MINNESOTA Management & Budget

June 25, 2009

Dear Legislative Advisory Commission Members:

Thank you for meeting with administration officials at the Legislative Advisory Commission (LAC) hearing last week and discussing the proposed unallotment plan announced on June 16, 2009. Attached to this letter, please find specific responses to questions posed to agencies at the hearing. We have met the consultation requirement specified in statute and will proceed with unallotment beginning July 1, 2009.

Commissioner Ludeman has informed me that DHS has submitted for publication in the *State Register* notices of the Medical Assistance rate changes that may occur due to the proposed unallotments. These notices will be published in Volume 33, Issue 52 of the *State Register* because this issue is published on June 29, 2009 and will be the last issue of the *State Register* published before July 1, 2009.

As you know, we have scheduled another LAC hearing for Tuesday, June 30 to provide an opportunity for additional discussion. We have invited State Economist Tom Stinson to provide additional insights on how these actions are likely to impact jobs.

In addition, we would like to inform you of several changes that have been made to the proposed unallotment plan. The following items are being adjusted:

Department of Human Services

Reduce County Mental Health Grants: The amount to be unalloted from the appropriation for adult mental health grants is increased from $8.10 million to $8.77 million for the biennium.

Children and Community Services Grants: The amount to be unalloted from the appropriation for the Children and Community Services block grant is increased from $22.3 million to $22.5 million for FY 2011.

Eliminate Chemical Dependency Grants: The amount to be unalloted from chemical dependency (CD) grants is decreased by $600,000, reflecting removal of the category of methamphetamine abuse treatment and prevention grants from the unallotment list. State funds for two other chemical dependency (CD) grant categories that fund legislatively designated special projects relating to prenatal alcohol and fetal alcohol syndrome intervention remain on the list of unallotments. The revised unallotment amount for this item is $786,000 for the biennium.

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Cap Chemical Dependency Payment Rates: The unallotment reduction of $7.24 million will be achieved by capping CD treatment payment rates at 160% of average (rather than at 150% as originally announced).

Group Residential Housing - 5% Supplemental Service Rate Reduction: The amount to be unalloted through a 5% reduction in the supplementary service rate is decreased from $1.83 million to $1.17 million for the biennium. Funding for Group Residential Housing providers with a supplementary service rate based on the same reimbursement system as other nursing facilities in Minnesota will not be unalloted.

Reduce Personal Care Attendant (PCA) Worker Hours to 275/Month: The amount to be unalloted was calculated incorrectly in my June 16 letter. This unallotment item will still be implemented eliminating payment for PCA worker hours in excess of 275 per month, but the amount of the unallotment reduction is decreased from $7.54 million to $2.15 million for the biennium.

Eliminate Carryforward of American Indian Child Welfare (AICW) grant: The amount to be unalloted is adjusted to $600,000 in FY 2010. The restored $200,000 will be available to the White Earth Band of Ojibwe.

Suspend Growth Factor in Developmental Disability (DD) Waiver Allocations: This new proposed unallotment which would reduce $5.97 million for the biennium from the DD waiver allocations to counties. This unallotment will be implemented by suspending, for an 18-month period from January 2010 to June 2011, the 1% growth factor in DD waiver county allocations.

Restructure State Operated Services: The projected improvement in collections associated with this item was not included in the fiscal estimates provided on June 16. The restructuring is expected to generate non-dedicated revenues to the general fund of $3.55 million in FY 2010 and $5.87 million in FY 2011.

One additional DHS unallotment item should be clarified – *Delay Continuing Care Grant Payments*. The amount being reduced is accurate, but DHS will manage the reduction within the contractual arrangements for each affected grant. Therefore, the exact implementation method for each grant has not yet been determined.

Department of Revenue

Property Tax Refund/Income Tax Interactions: The reductions in aids to local governments are assumed to result in property tax increases which increase state property tax refund payments and reduce state corporate and individual income tax receipts due to larger deductions. This cost was not included in the fiscal estimates provided on June 16. The estimated impact is $5.7 million for FY 2011.

As was noted last week, we are currently preparing allotment reduction plans for the remaining balance needed. Most state agency operating budgets will be reduced 2.25 percent for the biennium. Additional information on specific agencies and amounts will be transmitted when these plans are complete.

Sincerely,

Tom J Hanson

Tom Hanson
Commissioner, Minnesota Management & Budget

Appendix A: Department of Human Services

Legislators asked for information on the extent to which unallotments in the Human Services area affect federal funds. To the extent that an unallotment item is in the Medical Assistance (MA) program, reducing state funding through unallotment means that the state foregoes the related federal share of MA expenditures. The following table lists the proposed unallotment items for which a federal share of MA expenditures is foregone.

DHS Unallotment Items ($ in Millions)	FY 2010-11 Reduction	Federal Share
Suspend funding for ICF/ MR Occupancy Rate Adjustments	$(0.45)	$(0.63)
Cap Chemical Dependency payment rates	(7.24)	(0.72)
Limit funding for ICF/ MR Variable Rate Adjustments	(0.88)	(1.43)
Reduce PCA Worker Hours to 275/month	(2.15)	(3.00)
Suspend Nursing Facility rebasing	(5.94)	(8.79)
Suspend growth factor in DD waiver allocations for 18 months	(5.97)	(8.04)
Additional 1.5% reduction - non-primary care ("basic care")	(4.88)	(6.19)
Additional 1.5% reduction – specialists	(4.35)	(5.42)
Elim. MA critical access dental payments	(6.20)	(8.20)
Elim. GF funding for outreach incentives	(3.40)	(4.31)
Aligning asset limits	(6.10)	(6.10)
Reduce MnDHO rates	(2.00)	(2.52)
Increase managed care withhold to 9.5%	(12.20)	(16.69)
Total amount of MA federal share foregone		$(72.05)

In comparison, the Omnibus Health and Human Services budget bill enacted last month made a series of reductions in the state's MA program. Those provisions result in a total loss of $365 million in foregone federal MA share revenue to the state in the FY2010-11 biennium.

Appendix B: Minnesota Department of Education

SCHOOL DISTRICT PROPERTY TAX LEVY RECOGNITION

Statutes Relating to Levy Recognition: Response to House Fiscal Analyst Inquiry

School districts levy property taxes on a calendar year basis. The first half of property tax payments for the calendar year are received in May or June, and the second half are received in October or November.

Minn. Stat. § 123B.75 outlines procedures for school district revenue recognition, including property tax levy recognition:

- Subdivision 5 requires school districts to recognize certain portions of the calendar year levy in June of each year, including:
    - An amount equal to 31% of the operating referendum levy certified by the school district in 2000; and
    - the entire amount of the following levies:
      integration levy for Minneapolis, St Paul and Duluth;
      certain health insurance , health benefits and retirement levies;
      unemployment insurance levies;
      career & technical education levy; and
      levy adjustments for law changes.
- Subdivision 5 does not specify the fiscal year or years to which other portions of the levy are applicable.
- Subdivision 9 states that the Commissioner of Education shall specify the fiscal year or years to which revenue from aid and levy is applicable if Minnesota Statutes do not so specify.

Minn. Stat. § 123B.77 requires each school district to adopt the uniform financial accounting and reporting standards (UFARS) provided for in guidance adopted by the Department of Education. The Department maintains a UFARS manual outlining these standards, including standards related to levy recognition.

Change in Levy Recognition

Under the authority provided in Minn. Stat. § 123B.75, Subdivision 9, and Minn. Stat. § 123B.77, the Commissioner of Education has proposed a change in school district levy recognition beginning with taxes payable in calendar year 2011. Under the proposed change, the entire amount of each school district's May, June and July tax settlement revenue in the operating funds not already recognized as revenue in June under Minn. Stat. § 123B.75, Subdivision 5, would be recognized as revenue in June of each year, beginning in June of 2011.

State Aid Adjustment for Change in School Levy Recognition

Without an adjustment to state aid, the change in school levy recognition outlined above would create a one-time windfall of approximately $600 million to school districts in fiscal year 2011. Under this proposal, the Commissioner of Minnesota Management & Budget would use his authority under Minn. Stat. § 16A.152, subd. 4, to reduce the allotment for general education aid for FY 2011 by an offsetting amount to eliminate this windfall. The reduction would be allocated among districts in proportion to the increase in Fiscal Year 2011 revenue recognized by each district as a result of the change in levy recognition proposed by the Commissioner of Education.

For Fiscal Year 2012 and later, the change in levy recognition proposed by the Commissioner of Education would continue, but there would be no offsetting adjustment to education aids.

Responses to Questions from Senate Staff Regarding Levy Recognition

Instead of recognizing certain portions of the levy in June under Minn. Stat. § 123B.75, Subd. 5, and the balance on July 1, the entire amount of each school district's May, June and July tax settlement revenue in the operating funds would be recognized as revenue in June of each year, beginning in June of 2011. Only those UFARS accounts dealing with levy recognition will be affected.

The Department makes numerous changes in UFARS each year under the authority provided under Minn. Stat. § 123B.77. As a general rule, these changes are announced to school districts and charter schools through the School Business Bulletin and the Commissioner's weekly e-mails to school superintendents. In 2003, the Department established an Advisory Committee on Financial Management, Accounting, and Reporting, which meets regularly and advises the Department on matters of school accounting, reporting, budgeting and financial management. The committee charter, membership, and minutes are posted to the MDE web site at http://education.state.mn.us/MDE/Accountability_Programs/Program_Finance/General_Information/Advisory_Committee_on_Financial_Management/index.html

The group includes school district business managers, superintendents, independent auditors and representation from the State Auditor's office. The advisory committee is advisory; its advice is not binding on the Commissioner and the Department has sought the advice of the committee on many issues, but not every issue relating to UFARS.

In general, UFARS accounting and reporting is guided by GAAP, GASB, and other accounting guidelines, except where implementation of state law brings conflict.

The UFARS statute was enacted in 1976, and the practice since that time has been for the entire amount of the calendar year levy to be recognized in July, except as provided for in legislation calling for portions of the levy to be recognized in June. Prior to the implementation of UFARS, districts recognized revenues in variant manners.

Minn. Stat. § 123B.75, Subd. 5 specifies that school districts must recognize certain portions of levy receipts as revenue in June, including 31% of the referendum levy certified in calendar year 2000. This does not preclude the Commissioner from specifying that other portions of the levy, including other portions of the operating referendum levy, shall be recognized as revenue in June.

Appendix C: Department of Revenue

Below is the information requested from the Department of Revenue.

1. **How much has Minneapolis LGA been reduced since 2003?** Prior to the 2003 reduction, Minneapolis was estimated to receive $117.6 million annually in LGA. Under current law (prior to proposed unallotment), Minneapolis is estimated to receive $90 million in LGA. This represents a 24% reduction in LGA since 2003. If the proposed LGA unallotment is effectuated, the Minneapolis 2010 LGA amount will be reduced to $68.7 million. This would represent a 42% reduction in Minneapolis LGA since 2003.

2. **The Commission requested additional information regarding the administration of the proposed unallotment of the Renters Property Tax Refund:** The Renters Property Tax Refund program reduction is estimated to save $50.8 million in general fund expenditures for FY2011. The portion of the rent used to calculate the 2009 refund would be reduced from 19% of rent paid to 15% to more accurately reflect actual taxes paid. The proposed unallotment does not impact refund claims that will be paid beginning in August 2009 (for rent paid in 2008). The unallotment proposal only impacts refunds that will be paid beginning after August 2010 (for rent paid in 2009).

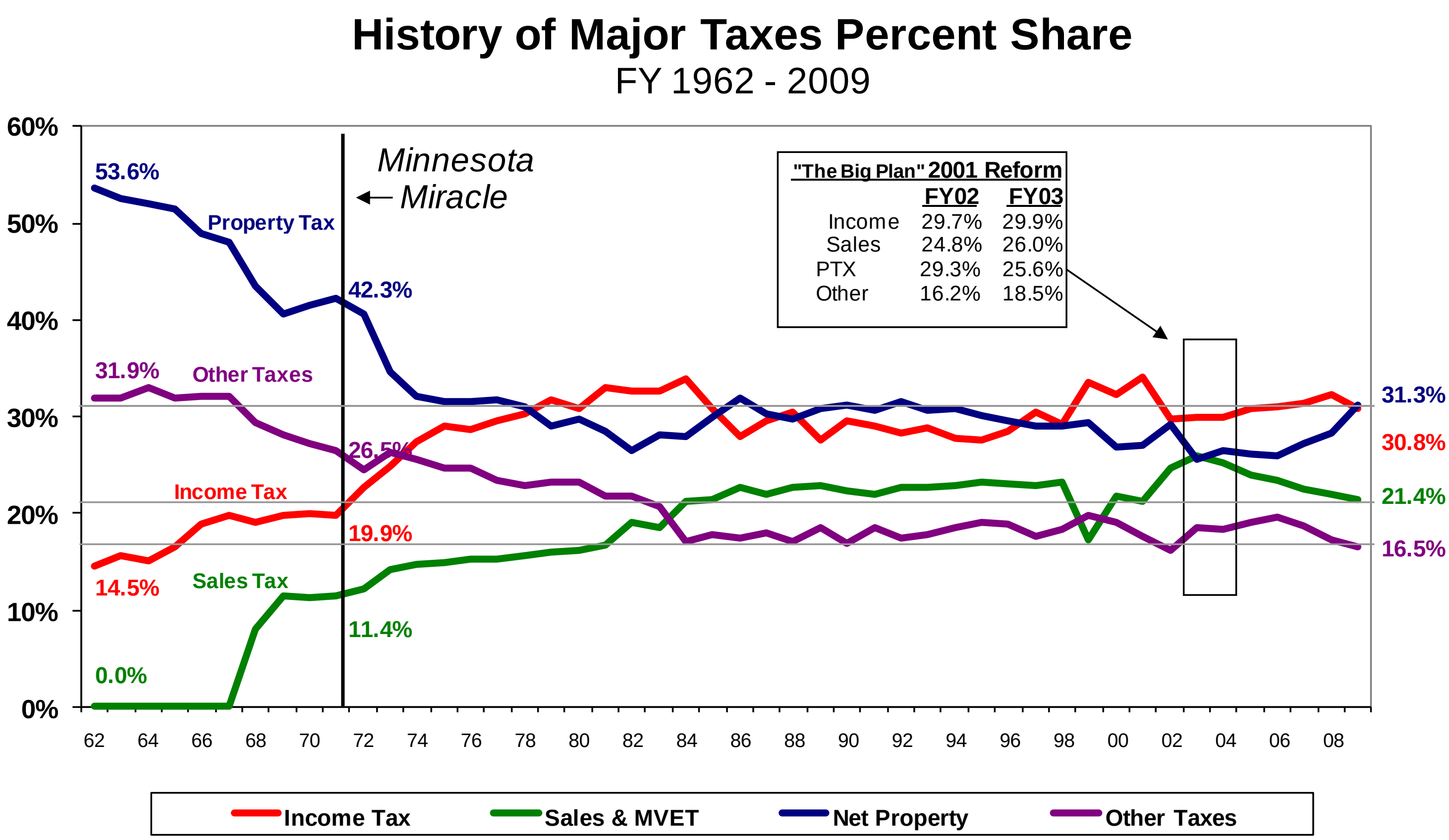
The Renters Property Tax Refund program is a state-paid refund to renters whose rent and property taxes are high relative to their income. Under current law, rent constituting property taxes is assumed to be 19% of rent paid. The property tax reforms enacted in 2001 resulted in a 24% reduction in apartment property taxes. The percentage constituting property taxes was not adjusted to reflect these systemic property tax reductions. The most current census data indicates that the actual percent of rent that constitutes property taxes is 14%. Consequently, the proposed unallotment will result in the Renters' Property Tax Refund more accurately reflecting the percentage of rent attributable to property taxes.

The Department of Revenue will send landlords in October of 2009 the certificate of rent paid (CRP) forms and instructions for refund claims for rent paid in 2009. These instructions will reflect the reductions from 19% to 15% for the CRP forms that landlords are required to provide to each renter by January 31, 2010. The property tax refund instruction booklet and forms for 2009 (M1PR) will also be updated to reflect the unallotment changes.

There are currently 304,900 renter property tax refund filers. The average refund is $570. The average refund would be reduced by $129 to $441 for refund claims beginning August 2010. 84,700 renter property tax refund filers are seniors or disabled. The average refund for seniors or disabled is currently $635 and under the proposed unallotment this would be reduced to $491 ($144 reduction).

Even with the above mentioned one year proposed unallotment, Minnesota will continue to have the most generous Renters' Property Tax Refund program in the country. A comparison of Minnesota's program to Iowa, North Dakota, South Dakota and Wisconsin is illustrative:

- Minnesota has the highest income ceiling $52,299 compared to Wisconsin's at $25,000, Iowa and North Dakota at $20,000 and South Dakota at $13,000.
- Minnesota's maximum refund for 2009 is $1,490. The maximum refund for Wisconsin and North Dakota is $1,160 and $240 respectively.



Source: Minnesota Department of Revenue and
Price of Government, February 2009