MINNESOTA
Management
& Budget

June 16, 2009

Governor Tim Pawlenty
Office of the Governor
130 State Capitol
75 Rev. Dr. Martin Luther King, Jr. Blvd.
St. Paul, MN 55155

Dear Governor Pawlenty:

The purpose of this letter is to inform you of reductions necessary to balance the state's general fund budget for the upcoming biennium. Based on the recently completed general fund statement, the enacted budget spends a projected $2.676 billion more than available for fiscal years 2010-11. No budget reserve remains to help mitigate this shortfall.

I have prepared a list of proposed unallotments and other administrative actions to balance the 2010-11 budget. I have also called a Legislative Advisory Commission meeting for later this week and, with your concurrence, will present these items for discussion. This list of reductions includes ideas proposed by your cabinet and from stakeholder groups and citizens.

Reductions identified demonstrate a targeted approached to resolving the deficit. In many instances, the proposed reductions are less than the reductions in your FY 2010-11 budget recommendations.

Major elements of the proposed plan are presented below. A detailed report outlining each proposed reduction is provided as an attachment to this letter.

- **$300 million** **Reduction of local aids and credits**
- **$67 million** **Reduction of refunds and other payments**
- **$236 million** **Reduction in human services spending**
- **$100 million** **Reduction in higher education appropriations**
- **$33 million** **Reduction in most state agency operating budgets**
- **$1.77 billion** **K-12 payment deferrals and adjustments**
- **$169 million** **Administrative actions**

***<u>Local Aids and Credits - $300 million</u>***

State aids and credits to cities and counties are proposed to be reduced by $300 million. The reductions would be split so that 1/3 is reduced in FY 2010 and the balance in FY 2011.

County aid would be reduced by $33 million in FY 2010 and $67 million in FY 2011. This amounts to a reduction of no more than 1.19 percent of each county's annual aid plus levy for 2009, and a reduction of no more than 2.41 percent for 2010. The five counties with a population of approximately 5,000 or less are exempted from these reductions.

City and township aid is reduced by $67 million in FY 2010 and $133 million in FY 2011. No city's reduction exceeds 3.31 percent of annual aid plus levy for 2009, and 7.64 percent of annual aid plus levy for 2010. No township's reduction exceeds 1.74 percent of annual aid plus levy for 2009, and 3.66 percent of annual aid plus levy for 2010.

Small counties, cities, and townships have less flexibility and fewer options to deal with budget challenges. Cities and townships with an adjusted net tax capacity per capita less than the statewide average and which have a population of less than 1,000 are exempted from these reductions. In total, 53 percent of Minnesota cities (454 of 854) and 35 percent of Minnesota townships (629 of 1,802) will not experience a reduction under this plan.

Unlike other parts of the budget, local aids and credits were not reduced as part of the recently enacted 2010-11 budget. Reductions made through unallotment are the total change in local aids and credits for the upcoming biennium.

***Other Refunds and Payments - $67 million***

Refunds for political contributions made between July 1, 2009 and June 30, 2011 are proposed to be eliminated, resulting in a savings of $10.4 million for the biennium. This would not impact individuals electing contributions to the State Election Campaign Fund as part of their state income tax returns, nor those contributions.

The renters' refund would also be reduced to more accurately reflect actual property taxes paid, saving $51 million. In addition, sustainable forest investment payments would be capped at $100,000 per enrollee, impacting only 4 of the 1,100 program enrollees for one year ($5.5 million in savings).

***Department of Human Services - $236 million***

DHS expenditures constitute roughly 28 percent of the state general fund and such expenditures are largely responsible for dramatically increasing state government costs. In an effort to limit direct impacts to individuals as well as avoid further reductions to hospitals and nursing facilities, numerous targeted reductions to grants, provider payments, authorized services, and operations are proposed.

Key items include:

- Ending General Assistance Medical Care (GAMC) coverage on March 1, 2010. This ends GAMC coverage one and one-half months sooner than would have occurred as a result of the line-item veto of GAMC funding for FY 2011.

- Reducing grants to counties for mental health services, chemical dependency treatment, housing and basic needs in emergency situations, child support administrative costs, and other flexible social service purposes. The availability of new federal stimulus funding in many of these areas will mitigate the impact of the reductions.

- Reducing rates an additional 1.5 percent for specialists and certain other non-primary care services. Inpatient hospital services are exempt from these additional rate cuts. Primary care, mental health, dental, and other critical services will be also be excluded, just as they were excluded from the ratable reductions passed during session. Medical education and disproportionate share quarterly payments to hospitals are also exempt from these reductions.

- Lowering the maximum number of hours one Personal Care Attendant (PCA) can work from 310 to 275 per month. Even with this cap, Minnesota still has a generous PCA program when compared to other states.

- Suspending nursing facility rebasing for FY 2010. This does not reduce current rates paid to nursing facilities, but suspends an increase for FY 2010. The 2009 legislature suspended rebasing from FY 2011 to FY 2013.

- Redesigning the State Operated Services (SOS) system towards specialty health care. The Department of Human Services will better meet the needs of clients through lower intensity, lower cost services and savings will be realized as a result. The Minnesota Sex Offender Program will not be impacted by these changes.

- Refinancing transitional MinnesotaCare. Individuals eligible for transitional MinnesotaCare will continue to receive coverage, but all six months will be paid out of the Health Care Access Fund, instead of the General Fund, until enrollment in GAMC ceases.

***Higher Education - $100 million***

The general fund operating budgets for the University of Minnesota and the Minnesota State Colleges and Universities System (MnSCU) are each reduced $50 million for a total savings of $100 million. All reductions are proposed for the second year of the biennium. These reductions leave sufficient state spending in place to ensure compliance with federal maintenance of effort requirements created by ARRA.

These reductions will present a challenge for our higher education institutions in FY 2011, but a manageable one. The unallotment represents an approximately 3.6 percent change in total general resources (state appropriations plus tuition and fees) and an even lower percentage of total revenues for these systems.

***Agency Operating Budgets - $33 million***

A reduction to most state agency operating budgets of approximately 2.25 percent to achieve $33 million for the biennium is proposed. This reduction is in addition to the approximately 5% reduction many, but not all, state agencies experienced as part of the recently enacted FY 2010-11 budget. Specific reductions will be identified over the next two weeks. Areas exempted from these actions include public safety, military and veterans affairs, corrections, State Operated Services and the Minnesota Sex Offender Program within the Department of Human Services.

The Governor's office will be included in these reductions. Other constitutional offices, the legislature, and the courts will maintain their current level of funding.

***K-12 Payment Deferrals and Adjustments - $1.77 billion***

Beginning in FY 2010, aid payments to schools will be temporarily reduced, generating $1.17 billion in savings. The reduced portion of those payments will be deferred such that school districts will receive 73 percent of their first year entitlement that year and the remaining 27 percent in the second year.

This deferral is similar to the school aid payment deferral proposal in your budget and the proposal passed by the legislature.

In addition, under M.S. 123B.75, the Commissioner of Education will require school districts to recognize a portion of their levy revenues when they are received. The savings resulting from such recognition of school district property tax receipts would be implemented in FY 2011, generating state general fund savings of approximately $600 million. This will result in a one-time savings in state aid similar to the property tax recognition shift you proposed and the legislature passed.

In total, these changes do not reduce aid entitlements to schools.

***Other Administrative Actions - $169 million***

Two administrative actions are also recommended. Modifying our income tax reciprocity agreement with Wisconsin will generate $106 million in additional revenue for the biennium. Currently, Wisconsin takes on average 17 months to reimburse Minnesota for tax losses. You recently sent a letter to Governor Doyle requesting Wisconsin pay tax amounts owed to Minnesota in the fiscal year in which the tax loss was incurred.

In addition, temporarily delaying FY 2011 capital equipment sales tax refunds for three months will generate $63 million. All refunds would be released immediately in FY 2012.

Sincerely,

Tom J. Hanson

Tom J. Hanson
Commissioner

cc: Legislative Advisory Commission