

# Health Care Reform And The State Budget Deficit

*Californians need health care reform now. As the state faces across-the-board spending cuts, many of them to health services, we must not walk away from the billions of dollars that the Governor's reforms will bring into our health care system. California cannot afford to leave this money on the table. The Health Care Security and Cost Reduction Act (the Act) secures these funds, and takes pressure off of the state budget to finance the Medi-Cal rate hikes that drive some of our most significant spending growth. The Act is fully funded, budget neutral and includes mechanisms to ensure strong oversight, evaluation and flexibility to prevent auto-pilot spending. Through the Act, California achieves a landmark reform that strengthens our health care system when we need it most.*

## **The Act brings billions into our healthcare system.**

- **It secures \$4 billion in new federal funds that California is leaving on the table today.** The Act brings in \$4.6 billion in federal dollars. Approximately \$4 billion of this is new funding. California has not been able to access this money in the past because of our inability to provide the matching state funds. We are eligible for these federal funds under current law.
- **And more than \$9 billion in other contributions.** The Act provides a dedicated financing stream to fully fund these reforms. Sources include individual contributions, employer revenues and hospital fees.

## **The Act is fully funded and budget neutral.**

- The Act does not utilize any new General Fund dollars to fund health care reforms.
- Modeling by MIT health care economist Jon Gruber demonstrates the Governor's plan is fully funded. Over the long-term, the Act's prevention policies and other cost controls will slow the rate of growth in health care costs.

## **The Act reduces pressure on the General Fund and the state's second-largest expenditure: Medi-Cal.**

Medi-Cal represents one of the fastest growing programs in state government, increasing from \$7.5 billion General Fund in 1998 to \$14.3 billion General Fund in the current budget year. Reforms will reduce long-term budget pressure by:

- **Reducing the burden on the General Fund to finance rising Medi-Cal hospital rates.** Hospital costs are the largest driver of Medi-Cal cost increases. Hospitals are canceling their contracts with Medi-Cal because of low reimbursement rates. California's health care reforms increase and stabilize hospital rates by bringing Medi-Cal payments up to Medicare payment levels.
  - The reforms will finance higher reimbursements with new hospital revenues and federal funds.
- **Funding programs to improve the health of current Medi-Cal beneficiaries.** These include "Healthy Actions" programs, diabetes screening and management, obesity prevention and smoking cessation. Keeping Californians healthier reduces the need for costly services.

## **The Act addresses the structural budget problems that drive deficits.**

Constitutional spending requirements, formula-driven programs and the volatile nature of the state's income tax system all contribute to California's structural budget deficit. The Act includes built-in mechanisms to ensure that health care reforms are financially self-sustaining and have a positive impact on our structural budget problem.

- **It can't go into effect until the Department of Finance certifies that there's enough money.** Under the Act, the state Director of the Department of Finance must certify that there is enough revenue for a three-year period in order for the entire Act to go into effect.
- **It will be reviewed throughout the budget process.** Once the Act is enacted, regular updates on these reforms will be provided in the Governor's January Budget and the May Revision. In addition, the state will engage in early and systematic evaluation at each step of implementation to identify the reform's impact on state costs, delivery systems, quality of care, and overall progress in moving toward universal coverage.
- **It requires ongoing evaluation.** The Secretary of Health and Human Services, in collaboration with other state agencies and external experts, will track and assess the effects of health care reform. They will submit this assessment to the Legislature and update it every two years.
- **It gives the state flexibility to manage costs.** Under these reforms, the state will have flexibility to make adjustments, reduce costs, and alleviate the need to reach for additional state resources.

## **The Act relieves counties of fiscal pressures driven by caring for low-income uninsured.**

- Public hospitals will gain approximately \$500 million a year in new revenue from health care reform.
- Today, every county must provide health care to many of the uninsured, generally using only county funds. Further, public hospitals face increasing costs for covering the uninsured and federal reimbursement for this

coverage is either flat or expected to decline. Without structural change these public hospitals may not be financially viable.

- Counties will be required to provide a share of the cost for providing this care, equal to approximately 50 percent of what they are currently spending.

### **The Act will contain costs and lower health care spending.**

This legislation addresses chronic illnesses, which account for 83 percent of national health care spending.

- According to the California Healthcare Foundation, 38 percent of the US population suffers from a chronic disease, accounting for 83 percent of health care spending.
- The Robert Wood Johnson Foundation reports in “Chronic Care in America: A 21<sup>st</sup> Century Challenge” that 40 percent of Americans will be living with one or more chronic condition by 2010.

The Act provides broad access to preventive care; targeting obesity, diabetes, smoking; and enacting “Healthy Actions” programs. Specific strategies include:

- **Diabetes:** Reforms will promote better, proactive diabetes prevention and treatment. The average annual medical expenditure for a person with diabetes is about five times that of someone without.
- **Smoking Cessation:** There are approximately 43,000 tobacco-related deaths in California each year. This translates into \$8.6 billion in direct medical costs and \$7.3 billion in lost productivity from illness and premature death.
- **Obesity:** Under these reforms, California will encourage healthy food choices and physical activity to fighting obesity as aggressively and effectively as tobacco use. The Centers for Disease Control and Prevention estimate obesity-attributable health care costs at \$75 billion, of which about half was publicly financed. They attributed approximately 6 percent of all adult health care, 7 percent of Medicare, and 11 percent of Medicaid expenditures to obesity.

The Act moderates spiraling hospital costs in two key ways:

1. Universal coverage and increased Medi-Cal reimbursement rates will help mitigate the shift of uncompensated costs by hospitals onto the insured and reduce General Fund pressure for Medi-Cal rate increases.
2. It modifies seismic retrofit requirements, focusing improvements on infrastructure with the highest risk while reducing short-term mandated hospital construction costs from \$19.7 billion to \$15 billion.

It also improves insurer efficiency and limits excessive profit margins and administrative costs. Health plans will be required to spend 85 cents of every premium dollar on patient care, not on profit or administration.

### **The Act will have a positive impact on the economy. Health care reforms will:**

- **Increase productivity.** The Institute of Medicine estimates that America’s health insurance gap reduces national economic productivity by \$65-\$130 billion dollars annually (2003 dollars) (Institute of Medicine, “Hidden Costs, Value Lost: Uninsurance in America,” National Academy of Sciences, 2003).
  - California has approximately 15 percent of the nation’s uninsured, so the economic productivity loss could be estimated at about \$10 billion-\$20 billion. More productivity means higher tax revenues.
- **Minimize the costs that the insured pay to cover the uninsured.** Coverage of the uninsured will reduce the “hidden tax,” helping to contain the rate of premium growth that employers experience on an annual basis. The New America Foundation has estimated that the average California family pays an additional \$1,186 in premiums each year to cover the hidden tax for the uninsured alone (New America Foundation, “A Premium Price: The Hidden Costs All Californians Pay in Our Fragmented Health Care System,” December 2006).
  - Reducing these costs allows employers to redirect those funds into new jobs and capital projects, which create new economic growth for the economy.
- **Generate health care savings.** An economic analysis of the “Illinois Covered” health care reform plan, authored by health care economist Ken Thorpe, found that “each \$1 of public revenues spent on Illinois Covered will generate more than \$2 in new health care savings – mainly through reduction in growth of health insurance premiums paid by Illinois businesses, families, and individuals.” (America’s Agenda Health Care Education Fund, Fact Sheet on Illinois Covered Health Care Reform Plan).
  - The premium savings generated were through three key elements that are contained in California’s health reform proposal: chronic care management, greater reliance on health information technology and a reduction of the uncompensated care cost shift.
- **Reforms will take the pressure off wages and tax revenues.** According to the National Bureau of Economic Research, “...the cost of increasing premiums is borne primarily by workers with employer-provided health insurance in the form of decreased wages.” (National Bureau of Economic Research Working Paper

11160 (Abstract), "The Labor Market Effects of Rising Health Insurance Premiums," Katherine Baicker and Amitabh Chandra, Spring 2005)

- Reversing or mitigating this trend means higher wages and higher consumer expenditures which mean more state revenues from the sales tax and state income tax.

**If the Governor's health care reforms were already in place, our budget would be stronger.**

In sum, if the Act were in place today:

- The federal government would have a significantly increased role in paying for medical costs of our population.
- California's health care system would have \$4 billion in new federal funds.
- General Fund pressure on the Medi-Cal program would be reduced.
- California would expect to see higher productivity, wages and tax revenues.

Taken together, these factors would contribute to an improvement in the California economic outlook and state budget.