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Health, Education, and
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June 10, 1996

The Honorable Thomas J. Bliley, Jr.
Chairman, Committee on Commerce
House of Representatives

Dear Mr. Chairman:

Medicaid is the largest federal program providing financial assistance to state governments. States received over $80 billion in fiscal year 1995, and the Congressional Budget Office estimates that they will receive $898.4 billion in federal funds between fiscal year 1996 and fiscal year 2002. The Congress is now considering alternatives that would slow the growth in federal Medicaid spending by giving states more flexibility in the administration of the program and by changing the mechanism for allocating federal assistance among states.

This letter responds to your request for an explanation of the relationship between federal funding and state funding needs under the current open-ended entitlement program and how it would change under H.R. 3507, being considered by your Committee. Under the open-ended entitlement the level of assistance provided to the poor varies from state to state depending on how many people are made eligible under state law and how extensive are the services the state provides. In contrast, under H.R. 3507 the distribution of federal assistance to states would be much less related to state spending patterns and become more closely related to measures of state funding needs, such as the number of poor, elderly, and disabled.

FEDERAL FUNDING NOT BASED ON STATE FUNDING NEEDS

The amount of federal aid that a state receives under Medicaid is not closely linked to measures of its potential funding needs. In many instances, states with larger numbers of poor and disabled individuals receive less federal assistance than states with both larger numbers of those in need and weaker tax bases. New York, for example, has fewer poor people than California yet it received $12.5 billion in federal assistance in fiscal year 1995 while California, with more people in need, received less than $9.2 billion that year. When expressed in terms of funding per person in poverty, New York received 60 percent more than California; more than $4,350 per person compared with less than $1,725 per person in California.

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Because the federal government matches whatever states spend on eligible services, states with the most generous eligibility requirements, that offer more extensive services, and that provide higher provider reimbursement rates receive more federal funding. Consequently, states with greater numbers of needy individuals can receive less federal aid because of their more restrictive eligibility rules and because they provide fewer services.

MOST FEDERAL PROGRAMS PROVIDE FUNDING BASED ON STATE NEEDS

The current linkage between state needs and the amount of federal assistance a state receives under Medicaid does not reflect how most federal grant programs are designed. Aside from the major entitlement programs (Medicaid, Aid to Families With Dependent Children, and Foster Care), most other federal grant programs distribute federal assistance on the basis of need measures (for example, high risk population groups such as the poor, children, or the elderly) rather than on the basis of state spending patterns.

A recent example of needs-based targeting is the Ryan White Comprehensive AIDS Resources Emergency (CARE) Act reauthorized by Congress earlier this year. The Senate Labor and Human Resources Committee and your Committee revised the formula used to distribute CARE Act funds to states and metropolitan areas to improve the needs-based targeting of that program. The new system would strengthen the relationship between federal funding and people in need by more closely linking the amount of federal aid a state or metropolitan area receives with the number of people with acquired immunodeficiency syndrome (AIDS).

Other examples of need-based targeting include the Chapter 1 program for the Educationally Disadvantaged and the Maternal and Child Health program, which target federal funding based on the number of children in poverty. Similarly, the Airport Improvement program provides funding based on the number of passengers using an airport and the Older Americans Act allocates federal funding based on the number of elderly. Based on work currently underway, it appears that over 90 percent of federal formula grant programs target funding based on measures of state need.

THE MEDICAID RESTRUCTURING PLAN WOULD GRADUALLY SHIFT FEDERAL FUNDING TO A NEEDS-BASED SYSTEM

A restructured Medicaid program under provisions in H.R. 3507 would gradually realign federal funding over a number of years so that it will be more closely related to state needs rather than state spending patterns. This would be accomplished by linking federal allocations to the number of people in poverty and giving greater weight to the number of elderly and disabled for whom care is more expensive. Additional adjustments would be made to account for cross-state

differences in the cost of health care, and low-income states' matching rates would continue to be higher.

Shifting to a needs-based funding system will be accomplished by allowing funding for states like California, whose federal funding is low in relation to the number of people in need, to grow at above average rates. Conversely, funding for states like New York would grow at slower rates until funding for all states is brought into line with state needs.

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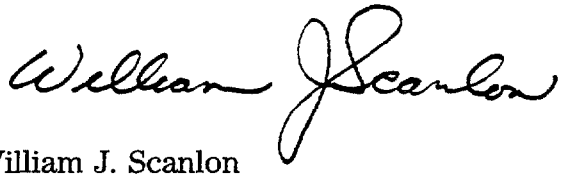
If you have any questions regarding this letter or if we can be of further assistance, please call Jerry Fastrup, Assistant Director, at (202) 512-7211 or me at (202) 512-4561.

Sincerely yours,



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