights to the state's tobacco settlements to BTASC on April 18, 2002. BTASC, after receiving the rights to the state's tobacco settlement payments, used the newly-acquired revenue stream to back the issuance of \$1.59 billion in revenue bonds. Under federal tax law, these bonds may only be refinanced once. In return for the rights to the state's tobacco settlement payment revenues, BTASC provided the state with the net proceeds from those bonds. The securitization transaction resulted in \$1.275 billion in net bond proceeds being available to the state.

Under the 2002 securitization transaction, the state assigned the rights to the next 30 years of its tobacco settlement payments to BTASC. However, as indicated in the offering circular on the bonds, fewer years of the state's settlement payments are expected to be needed to retire those bonds. The repayment requirements associated with most of the bonds that were issued require that any excess, annual tobacco settlement revenues, after all the scheduled, annual debt service payments are made, must be used to prepay the outstanding principal on the BTASC bonds. Therefore, according to the offering circular, using a conservative, independent forecast of the annual tobacco settlement revenues to be received by BTASC, it is

projected that all of BTASC's outstanding tobacco bonds will be paid off by 2018. Therefore, beginning during 2018 tobacco settlement revenues currently assigned to BTASC, will again flow to the state. In 2019, the state expects to regain access to the full annual amount of tobacco settlement revenues.

DOA has provided some details of a potential 2008 securitization transaction. This second securitization transaction, which could be implemented under current law, would involve BTASC issuing \$1.5 billion in new bonds to pay off their outstanding bonds. Under the proposal, BTASC would use its one opportunity to refinance the existing BTASC bonds by issuing the new bonds at rates similar to the rates currently being paid on the existing BTASC bonds. However, the repayment of the new BTASC bonds would be structured in a way that would significantly lower the annual amount of tobacco settlement revenues needed to retire the obligations compared to the old BTASC bonds. The lower annual debt service costs would primarily be the result of extending the expected repayment date on the bonds from 2018 to 2027. Based on cashflow projections prepared for the administration, extending the expected repayment schedule for the new bonds through 2027 would lower the required annual debt service amount needed to retire the bonds by approximately \$68 million annually through 2020. This \$68 million in annual tobacco settlement revenues would be deposited to the permanent endowment fund each year and then \$65 million would be transferred under the bill to the medical assistance trust fund and be available for medical assistance expenditures. If annual revenues would exceed the proposed \$65 million transfer amount, any balance could remain in the permanent endowment fund.

The following table lists the expected tobacco settlement revenues to be received by the state through 2028 under the existing securitization transaction and under the proposed second securitization transaction.

**Comparison of Estimated Tobacco Settlement Revenues Available to the State  
Under the Existing and Proposed Securitization Transactions  
(\$ in Millions)**

<u>Year</u>	<u>Estimated Revenues Under Existing Securitization</u>	<u>Estimated Revenues Under Proposed Transaction</u>
2008	\$0	\$68
2009	0	68
2010	0	68
2011	0	68
2012	0	68
2013	0	68
2014	0	68
2015	0	68
2016	0	68
2017	0	68
2018	115	68
2019	179	68
2020	181	68
2021	183	0
2022	185	0
2023	188	0
2024	190	0
2025	192	0
2026	195	0
2027	197	2
2028	200	200

As indicated in the table, the proposed securitization transaction essentially involves the restructuring and timing of future cash flows to the state. Effectively, in exchange for receiving \$68 million in tobacco settlement revenues annually from 2008 through 2020, the state would forgo annual tobacco settlement payments ranging from \$115 million to \$195 million from 2018 through 2027.

Based upon the estimates shown in the table above, under the proposed transaction, the state would receive \$1,086 million from 2008 through 2028, but would forgo \$2,005 million over the same period, resulting in a net reduction of \$919 million. It is also necessary to compare the two cashflow streams using a net present value calculation. Using an annual discount of 6.5%, which approximates the projected interest rate on the bonds issued under the proposed transaction, the revenues under the proposed transaction from 2008 through 2028 would have an estimated net present value of \$639 million. In comparison, the revenues under current law from 2008 through 2028 would have an estimated present value of \$733 million. Based on this

comparison, the net present value of the revenues that would be received by the state under the proposed transaction would be an estimated \$94 million less than under current law.

**7. PUBLIC LIBRARY SYSTEM AID FROM THE USF**

**Summary of Provision**

Delete \$11,297,400 GPR and provide \$11,297,400 SEG in 2008-09 for public library system aid. Public library system aid under 2007 Act 20 totals \$16,138,000 (\$2,097,400 GPR and \$14,040,600 SEG) in 2007-08 and \$16,783,500 (\$11,297,400 GPR and \$5,486,100 SEG) in 2008-09. The segregated revenue is from the universal service fund (USF), which receives its funding through assessments on annual gross operating revenues from intrastate telecommunications providers. The effect of the Governor's recommendation would be to replace all general fund supported library aids with funds from the USF in 2008-09. The amounts that the Public Service Commission (PSC) would assess telecommunications providers related to the USF would increase by \$11,297,400 (from a total of \$32,038,400 to \$43,335,800) in 2008-09 under this recommendation.

Change to Current Law	
SEG-REV	\$11,297,400
GPR	- \$11,297,400
SEG	<u>11,297,400</u>
Net	\$0

[Bill Section: 9237(1)]

**Discussion**

Total USF assessments are budgeted at \$31,591,600 in 2007-08 and \$32,038,400 in 2008-09. In addition, Act 20 specified that \$9,200,000 SEG from the 2006-07 USF ending balances (unused portions of prior assessments) would be used to offset a portion of GPR funding for public library system aids in 2007-08. Because this \$9,200,000 was taken from carryover balances in the USF, it did not result in a rate increase in assessments. In contrast, the increase of \$11,297,400 SEG for public libraries recommended by the Governor would result in an equal increase in USF assessments on telecommunications providers. Telecommunications providers are allowed to fully recover their share of USF assessments, including funding provided for public library systems, through a "pass-through" adjustment applied only to subscribers' local exchange service rates.

The USF currently funds universal telecommunications services programs under the PSC, the telecommunications access program under the Department of Administration (DOA), BadgerLink and public library system aid under the DPI, and BadgerNet under the University of Wisconsin System. The PSC requires telecommunications providers to contribute annually to the USF to support the provision of essential telecommunications services and advanced telecommunications service capabilities in the state. The assessment must be sufficient to fund the amounts appropriated under the statutorily enumerated DPI, PSC, DOA, and UW System telecommunications-related appropriations. Except \$6 million annually related to universal telecommunications service programs under the PSC, all of these assessments may be recovered through the "pass-through" assessment on subscribers.

## 8. LIMIT ON INTERFUND CASHFLOW BORROWING

### Summary of Provision

Increase the limit on interfund borrowing to support the general fund's cashflow from 8% of GPR appropriations in that fiscal year to, instead, be 13% of GPR appropriations for that year. Specify that this increase would no longer apply after June 30, 2009.

[Bill Section: 9101(3)]

### Discussion

The state uses the state investment fund as an investment pool for portions of retirement trust assets and cash balances of the state's various funds. In addition, local governments can elect to invest their cash balances in the fund. The state investment fund, which is managed by the State of Wisconsin Investment Board, had approximately \$7.1 billion in assets during February, 2008.

The Secretary of DOA is authorized to temporarily reallocate to the general fund an amount equal to 5% of total GPR appropriations in order to support the general fund's cashflow (approximately \$689 million in 2007-08 and \$709 million in 2008-09). The bill would increase this 5% limit to be 10% in the 2007-09 biennium, which would allow additional temporary reallocations in 2007-09. Under current law, the Secretary may permit an additional 3% to be used for temporary reallocations to the general fund for a period not to exceed 30 days (approximately \$413 million in 2007-08 and \$425 million in 2008-09). Reallocations of the additional 3% may not be made for consecutive periods. In total, under current law, 8% of GPR appropriations (\$1,102 million in 2007-08 and \$1,134 million in 2008-09) may be allocated to the general fund on a temporary basis. Under the bill, these aggregate limits would be \$1,781 million in 2007-08 and \$1,830 million in 2008-09. No limit applies to temporary reallocations from the budget stabilization fund to the general fund. The following table compares the limits under the proposal with current law.

### Limits on Temporary Reallocations to Support the General Fund's Cashflow (\$ in Millions)

<u>Limit</u>	Current Law		<u>Limit</u>	Proposal	
	<u>2007-08</u>	<u>2008-09</u>		<u>2007-08</u>	<u>2008-09</u>
5%	\$689	\$709	10%	\$1,370	\$1,408
3% (30-day limit)	<u>413</u>	<u>425</u>	3% (30-day limit)	<u>411</u>	<u>422</u>
Total	\$1,102	\$1,134	Total	\$1,781	\$1,830

For funds other than the general fund, up to \$400 million can be reallocated between the general fund, certain segregated funds, and the local government investment pool.

Funds that borrow money through temporary reallocations are charged interest at the

earnings rate of the state investment fund. No interest is charged to the general fund if it borrows from the budget stabilization fund. In no case can moneys be borrowed from retirement trust assets or from several specific segregated funds. DOA estimates that the state investment fund had \$1.9 billion of moneys available for temporary reallocations in January, 2008.

In a report to the Co-Chairs of the Joint Committee on Finance dated January 30, 2008, DOA indicated that the general fund could have a worst day cash balance of -\$944 million in June, 2008. Although this was a preliminary cash forecast, it is within \$158 million of the current statutory limit of \$1,102 million.

The state also can issue operating notes to support the general fund's cashflow. The state issued \$600 million of such notes in 2007-08, which will be repaid by the end of the fiscal year. These notes allow the state to borrow externally at tax exempt rates to support its cashflow. However, because operating notes have to be repaid in the same fiscal year of issuance, they have not been used to address a cashflow problem in June.

## **9. THRESHOLD FOR BUDGET ADJUSTMENT BILL**

### **Summary of Provision**

Increase the current threshold above which the Governor is required to submit a budget adjustment bill from a shortfall of 0.5% of GPR appropriations to a shortfall of 2.0% of GPR appropriations. Sunset this modification on June 30, 2009.

[Bill Sections: 9101(1)&(2)]

### **Discussion**

Under current law, the Secretary of DOA can use the state's allotment process to withhold payments from appropriations to state agencies, except appropriations for general school aids, supplemental appropriations under the Joint Committee on Finance, and appropriations for shared revenue and tax relief. Under this provision, the DOA Secretary can force lapses by preventing the expenditure of appropriated moneys, so that they are retained by the general fund, or by whichever program revenue account or segregated fund that the appropriation is drawn from.

However, under current law, once the Secretary of DOA determines that a shortfall is projected to be greater than 0.5%, then the Secretary cannot use the allotment process to reduce spending. Instead, the Secretary is required to immediately notify the Governor, the presiding officer of each house of the Legislature and the Joint Committee on Finance of the revenue shortfall. Following this notification, the Governor is required to submit a bill containing his or her recommendations for the correcting of the imbalance between projected revenues and authorized expenditures.

Using the current law thresholds, 0.5% of estimated GPR expenditures is \$67.9 million in

2007-08 and \$70.3 million in 2008-09, and these are the deficit amounts that would trigger the requirement for a budget adjustment bill. Under the proposed 2.0% amount, the thresholds would be \$270.0 million in 2007-08 and \$279.5 million in 2008-09. As a result, under the proposal, the Legislature would delegate authority to the Secretary of DOA to use the allotment process to withhold funding from state agencies to address a significantly larger budget shortfall, if one should materialize later in the 2007-09 biennium.

## **10. AUTHORIZE TRANSFERS FROM THE BUDGET STABILIZATION FUND**

### **Summary of Provision**

Authorize the Secretary of the Department of Administration (DOA) to transfer moneys from the budget stabilization fund to the general fund during either year of the 2007-09 biennium, if the projected gross balance in the general fund is less than \$65 million in that year.

[Bill Section: 9201(1)]

### **Discussion**

The budget stabilization fund currently has a balance of \$57.5 million. Under current law, there is an appropriation from the budget stabilization fund to the general fund. However, this appropriation is currently set at \$0, so that no transfer can be made without an appropriation increase by the Legislature.

Under the bill, the Legislature would delegate authority to the Secretary of Administration to transfer moneys from the budget stabilization fund to the general fund during either year of the 2007-09 biennium, if the projected balance in the general fund is less than \$65 million in that year. The administration estimates that it would transfer \$9 million in 2007-08 and \$12.7 million in 2008-09 to the general fund under this provision, which would result in an estimated general fund balance of \$65.1 million in 2007-08 and \$65.0 million in 2008-09. This would leave an estimated balance of \$36.6 million in the budget stabilization fund on June 30, 2009, including interest earnings on the balances in the fund during the 2007-09 biennium.

## **11. MODIFY THE STRUCTURAL BALANCE REQUIREMENT**

### **Summary of Provision**

Modify the requirement for a structural balance so that the calculation of the structural balance would include moneys held in the budget stabilization fund during the 2007-09 biennium.

[Bill Section: 9130(1)]

## **Discussion**

Under current law, no bill may be adopted by the Legislature if the bill would cause expenditures, less any transfers to the budget stabilization fund, to exceed taxes plus departmental revenues in any fiscal year. This provision compares expenditures with revenues, after subtracting the opening balance.

The bill would modify this calculation for the 2007-09 biennium so that the balances held in the budget stabilization fund would be considered revenue in determining whether there is a structural balance in the general fund. The administration indicates that without this modification, the bill would have a structural imbalance of -\$1.1 million in 2007-08 and -\$0.1 million in 2008-09. Under the bill, the administration estimates that the budget stabilization fund would have a closing balance of \$36.6 million.