

STATE  
FINANCE  
TASK FORCE  
REPORT TO  
THE 78<sup>TH</sup>  
LEGISLATURE:

A ROADMAP  
TO RESPONSIBLE  
REFORM



Texas Conservative Coalition  
Research Institute



A Principled  
Approach to  
Government

January 14, 2003

Dear Colleagues,

Most states have faced budgetary crises due to a slowing national economy. Initial reports and review of the state's fiscal nature show that Texas will be no exception. The Texas Conservative Coalition Research Institute State Finance Task Force's Report to the 78<sup>th</sup> Legislature is the result of more than a year's work evaluating the state budget and how Texas spends taxpayer dollars. The mission of the task force, beginning in November 2001, was to prevent tax increases by focusing policy makers on innovative reforms that will allow the state to deliver essential services while improving the impact of those services. Our task, in other words, was to find a way for the state to do more with less.

We believe that we have met our objectives and stand resolute in our commitment to restore fiscal responsibility and a common sense approach to state spending. This report provides a framework for members by reviewing state spending priorities, laying out possible structural changes in state appropriations and management, and pointing to other areas for possible cost savings. It is our intent that this report lay out conservative principles that will guide legislators through the upcoming legislative session and provide a roadmap for responsible reform.

We would like to extend our thanks to those who have contributed to this report as members of the task force. We look forward to working together in the upcoming session to address these issues and in support of our shared vision for innovative and responsible reforms that will improve the way the state does business and serves the people of Texas.

Sincerely,

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Texas Conservative Coalition Research Institute  
State Finance Task Force  
Report to the 78<sup>th</sup> Legislature:

# **A Roadmap to Responsible Reform**

**January 2003**

The contents of this document do not represent an endorsement from any individual member of the Texas Conservative Coalition or the Texas Conservative Coalition Research Institute State Finance Task Force. There may be some policy recommendations that individual members may be unable to support. We recognize and respect their position and greatly appreciate the work of everyone involved with the task force.

# Acknowledgements

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We would like to acknowledge the efforts of all the participants in the Texas Conservative Coalition Research Institute's State Finance Task Force. This document represents countless hours of research and investigation on the part of the members and their legislative staffs. In particular we would like to thank Senator Florence Shapiro, Representative Carl Isett, Representative Arlene Wohlgemuth, and their staffs for leading this effort. In addition, we would like to acknowledge the contributions of John Colyandro, Mary Katherine Stout, and Michael Price for coordinating the Task Force and the final publication of this report.

# Executive Summary of Recommendations

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## **Structural Changes**

### Exceptional Items

End practice of funding exceptional items.

### Contingency Appropriations

Eliminate contingency appropriations.

### Constitutional Spending Limits

Amend the Texas Constitution to limit the growth of the state budget to the rate of growth in Texas' personal income.

### Super-Majority

Amend the Constitution to require a 2/3 super-majority for all tax or fee increases.

### Line-Item Reduction Veto

Amend the Constitution to allow the Governor use of the line-item reduction veto.

### Strategic Planning

De-link the strategic planning process from the budgeting process.

Require agencies to submit specific sub-strategies as a part of their strategic plan presented to the Legislature.

Require interim committees to study certain aspects of agency budgets and strategic plans for agencies under the committee's oversight.

### Balanced Scorecard

Implement the balanced scorecard management approach in the ten largest state agencies, incorporating the information into the strategic planning cycle.

### Pay for Performance

Use merit raises and merit bonuses to reward employees on performance rather than emphasizing length of service.

Appoint an interim committee to review the state classification system.

### Activity-Based Costing

Implement Activity-Based Costing and Activity-Based Management methods in the ten largest state agencies.

### Prevailing Wage

Repeal the prevailing wage law.

### Legislature

Review services under the Legislature to consolidate duplicative services and outsource other services to the private sector.

### State Auditors Office

Direct the State Auditors Office to re-focus its efforts toward financial audits only, and remove statutes directing the SAO to engage in other activities that may compromise the agency's ability to perform independent financial audits. Transfer the SAO to the executive branch.

### Appointments

Amend the Constitution to allow the Governor to remove appointees of that Governor at any time during the term of appointment.

## **ARTICLE I, General Government**

### Information Management

Integrate data centers.

Consolidate small agency IT functions.

Establish a seat management pilot program and a Seat Management Office within DIR to coordinate related planning efforts and study the effectiveness of the program.

Consolidate state agency area wide networks under DIR management.

Direct DIR to aggressively enforce and encourage state agencies to use Texas Online.

Abolish the Texas Information Technology Academy.

### Employees Retirement System

Change the existing ERS plan by introducing additional cost sharing for ERS members.

- Reduce dependent coverage for certain employees.
- Index retiree premium share to years of state service.

- Eliminate state contribution for individuals not retiring directly from active employment.
- Increase new hire wait time.
- Increase calendar deductible.
- Increase primary care and specialist office visits co-payments.
- Increase annual out-of-pocket maximum to \$1000.
- Increase in-patient and out-patient co-pays.
- Reduce coverage for part-time employees from full to partial coverage.

Change the request for proposals (RFP) process for ERS to allow for lower cost options.

#### Texas Building and Procurement Commission

Employees at state agencies who have job responsibilities that are performed by TBPC should be terminated to eliminate duplication.

#### Texas Commission on the Arts

Transfer the Texas Commission on the Arts to the Office of the Governor and eliminate current FTEs.

#### Texas Historical Commission

Eliminate the Texas Historic Courthouse Preservation Program.

#### Councils of Governments

Eliminate funding for regional grant assistance through the Office of the Governor.

#### State-Federal Relations

Remodel the Office of State-Federal Relations

## **ARTICLE II, Health and Human Services**

#### Medicaid Funding

Request block grant of Medicaid funds.

#### Medicaid Program Integrity

Amend state law to provide that Medicaid eligibility shall be granted to eligible children for a period of three months upon initial enrollment.

Direct the Health and Human Services Commission to apply for a Section 1115 waiver that would allow families to choose between Medicaid and CHIP coverage.

The Department of Human Services should verify income and assets eligibility by using certain information available to third parties.

### Medicaid Benefits: Pharmaceuticals and Services

Set a maximum 34-day supply and 4-brand maximum on prescriptions for all Medicaid recipients with exceptions only by doctor authorization.

Pursue additional cost savings through Medicaid co-payments for emergency room visits and prescription drugs.

Reduce the coverage of pregnant women and infants in Medicaid to the federally mandated levels.

Institute a system of co-payments for optional Medicaid services.

### CHIP Cost Sharing

Increase CHIP premium sharing and co-payments for emergency rooms and generic and brand name medications.

### Pharmacy Benefits Management

The state should contract with a Pharmacy Benefits Manager to administer the drug benefit in the Texas Medicaid program.

### Disease Management

Introduce a disease management program in the Texas Medicaid program.

### Estate Recovery

Develop an estate recovery system in the Texas Medicaid program.

### State Kids Insurance Program (SKIP)

Eliminate the State Kids Insurance Program and return funds to General Revenue.

### HHSC Riders

Repeal certain riders from the 77<sup>th</sup> Legislative Session.

### Nursing Home Liability

Enact meaningful tort reforms by placing a cap on exemplary damages and remove DHS from nursing home supervision in favor of private accreditation.

### Medical Malpractice

Texas should enact legislation similar to California's Medical Injury Compensation Reform Act (MICRA) and take certain additional steps to address the medical malpractice problems.

- Placing a hard cap on non-economic damages.
- Collateral source reform.
- Limiting contingency fees.



- Limiting when a minor can bring suit.
- Periodic payments for future damages.
- Good Samaritan Law.
- Judicial discretion.
- Arbitration/Special Courts.
- Bad Faith Cause of Action.
- Screening panels.

#### Temporary Assistance for Needy Families

Implement the “Full Engagement” work model so that all families must participate in work and other constructive activities leading to self-sufficiency. Amend state law to remove all exemptions from work requirements and workforce orientation, and allow Choices case managers to screen participants for good cause.

Establish a pay-for-performance program for TANF recipients, or implement full grant denial for individuals who are not in compliance.

#### Interagency Council on Early Childhood Intervention

Transfer the Interagency Council on Early Childhood Intervention into the Texas Department of Health and reduce the number of FTEs that manage the program.

#### Texas Cancer Council

Abolish the Texas Cancer Council.

#### Texas Health Care Information Council

Abolish the Texas Health Care Information Council.

### **ARTICLE III, Education**

#### Adequacy

Study the cost of a thorough and efficient education.

#### Flexibility and Local Control

Relieve school districts from state mandates and grant more local control.

- Let schools focus on academics.
- Help schools improve personnel resources.
- Grant relief on restrictions and paperwork.
- Give incentives to create more choice.

#### Total Returns

Monitor the performance of other total return funds to project long-term distributions and fund growth possibilities.

### Regional Education Service Centers

Abolish Regional Education Service Centers and redistribute any necessary functions to related agencies, or reorganize the Regional Education Service Centers to provide services and programs to targeted school districts.

### Teacher Retirement System

Increase prescription drug co-payments in TRS-Care.

Amend provisions of TRS-Active Care to give districts greater flexibility and ensure that the program is truly a health benefit.

- Change the delivery of services to allow regional risk pools and competition, rather than a sole provider, and introduce patient choice through the option of a defined contribution.
- Adopt a defined contribution bill devoting funds solely to health care.
- Merge ERS with TRS and separate functions.
- Offer health coverage only to full-time employees, eliminating the provision of health insurance for part-time employees.
- Limit the ability of large districts to enter the program based upon the financial effect their entry would have on the plan.
- Rescind mandated participation and extend limited ability to districts to opt out of TRS Active Care if school districts can offer evidence that they are providing their employees with a state comparable plan.
- Provide financial relief for district already contributing the full amount to health coverage prior to implementation of the state plan.

### Higher Education Funding

Prevent reductions in the Higher Education Fund before the \$2 billion corpus is built.

Repeal HB 1839 from the 77<sup>th</sup> Legislative Session, which created the Texas Excellence Fund and the University Research Fund.

### Capital Equity and Excellence

Enforce the rider eliminating Capital Equity and Excellence Hold Harmless funds after the 2002-2003 biennium.

### Special Items Matching

Create a matching funds ratio for special item matching.

### Institutional Enhancement

Institutional enhancement should either be eliminated or cut across the board, or cut from schools with special item funding.

### Teaching Experience Supplement

Eliminate the teaching experience supplement.

### Tuition Waivers

Restore non-resident tuition rates for all non-residents.

### University Tuition

Remove the cap on tuition at four-year, public universities.

Eliminate the Tuition Equalization Grant Program.

### Developmental Education and the TASP Test

Abolish the Texas Academic Skills Program.

Expend all developmental education funds at the community college level.

### Community College Funding

Clarify that public community college tuition and fee revenues be used for a portion of instruction and administration costs, and amend statutes or add language to the Appropriations Act accordingly.

Direct the Texas Higher Education Coordinating Board to develop a contact hour-based allocation that does not depend on a biennial cost study.

## **ARTICLE V, Public Safety and Criminal Justice**

### Adjutant General's Department and Texas Military Facilities Commission

Merge the Adjutant General's Department and the Texas Military Facilities Commission.

## **ARTICLE VI, Natural Resources**

### Texas Commission on Environmental Quality, Air Programs

Create a Title V fund specifically for Air Emissions Fees used to run Title V programs.

### Lower Colorado River Authority

Privatize the Lower Colorado River Authority.

### State and Local Parks

Withhold appropriations for grant assistance to local governments for local parks, using half of the savings to fully fund state parks.

### Adopt-A-Beach

Turn the adopt-a-beach program over to local entities.

### Oil Spill Response

Consolidate the oil spill response activities within one agency.

### Energy Conservation and Alternative Fuels

Abolish the State Energy Conservation Office and transfer oversight of oil overcharge settlement funds to the Texas Building and Procurement Commission.

Abolish the Alternative Fuels Research and Education Division and conduct an interim study on state alternative fuels programs.

### General Land Office

Do not limit the sale or lease of state-owned properties to land that is unused or underutilized; consider additional ways to determine whether state land should be for sale.

## **ARTICLE VII, Economic Development**

### Texas Department of Economic Development

Abolish the Texas Department of Economic Development and redistribute some of its functions to appropriate agencies.

### Texas Aerospace Commission

Abolish the Texas Aerospace Commission.

### Texas Department of Transportation

Eliminate appropriations to the Texas Department of Transportation for tourism.

Abolish the Texas Automobile Theft Prevention Authority.

### Transportation Funding

Undo the past county fee switch. Support county road assistance from the state with a portion of vehicle sales taxes, and return current vehicle registration fees to the state highway fund for infrastructure needs.

Use dedicated highway funds for infrastructure spending only.

## **ARTICLE VIII, Regulatory**

### Texas Mutual Insurance Company

Authorize the sale of the state's worker compensation insurance fund, the Texas Mutual Insurance Company.

Personal Vehicle Usage Policies

Require each agency to review personal vehicle usage policies to determine if renting a car is more cost efficient than providing reimbursements.

Information Resources Manager

Direct the Funeral Services Commission, the Board of Examiners of Psychologists, and the Executive Council of Physical Therapy and Occupational Therapy Examiners to share an Information Resources Manager through interagency contracts.

Cosmetology Commission and Barber Examiners

Consolidate the Cosmetology Commission and the Barber Examiners.

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# OVERVIEW

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In November 2001, the Texas Conservative Coalition Research Institute's State Finance Task Force began to evaluate the budget to identify possible structural changes and opportunities for cost savings. In keeping with its mission, the task force set out to find alternatives to tax increases, focus policy makers on innovative and responsible reforms, and to encourage fiscal responsibility now and in the future. Thus far, the conservative voice has been quiet in the public debate, and the task force intends to introduce a new voice and perspective in the dialogue on the budget. This document will demonstrate that conventional wisdom is wrong on two fronts: that taxes must be raised or that services must be cut, and shortfalls in revenue are the source of the state's financial distress. We argue that the *easiest* answer—to increase taxes—is the wrong answer for Texas. The idea that there is nothing to do but raise taxes rests on the assumption that the state is running at its highest level of efficiency and only engaging in the real necessities of government.

As the general election heated up, virtually every newspaper included some reference to the state budget: a crisis, a shortfall, a mess, more bad news, and a dark budget outlook. Prognosticators came out to tell of how bad things would be and how it reminds them of previous times—only worse. Although everyone recognized the problem, there were no interim committees assigned to deal specifically with the issue. Many publicly resigned themselves to the idea that there was nothing that could be done and there was nothing in the budget to “scrub.”<sup>1</sup> The statement that “scrubbing the budget finds pennies” came to be known as a fact, stifling any real discussion of alternatives in spending.<sup>2</sup> And as the media reported the budget shortfall creeping up from \$5 billion, to \$7 billion, to \$10 billion, to \$12 billion, talk of the need to increase fees and even taxes began in earnest.<sup>3</sup>

State agencies added to the rhetoric by inappropriately responding to questions about possible cuts in agency budgets and programs. The Houston Chronicle reported that in more than 100 letters to the Governor, state agencies outlined the dire consequences if the Governor's request to cut three to five percent of their budgets in the next biennium were enacted. Among the calamitous predictions were 104 more drunk driving deaths, eliminating some state treatments for epilepsy, longer hold times on phone calls reporting child abuse, and declines in the percentage of baccalaureate recipients who are first-generation college students.<sup>4</sup> Threatening the most extreme consequences is unnecessary and irresponsible. All of these types of claims are speculative at best and assume there are not performance enhancements that could take up the slack. To be fair, when the Governor asked agencies to look for potential savings in their current budgets, some agencies responded by identifying some measure of cost savings, but others only complained that there was no money to be saved, that they were already

running efficiently, or that they have cut so far there is no money left to cut. In fact, one state agency responded to the Governor's request by stating that "our small budget has never had any fat in it, and now we're into the bone and being chopped off at the knees."<sup>5</sup>

However, in all of the discussion about "slashing" services and cutting state budgets, the overall state spending pattern is rarely addressed. The final Appropriations Act signed by Governor Bush totaled \$98.2 billion; the first budget signed by Governor Perry totaled \$113.765 billion, the largest budget in state history and nearly a 16% increase over the previous biennium. State spending increased dramatically during the 1990s, but increased the most in two areas: health and human services spending jumped from \$5.6 billion in 1990 to \$20 billion in 2002, and education spending grew from \$10 billion to \$20 billion.<sup>6</sup> While it is often suggested that population increases fuel the need for greater government spending, general revenue spending has far exceeded growth in population, inflation or gross state product. Over the last decade, the Legislature has not had the will to restrain spending when there was extra money available to the state. What is often characterized as a revenue problem is actually a spending problem. The disappearance of more than \$14 billion in total budget surpluses since 1990-91, illustrates the reckless spending that is to blame for the current budget problem. The budget leaders at the end of the 77<sup>th</sup> Legislative session proudly announced that they had spent everything they could get their hands on, highlighting the need for institutional and program changes to protect and be responsible with taxpayer dollars.<sup>7</sup>

In addition, as the flirtation with increasing taxes continues, conservatives must remember there are fundamental differences between the liberal philosophy of more spending and more government and the conservative philosophy of limited government that includes developing alternative means of delivering services. The conservative philosophy recognizes that government is not always the best the answer. That the state of Texas is 49<sup>th</sup> of 50 states in state taxes per capita- meaning that it has one of the lowest state tax burdens- somehow suggests that taxpayers can afford to give more of their hard-earned money to the government. This is shortsighted and wrong and shows a total disregard for the taxpayer's money. In fact, an August report from the Center for Public Policy Priorities outlines the additional \$19 billion Texas' state and local governments would have to spend "just to get Texas up to the U.S. average."<sup>8</sup> Among the places the additional money would go, the most (\$4.6 billion more) would be for Medicaid, cash assistance, and other social welfare programs.<sup>9</sup> However, the answer is not more money. That approach is a failure. The last decade saw a three-fold increase in health and human services spending. Even after all the additional spending and creation of programs to provide health insurance to low-income Texans, Texas' rate of uninsured remains virtually unchanged. Asking for more money does not require any innovation or ensure that a program does what it should do, and in the case of Medicaid, more money has only served to bloat the program, because it has veered

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from its mission of providing a safety-net for the truly poor who cannot afford health care.

Furthermore, the conservative philosophy acknowledges that government cannot solve every problem or meet every need. In evaluating the proper role of government, it is appropriate not only to determine what government activities are and are not working, whether the activities could be better handled by the private sector, or whether government should even be doing them at all. Agencies are engaged in activities and administration of programs that are not in support of their core mission, often escaping scrutiny when it becomes a generally accepted part of an agency's responsibilities. Activities that are either not essential to the core mission of an agency or have failed should be considered for privatization, elimination, or, at the least, restructuring. Lawmakers must acknowledge the shortcomings of government and follow the written philosophy of Texas State Government to restore government to its proper role.

"Government cannot solve every problem or meet every need. State government should do a few things and do them well."

--Vision Texas, Office of the Governor, February 2000

When the TCCRI State Finance Task Force was formed, Senator Florence Shapiro noted that, "Texans are faced each day with determining how they will pay their bills and meet their families' needs. In bad economic times they have to tighten their belts and make hard decisions on how they stretch their dollars to make ends meet. Taxpayers should expect no less from Texas lawmakers." It is unreasonable to expect that state budgeting be any different than family budgeting, and it is irresponsible to suggest that when the state has mismanaged its finances and spent beyond its means, Texas' families must pick up the tab. The state Legislature does not have an unlimited claim to Texans' dollars and it is unconscionable for the budget shortfall to be passed on to Texans through additional taxes. Additionally, agencies should operate under the same budgeting principles as Texas families, and it is outrageous that agencies would reject tightening their own budgets and make extreme statements about what reductions in their budgets would do. The truth is that legislators and agencies avoided the hard decisions when the state was awash in money, and they must now face the same reality that Texas families do, which requires establishing priorities and staying within a budget.

The TCCRI State Finance Task Force presents the recommendations of its study to stand in stark contrast to those who say there are only two solutions, either to cut services or raise taxes. The message here is simple: this is not an exercise in cutting budgets; it is an exercise in saving tax dollars through setting priorities, finding innovative reforms, and restoring the vision for limited government. The recommendations in this report are an evaluation of the role of government, the success

or failure of programs to meet stated goals and objectives, and structural changes that will help restrain the biggest driver in the budget crisis: state spending.

The truth is that across-the-board budget cuts or raising taxes are the two *easiest* ways to fix the state's budget problems. However, this mindset does not require taking responsibility for the current situation, nor does it ensure that the state can be financially stable in the future. It is the task force's hope that this document be used as a resource for members of the 78<sup>th</sup> Legislature to identify spending priorities, highlight possible structural changes, and present options for possible savings that are in keeping with a conservative vision for government. Legislators must be prepared to make the hard choices they were elected to make.

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<sup>1</sup> Gary Susswein, "A budget in crisis: Something has to give," Austin American-Statesman, July 13, 2002.

<sup>2</sup> "Straight talk essential on budget issues," San Antonio Express-News, May 30, 2002.

<sup>3</sup> Center for Public Policy Priorities, "The Texas Revenue Primer," December 2002.

<sup>4</sup> Polly Ross Hughes, "Texas' budget solutions promise to be painful," Houston Chronicle, October 14, 2002.

<sup>5</sup> Texas Pension Review Board, letter to Mike Morrissey and John Keel, 12 March 2002.

<sup>6</sup> Comptroller of Public Accounts, "Texas Expenditure by Function '78-'02.

<sup>7</sup> John Mortiz, "\$113.8 billion budget goes to governor," Fort Worth Star Telegram, May 25, 2001.

<sup>8</sup> Center for Public Policy Priorities, The Texas Budget & Tax Primer, August 2002, p.12.

<sup>9</sup> CPPP, p.12.

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# Spending Priorities



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# SPENDING PRIORITIES

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Conservative lawmakers must now reestablish their commitment to fiscal responsibility and responsible reform by setting spending priorities to serve as a guideline for governing the state of Texas. At the heart of this document is the acknowledgement that government cannot and should not do everything. As former Governor Bush wrote, “Government cannot solve every problem or meet every need. State government should do a few things and do them well.”<sup>1</sup> Government should focus solely on the things that only it can do. A government that expands to meet every “need” not only loses sight of its priorities and becomes unwieldy to manage, but also ensures that it will not do the basics very well. It also guarantees that government will inevitably pass more tax and fee increases to fuel that growth. Restoring the limited role of government as a way to improve government efficiency and to control the growth in government spending is one of the primary goals of conservative lawmakers.

In some respects, the state is in the best position to establish a coherent vision for the basic activities of the state and allow private enterprise or citizen groups to handle the rest. There have been a few very modest attempts at privatization, more for outsourcing, and former Governor Bush’s faith-based initiatives provide a sound basis for citizen empowerment and engagement in the social service areas. Legislators must establish a new blueprint for Texas state government immediately while the budget crisis focuses attention on state spending and agency operations.

**Law Enforcement:** The state must provide for the protection of its citizens and the enforcement of laws. Maintaining order and providing a safe society that allows people to move freely and go about their lives is of the highest importance.

**Public Health:** Public health does not require that the state be responsible for all aspects of individual health care. The state’s role in public health must be an ability to respond and prevent the spread of disease and treat epidemics, disseminate information regarding threats to public health, and provide protection from bio-terrorism. When the state experiences outbreaks of meningitis, as has happened in recent years, the state Department of Health responds by providing information to people regarding symptoms and urging people to seek treatment; this is truly what public health is about. There should be no confusion: public health is not about government being a provider of insurance to everyone. Public health is to protect the general health of people and to provide a safety net.

**Education:** The Texas Constitution clearly charges the Legislature with establishing and making suitable provision “for the support and maintenance of

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an efficient system of public free schools.” Certainly an educated society provides the most opportunities for economic development and prosperity. The issue of education is one that most lawmakers rank among the highest of their priorities, yet should be cautious about. The state should be responsible for ensuring access to a core curriculum. Extra-curricular and programs outside of the core of education- even if edifying in some way- are the responsibility of families and local school districts. The state must provide only the tools for basic classroom instruction, and not a blank check to anything that is nominally considered educational and that might fit under the rubric of education.

Also, the state should repeal existing mandates and reject additional mandates- particularly unfunded ones- on local school districts and local property taxpayers. Mandates keep districts from directing their money, personnel, and resources in a manner that best serves their students and their ability to meet the state accountability standards.

**Infrastructure:** Sound infrastructure is at the heart of providing a catalyst for economic development and job creation, and must be done through coherent planning at the state level. While local governments are responsible for local infrastructure, the state must ensure that goods can be moved throughout the state on a safe and efficient system of transportation, mainly highways. A state’s infrastructure is paramount to providing economic opportunity to the people of the state.

The state should fulfill its basic obligations and then make room for private enterprise, local governments, churches, social service organizations and community groups to go beyond those basic functions and respond to local and special needs. Where private enterprise and individual action can do something, the state should allow it that opportunity. Since government lacks competition and the need to make a profit, it has no inherent forces compelling it to make changes and advancements in its management or in the delivery of services. The state must give up some of the control when activities can be managed by private enterprise. Government is sometimes the least desirable vehicle to deliver a service, and often, the private sector can do it better.

Local needs are best met close to home where there is a greater connection between the people and the government, and where the results of local decisions are most clearly seen. Each level of representative government narrows its constituency at each step from the President of the United States down to city councils and school boards. Just as we believe that Texas is better able to respond to the needs of Texans than the federal government, so too are the cities and counties in Texas better able to respond to the needs of citizens than state government in Austin. Local priorities differ around the state, and one-size fits all approaches do not always address the true needs or priorities of all the people. In terms of public health, different communities may face different challenges, ranging from nutrition to concern over the spread of a particular



illness or disease. In terms of education, communities will place varying levels of importance on the strength of a school district and the provision of extra-curricular activities. Local school districts are held directly accountable by their respective communities and should have the opportunity to respond to those needs first. Not all programs can be locally devolved, but to the extent that the nature of the program allows it, decisions should be made at the local level.

“The best form of government is one that is closest to the people. State government should respect the right and ability of local communities to resolve issues that affect them.”

--Vision Texas,  
Office of the Governor,  
February 2000

Lawmakers should also be wary of traps that induce unnecessary spending. In particular, the federal government often offers states an opportunity to receive federal funding if the state agrees to participate in certain programs. In truth, the federal government creates a plan that states can first buy into with the incentive of getting more federal money, while explicitly restricting the state's ability to use the dollars in administering the program exactly how the state deems best—essentially making state government a branch office of the federal government. Often lawmakers who are intent on expanding the reach of government suggest that this is the way to “freely” fund a program. This is a very short-sighted approach. Lawmakers should not be fooled; the mere existence of dollars for a program does not mean that there is a “need” for the program. These dollars are not free, they come with strings attached, they often expand the government's reach, and they usually require the state to put some portion of money up first in order to get the matching federal dollars. Furthermore, federal dollars are our dollars. They derive from federal income taxes, which are paid by the people of Texas (as well as taxpayers from every state). Over time, the promise of additional federal dollars locks the state into unrealistically expensive programs that hijack state budgets. The merits of the program aside, Medicaid is a very clear example. Lawmakers must reject the temptation to seize the availability of “free” dollars as an excuse to justify the expansion or creation of programs. It is vitally important that conservatives question the very prudence of the federal government taking these dollars to redistribute in the first place, and should make the fact known that these dollars should never have to return to Texas via the federal government.

The state's spending priorities should focus only on what the government, and the government alone, can and must do. Agencies must justify their requests based upon the success of a program. Inefficient and ineffective programs must be eliminated or restructured. Areas of the government that are better handled by the private sector or at the local level should be turned over to those entities.

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Additionally, the state must have a commitment to truth in budgeting, making the process as transparent and honest as possible in order to establish clear accountability to the taxpayer. One-time accounting gimmicks, such as those implemented in the early 1990s, may be tempting, but they avoid the inevitable and necessary changes to government that would make service delivery more effective while minimizing the tax burden.

The responsibility of the 78<sup>th</sup> Legislature is to prioritize and scrutinize government so that it operates within its available revenue streams. The Legislature must stand committed to these priorities, or it will continue to let government and spending grow unrestrained.

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<sup>1</sup> State of Texas, Office of the Governor, Vision Texas: The Statewide Strategic Planning Elements for Texas State Government, February 2000.

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# Structural Changes



# STRUCTURAL CHANGES

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Texas reaped many of the benefits of a booming economy. But now our state faces the consequences of tremendous growth in government and programs born of profligate spending, now borne by the taxpayers. Even with a booming economy, the state was more interested in spending than saving, as evidenced by the fact that the Rainy Day Fund, which began 1988, has failed to amass even \$1 billion.<sup>1</sup> Reining in the growing budget requires a comprehensive look, not only at where money goes, but the entire budgeting process as well. Improving the state's budget structure is at the heart of improving the way the state spends money and the current process is difficult to navigate, often deceitful, and hard to control.

Fundamentally, the conservative philosophy favors limiting government growth and safeguarding against unnecessary spending of the people's money. When money has been made available, the Legislature has found a place to spend it, often without considering how these new and expanded government programs and projects will be funded in the future. The Legislature must consider amending the Texas Constitution to ensure that there are appropriate controls on taxing and spending in this, and in future, legislative sessions.

Equally important to the discussion of how much money is appropriated is how well the dollars are being used. Duplicative services and programs that do not meet established performance measures should be eliminated. Additional efficiencies may be achieved by identifying the value of any dollar spent and better determining the cost of providing services, while tying performance standards to funding. At all times, but particularly when dollars are tight, it is important that money be wisely spent.

While many of our recommendations for improving the general budget structure have no quantifiable cost savings, improving how and where the government allocates taxpayer money is certainly at the soul of improving government. Looking for money when times are lean is not as important as taking charge of spending when times are good. Where the Legislature has failed to do this in the past, we must begin to reinvent the approach to government and the appropriations process, not only to find immediate resolution to current fiscal challenges, but to be better prepared to restrain spending in the future.

## **Exceptional Items**

### **End practice of funding exceptional items.**

Each state agency submits its legislative appropriations request (LAR) to the Governor and the Legislative Budget Board (LBB) outlining what the agency will require in base funding for the current biennium. As a part of this process, the agencies also submit requests for funding of exceptional items, which are separate from the funding requested in its base. This process allows the agencies to ask for extra money for activities that could be outside of an agency's core functions and current services.

In evaluating the LARs, the LBB makes a recommendation to the Legislature on what they believe is needed to fund state government, allowing members to add in the extra requests in the appropriations process. Any exceptional items that are funded in one biennium are factored into the base for following biennia, unless it is funded as a one-time rider. One-time riders do not automatically become part of the agency's base. These exceptional items may reflect the desires of an agency to address a specific situation, to emphasize something new, or to respond to the respective priorities and pressures of advocates or interest groups associated with an agency. In the future, automatically funding these items as part of the base neglects to evaluate whether the funding continues to be necessary, or whether these needs were to be addressed only temporarily.

Furthermore, funding exceptional items, and thereby rolling them into an agency's future base, creates tremendous opportunities for unchecked and wasteful spending that allows an agency to deviate from focusing on its core mission. This is a recipe for both government and budget growth. Although funding exceptional items through one-time riders may seem to be an alternative to committing funds for subsequent years, even the one-time appropriation allows agencies to add to their current functions. As evidenced by the fact that it is easier to increase spending than to cut it, agencies that receive even one-time funding for an exceptional item will not easily give up that money in the future.

The LARs for the 2004-2005 biennium have already been submitted, and many agencies have already asked for funding for exceptional items. According to the Legislative Budget Board, the biennial All Funds total of exceptional items requested for the coming biennium is \$9.1 billion.<sup>2</sup> The fact that agencies would ask for this kind of additional funding during a knowingly tight fiscal session is an embarrassment. These requests are a perfect illustration of how the budget can grow tremendously from one biennium to the next if Legislators do not set priorities and require agencies to justify their needs. The Legislature should reject funding exceptional items and ask agencies to best prioritize their duties within their current level of funding. In addition, the Legislature should carefully review agency funding to determine what was originally requested as an

exceptional item and whether it is appropriate to continue to fund them as a part of the agency's baseline budget.

## **Contingency Appropriations**

### **Eliminate contingency appropriations.**

The appropriations process is the Legislature's balancing act, with the legislation on one hand and the dollars in the other. The Legislature is responsible for determining the state's priorities and funding them accordingly. Contingency appropriations are items that are not included in the appropriations bill, but that may be funded contingent upon the availability of funds and certified by the Comptroller. This process allows the Legislature to spend all money available, plus any other money that can be found after the Appropriations Act has been passed and signed into law. While the Legislature must prioritize the items to be funded up front, contingency appropriations also encourage spending every last penny for these "extras" and abdicate responsibility to the Comptroller of Public Accounts.

Simply put, items that are important enough to receive funding should be written into the appropriations bill. Setting priorities is the most basic responsibility of the Legislature, and the funding granted to an item should be a measure of where that item falls within the state's priorities. Each bill and its fiscal impact should be weighed against whether the proposed policy is a prudent use of the taxpayer's money, and the Legislature should not abdicate its responsibility to the Comptroller to set budget priorities.

The 77<sup>th</sup> Legislature approved a \$113.8 billion budget for the 2002-2003 biennium, which was \$15.6 billion more than the previous budget. According to the Legislative Budget Board, there was approximately \$881 million appropriated for contingencies, including the enactment of legislation, that have occurred, and an additional \$493 million appropriated for various items contingent upon the Comptroller's certification of funds.<sup>3</sup> Had Governor Perry not vetoed \$230 million in contingency appropriations, the growth in the biennial budget would have been around 16.5%.<sup>4</sup> Consider that at this rate, the state budget would be almost 50% greater in six years. Arguably, nothing changed in the years between the 2000-01 budget and 2002-03 budget to drive this increase, but legislators chose to continue to spend at an accelerated rate. Certainly, contingency appropriations, as well as funding for exceptional items, contribute to the growth in spending.

Contingency Appropriations for 2000-01: \$631 million appropriated for contingencies that occurred. For 2002-03: \$881 million appropriated for contingencies that have occurred, and an additional \$493 million for items requiring the Comptroller to certify availability of sufficient revenue.

Spending all available money and planning for ways to spend money that doesn't yet exist should be an indicator that spending is out of control. The pitfall of funding items contingent upon available funds is that legislators lose their grasp on what money is truly being spent on. The principled approach to the appropriations process requires full evaluation of the priorities that should be funded and limiting spending on the extras. The Legislature should, by rule, end the practice of passing contingency appropriations in an effort to control unnecessary spending and only commit funding to real priorities.

## **Constitutional Spending Limits**

**Amend the Texas Constitution to limit the growth of the state budget to the rate of growth in Texas' personal income.**

Despite the Texas Tax Relief Act of 1978, which was intended to restrain growth in state government, the state budget topped \$110 billion in 2001 and continues to grow rapidly. In fact, since the passage of this constitutional amendment, state spending has risen about 500% while personal income has only grown about 400% and gross state product has grown 366%.<sup>5</sup> This increase illustrates that state spending has grown beyond its means.

Loopholes in the Tax Relief Act allow spending to grow faster than the state's economic growth. First, the current provision only limits appropriations from state tax revenues not constitutionally dedicated, which accounts for less than

Since the passage of the Texas Tax Relief Act of 1978, state spending has risen about 500% while personal income has only grown about 400% and gross state product has grown 366%. This increase illustrates that state spending has grown beyond its means.

*Texas Public Policy Foundation, "The Texas Tax Relief Act in Retrospect."*

half of all appropriations, leaving the bulk of the budget exempt from the constitutional restraints. Second, the Legislature can currently use actual spending as the baseline for the next year's budget instead of the amount appropriated. Third, only a simple majority is required to circumvent the spending restrictions altogether. Amending the Constitution to close these existing loopholes would help curb the growth in state spending, making it harder for legislators to exploit these holes when there is desire for additional money.



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## **Super-Majority**

**Amend the Constitution to require a 2/3 super-majority for all tax or fee increases.**

As talk of income taxes has already surfaced, it is important that conservative legislators hold the line on any tax or fee increases. Requiring a 2/3 super-majority would eliminate some of the temptation of increasing taxes, as well as require a larger coalition of members willing to put their names on a tax increase.

Fourteen states currently have super-majority provisions, which, for many, has been an effective mechanism for restraining tax increases. Of the states without a super-majority requirement, taxes went up 104%, while states with this provision saw an 87% increase in taxes by comparison.<sup>6</sup> By controlling tax increases, super-majority provisions also force Legislatures to be constrained, thereby slowing the rate of government spending. Fundamentally, in order to protect taxpayer dollars, it should be difficult to pass a tax increase.

## **Line-Item Reduction Veto**

**Amend the Constitution to allow the Governor use of the line-item reduction veto.**

The Governor has the authority granted by the Constitution to use the line-item veto in any spending bill containing more than one item of appropriation, but generally may not veto a rider in an appropriations bill unless it is in itself an item containing a specific appropriation of money.

Governors in 43 states have the authority to reduce state spending through the use of the line-item veto, and ten of these states grant governors the use of the item-reduction veto. This item-reduction allows governors to reduce spending without striking the entire amount of a given appropriation.

The Governor, as the statewide elected executive of the state, is held the most accountable for the fiscal health of the state. Just as the Governor vetoes and signs individual legislation, the Governor also should have the opportunity to approve or veto any or all parts of any appropriations bill. The Governor should have the tools to restrain legislative spending without being forced to choose between the complete elimination or approval of a given appropriation, and should be allowed the full authority to veto any or all of an agency's budget.

## **Strategic Planning**

From 1973 to 1991, the state budget was constructed using a zero-based budgeting system, which effectively set the clock back to zero in writing the budget each year. In 1992, the LBB and the Governor adopted a strategic

planning and budgeting system in response to new strategic planning statutes and budget reform proposals. From the beginning, the purpose of integrating strategic planning and performance-based budgeting has been to “recognize the relationship between funding and performance, between accountability and resource allocation, and between spending and results.”<sup>7</sup>

**De-link the strategic planning process from the budgeting process.**

In strategic planning, every executive-branch agency must produce a five-year strategic plan in each even-numbered year. In each plan, the agency is required, but not limited to, identifying its mission and goals, setting performance measures, identifying the populations served, analyzing the necessary resources and how changes in law will affect the agency’s service. However, the strategic planning process has become so tightly linked with the budgeting process that the opportunity for creativity has been lost. Strategic plans should be de-linked from the budgeting process to ensure that agency strategic plans are an opportunity to be innovative rather than an additional prescriptive step in the budget process, and to provide the long-term framework for agency operations that a strategic plan is intended to be.

**Require agencies to submit specific sub-strategies as a part of their strategic plan presented to the Legislature.**

Agencies are required to provide the specific strategies detailing methods that will be used to reach goals and objectives. Sub-strategies give additional budget information for each of these strategies for closer evaluation of appropriations needed for each strategy. Although the agencies develop sub-strategies, this information must be requested, and the mark-up for legislative appropriations does not necessarily include detailed sub-strategies.

However, without the use of sub-strategies, the strategic plans presented to the Legislature are essentially an outline of a basic program and its cost. Legislators need more specific information to make decisions in allocating money to

agencies and programs. Requiring agencies to provide sub-strategy information would allow legislators to evaluate the specific methods planned to achieve goals and objectives in relation to resources.

When used effectively, the strategic planning process can be an important part of the budgeting process. The strategic plan offers legislators an opportunity to evaluate agency performance and identify

On President Bush’s approach to performance-based budgeting:  
“[budgeting] shouldn’t be merely how much, but how well... there are plenty of places to reduce spending when you separate the effective programs from the ineffective programs”

--Mitch Daniels, Budget Director for President Bush.

success, failure, and additional needs. President Bush has also taken this performance-based budgeting model to Washington, D.C. to turn the attention at the federal level to how well any given program has performed in meeting its objectives. The President's budget director, Mitch Daniels, said that this new approach in Washington "shouldn't be merely how much, but how well," and that, "there are plenty of places to reduce spending when you separate the effective programs from the ineffective programs."<sup>8</sup> Taking this to heart, the use of sub-strategies as a way to emphasize benchmarks for success is important to legislators with an interest in cutting wasteful spending.

**Require interim committees to study certain aspects of agency budgets and strategic plans for agencies under the committee's oversight.**

The appropriations process is limited to a short period of time and often does not allow members to fully evaluate the agency's appropriations request in relation to its strategic plan. In addition to including sub-strategy information in the strategic plan, interim committees should have a standing directive to exhaustively evaluate the current strategic plan, the operating budget, performance measures, the base budget, sub-strategies, and all agency contracts for all agencies in their purview. For example, in areas that could be outsourced or already are, legislators could see if additional Request for Proposals by the agency for any of its services would be beneficial and allow increased competition, lower prices, and better service. This could be especially helpful in high-cost areas like health care, Medicaid, and CHIP.

Careful review of these areas outside of the hurried legislative session will not only provide legislators with a better understanding of the agency budgets they oversee, but should strengthen the Legislature's role in oversight of these agencies. By spending time in the interim evaluating the construction of the agency budget and strategies, the Legislature will be better able to assess the agency's needs and performance history in relation to its budget requests during the appropriations process.

**Balanced Scorecard**

**Implement the balanced scorecard management approach in the ten largest state agencies, incorporating the information into the strategic planning cycle.**

In 1992, Robert Kaplan and David Norton developed a new management tool known as the balanced scorecard, which has now come to be used by more than half of all Fortune 500 companies.<sup>9</sup> The method was developed in response to disconnects in strategic planning at all levels of an organization and provides a framework for examining performance across different perspectives. While the business and government perspectives may be different, the evaluation of performance allows an organization to establish cause and effect relationships

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between its policy or financial mission, its relationship with its customers, its methods of service delivery, and the required skills its employees need to operate at peak effectiveness. These cause and effect relationships, as established in the balanced scorecard, help an organization focus the expenditure of its resources and to avoid unnecessary or insignificant performance measures, and concentrate on those that define the success of the organization. This further requires the organization to firmly establish its mission and purpose, and clearly articulate to both its employees as well as the public how it can achieve that mission through the use of performance measures.

Many state and local governments around the nation have adopted or have begun to adopt a balanced scorecard approach. In Texas, the Texas Education Agency began using the balanced scorecard in 2000 in order to strengthen the ties between agency performance and legislative policies. Using the balanced scorecard, the agency developed two goals for its 2003-2008 strategic plan and appropriations structure, and it captures the agency's philosophy that every employee's job and every business process is tied to achieving its mission of fulfilling the promise for all Texas children, by ensuring that every child graduates from high school with a world-class education. This mission is the single most important policy goal and is the focus of the agency's system of communicating performance. The scorecard has been an effective way of driving the agency with a focus on meeting its strategic plan.

In previous strategic plans, the agency reported more than 160 performance measures across three goals and 18 strategies, and no measure or strategy was most important. Funding was tracked and tied to performance but not function. However, in the balanced scorecard proposed by the agency, there is a single most important measure, and the number of strategies and measures are reduced and only listed if they support the primary policy goal. By including agency operations and staffing, funding is tied to function in ways that policy makers, educators, and the public can understand. The value the agency adds to the state's education system is clearly defined. For the 2002-03 biennium, TEA requested almost \$500 million in exceptional items and in 2004-05 the agency requested none. While some of this may be attributable to respect toward statewide fiscal concerns, it is remarkable that a large agency like TEA has managed to create an LAR that works within its strategies without requesting additional funding. The agency believes that much of this credit belongs to the success of their balanced scorecard approach.

Fundamentally, the balanced scorecard is a tool that allows agencies to organize performance measures established by the Legislature into a comprehensive system focused on achieving the mission of the agency. It also provides a framework to critically evaluate performance measures with regard to their efficacy towards attaining agency missions.

One of the many frustrations with government is that agencies get mired in processes that appear to serve little purpose, have agency personnel are uninvolved in understanding the purpose of their job or how it fits into meeting the overall mission objectives of the agency, or are driven by performance measures that have little to do with the agency missions. Government should meet the needs of its customers as efficiently and effectively as possible, not become a morass of red tape and ineffectual process. The balanced scorecard approach allows agencies to comprehensively organize their performance measures in relation to the end objectives of their mission. This allows agencies to critically analyze the performance measures they are given and to determine their end objectives and the steps need to achieve them. The balanced scorecard should allow agencies to achieve greater efficiencies, thereby reducing costs associated with waste within an agency. While early in its implementation, TEA shows that agencies can adopt new management approaches to make them more efficient.

## **Pay for Performance**

**Use merit raises and merit bonuses to reward employees on performance rather than emphasizing length of service.**

A recent report from the Employee Compensation System Evaluation Task Force found that state employees would perform better if a fully-implemented pay-for-performance system were in place.<sup>10</sup> The state's current pay for performance policy allows for employee merit raises up to the limits established for each salary schedule, and these raises can either roll into the employee's base pay or be granted as a one-time reward. Through the strategic planning process, agencies participate in performance budgeting and must report the goals and objectives established by an agency, as well as the incentive rewards and penalties for meeting these performance goals.<sup>11</sup> However, while the pay-for-performance provisions exist, agencies generally don't use the system to make a merit raise an incentive to rank and file state employees.<sup>12</sup>

According to the Employee Compensation Task Force, one-time awards were only given to 2.7% of employees in 2001 and 4% of employees in 2002.<sup>13</sup> Part of the problem of merit-raises is that most often, the Legislature does not appropriate money specifically for agency merit increases, forcing agencies to fund their merit raises from agency services budgets.<sup>14</sup> Although agencies may want to award merit raises to employees, forcing agencies to do so out of their own budget may discourage the practice. In addition, many agencies may lean toward rewarding seniority in the agency, essentially by giving longevity pay increases.

While Texas has many of the systems in place to have a successful pay-for-performance system, much of that rests on tying merit raises to demonstrated performance. To make this work, agency strategic goals must be tied to individual jobs and individual job performance objectives that are measurable

and which truly reward exceptional work. Setting loosely defined, difficult to measure, or easily achieved performance goals only requires employees to meet the most basic work requirements. However, of these three, measuring performance is perhaps most important because it shows an agency's commitment to evaluating employees based on their success in reaching established measure and objectives and highlights the importance of service delivery for the taxpayer.

Furthermore, longevity pay is counter productive and the worst rationale for a pay increase. Longevity pay is a disincentive for younger workers if emphasis is on how long employees have worked for the agency, rather than the quality of work.<sup>15</sup> The pay-for-performance system is intended to encourage employees to exceed basic expectations and recognizes the best performers; longevity pay simply undermines attempts to reward exceptional performance.

Around 70% of private companies have a form of pay-for-performance in place, and in 1999, 89% of companies with a strong pay-for-performance plan reported higher performance results.<sup>16</sup> The Texas Comptroller's e-Texas report from December 2000 also addresses pay-for-performance, and points out that the private sector organizations using this system have an advantage over competitors with "higher revenues, cost containment, and a marked improvement in professional and individual competencies."<sup>17</sup> In a tight job market, the state often complains that it has difficulty competing with the private sector for employees; a system that mirrors what private organizations use should help to combat difficulties in recruitment and retention. Additionally, the state often cites employee turnover as a problem when the state trains an employee, only to shortly thereafter train another employee that replaces the first. Rewarding exceptional employees by pay according to performance recognizes employees for their efforts, sets a standard for others, and keeps employees not only working toward agency goals, but invested in the agency's work.

### **Appoint an interim committee to review the state classification system.**

The state classification system assigns and titles employee positions to state agencies and establishes a standardized pay scale for state employees. This method is too prescriptive and does not allow agencies to best allocate their resources to meet the agency's demands and needs. One outstanding employee may make it unnecessary for an additional employee to be assigned to the same function, which the state classification system is unable to consider, but which agency management may be able to identify. While it is important that the Legislature maintain FTE caps and salary caps for state employees, it is not necessary for the Legislature to lay out how the FTEs and salaries must be distributed within the agency. Where it is possible, agency heads should be able to employ fewer people and provide far better compensation to employees with exceptional talent. As it is, many of the best state employees have their salaries supplemented through officeholder accounts making them, in part, political staff

working in state buildings. State agencies should be given the flexibility to respond to their individual needs and best manage their workforce.

The Legislature should establish an interim committee to study the state classification system and whether there is a better, more flexible system. The study should consider overhauling, or even abolishing, the classification system and allowing state agencies more autonomy in setting salaries.

## **Activity-Based Costing**

### **Implement Activity-Based Costing and Activity-Based Management methods in the ten largest state agencies.**

The large size of government and the many roles it assumes makes it hard to measure one activity or service, and without such measures, government is often allowed to run without examination of whether it is cost-effective and efficient. Management tools like Activity-Based Costing (ABC) assist organizations in capturing the true costs of delivering a product or service by considering the direct, indirect, and overhead costs tied to providing the service.<sup>18</sup> Activity Based Management (ABM) uses the principles of ABC to make business more effective and efficient through management methods.<sup>19</sup> Current ABC pilot programs in select state agencies have been inconclusive, but may be more successful if the participating agencies are better able and willing to participate fully. Much of the success of ABC and ABM is a direct result of the organization “buying in” to the program and making a concerted effort to make this basic cost accounting process work for their enterprise.

ABC and ABM have been effective in both the private and public sectors, and the state would benefit from not only knowing what a service costs, but by establishing cost comparisons between private and public sectors, and identifying redundant and unnecessary activities. ABC allows the state to identify areas of state business that may be privatized when cost comparisons show that private enterprise does a better job providing a service than the state, and consolidation of redundant or unnecessary activities ensures that the money spent for services is used efficiently and is not duplicated in other unnecessary areas of government.

Texas’ fiscal challenges highlight the necessity of spending existing dollars wisely. While it is widely assumed that there is waste in the state budget, it is hard to quantify the existing waste without a full accounting of what it actually costs the state to provide its services. Comparisons between the cost of services provided by the public and private sectors are particularly instructive when the private sector is expected to run at the most efficient levels and the public sector is often allowed to be inefficient. A realistic assessment of how well the state provides services cannot be made without these comparisons.

By targeting ABC and ABM methods toward specific agencies that have significant increases in their client base and need to work within the constraints of their existing budget, these costing and management tools will assist agencies in understanding their budget and its cost drivers. Once the agencies have been identified as candidates for ABC and ABM, implementation efforts must include elements of independence, competency and communication structures at the agency level, cost effectiveness of the implementation process, and accountability in state and agency policies. There have been limited attempts to implement ABC in the past, but the approach has often been inconsistent and has not been comprehensive enough for agencies to realize the full benefit of ABC and ABM. The state must make expectations for implementation clear and must encourage employees to buy in to the activities associated with an ABC study.

Implementing ABC and ABM significantly increase the accounting and visibility of business processes in those state agencies implementing ABC analysis, which can be a catalyst for consolidation and cost savings. Additionally, implementing these management tools can introduce an element of fiscal accountability and help agencies maintain control of their budgets in future years as well.

## **Prevailing Wage**

### **Repeal the prevailing wage law.**

During the Great Depression, Congress passed the Davis-Bacon Act, requiring contractors to pay prevailing wages on projects for the federal government. This act led to the passage of prevailing wage laws in over forty states, including Texas. Prevailing wages are essentially minimum wages for specific occupations set at the union-scale rate. The act is a relic and a reflection of both anti-competitive and discriminatory attitudes that were common during that time, which should not be supported today.<sup>20</sup>

The Texas Government Code, Chapter 2258, establishes the prevailing wage law in Texas. The prevailing wage law states that contractors working for political subdivisions are required to pay prevailing rates. The political subdivision must determine the prevailing wage for each type of worker and specifically state those wages in both its contract with the contractor, and in the call for bids.

One major argument against the prevailing wage law is the increased costs that the artificial wage levels cause. Prevailing wages, especially in a right-to-work state such as Texas, are higher than wages normally agreed upon between employers and workers in the private sector. So how much do prevailing wage laws increase construction costs? In Ohio, when school construction was exempted from the prevailing wage law, school construction savings averaged 10.5%.<sup>21</sup> When the same exemption was granted in Florida, a 15% savings in



total construction costs was realized.<sup>22</sup> In Washington, school districts would save 12.7% of total construction costs and 27% of labor costs if their prevailing wage law were repealed.<sup>23</sup> For Texas, the Florida study is most important because both Florida and Texas have similar labor markets and are both right-to-work states. Although these studies only deal with public school construction, all publicly financed construction costs could realize similar cost savings in the absence of prevailing wage laws.

Michigan has served as a model for these studies because their prevailing wage law was temporarily suspended by court order from December 1994 to 1997. During that time of repeal, Michigan public construction costs decreased around 10% from the costs with prevailing wage law in place.<sup>24</sup>

In 1999, Texas led the nation with approximately \$1.9 billion in school construction projects.<sup>25</sup> As enrollments are certain to continue to increase, so will the need for school construction projects. Among the state agencies with large construction budgets, in fiscal year 2002, the Texas Department of Transportation (TxDOT) spent around \$4.8 billion on highway construction projects, and the state is appropriated \$80 million for the construction of prisons in 2003. If the state were to save 10% on construction projects by repealing the prevailing wage laws, the state could save \$680 million per year on just the \$6.8 billion in the above areas. If Texas realizes the same 15% that Florida saved, that number jumps to slightly over \$1 billion in annual savings. While the sources of funding for all of these projects are different, and the entire total savings would not necessarily be to the state's general revenue, the savings would be realized by Texas taxpayers who foot the bill regardless of where the funds originate.

The second major argument against prevailing wage law is its effect on the construction labor market. If this wage rate is set too high, there may be more individuals ready to work construction with fewer jobs available, thereby reducing employment opportunities in construction. Therefore, the prevailing wage may actually depress the construction industry and make jobs scarce. The fact that poverty rates are higher in prevailing wage states may be one of the unintended consequences of the prevailing wage law.<sup>26</sup> This is clearly counterproductive to the state, as the prevailing wage law was intended to help lower poverty levels.

Prevailing wage laws result in slowed job creation, lowered economic growth, and higher government spending. Construction labor rates in Texas should be determined by free markets and private negotiation, not by a governmentally determined wage that adds significant cost to taxpayer-funded construction projects.

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## **Legislature**

### **Review services under the Legislature to consolidate duplicative services and outsource other services to the private sector.**

Duplicative services in any agency should be consolidated or eliminated, and those activities that can be privatized, should be privatized. In directing agencies to eliminate duplicative services and privatize certain services, the Legislature should use the same standard and initiate these changes to activities under the Legislature's purview. There are a variety of research organizations under the Legislature providing essentially the same services, as well as obvious duplication in the media and print shops belonging to both the Senate and the House.

The research divisions of the Texas Legislative Council, the House Research Organization, and the Senate Research Center are virtually the same. While there may be some unique activities of each, the majority of their work could be handled by one consolidated staff, rather than three separate staffs. Consolidating the staff of these organizations would ensure that the knowledge and the experience of research staff is preserved, but not duplicated, as well as provide a central organization and point of contact for legislative research needs. Additionally, the Council's research division also contains a demographics division, which is duplicative of the Office of the State Demographer, and should be abolished.

Similarly, the Senate and the House each have printing and media operations that each could be consolidated to serve both chambers of the Legislature. These operations are important to the Legislature and should be preserved, but can provide the same services as two consolidated offices. There may be opportunities for additional efficiencies by combining staff and pooling existing equipment.

Services like the Legislative Council's redistricting and information systems divisions can and should be outsourced to private industry. There is no need to have a redistricting staff in place for an entire decade when redistricting is not an issue every session and outside experts are immediately available. In addition, it is unnecessary for the state to provide information systems support when these services can be contracted to the private sector, which is already equipped to handle projects of this magnitude. It is unnecessary for the state to be engaged in these activities when the private sector is already able to effectively provide these services.

## **State Auditors Office**

**Direct the State Auditors Office to re-focus its efforts toward financial audits only, and remove statutes directing the SAO to engage in other activities that may compromise the agency's ability to perform independent financial audits. Transfer the SAO to the executive branch.**

The State Auditors Office, a \$13 million agency, was created to be the legislative branch's audit arm, to review the financial aspects of state agencies and inform the Legislature of any financial inefficiencies or even malfeasance at the agency level. Fundamentally, the SAO should be the independent auditor of the state and should focus on conducting financial audits of state agencies.

Despite the SAO's position as an independent audit arm of the legislative branch, the Legislature charges the SAO with additional responsibilities that divert the agency's attention away from doing financial audits and could raise questions as to the independence of the financial audits. A review of the Auditor's web site shows that the agency has less focus on pure financial audits as it expands into management audits and consulting style projects. For example, the SAO has taken the initiative to provide training on contract management and offering management advisory services. As the SAO expands its scope, the financial audits become one of many things the office does, opening the possibility for financial audits to fall in priority, or spend less time on those audits, and as their own website shows, the majority of their publications actually focus on the results of consulting-like activities rather than focusing on financial audits. Simply, the focus of the SAO should strictly be to perform financial audits of state agencies and maintain the agency's independence from the agencies it audits.

The independence of a financial auditor is paramount. As the financial improprieties of American corporations, such as Enron and WorldCom, have been exposed over the last year, there is new emphasis placed on separating the financial auditor and the management consultant. The obvious reason for this concern is that due to a conflict of interest an auditing and consulting firm could be unduly influenced to gloss over or hide shortcomings of the other's job- a management consulting arm may be persuaded not to identify management behaviors of a company that would bring scrutiny and attention to unsound practices of the financial auditor. Arthur Andersen, one of the world's leading accounting firms, collapsed for this reason. In order to address these concerns, the Government Accounting Office has updated the "Yellow Book," the government's standard for all audits, to set an independence standard that attempts to clearly separate any obvious conflict of interest between the management and financial audits. In the case of the SAO, the office may be uncertain about drawing attention to contract management problems an agency has if the agency has participated in the SAO's contract management training. These independence standards go into effect in 2003 and may very well require

the SAO to eliminate or reorganize the way that the agency provides management consulting services in addition to financial audits.

It is important for the Legislature to consider the importance of an independent auditor when considering legislation that might expand the SAO to areas outside of financial audits. Similarly, the Legislature should look at roles that the SAO currently fills, such as management consulting and training, and consider removing them from under the purview of the SAO.

## **Appointments**

### **Amend the Constitution to allow the Governor to remove appointees of that Governor at any time during the term of appointment.**

The Texas Constitution currently provides a mechanism for removing gubernatorial appointees from their offices through either what is essentially a trial, or through the advice and consent of the Senate. The latter of the two is thought to be the easiest way to remove an appointee, but still requires that the governor may only remove one of his own appointees and that it must be done either in the regular session or in a special called session. Due to these obstacles, that option is rarely, if ever, used.

The Governor is held responsible for every appointment made and ultimately responsible for the proper management of state agencies and the boards and commissions of the state. Problems at the Funeral Services Commission are indicative of the political responsibility held by the Governor, as the management problems there were an issue for former Governor Bush in his campaign for president. Given this responsibility, the Governor should have the opportunity to remove appointees, with cause, who are not adequately fulfilling their duties. Whether the appointment is to a licensing board or to an agency's governing board, an appointee should be accountable to the Governor for the decisions and management of that body, because they reflect primarily upon the Governor and affect general management of state government. Appointees are representatives of the governor and as such, they should be removed if their representation is either in conflict with the governor or, and especially, if they fail to execute their position appropriately.

Additionally, members of these boards and commissions are often treated to trips and meals as a part of their service and representation on a state board. With such treatment (and because the positions demand little time commitment), the opportunity arises for these members to become something of a rubberstamp for agency executive directors, thereby creating the dangerous prospect that their provision of oversight may be limited or diminished. Certainly training board members thoroughly in management and oversight practices should reinforce the boards' role and relationship to the agency they serve. Increasing and reinforcing the training of board members, as well as strengthening

accountability, would help to ensure that the appropriate level of oversight is applied.

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<sup>1</sup> “Texas Comptroller of Public Accounts, “Texas Comptroller Carole Keeton Rylander Draws Line in Sand to Protect Rainy Day Fund and Balance the Budget,” Press Release, Aug. 20, 2002.

<sup>2</sup> John Keel, Legislative Budget Board Director, letter to Representative Arlene Wohlgemuth, January 7, 2003.

<sup>3</sup> John Keel, LBB Director, letter to Representative Arlene Wohlgemuth.

<sup>4</sup> Texas Comptroller of Public Accounts, “Legislature Significantly Increases Appropriations for 2002-2003,” Statewise, July 2001.

<sup>5</sup> Texas Public Policy Foundation, “The Texas Tax Relief Act in Retrospect,” by David A. Hartman, November 2000, p.6.

<sup>6</sup> American Legislative Exchange Council, “Crisis in State Spending: A Guide for State Legislators,” January 2002, p.25.

<sup>7</sup> “LBB History”, Legislative Budget Board website, <<http://www.lbb.state.tx.us>>.

<sup>8</sup> William Eggers, “The Accountability Project,” The Wall Street Journal, February 4, 2002.

<sup>9</sup> Texas Comptroller of Public Accounts, e-Texas, Recommendations of the Comptroller, “Use the ‘Balanced Scorecard’ Concept to Optimize Texas State Government Performance,” GP-2, <<http://e-texas.org/recommend/ch03/gp02.html>>.

<sup>10</sup> Employee Compensation Task Force, Pay-for-Performance, A Report on the Texas Employee Compensation System, November 6, 2002, p.1.

<sup>11</sup> Texas Comptroller of Public Accounts, e-Texas, Recommendations of the Comptroller, “Link Employee Performance and Compensation to Agency Performance”, HRM-3, <<http://e-texas.org/recommend/ch04/hrm03.html>>.

<sup>12</sup> Employee Compensation Task Force, p.3.

<sup>13</sup> Employee Compensation Task Force, p.3.

<sup>14</sup> Employee Compensation Task Force, p.2.

<sup>15</sup> American Legislative Exchange Council, “Show Me the Money”, July 2002, p.10.

<sup>16</sup> Employee Compensation Task Force, p.6.

<sup>17</sup> e-Texas, “Link Employee Performance”.

<sup>18</sup> Texas Comptroller, Activity-Based Costing in Texas State Government, Executive Summary, Jan 2001, <<http://www.window.state.tx.us/specialrpt/abc/>>.

<sup>19</sup> Comptroller, Activity-Based Costing.

<sup>20</sup> Mackinac Center for Public Policy, Michigan’s Prevailing Wage Law and Its Effects on Government Spending and Construction Employment, by Richard Vedder, Sept 1999, p.3&4.

<sup>21</sup> Ohio Legislative Budget Office, A Study of the Effects of the Exemption of School Construction and Renovation Projects from Ohio’s Prevailing Wage Law, An Interim Report Of a Five-Year Study, Year Two, by Allan Lundell, January 2000, Introduction and Overview.

<sup>22</sup> Washington Research Council, “Prevailing Wage Laws Mandate Excessive Costs”, Policy Brief, PB 99:33, November 1999.

<sup>23</sup> Washington Research Council, “Schools Would Benefit from Repeal of Prevailing Wage,” Policy Brief, PB 99:34, December 1999.

<sup>24</sup> Mackinac Center for Public Policy, p.15.

<sup>25</sup> US Department of Education “K-12 School Construction Facts”, October 1999.

<sup>26</sup> Mackinac Center for Public Policy, p.2.



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**ARTICLE I**  
**General Government**





# GENERAL GOVERNMENT

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Article I encompasses the core business functions of the state, including the Office of the Governor, the Comptroller, the Secretary of State, the Attorney General, and other agencies that are involved in coordinating the general business of the state. In terms of Total Funds, the Article I appropriations in the 2002-03 budget were 2.3% of the total state budget.

In creating these recommendations, the TCCRI State Finance Task Force concentrated on information management issues related to the Department of Information Resources, and the benefits to state employees through Employees Retirement System. The additional recommendations address activities that are not necessities for the state to be engaged in, and make efforts to consolidate duplicative services.

The explosion in information technology (IT) around the country and in the state of Texas has in many ways revolutionized the way the state provides services, manages state business, and communicates with the people of Texas. Of course, a balance must be struck between the large outlays required to construct a comprehensive IT architecture and the efficiencies gained through IT. The evolving nature of IT often means that states often approach IT policy one piece at a time, and tight budgets can further complicate the development of a statewide IT approach. Review of the state's current IT structure was done with an eye toward improving coordination in IT in order to continue to improve the way the state uses its IT resources to control costs and provide better service to the citizens of Texas.

The Employee Retirement System was created in 1947 with a goal to provide state employees with benefits comparable to the private sector, and in September 1976 ERS took on what is its largest role, providing health care insurance and other services to state agency employees, retirees, and their dependents.<sup>1</sup> In truth, ERS has not only provided a benefits plan for state employees that is comparable to the private sector, but it has, in fact, provided one of the richest benefits plans available, often exceeding the benefits and coverage offered through private sector plans and over-insuring the majority of state employees. Of course, these generous benefits come with a price, and as is the case in all health care plans, the cost of administering the plans is increasing. According to a May 22, 2002 presentation to the Joint Meeting of the House Appropriations Committee and the House Insurance Committee, the average monthly participation in all health plans in 2003 is 531,272 members and dependents, 88% of which are covered under the Health Select or Health Select Plus plans.<sup>2</sup> Recommendations for controlling the costs in ERS focus on

addressing the acknowledged cost drivers in the Health Select and Health Select Plus plans, including increased cost of services, increased utilization of services, and the increased cost and utilization of prescription drugs.<sup>3</sup> Unaddressed, it is projected that ERS would require a roughly 27% increase in All Funds to maintain the current level of benefits over the next biennium.<sup>4</sup> Clearly, the Legislature will have to take a serious look at controlling these costs.

The remaining recommendations for Article I highlight areas in which the state can find savings by eliminating duplicative and extraneous activities within the state government. With a fundamental belief in limited government, reducing the size and scope of government must include reducing and consolidating workforce for greater efficiency.

### **Information Management**

The state of Texas is recognized as a leader among state governments in using information technology (IT) to transform government activities and services. According to a 2002 study by the Progressive Policy Institute, Texas is third nationwide in implementing Digital Government Initiatives.<sup>5</sup> Also, to Texas' credit, a 2002 Brown University study of accessibility, security, and privacy of government websites placed Texas sixth in the nation.<sup>6</sup>

However, despite Texas leadership in government IT initiatives, the state can take steps to further maximize the potential of IT to transform state government. So far, only one third of all state agencies share any type of data with other agencies, and only 10% of all agencies share any IT resources or data to prevent duplication of services.<sup>7</sup> Furthermore, the top 44 quality assurance team projects are an average of 17 months late and \$8 million over budget. Overall, 70% of state IT projects are late and 59% are over budget.<sup>8</sup>

In addition, there is no consistency in IT contract negotiation and management. Some agencies do it well, but many others do not have the business and technological expertise to properly define needs, negotiate with experienced IT vendors, build business cases, or craft realistic fiscal notes. Moreover, many small agencies often purchase unnecessary products or services and have been known to have up to a nine-month negotiation cycle.<sup>9</sup>

As IT becomes a more important part of the way business gets done, the state should examine ways to strengthen the state's IT resources.

#### **Integrate data centers.**

Currently, there is a data center in West Texas where several state agencies house their computers, software, and databases in a location separate from their main office. These agencies do not share their systems or software and may have totally different hardware and software, driving up acquisition, upgrade, and

support costs. While this model allows for some efficiencies in housing and managing assets, the state could gain significantly more savings by standardizing the hardware and software used at the data center by following an “integrated” model, where the data center:

- Manages a standardized software image that enables economies of scale in purchasing, training, and support
- Shares computing and storage resources across agencies according to their needs
- Parcels out networking assets and bandwidth to agencies according to their needs
- Enables easier data sharing with a common computing infrastructure

**Consolidate small agency IT functions.**

While this recommendation has been specifically made for several small state agencies in Article VIII of this document, consolidation of all small agency IT functions is an important way to achieve efficiency in state government. Most small agencies do not have the appropriate technical knowledge or business savvy to negotiate with experienced IT vendors, nor the resources to properly manage their IT assets. Small agencies may also run into similar problems when it comes to IT project management. With IT projects, there is often not a clear business case, proper scoping, or realistic project plan.<sup>10</sup> Giving the Project Management Office within the Department of Information Resources greater authority to oversee all state IT projects would help ensure that projects stay on time and within the budget.

**Establish a seat management pilot program and a Seat Management Office within DIR to coordinate related planning efforts and study the effectiveness of the program.**

Government agencies face many challenges in managing IT resources in the constantly changing IT environment. The federal government has begun to address these issues through “seat management”, a contractual arrangement where complete responsibility for government personal computer resources is transferred to a private contractor. Through this arrangement, the contractor is responsible for PC acquisition, planning, installation, configuration, testing, maintenance, disposal, and other services.<sup>11</sup>

Among the benefits of seat management is standardization, which allows support staff to troubleshoot computer applications, and eliminates compatibility problems affecting programs, files, and e-mail attachments. Purchasing of computer goods and services by various government agencies can cause these compatibility problems, and can also cost more because of less purchasing power and the acquisition of the components separately.

Also, seat management requires the contractor to keep installed technology current. The industry recommends that computers be replaced every three years to keep pace with changing technologies. However, government-purchased equipment must be used longer than three years to realize the full benefit of the capital investment, leading government agencies to refresh their equipment sporadically, and often less often than recommended. By contrast, seat management contracts include refresh costs in a monthly price paid over the term of the contract.<sup>12</sup>

Furthermore, outsourcing gives government access to individuals with specialized skills that might otherwise be both expensive and difficult to attract to public employment. Anecdotal evidence from the past several years suggests that the state had difficulty in recruiting and retaining IT professionals to work for the state rather than in industry. In August 2000, the Comptroller announced plans to create an IT Academy that provided both entry-level training to individuals who would work in IT for the state and continuing education for current employees, highlighting the difficulty the state has in employing IT professionals.<sup>13</sup> By outsourcing the state's IT needs, these professionals are available to the state without having to employ additional people or compete with the private sector for employees, and without having to divert state resources to programs to train and keep state IT employees. Seat management also frees state agencies from the need to offer day-to-day computer support and allows the agency to concentrate on its core mission, rather than its IT needs.

In its purest form, seat management turns PC resources into a utility, where the customer purchases the right to use the vendor's equipment and resources, but the vendor is responsible for the upkeep. Seat management arrangements rely on outcome- or performance-based contracts, in which the customer pays a fixed price in return for a specific level of service. These arrangements allow the agencies a predictable IT cost and an expected level of service, if the vendor does not meet those obligations, it risks losing the business.

The most significant savings from seat management are due to standardization and centralized control, not necessarily the acquisition costs. Several governmental organizations have employed seat management in their business practices with promising results, including NASA, the Virginia Department of Transportation, the Virginia Retirement System, and the University of Texas Medical Branch at Galveston. Seat management efforts are also already underway in some Texas agencies. While the exact savings for Texas is hard to project, each of the agencies has reported improved service delivery and expected savings.<sup>14</sup> Flexibility in contracts makes comparison between contracts difficult, as well as variances in service levels, and in individual agencies' IT requirements.

In order to learn the true cost savings of seat management for the state, pilot studies should be undertaken by a several agencies of varying sizes and IT

needs. These pilot studies should be used to benchmark the current computer environment of the agencies and be used to identify steps for statewide implementation.

Establishing a Seat Management Office within the Texas Department of Information Resources, would centralize the coordination of seat management efforts within a department that is already equipped to handle issues of this nature. This office would coordinate the development of contracts, set minimum standards, provide information on “best practices,” manage and evaluate the pilot studies, and develop transition recommendations and guides for implementing seat management statewide. Once the pilot studies are completed, the Seat Management Office will be able to recommend a comprehensive seat management package to the Legislature with more accurate estimates of cost savings.

### **Consolidate state agency area wide networks under DIR management.**

Currently, each agency has the ability to manage its own wide area network. While some agencies share networks, others do not, such as the Texas Cancer Council, which has only 8 employees, but runs and manages their own network. The Health and Human Services Consolidated Network (HHSCN) should serve as an example of the efficiency and cost savings available by consolidating networks. HHSCN is a partnership between government agencies that “connects and manages networks from the data center to the desktop.”<sup>15</sup> HHSCN is saving \$33,392 a month by adding the Texas Commission on Alcohol and Drug Abuse and the Texas Department of Health to the other HHSC-related agencies already a part of the HHSCN network, and reports that the network allows them to provide innovative solutions to their customer’s diverse telecommunications needs.<sup>16</sup>

By virtue of DIR’s involvement in managing TEX-AN, the statewide telecommunications network, and the fact that all state agencies, except universities and legislative bodies, are required to use “intercity telecommunication services” provided by TEX-AN, DIR should manage the consolidation of agency area wide networks. With an eye toward greater government efficiency, DIR can use the success of HHSCN as a benchmark for consolidating these agency networks.

### **Direct DIR to aggressively enforce and encourage state agencies to use Texas Online.**

Texas Online currently processes more than 800,000 financial transactions and close to 1 million citizen visits per month. Texas Online offers best-of-breed security, electronic payment, and hosting services to state agencies. Over the past 18 months Texas Online has deployed over 60 applications on a common

integrated technology platform. It provides a scalable, state-of-the-art architecture that can serve more than its current 30 agencies. Senate Bill 87 from the 77<sup>th</sup> Legislative Session provides that no agency should duplicate the architecture and services of Texas Online. The Project Management Office of DIR is tasked with monitoring compliance with this legislation. The office should aggressively hold agencies to considering using Texas Online. Its use will provide assurances that the state and its citizens' data are properly safeguarded and that the state is achieving cost savings by the economies of scale of more fully utilizing Texas Online assets.

### **Abolish the Texas Information Technology Academy.**

The Texas Information Technology Academy was begun in 2000 under the Comptroller's office, with a goal of providing IT training to individuals who would commit to working for the state for two years, in order to recruit and maintain an IT educated workforce capable of competing with the private sector. Reportedly, higher salaries and more attractive benefits, as well as a perception that the state is behind in its IT capabilities and therefore not a valuable place to gain experience in comparison to the private sector, hinder the state's ability to attract these high-tech workers.<sup>17</sup> The Academy is open to new or existing state employees, with specific mention of those with liberal arts or other degrees that lack high-tech skills or those looking for a career change who also lack IT skills; presumably, targeting the academy to these types of individuals means that the state recognizes that it is not competitive with the private sector and cannot attract the most qualified workers, yet it insists on manufacturing a workforce to fill its IT needs. It is simply not the state's role to educate and train a workforce that is admittedly less competitive than what is available in the private sector.

The notion that the state must create such a workforce fails to recognize that there are alternatives to expanding the state government's activities. This should be an opportunity for the state to privatize IT functions and allow the skills and experience of the private sector to fulfill the state's IT needs, without the addition of state employees or the expense and burden of completely training state employees to meet this need. The state must recognize where the private sector is already equipped to effectively and efficiently meet some of the state's needs, and where it is inefficient for the state to compete with the private sector. Furthermore, the state has budgeted \$400,000 annually to provide training through the Academy, yet there are now skilled and experienced high-tech workers looking for jobs as a result of private sector layoffs. The training academy is unnecessary and only reflects the immediate needs of the state without looking for innovative ways that the state can tap into the knowledge of the private sector. In addition, the changing economy and its impact of the workforce picture as a whole, illustrates just how quickly circumstances and needs may change, which the state must become better prepared to handle. Abolishing the training academy would eliminate unnecessary activities that

simply stretch state agencies, and should be used as an opportunity for the state to meet its' IT needs through innovative solutions.

## **Employees Retirement System**

### **Change the existing ERS plan by introducing additional cost sharing for ERS members.**

Texas, like private employers and other states, faces a significant challenge in funding state employee's health care. While the Employees' Retirement System (ERS) has worked to control increases in costs incurred by the state, ERS anticipates an 11% increase in health care costs in FY 2003.<sup>18</sup> As a result of the increasing costs, ERS projected a health plan funding shortfall of \$27.3 million in 2002 and \$14.9 million in 2003.<sup>19</sup> As the trend in increasing health care costs continues, Texas will be forced to confront the health care costs associated with both state employees and teachers.

ERS compared the state health plan for employees to the plans offered by large private employers in the state of Texas, such as HEB, Southwest Airlines, IBM, Motorola, and Dell (See Appendix A). This comparison shows that in some areas, the state health plan offered by ERS is dramatically better than the private plans. In identifying the places where the state plan is more generous than the private plans, recommendations for scaling back those areas have been tempered with concern that reduced benefits may hurt the state in recruiting employees, as a better benefits package may offset the comparatively low compensation that public sector employees receive. The following recommendations are options that, with few exceptions, ERS presented as options would only bring the state's plan more in line with private plans being offered in the state while still maintaining an attractive benefits package. More aggressive measures would net more savings.

- **Reduce dependent coverage for certain employees:** Most private sector plans cover 80% or more of dependent premiums, however, most do not cover 100% of the employee premium as the state does and the only private employer that covers employee premiums at 100% covers dependent premiums at a considerably lower percentage than the other private plans as well as the state. 53.1% of health coverage through ERS is for the employee only and their premium is paid 100% by the state, the small reduction in the state's portion of dependent premiums saves \$46.1 million and preserves coverage for employees at levels that are still more generous than private plans.<sup>20</sup>
- **Index retiree premium share to years of state service:** No private plans cover retirees, whereas the current ERS plan offers retirees full coverage and 50% coverage for dependents of retirees. Bringing this benefit more in line with private coverage, while preserving the benefit, the proposed

indexing schedule is: 50% coverage for 10-15 years of state service, with 25% dependent coverage; 75% for 15-20 years of service, with 37.5% dependent coverage; 100% for 20 plus years of service, with 50% dependent coverage. This change could potentially result in cost savings of \$87.1 million for the biennium.<sup>21</sup>

- **Eliminate state contribution for individuals not retiring directly from active employment.** According to ERS' survey of private sector plans, none of the major private plans in the state included a contribution for retirees. Changing the benefits plan to eliminate coverage for only those employees who did not retire directly from state service preserves coverage for those individuals who have already retired from state service and for those individuals who retire directly from their service to the state. Eliminating this coverage would align the state's plan with private plans while still providing generous benefits to those who retire directly from state employment. This recommendation has a potential cost savings of \$63.8 million for the biennium.<sup>22</sup>
- **Increase new hire wait time:** The state should consider implementing a wait time, or a delay between when a new employees starts and the day that their insurance begins. Currently, the state begins a new employee's insurance coverage on the day they begin work. Wait times vary among employers and of the private employers surveyed, Southwest Airlines has a 30-day wait time, and even in a survey of health plans in major Texas cities, the City of Houston has a 90-day wait-time.<sup>23</sup> The addition of a 30-day wait time for new employees would save the state \$39 million for the biennium.<sup>24</sup>
- **Increase calendar deductible:** Three of the five private plans surveyed have calendar deductibles of \$150/year or higher. Increasing the deductibles in the state plan to \$100/\$500/\$200 for in-network, out-of-network, and out-of-area services, respectively, would still be less than the private plans, and still at a relatively low cost to employees.
- **Increase primary care and specialist office visits co-payments:** The current ERS plan is equivalent to the private plans studied, however, the trend to increase co-pays is expected industry wide and consumers will be expected to share in the cost of increasing health care, making this recommendation the only one that would be more aggressive than private plans in comparison to the ERS survey of private plans.<sup>25</sup> There is some indication, however, that even the figures from ERS' survey of private carriers are low and that the cost sharing responsibilities for the participants are much higher. According to ERS' figures, raising this co-pay from \$15 to \$20 per office visit would result in a biennial saving of \$25.2 million for specialist visits and a \$70 million biennial savings for primary care physician visits, and raising the co-payment for specialist



visits from \$15 to \$25 would result in a biennial savings of \$50.2 million.<sup>26</sup> The goal of increasing these co-pays is to discourage inappropriate utilization of both types of office visits by increasing the patient's share of the cost, while keeping the cost of the office visit reasonable when such visits are medically necessary. The task force recommends that these co-payments be even more aggressive than the ERS figures indicate possible; the specialist co-payment should be no less than a \$10 increase.

- **Increase annual out-of-pocket maximum to \$1000:** Calendar year stop-loss, or the annual out-of-pocket maximum, amounts for the private plans studied are dramatically higher than the current ERS plan, and range from \$1500 to \$2300 per year. The current ERS plan has a \$500/year maximum for in-network benefits. Increasing the state plan to \$1000/3000/800 for in-network, out-of-network, and out-of-area, respectively, would double the in-network and out-of-network patient portion, and would still be more generous than the private plans. This increase would result in an estimated savings of \$28.4 million for the coming biennium.<sup>27</sup>
- **Increase in-patient and out-patient co-pays:** Two of the five private plans surveyed have percentage co-pays for in-patient and out-patient visits. The state can share the cost of these services with the patient while still keeping them affordable to the patient when medically necessary. The state should set a new inpatient co-payment of \$100 a day with a \$500 maximum and a new outpatient facility co-payment of \$100, to realize an estimated savings of \$45 million combined.<sup>28</sup>
- **Reduce coverage for part-time employees from full to partial coverage:** Compared to typical private sector benefit plans, the current ERS plan is very generous, providing full coverage to employees working as little as 20 hours a week. Part-time employees should not receive full-time employee benefits. The state health plan is already generous and is a form of compensation that should be reserved only for full-time employees. It is simply unreasonable for a part-time employee to expect benefits that are equivalent to those of full-time employees. Reducing the coverage for the part-time employees could result in a \$20 million biennial savings.<sup>29</sup> Also, since so few private plans offer coverage to any part-time employees the state could save in completely doing away with part-time coverage.

The state should respond to rising health care costs as private business has been forced to do by passing some of the increased costs to the consumer. Increasing premiums and utilization charges, like co-payments and deductibles, should be considered as the state tries to contain costs in the state health plan.

Also, lawmakers should consider that this package is extremely generous to state employees, but has encountered difficulty in attracting carriers. The ERS presentation to the House committees says that the “single most important factor contributing to success of UGIP [Uniform Group Insurance Program] is near 100% participation of employees; made possible by the state paying the full cost of employee coverage.”<sup>30</sup> This is a misleading way of measuring the program’s success since ERS offers a rich benefits package to employees and dependents, but has little competition and offers little in the way of employee choice. In truth, 100% participation is expected since the package is so generous, but there seems to be little control of cost on the part of the state. In addition, a truly successful program with so many enrollees should be attractive to HMOs and other carriers, yet the state has had difficulty attracting providers, which raises questions about how successful the program truly is. Competition and employee choice would likely offer employees better options in their health coverage and improve cost containment for the state, yet as long as the state measures success by enrollment numbers, the state will continue to see increasing costs and attract fewer providers. Simply put, focusing on the number of enrollees in the state employee benefits plan is an incorrect measure of success.

**Change the request for proposals (RFP) process for ERS to allow for lower cost options.**

According to ERS, about 75% of covered employees incurred medical costs of \$1,000 or less for FY 2001, illustrating that most state employees are over-insured.<sup>31</sup>

The state should also examine the RFP process in an effort to allow insurers to present lower cost options that could be provided to ERS and the Teacher Retirement System. ERS has had difficulty attracting commercial HMOs to bid on the state account, in part because the request specifically states that they would not recognize proposals that differed from the established

requirements. This discourages private plans from bidding on the state account, and fails to recognize that there may be better and more innovative ways that these plans could be administered. In addition, according to ERS, about 75% of covered employees incurred medical costs of less than \$1,000 in FY 2001, illustrating that most state employees are over-insured.<sup>31</sup> While individuals may be over-insured in the private market as well, the biggest problem is that ERS offers virtually no choice in plans and may over-insure employees unnecessarily. As such, it is in the interest of the state to review the RFP process to determine if it is too prescriptive to bidders, and thus limiting, or possibly excluding, the presentation of lower cost options that insurers could provide to ERS. If the RFP process does not allow for innovative, potentially cost-saving plans to even be presented to ERS and TRS, then cost savings will never be realized. Furthermore, the possibility also exists that the process will continue to have

difficulty finding bidders, and will eventually drive away all bidders, leaving the state without an insurer.

Furthermore, the Legislature should consider fundamental changes to the state employee benefits plan using the Federal Employee Health Benefits Program (FEHBP) as a model. One of the most attractive features of such a plan is that it is responsive to consumer demand and offers choices to the consumer. The FEHBP is no single, comprehensive standardized benefits package, but allows the almost 9 million people it serves to choose from several plans that best meet their individual needs. The goal should be to develop a system that empowers consumers and offers meaningful choices to employees.

### **Texas Building and Procurement Commission**

**Employees at state agencies who have job responsibilities that are performed by TBPC should be terminated to eliminate duplication.**

The Texas Building and Procurement Commission (TBPC) is statutorily responsible for the leasing of commercial office space for all agencies. TBPC has the procedures and staff in place to obtain this space at the very best value available.<sup>32</sup> Despite this, various state agencies have assigned staff to handle duties and responsibilities related to facilities leasing and space management. According to a legislative survey, there are 239 employees and 3 contract workers in the state devoting some portion of their time to activities for which the TBPC is already responsible.<sup>33</sup> By the TBPC's own admission, their record of service to these agencies prior to coming under new management, made it necessary for individual agencies to handle some of these duties on their own. However, under new management TBPC has addressed the previous problems, and should handle the leasing and space management functions for the state. TBPC has the statutory and fiduciary responsibility to lease commercial office space and is equipped to do so. There are significant savings available to the state through competitive bidding, aggressive negotiation, and elimination of unneeded employees at state agencies. The state should pursue the savings available through workforce reductions and by consolidating the services that are duplicated throughout the state agencies.

### **Texas Commission on the Arts**

**Transfer the Texas Commission on the Arts to the Office of the Governor and eliminate current FTEs.**

The Texas Commission on the Arts (COA) was created in 1965 to distribute grant funds from the National Endowment for the Arts to arts organizations and artists in Texas. In 1993 the 73<sup>rd</sup> Legislature created the Texas Cultural Endowment Fund (CEF) as a permanent trust fund outside the State Treasury. The 77<sup>th</sup> Legislature appropriated \$2 million in General Revenue Funds to the CEF,

bringing the total state support since 1993 to \$10.2 million. The agency uses the corpus of the fund as leverage to secure private funds for the CEF, and the interest generated on the fund is allocated to the agency's operating account, and used by the agency to further develop the fund.

The 73<sup>rd</sup> Legislature also authorized the "State of the Arts" license plate, sales of which are deposited into the agency's operating account. Since the license plates were first made available in June of 1996, there have been 22,000 sold, making it one of the top-selling state specialty plates. For the 2002-2003 biennium, \$1.9 million was appropriated to the agency in prior-year balances and estimated revenue from the sale of license plates for the 2002-2003 biennium.<sup>34</sup>

COA grants money for several ongoing arts education programs, such as the Arts in Education Residency Program that emphasizes arts education in schools or in lifelong learning opportunities, the County Arts Expansion Program to promote the arts in small counties, and the Touring Company and Artist Roster Program to provide support for Texas-based artists to tour statewide.

According to a State Auditor's Report in June, the COA has been inaccurately reporting on the agency's performance measures, the agency does not expedite the process of awarding grants, and the agency also lacks controls in monitoring the use of grant monies awarded. In addition, the auditor's report also found that the COA does not have written procedures for determining amounts awarded to grantees, and as a result COA estimates that grantees returned \$80,000 in unused funds in fiscal year 2001.<sup>35</sup> These management weaknesses and grant monitoring inadequacies documented in the auditors report highlight the need for reforming the agency's structure and better controlling the COA's business practices.

The impact of arts education, preservation, and celebration of the Texas arts culture is immeasurable. Transferring COA programs to the Office of the Governor would allow grouping of like agencies, such as the Texas Film Commission and the Texas Music Office, which are already a part of the Governor's office, and do not suffer from the same management and grant monitoring difficulties that have troubled the Commission on the Arts since 1991. Abolishing COA would result in a GR savings of \$8.5 million, less whatever is needed to allow the Governor's office to implement programs.

## **Texas Historical Commission**

### **Eliminate the Texas Historic Courthouse Preservation Program.**

In 1999 the Legislature established the Historic Courthouse Preservation Program to provide grants to restore historic county courthouses. The program grants are awarded as a reimbursement to counties that submit architectural plans for approval before beginning the construction.<sup>36</sup> Initial funding began with

\$50 million in appropriations for grants, and in 2001 legislators allocated another \$50 million to fund another round of grants. According to the Texas Historical Commission's website, the Commission's architects have determined that the estimated cost of repairing and restoring all of the state's historic courthouses could exceed \$750 million.

County courthouse preservation and restoration is not a priority for state spending. The future of these buildings should be determined and controlled by the local community, not by the state and through general revenue. The state should not be expected to subsidize the repair and restoration of courthouses that are deemed historic just because of their age, and at such a high price the state would have to continue with the program indefinitely if it expected to grant money to all the "historic" courthouses. At this time, the state can save \$50 million in general revenue by not funding this program.

## **Councils of Governments**

### **Eliminate funding for regional grant assistance through the Office of the Governor.**

Councils of Governments (COGs) are a cooperative effort between local government entities, such as cities, counties, special districts, and school districts, to address common concerns that stretch beyond their individual jurisdictions. The 77<sup>th</sup> Legislature appropriated \$5 million for regional assistance grants to COGs in the 2002-03 biennium, in addition to local funds and federal funds, which are distributed either directly to the regional councils or by pass-through funds from state agencies. Certainly, there are issues best addressed at the local and regional levels; however, COGs are an extra layer of government that is almost never necessary and should not be funded with state dollars. COGs are essentially voluntary and are only one of many collaborative efforts at the local level. Reportedly, federal funds are now a smaller portion of COGs' budgets while the bulk of the funding comes from state and local dollars. COGs handle local needs and should not rely on the state for grant support, but should pool resources just as they collaborate on ideas, in order to meet their individual needs.

## **State-Federal Relations**

### **Remodel the Office of State-Federal Relations**

The Office of State-Federal Relations (OSFR) started out as a division of the Governor's office and became a state agency in 1971. The stated goal of the OSFR is to "increase the influence of the Governor and the Legislature of federal action that has a direct or indirect economic, fiscal, or regulatory impact on the state."<sup>37</sup> OSFR has had an annual budget of around \$1.15 million with 17 FTEs and has offices in Washington, D.C. and Austin.

There is simply no need for an intermediary of this size between Washington and Austin as every member of the Texas Legislature, as well as the Governor and other statewide elected officials, are capable of communicating the interests of the state of Texas to the United States government through the Office of the Governor. Furthermore, the people of Texas elect representatives to the Congress whose responsibility is to secure federal benefits on behalf of the state of Texas. It is unnecessary to have an entire state agency to do the same things that all of these elected leaders already do. However, remodeling the agency and limiting it to a few contract lobbyists that can work in cooperation with state and federal officials, would make the agency more effective. Reducing the number of FTEs and contracting for lobbyists would reduce the overall size of the agency while strengthening the OSFR.

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<sup>1</sup> Employees Retirement System website, <<http://www.ers.state.tx.us.abouters.history.html>>.

<sup>2</sup> ERS presentation to Joint Meeting of House Appropriations Committee and House Insurance Committee, May 22, 2002, p.3, 6.

<sup>3</sup> ERS presentation, p.19, 20.

<sup>4</sup> ERS presentation, p.27.

<sup>5</sup> Texas Department of Information Resources, Catalyst for Government Transformation: 2002 Biennial Report on Information Resources Management, November 2002.

<sup>6</sup> DIR, Catalyst for Government Transformation.

<sup>7</sup> DIR, Catalyst for Government Transformation.

<sup>8</sup> Interview with Pat Keith, State Auditor's Office, November 12, 2002.

<sup>9</sup> Interview with Pat Keith.

<sup>10</sup> Interview with Pat Keith.

<sup>11</sup> Commonwealth of Virginia, Council on Technology Services Seat Management Workgroup, Seat Management for the Commonwealth of Virginia, September 15, 1999, p. 8.

<sup>12</sup> Virginia Council on Technology Services, p.13.

<sup>13</sup> Texas IT Academy website, <<http://www.texasitacademy.org>>.

<sup>14</sup> Virginia Council on Technology Services, p.2.

<sup>15</sup> HHSCNET website, <<http://www.tx.net/general-description.asp>>.

<sup>16</sup> HHSCNET website

<sup>17</sup> Texas Comptroller of Public Accounts, "Ensure the Availability of State Information Technology Staff by Continuing the Texas State IT Academy," Recommendations of the Comptroller, December 2000, HRM-6, <<http://www.e-texas.org/recommend/ch04/hrm06.html>>.

<sup>18</sup> ERS Presentation, p.8.

<sup>19</sup> ERS Presentation, p.8.

<sup>20</sup> ERS Presentation, p.4.

<sup>21</sup> ERS Presentation, p.28.

<sup>22</sup> ERS Presentation, p.28.

<sup>23</sup> ERS Presentation, Appendix.

<sup>24</sup> ERS Presentation, Appendix.

<sup>25</sup> Texas Association Business, Texas Health Insurance Crisis: Employers & Health Care 2002 Report, p 18.

<sup>26</sup> ERS Presentation, p.28.

<sup>27</sup> ERS Presentation, p.29

<sup>28</sup> ERS Presentation, p.29.

<sup>29</sup> ERS Health Plan Presentation to joint meeting of House Appropriations Committee and House Insurance Committee, Executive Director, Sheila W. Beckett, May 22, 2002, p28.

<sup>30</sup> ERS Presentation, p.9.

<sup>31</sup> ERS Presentation, p.9.

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<sup>32</sup> Interview and email, Gene Morrison, State Leasing Officer, Texas Building and Procurement Commission, Austin, Texas, November 12, 2002.

<sup>33</sup> Legislative Survey Results, State of Texas Human Resources website  
<[http://www.hr.state.tx.us/apps/realestate/survey\\_results.html](http://www.hr.state.tx.us/apps/realestate/survey_results.html)>.

<sup>34</sup> Legislative Budget Board, Fiscal Size Up 2002-03, p 57.

<sup>35</sup> State Auditor's Office, Report No. 02-056, June 24, 2002,  
<<http://www.sao.state.tx.us/Reports/report.cfm/year/2002/report/02-056>>.

<sup>36</sup> Texas Historical Commission website, "Courthouse Frequently Asked Questions",  
<[www.ths.state.tx.us](http://www.ths.state.tx.us)>.

<sup>37</sup> General Appropriations Act, 77<sup>th</sup> Legislature, Regular Session-May 2001, I-82.





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**ARTICLE II**  
**Health and Human Services**



# HEALTH AND HUMAN SERVICES

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Health and Human Services programs and agencies are one of the two biggest cost drivers in the state budget. In fact, the thirteen health and human services agencies in Article II account for more than 20% of general revenue-related spending. Programs within these agencies are complicated by federal regulations that dictate the state's responsibility in providing services and the entitlement programs it must maintain. Medicaid and the State Children's Health Insurance Program (CHIP) are only two of a broad range of programs administered by these agencies and serving growing numbers of Texans each year. In addition, programs such as Temporary Assistance for Needy Families have seen dramatic changes, allowing for greater flexibility, in recent years as a result of federal welfare reform.

Outside of the medical assistance programs, the state also faces challenges in access to care issues, brought on particularly by liability issues with nursing homes and medical services. Rising liability insurance premiums for doctors, resulting in part from medical malpractice claims, are causing doctors to weigh their risks in continuing to practice medicine. Last session, liability insurance for nursing homes was the primary liability issue on the Legislature's radar, and the 77<sup>th</sup> Legislature balked at its opportunity to stave off the impending crisis to nursing homes. This problem was not solved in the interim, and in fact, while medical malpractice has been the focus of much of the liability discussion of late, the 78<sup>th</sup> Legislature must also respond to the liability issues for nursing homes.

Arguably health and human services programs are something of a third rail for state governments, resulting in hesitation to strictly evaluate the necessity of some of the states efforts in this regard. The attitude that these services are important to even one person, coupled with visions of the poor and sick in distress, are enough to discourage many from beginning to tackle the issues. Like any other program or service in state government, ineffective agencies and programs should be eliminated. Furthermore, in an area that seems to have so many services spread between multiple entities inside and outside of state government, duplication of effort is a certainty. As in all areas of state government, the goal should be to consolidate all duplicative services under one umbrella, or eliminate the program all together. In keeping with this philosophy, the task force has evaluated the Texas Cancer Council and the Texas Health Care Information Council and recommends that they be abolished.

While the bulk of this review of Article II spending focuses on specific programmatic and policy changes to be made in the agencies and in delivering services, it is important to preface this discussion on cost savings with the issues

and attitudes that influence policy decisions. The rhetoric surrounding these programs is often emotional and potentially misleading, and as a result legislators and the community alike may feel uncertain about treading on a sensitive issue. Misguided public policy in health and human services may be, in part, a result of misconceptions and hesitation to address an emotionally charged issue.

Almost all health and human services programs involve eligibility tests to determine the services allowable for each applicant. The most common of these measures is the federal poverty level (FPL), which compares the United States Department of Agriculture's economy food plan to annual household income to determine a family's ability to meet basic dietary needs. The resulting number from this comparison assigns anyone living a dollar below that threshold as living in poverty. This is a fundamentally flawed measure for several reasons.

First and foremost, economic mobility and income variability make setting income benchmarks difficult.<sup>1</sup> Jobs change, the economy changes, and some people will move from employment to unemployment and back again. Certainly, a measure of income at any one moment is merely a snapshot in time and not a good indicator of overall economic health. For this reason, consumption is a better measure of living standards than incomes, as illustrated by the Bureau of Labor Statistics Consumer Expenditure Survey, which shows that the poorest fifth of American households report spending \$2.30 for every \$1 of reported pre-tax income.<sup>2</sup> Thus the real question is not what an individual makes at any given point, but how much has been earned and where and how the money is spent.

Second, the poverty level does not include the corresponding dollar benefit of Temporary Assistance for Needy Families, medical assistance, food stamps, or child care that is paid on behalf of a client. A single parent with two children making \$7 an hour would be considered slightly below the poverty line at an annual income of \$14,544, but would be eligible for certain benefits that could bring total annual income and benefits to \$28,360.<sup>3</sup> In this example, this family at some point crosses the poverty threshold if the value of these additional benefits is factored into the comparison. While \$7 an hour does not afford a luxurious standard of living, the value of benefits would certainly change the individual or family's economic outlook.

Lastly, references to "poverty" are misleading, even when the percentage relative to the poverty line is included. The meaning of "in poverty"- does not address the difference between being in real poverty and simply fitting into a government determined category. Many programs extend services to people at 150% of poverty because these individuals are considered poor. These individuals are not middle class; however, a person at 150% of poverty exceeds the poverty level by 50% and would no longer be defined as living in poverty. These neatly defined categories often do not account for the \$1 differences between eligibility to ineligibility, and certainly a person is not much better off at 151% of poverty

than they were at 150% of poverty. In addition, even regional differences in Texas mean that while the poverty level is calculated the same, the standards of living at each level can vary widely across the state. It simply costs less to live in Freer, Texas than it does to live in Austin, Texas. Lawmakers should redefine poverty and be prepared to challenge the assumption that poverty is the same for all peoples in every region of the state.

In addition to a clear definition of the poverty level, it is important that evaluation of programs accurately measure success. Particularly in health and human services programs, the state mistakenly measures the success of a program by how many people are served rather than how well the service is rendered. Holding up enrollment numbers for Medicaid, CHIP, TANF, or any of the myriad services the state provides, tells nothing of whether the enrollees have access to doctors, receive sufficient support and direction from the state, or whether the programs appreciably improve the enrollees' lives. These measures also neglect to address whether the state program is the best way to provide or receive services, which allows the state to continue in providing services regardless of whether better alternatives exist. As lawmakers make performance-based budgeting decisions, it is important that success be measured by outcomes and not merely how many people have been put into the system.

Finally, growth in enrollment in health and human services programs is often cited as a major cost driver, which fails to address the fact that much of the growth in enrollment is due to policy decisions that simply expand existing programs. It is misleading to imply that enrollments are simply growing on their own. That is only half of the story, and as the tremendous growth in Medicaid demonstrates, the large cost increases in the Medicaid program coincided with program expansion that increased eligibility with the express purpose of covering more people. It is not the case that Texans are somehow getting poorer and thus needing more state assistance; it is simply that the state has made participation in state programs easier and expanded eligibility to even larger numbers of people.

Too often the preoccupation with creating and expanding state programs in Article II has resulted in public policy that neglects to limit the state to the activities that only the state must fulfill. In evaluating the Article II budget, the specific recommendations often delve into the specifics of programs and agencies; however, it is vital that the Legislature recognize the difference in public policy that allows the state to fill a need that only the state can address and the unnecessary expansion of government in the name of addressing any and every need. It is important that the priorities set in evaluating Article II reflect the attitude that programs that provide state-funded health care is a safety net, not a lifelong, comprehensive health care plan.

## **Medicaid and CHIP**

There is no budget item that affects state budgets more profoundly than Medicaid. It is the second largest ticket item in Texas behind spending on education. Medicaid is an entitlement program, meaning neither the federal government nor the state can cap the number of enrollees or the amount of money available to cover services. The program is considered a state-federal partnership where the federal government sets baselines for what states must cover to participate in Medicaid and provides roughly 60% of the funding and the state covers approximately 40%. The funding split between the state and federal government changes according to a formula called the FMAP, whereby Texas gradually become more responsible for a greater share of the cost of Medicaid over time. While states may have some flexibility in program structure at the state level, the states must cover certain populations and provide federally defined certain benefits.

In Texas, approximately 21% of state expenditures in SFY 2002 were for payments for Medicaid.<sup>4</sup> Texas Medicaid began in 1967. In 1987 it reached \$2 billion, and it grew almost 500% between 1987 and 2001 to reach \$12.3 billion, even while Texans became wealthier and gross state product increased.<sup>5</sup> Texas Medicaid is expected to reach \$14.8 billion in 2003.<sup>6</sup> Increasing costs and caseloads, particularly as a result of Medicaid expansion, are the primary cost drivers to the state.

Interestingly, the TANF program was considered an entitlement program before federal welfare reform through the Personal Responsibility and Work Reconciliation Act (PRWORA) in 1996. Through PRWORA, the federal government transitioned from funding TANF according to the number of enrollees, to a block grant where the state gets a fixed sum regardless of the number of enrollees in the state. This, among other changes such as “work first” requirements and the establishment of time limits on benefits, has made welfare reform a success, even in the face of opponents who claimed it would be disastrous. In fact, according to the Heritage Foundation, since 1996 the national welfare caseload has been cut in half, employment rates of disadvantaged single mothers rose, and the poverty rate among the disadvantaged single mothers dropped by a third.<sup>7</sup> Certainly, the lessons from welfare reform illustrate how ending an entitlement program can be successful and control the costs to the state.

Finally, the CHIP program is not an entitlement, although it is often treated as one. Medicaid cannot limit enrollment into the program to anyone who is eligible, but the same provision is not made in CHIP. The state may consider capping enrollment in CHIP or may consider approving eligibility based on need, but the state should not feel bound by matching CHIP to Medicaid, an entitlement program that continues to take on enrollees regardless of whether the budget can handle the additional enrollment. This proposal may be unpopular to some

as this may mean fewer children are covered under a state health plan, but CHIP is not an entitlement and lawmakers can make decisions either to modify the eligibility or cap the enrollment in the CHIP program altogether.

## **Medicaid Funding**

### **Request block grant of Medicaid funds.**

As recently as 1997, there was talk in Washington, D.C. of “block granting” Medicaid to the states. This would fundamentally alter the operation of the Medicaid program. A block grant would also end Medicaid as an entitlement program, allowing states to set eligibility, asset, enrollment, and per capita spending limits. In return for greater state flexibility, Texas would have to meet some measure of effectiveness and commit to a defined state maintenance of effort. Block granting these funds would allow states to blend funding, avoid costly federal mandates and reporting, simplify administration, tie Medicaid to welfare reform efforts, and save taxpayer dollars.

The one-size-fits-all states approach in the federal Medicaid regulations does not recognize the unique needs of Texas, or any other state, in administering the Medicaid program. It does not account for changes in state financial conditions because it is an entitlement, it does not account for drastic differences in state populations, and it has not effectively provided health care. A Medicaid block grant would allow the state to cover families as a group rather than having Medicaid pay a premium for one child, CHIP pay for another, indigent care for another, and employer insurance for a parent. A block grant would also allow Texas to subsidize employer-sponsored insurance or offer health care tax credits similar to the Earned Income Tax Credit (EITC). Texas has unique needs, and a block grant would certainly provide additional flexibility to improve the state’s ability to design the state Medicaid program to best meet the needs of the state. Importantly, however, is that Texas only pursues a block grant without the federal government’s strings attached. A block grant to Texas should truly provide the state with flexibility to be innovative in administering programs.

## **Medicaid Program Integrity**

### **Amend state law to provide that Medicaid eligibility shall be granted to eligible children for a period of three months upon initial enrollment.**

“Medicaid Simplification,” as it was known during the 77th session, refers to the effort to make the Medicaid enrollment process easier, the eligibility period longer, and loosen eligibility requirements. The specific pieces that made up simplification were:

1. Removal of the assets test for Medicaid recipients
2. Adoption of 12 months continuous eligibility

3. Identical verification and documentation policies as CHIP
4. Elimination of the face-to-face interview

The Legislative Budget Board first estimated that that cost of implementing these policies over a five-year period would be over \$1.3 billion.

In the end, SB 43 from the 77<sup>th</sup> Legislature, the simplification proposal, was modified to contain 6 months continuous eligibility, verification and documentation policies identical to CHIP except as prescribed by federal law, and elimination of the face-to-face interview. The legislation also provided that 12 months of continuous eligibility would be provided after June 2003, unless amended by the Legislature. This was intended to allow the 78<sup>th</sup> Texas Legislature to review the success or failure of the provisions of SB 43 before committing to 12 months of continuous eligibility. Additionally, SB 43 required recipients to go through a Health Care Orientation (HCO) on proper use of Medicaid and to comply with the regimen of care prescribed by the Texas Health Steps Program (also known as EPSDT). Failure to do so would result in a requirement for a face-to-face interview with a caseworker and elimination of other benefits of simplification. The assets test was removed because it would push more children out of CHIP, a program that parents prefer to Medicaid, and back into Medicaid, which many parents regard as welfare. The enrolled version of SB 43 was estimated by LBB to cost \$852 million over five years; it is unclear whether or not the LBB's figure accurately represented the enrollment now being experienced by the Texas Medicaid program as a result of Medicaid and CHIP outreach efforts. HHSC recently estimated that moving from six to twelve months continuous eligibility would cost the state \$322 million.

While the compromise version of simplification included measures such as Health Care Orientation that were designed to ensure that primary and preventive care were not actually encouraged, there is concern that the Department of Human Services is not enforcing the HCO requirement. Furthermore, there is concern that the Department is not verifying income assets during the recertification process. The assets test and income limits are present in Medicaid to ensure that priority is given to those in most need of service and to ensure that Medicaid does not undermine the private health insurance market through "crowd out," in which people drop private insurance in order to receive government sponsored insurance. Unfortunately, the latest numbers provided by the Census Bureau indicate that crowd out is indeed occurring and that despite the massive enrollment of CHIP and Medicaid recipients, Texas has the virtually the same number of uninsured children now as it did when the simplification effort started.

The Health and Human Services Commission has also revised its projected enrollment number for Medicaid and CHIP, and both programs appear to be far beyond what was predicted under SB 43.



In truth, Medicaid simplification did not make more children eligible for Medicaid, it simply allowed for a longer period of enrollment and a looser standard of income and assets limitations. In fact, Medicaid simplification through continuous eligibility may allow some families to stay in Medicaid even once their income increases to a level that would make them ineligible for Medicaid, but eligible for CHIP. In addition, removing means-testing of Medicaid under the guise of “simplification” diverts precious resources from a program that is, has been, and will continue to be in financial distress. While Medicaid should be user friendly, it must also ensure that its recipients are eligible and that limited dollars are prioritized for those most in need. Medicaid should not cover people who are ineligible for its services and simplification should not make it easier to keep people in a program they are ineligible for. Furthermore, this simplification effort does not match the intent of the Medicaid program; Medicaid and CHIP were never intended to be long-term insurance programs, but only a short-term safety net. Providing for continuous eligibility of six months, much less a year, suggests that the Legislature has lost sight of what Medicaid is intended to do, and, in fact, assumes that the state is to become a long-term insurance provider.

State law should be amended to grant Medicaid eligibility to children for an initial period of three months. During the time of initial enrollment, the recipients should be educated in how to access the Medicaid system properly, the health care regimen of Texas Health Steps, the patient’s rights and responsibilities under Medicaid, and the requirements of the program thereafter. After the initial period of three months, recipients will be responsible to verify to the state on a monthly basis that their income and assets have not changed. If a recipient has had a change in income or assets, those changes should be reported so that the state may determine eligibility.

Providing three months continuous eligibility to new applicants will allow recipients to receive an orientation to the system, allow the state to provide educational opportunities on how to access the system, and allow time for the primary and preventive care to demonstrate benefits to the recipient. This will guarantee that those who are eligible for the program are the ones receiving services. In exchange for taxpayer-funded health care, it is not unreasonable that the state ask recipients to verify their income and assets. This process should be made user friendly and notification of deadlines for recertification or renewal can be largely automated.

**Direct the Health and Human Services Commission to apply for a Section 1115 waiver that would allow families to choose between Medicaid and CHIP coverage.**

Furthermore, directing the Health and Human Services Commission to apply for a Section 1115 waiver that would allow families to choose between Medicaid and CHIP coverage allows families some additional choice in their health care. This

proposal would be cost neutral to the federal government as the state would be reimbursed based upon eligibility criteria. That is, the state would receive Medicaid level reimbursement from the federal government if a Medicaid eligible child was placed in CHIP by the child's parents. Arkansas has received permission from the federal government to do so, and Texas should allow its families the same opportunity. Similarly, the state should ensure that families currently enrolled in CHIP are able to maintain CHIP coverage, even if, upon recertification, they are found to be eligible for Medicaid.

**The Department of Human Services should verify income and assets eligibility by using certain information available to third parties.**

The Department of Human Services should verify income and assets by using information available to third parties, such as credit applications, social security tax payments, loan applications, and unemployment benefits applications. Although simplification means less of a burden on the applicant, it does not mean that the state should be obligated to provide coverage without examining an applicant's assets.

**Medicaid Benefits: Pharmaceuticals and Services**

By all estimates, one of the biggest cost drivers in Medicaid is in the pharmaceutical benefits, and increases in this area are primarily attributable to increased utilization, newer and more expensive drugs, and price increases in existing products. This trend is expected to continue as the federal government projects that prescription drug costs will increase an average of 12.6% per year over the next ten years, which would mean expenditures in the state vendor drug program jumping from \$3.1 billion to \$7.6 billion by FY 2010/2011.<sup>8</sup>

Medicaid cost containment can be difficult because of federal constraints on the state programs. With few exceptions, states that cover outpatient prescription drugs under Medicaid must cover all FDA-approved drugs of every manufacturer that has an agreement to pay rebates to states for the products they purchase. More than 500 manufacturers with a combined 55,000 products are covered under the federal rebate agreements.<sup>9</sup> In addition, the federal rebate agreement limits the price negotiation between the manufacturer and individual Medicaid programs. Therefore, the state is not able to simply refuse to cover particular medications to curb utilization, nor is there much room to recoup the cost of providing free prescriptions to Medicaid clients.

**Set a maximum 34-day supply and 4-brand maximum on prescriptions for all Medicaid recipients with exceptions only by doctor authorization.**

In 1971, Texas limited Medicaid drug purchases to 3 prescriptions a month of 180-day supply, which is applicable to TANF mothers not in managed care and to the aged, blind, and disabled who are in the community and not in a waiver

program. Currently, however, nursing home residents and children under 21 are allowed unlimited prescriptions, and Texas also requested a federal waiver to make prescriptions unlimited to Medicaid recipients who are in managed care.

Twenty-six states and most private payers limit prescription drug day supplies to minimize the waste that occurs due to changes in drug therapy, poor tolerance of the medication, or discontinuation of the medication.<sup>10</sup> Florida was able to dramatically reduce pharmaceutical costs by limiting brand-name drug purchases to four per month. Florida has set a 34-day/4-brand limit on prescriptions for their Medicaid recipients, excluding children and institutionalized adults. Florida's FY 2000-01 savings was \$70 million.<sup>11</sup> Commercial health plans most commonly allow a maximum of a 30-day supply.

Texas should set a 34-day supply and a 4-brand maximum on prescriptions for all Medicaid recipients, with exceptions only for doctor authorization. Repeal the current limitations of 3 prescriptions a month, 180-day supply. Cost savings of four brand and 34-day supply limitations were estimated by HHSC, in early 2002, at \$25 million annually; however, since their original estimation, HHSC has said that the estimated savings would be significantly less than originally expected. In Texas, pharmacists are required to substitute a generic drug for a brand name if a suitable generic is available. HHSC has estimated that a generic drug is dispensed 99% of the time when it is available.

#### **Pursue additional cost savings through Medicaid co-payments for emergency room visits and prescription drugs.**

With certain limitations, federal regulations give states the authority to devise a system of co-payments that encourages the use of generic drugs. Co-payments cannot be more than \$3. The drugs must be dispensed regardless of whether the client is willing or able to pay, and states may not impose co-payments on children, pregnant women, people in institutions, or people receiving either emergency services or family planning services.<sup>12</sup> However, states may request a waiver to increase the amount of the co-payment and to extend the co-payment requirements to the federally excluded categories of people.

States realize cost savings through co-pays primarily by reducing the reimbursement to providers, as well as by redirecting clients away from costly, brand name drugs and inappropriate emergency room use. At the prospect of the reimbursement reduction, many providers have voiced concerns about their ability to collect a co-payment and what the reduction will mean for their business. However, an HHSC survey of states with ER and medication co-pays shows that many states reduce the provider reimbursement by the entire co-pay amount, but no state reported a negative effect on provider participation as a result.<sup>13</sup>

The Medicaid Cost Containment Rider 33(k) of the General Appropriations Act for 2002-2003, requires the Health and Human Services Commission to implement a co-pay system in an effort to find cost savings in Medicaid. To meet this directive, HHSC convened a workgroup to discuss the co-payment issue, and submitted a co-payment plan to the Medical Care Advisory Committee (MCAC) that is now in effect, and submitted a more aggressive co-payment proposal to the Centers for Medicare and Medicaid Services (CMS) that was recently declined.

The Cost Sharing Workgroup submitted a preliminary report in April 2002 acknowledging that they were philosophically opposed to any co-payments for Medicaid, but nevertheless explored some options and made recommendations as directed. According to the report, the group considered establishing co-payments either by an enrollment fee, or at the point of service for emergency rooms and brand-name drugs. Though the workgroup maintained their opposition to any co-pays, it preferred implementation of an enrollment fee because it is unrelated to the delivery of services.<sup>14</sup>

As illustrated below, the co-pay proposal approved by the MCAC and the proposal submitted to CMS are similar in structure, but the proposal to CMS has more aggressive terms that cannot be implemented without a federal waiver. Despite slight wording changes, the two proposals in effect require co-payments but cannot enforce nor deny service to anyone unable or unwilling to pay. However, in the co-pay system approved by the MCAC, hospitals and pharmacies may bill for unpaid co-payments and request payment for unpaid co-payments from previous months.<sup>15</sup>

Proposal	State Fiscal Year	% of Federal Poverty Level	ER Services	Generic Medications	Brand Name Medications
MCAC	Starting 2002	All	\$3.00, Non-Emergency services	\$0.50	\$3.00
CMS	2003	All	\$3.00	\$0.50	\$2.00
	2004-2005	≤ 100%	\$3.00	\$0.50	\$2.00
		101%-150%	\$5.00	\$0.50	\$3.00
		≥ 151%	\$20.00	\$0.50	\$5.00

The expected savings resulting from each of the co-payment plans would differ as the plan is phased in, as follows:<sup>16</sup>

**Estimated Savings in General Revenue from Medicaid Co-payment Policy  
(without requiring a federal waiver)**

Service Type	FY 2003 GR Savings	FY 2004-2005 GR Savings
ER Services	\$200,000 GR for each 1% reduction in ER use.  No reduction in provider reimbursement.	\$400,000 GR for each 1% reduction in ER use.  No reduction in provider reimbursement.
Generic and Brand Name Medication	\$1.5 M for GR for each 1% redirection away from Brand Name Drug.  \$3.9 M GR from reductions in provider reimbursement.	\$3.6 M GR for each 1% redirection away from Brand Name Drugs.  \$9.5 M GR from reductions in provider reimbursement.

**Estimated Total Savings from Medicaid Co-Payment Policy,  
Submitted to the Centers for Medicare and Medicaid Services**

<b>Service Type</b>	<b>SFY 2003 Total Savings</b>	<b>SFY 2004-05 Total Savings</b>
Emergency Services	\$1 M for each 1% reduction in ER use.  No reduction in provider reimbursement.	\$2.25 M for each 1% reduction in ER use.  No estimates available for savings from reduction in provider reimbursement.
Generic and Brand Name Medication	\$9.5 M for each 1% redirection away from Brand Name Drugs.  \$17.5 M from reduction in provider reimbursement.	\$21.25 M for each 1% redirection away from Brand Name Drugs.  \$46.5 M from reductions in provider reimbursement.

It is important to note that each of the above charts shows savings in different figures, the top chart shows the savings in GR and the bottom in Total Savings, which includes the federal government's contribution of around 60% of the total. Furthermore, it is also important to note that under the first proposal, the savings in GR for FY 2003 were based on expected implementation in fall 2002 to be in place for ten months; however, implementation of the program is slightly behind schedule and was scheduled to begin in mid-December 2002. Information provided by HHSC regarding the co-payments says that as directed by the 77<sup>th</sup> Legislature, the commission has found ways to save \$205 million in the Medicaid program.<sup>17</sup> However, total savings for the plans is difficult to determine as the reduction in inappropriate usage is not easy to project.

These co-payments have become a necessity in containing the costs of Medicaid. Medicaid clients have no incentive to control costs when all of their services are absolutely free, and providing these services without charge assumes that they have absolutely no means to participate in sharing the cost of their health care. The best way to achieve cost savings in Medicaid is by giving clients some ownership of their health care thereby inducing sensitivity to their health care costs, and as their ability to pay increases their portion of their health care costs also increases. The current system not only insulates these clients from the cost of their health care, but also provides no preparation for the time they assume the entire cost of their health care when they move off of Medicaid. In attempting to address utilization, the simple co-payment or enrollment fee to enter the Medicaid program is useless as once the initial payment is made the client has no reason to be sensitive to the cost of their medical care. The objective in collecting co-payments is not to make money, but it is an attempt to control increasing costs resulting from inappropriate utilization. In an effort to control costs, somewhat more than half the states currently have some form of cost sharing for prescription drugs through the use of co-payments.<sup>18</sup>

The state should continue to pursue a waiver for the federal regulations that immediately exclude 82% of the Medicaid population from cost sharing programs, groups such as women, children, or people in institutions.<sup>19</sup> In determining eligibility, the categories are divided not by who is most able to pay, but by characteristics all clients in the group share, such as gender, medical

needs, or age; however, this neglects to recognize that regardless of these characteristics each of these categories can further be divided by income and ability to pay. It is not unreasonable to expect that a client, whether a pregnant woman or an elderly individual, be asked to pay for their services. Additionally, the federal poverty level has more than doubled since the federal co-payment regulations were adopted, making the \$3 maximum co-pay an antiquated figure.<sup>20</sup>

Texas' goal should be to enact responsible reforms to the delivery of Medicaid, including the establishment of a Medicaid co-payment policy. While federal constraints limit the range of an allowable co-payment but allow the state to make a good first step, the state must continue to pursue the proposal sent to CMS. Furthermore, any proposal for a waiver should include an aggressive effort at reducing inappropriate utilization, should mirror the co-payments required in private plans as much as possible. In the proposal to CMS and in the plan approved by the MCAC, the co-payment for generic drugs remains at \$.50 regardless of income. The co-payment policy can increase the recipient's share of the cost as income increases, and still discourage any inappropriate use of brand drugs over generics. By simply increasing the co-payments by fifty cents at each tier in income, to \$.50, \$1.00, and \$1.50, the total savings for prescription drugs under the co-payment policy proposed to CMS for prescription medication would increase by \$2.5 million for 2004 and \$2.6 million for 2005 all funds."<sup>21</sup> This more aggressive approach not only results in additional cost savings to the state, but also better reflects what the private market requires once the client is no longer on Medicaid.

Opponents to the proposals argue that co-payments create a barrier to service, but CHIP has both enrollment fees and co-payments for service, yet enrollment figures suggest that co-payments do not deter participation. Additionally, where income levels are equal between CHIP and Medicaid enrollees, CHIP clients may be responsible for an enrollment fee as well as co-payments for the ER and for brand name drugs, both of which the Medicaid client receives for free. With CHIP enrollments over half a million children, there is no indication that co-payments present a barrier to service or a deterrent to medical care.

**Reduce the coverage of pregnant women and infants in Medicaid to the federally mandated levels.**

According to federal requirements, Texas must cover pregnant women and infants up to 133% of poverty and has an option to extend this coverage to 185% of poverty. Texas exercises the option to cover pregnant women and infants up to 185% of poverty. Of the pregnant women covered under Texas Medicaid, 17%, or 12,354 women fall into this optional population.<sup>22</sup> Texas spends \$41.8 million in General Revenue, or \$105.1 million All Funds, to cover only this optional population.<sup>23</sup> Staggeringly, as a result of this expanded coverage,

Medicaid covers half of all births in the state of Texas at an annual per capita cost of \$4,072 (FY 2000).<sup>24</sup>

Under the current structure, Medicaid provides coverage for any pregnant woman meeting the income eligibility guidelines without regard to age. By limiting coverage to the federal minimum for women over 18, the state would take 85.8% of the optionally covered pregnant women off the state's Medicaid rolls. Simply reducing the general revenue used to provide services to the

optional category of pregnant women by the reduction in eligible clients, could reduce state funding for this program by approximately \$35.8 million.

Medicaid covers half of all births in the state of Texas.

*Source: HHSC, Texas Medicaid in Perspective, 4<sup>th</sup> Edition.*

There are no federally mandated categories that require Medicaid coverage over 133% of poverty. The federal government has effectively said that nobody, not even children, with a household income over 133% of poverty is entitled to Medicaid services. Accordingly, the state should expect pregnant women over this federally established threshold to bear responsibility for the birth of their child, just as they would any other medical service. To be sure, this policy recommendation is not to suggest that prenatal care is a luxury or to minimize its importance, however non-profit and community resources that provide assistance to pregnant women are available to the pregnant women that are truly in need. Furthermore, pregnant women in this category would likely qualify for services from the family planning program under Title X. Immediately upon birth, the infant would be covered under Medicaid or CHIP, depending on family income, providing care to the baby once born.

### **Institute a system of co-payments for optional Medicaid services.**

Medicaid, like any private health insurer, has a list of services that the state is not required to cover. Most services in this list are not deemed to be medically necessary and are not preventive in nature, and many are provided at significant cost to the state. These services are a factor in the increasing cost of Medicaid and money available for care that is not medically necessary should be well guarded. By charging co-payments on these optional services, the client chooses how important these services are by how willing they are to share in the cost of the medical extras.

Co-payments for these services would be similar to out-of-network benefits, as provided by private insurance. The goal of co-payments, like the goal of co-payments proposed to ER visits and medications, is to introduce cost sensitivity and discourage inappropriate utilization. Structuring the co-payment system for optional services like the co-payment system for medications and ER visits would

hopefully result in the same types of savings, first by better utilization and then additionally, perhaps by reductions in provider reimbursement.

Using the federally established maximum for co-payments at \$3, Texas could require a \$3 co-payment for optional services currently covered under Medicaid to realize a \$27.1 million savings for all funds. This does not take into account any savings potential from reducing provider reimbursement. Again, \$3 is truly a nominal amount, and because these services are not considered medically necessary, clients should be responsible for deciding how valuable the service is to them.

Any opponent to such a system should be reminded that if we continue on the path of giving free medical care away without regard to cost, the time is fast approaching when the state will no longer be able to afford to provide this coverage. A nominal co-payment for these optional services is surely more bearable than discontinuing these services altogether.

### **CHIP Cost Sharing**

#### **Increase CHIP premium sharing and co-payments for emergency rooms and generic and brand name medications.**

The Children's Health Insurance Program provides health insurance to children under the age of 19, with household incomes below 200% of the federal poverty level, and who are not Medicaid eligible. CHIP enrollees receive health and dental care through a sliding scale, cost sharing program. Depending on income level, CHIP enrollees may pay an enrollment fee, a monthly premium, as well as traditional co-payments on office visits, emergency room use, generic and brand name drugs, or inpatient admission to a facility. CHIP also caps enrollee cost sharing at either \$100, or 5% of the family's net income, depending on household income.<sup>25</sup>

In March 2002, HHSC reduced the co-payments for generic drugs in CHIP to \$0 and \$5, depending on income level. Due to the implementation of co-payments in Medicaid, the generic co-pay for Medicaid clients will be \$.50. Obviously, HHSC will have to consider re-raising the co-payment in CHIP so the two plans are equitable. HHSC should not only raise the CHIP co-payment, but it should raise it higher than \$.50.

Just as a \$0.50 co-payment is low in Medicaid; it is also low in the CHIP program. Furthermore, when the state has the flexibility to set reasonable co-payments in the CHIP program, it should take advantage of that and set realistic rates that come closer to the actual cost while still providing the service at low cost. Even with the present system of cost sharing in CHIP, utilization exceeded expectations in prescription drugs and other services by an average of 25%.<sup>26</sup> These continued increases in utilization suggest that there is still room to change



inappropriate utilization patterns, particularly in relation to prescription drug use. Co-payments on generic medications should be increased to better tier the enrollee's cost relative to income, and should not be offered at no cost.

At each of the four income levels used to increase cost sharing, the emergency room co-pays are \$3, \$5, \$50, and \$50. These co-payments should be restructured to provide gradual increases at each level and structure a meaningful system of cost sharing for these services. Furthermore, charging \$5 for an emergency room visit and \$2 for an office visit for clients between 101 and 150 % of poverty is such a negligible spread that preventive care through an office visit does not come at substantial enough savings to discourage inappropriate ER use.

Enrollment fees are applied to CHIP clients beginning at 101% FPL, and monthly premiums are added at 151% FPL. Monthly premiums simulate the cost of health insurance outside of a government program, and require CHIP enrollees to budget for their health care coverage as a priority. CHIP enrollees should incrementally increase their responsibility in cost sharing in preparation for providing their own health care coverage without CHIP.

## **Pharmacy Benefits Management**

**The state should contract with a Pharmacy Benefits Manager to administer the drug benefit in the Texas Medicaid program.**

Pharmacy Benefit Managers (PBMs) administer drug benefit plans for employers and health insurance providers and today serve almost 190 million people and manage about 70% of the more than 3 billion prescriptions dispensed each year.<sup>27</sup> PBMs are widely recognized as an effective method for reducing the cost of offering a drug benefit by negotiating price discounts on pharmaceuticals, using formularies to encourage doctors to prescribe those drugs with the best value, providing drug utilization and review, and clinical services using a disease management model to control long-term costs. These programs have been so successful that nearly 85% of Fortune 500 companies use PBMs to administer their drug benefits.<sup>28</sup>

#### Pharmacy Benefit Managers...

- Reduce administrative cost through electronic processing of claims at the point of service. Over 99% of pharmacy claims are processed this way, at an average cost of \$.30 to \$.40 per claim.
- Receive pricing discounts from dispensing pharmacies, and rebates from manufacturers. The cost of prescriptions averages \$60.00 and can be reduced 30%-35% with a PBM.
- Manages utilization and favors lower cost medications by using clinical services to influence the behavior of physicians, pharmacists and patients.

*Source: Centers for Medicare and Medicaid Services, Study of Pharmaceutical Benefit Management, June 2001, p 5.*

The Texas Medicaid program currently has a drug utilization and review process in place; however, allowing a PBM to manage the program's drug benefit and conduct the utilization reviews would potentially help the state save millions of dollars in the Medicaid program. The state should take advantage of the PBMs ability to leverage better prices for pharmaceuticals and turn the drug utilization review (DUR) process over to a PBM as well. The fact that PBMs adjudicate around 2 billion claims a year is evidence that they can efficiently deal with a high volume of claims.<sup>29</sup> Furthermore, client surveys and the large number of people that PBMs cover is a reflection not only of their success, but also of the PBMs successful business practices that balance client satisfaction with the efforts to contain costs.

The current drug benefit in Medicaid attempts to ensure appropriate utilization and control costs, but cannot

be as effective as a PBM as the state has outside interests that pressure it to run inefficiently. The success of PBMs shows that there is a more efficient way to deliver this service. By essentially privatizing this activity, the state can demand cost containment, and offers an opportunity to competitively award the PBM contract to those companies that can best meet the state's needs. Under the current situation, the state has no competition to encourage the most efficient delivery of a drug benefit, nor has the state been able to establish effective methods to contain costs. PBMs offer a range of services, including home delivery, choice of pharmacies, patient education through disease management programs and physician education through use of preferred drug lists managed by the PBM, audit services to prevent fraud and abuse, and utilization review.

## Disease Management

### **Introduce a disease management program in the Texas Medicaid program.**

The general rule in health care is that 20% of the people spend 80% of the money, or rather that a small number of very sick patients are responsible for an inordinate amount of the costs. The Texas Medicaid program bears proof of this in Texas as the aged, blind, and disable recipients constitute a small percentage of the Medicaid population (24%) and account for a large proportion of the dollars spent (65%).<sup>30</sup> While long-term care patients have traditionally been the biggest users of health care in Medicaid, there is a burgeoning new category of Medicaid recipients afflicted with chronic illnesses that require considerable medical attention. These patients are very costly to treat, in part because their illnesses are often left untreated or unmanaged and resulting in costly trips to the emergency room rather than a less expensive office visit. In fact, some studies have shown that Medicaid patients are more than twice as likely as non-Medicaid patients with the same type of illnesses to be admitted to the hospital via the emergency room because of an acute event. The majority of these hospitalizations are, in theory, controllable through the use of preventive care and disease management.

Managing disease is particularly important in the Medicaid program as it is an effective way to contain cost to the state by better delivering health care through management of chronic illness. A cursory look at the Texas Medicaid program shows that about 280,000 recipients, or 9% of the total Medicaid population, have asthma, diabetes, heart failure, or a combination of the three. These three illnesses, as well as hypertension, are among the most prevalent chronic illnesses, yet are also the most manageable. Disease management puts the state on the offensive in tackling chronic illness, and works to avoid costly treatments when chronic illnesses go untreated.

In the months since the Pfizer program began in Florida:

Forty-five percent of patients have improved their blood pressure scores.

Thirty-nine percent of bedridden congestive heart failure patients have shown improvement over the course of the program.

About fifty percent of asthma patients now use their peak-flow monitors at home, compared to only twenty-five percent at the beginning of the program.

Source: "Florida's care pact with Pfizer saving millions", Karen Pallarito, Reuters Health Information, November 27, 2002.

### The Pfizer Plan in Florida

- **Identify Candidates:** As Pfizer found, this can be an expensive proposition as Medicaid clients move, disconnect phones, have language barriers, and other obstacles that are unique to that population. According to Pfizer: up to 40% of the contact numbers provided by the state of Florida were incorrect.
- **Assess Patients:** Determine the severity of the disease, how the patient's life is affected by it, and if they are complying with any prescribed regimen of care.
- **Set Treatment Goals:** Determine how disease management can improve the health and quality of life for patients.
- **Develop Plan:** Develop a regimen of care for each patient.
- **Monitor Participation:** Ensure that patients are complying with their regimen of care and ensuring that medications and care are appropriate.
- **Patient Education:** Prepare patients to be more self-sufficient in managing their disease on their own.
- **Referrals:** Ensure that specialty care is available and that patients are able to establish relationships with primary care physicians.

Critics of disease management contend that such programs do not work and they are nothing more than a government handout to pharmaceutical companies looking to increase their market share. However, pharmaceuticals like Pfizer are so confident that disease management can save the state money they are guaranteeing it with their own money. Washington State negotiated a contract with three pharmaceutical companies that will guarantee a 5% savings and Florida made headlines with its agreement with Pfizer that guarantees savings of \$33 million over two years. In addition, Pfizer is paying all of the start up costs associated with

the program.<sup>31</sup> Pfizer is convinced that the company will save the state money by helping clients avoid hospitalizations and unnecessary emergency room use.

While treatment of illnesses such as diabetes now allows patients to live a more normal life, the explosion of children now afflicted with diabetes, especially in the Hispanic population, demands educated patients prepared for a lifetime of managing their disease. While Medicaid is not intended to be a long-term insurer, and a disease management program in Medicaid might imply otherwise, it is important that the Medicaid clients get started in the right direction of managing chronic disease. Much of the Medicaid population faces greater barriers to managing disease than much of the state at large, and dedicated efforts to manage disease may not only allow the state to realize costs savings in the near term, but also in the long term as more people are better equipped to manage illness on their own. To reach this end, Texas should institute a disease management program in the Texas Medicaid program and target those populations with the most prevalent and manageable chronic illnesses such as

diabetes, heart problems, hypertension, asthma. Furthermore, the state should attempt to leverage its huge Medicaid population to secure an agreement similar to the agreement in Florida, by allowing a pharmaceutical company the opportunity to run a disease management program and assume the risk for proper management and guarantee the savings.

## **Estate Recovery**

### **Develop an estate recovery system in the Texas Medicaid program.**

Estate recovery is the process by which the state, as the provider of Medicaid benefits, seeks to recoup its expenses by recovering funds from the estates of Medicaid recipients when they die. While estate recovery was optional for states prior to 1993, the Omnibus Budget Reconciliation Act of 1993 (OBRA 93) amended federal law to mandate that all states engage in estate recovery. States are still permitted wide latitude when determining what assets shall be recovered and which recipients are subject to estate recovery. For instance, a state could decide that it would not subject an estate to recovery if it was valued under \$20,000, or it could limit estate recovery to recipients who received benefits for longer than a specified period of time. This allows state to determine whether or not it is cost effective to recover assets or whether and estate's value does not merit recovery.

While estate recovery is mandated by federal law, Texas is the only state in the country that has yet to establish an estate recovery program.<sup>32</sup> Although it has not been an issue to date, there is little question that the federal government could limit reimbursement to the Texas Medicaid program, or remove it altogether, if the state does not comply with the law. The Texas Legislature did pass legislation in the late 1980s that allowed for a lien to be filed against the property of individuals in order to collect repayment of the cost of Medicaid benefits, but the law was repealed the following session before it was ever implemented. A 1995 letter opinion by the Office of the Attorney General ruled that the Health and Human Services Commission (HHSC) could not pursue Medicaid estate recoveries absent express statutory authority.<sup>33</sup>

The exact amount of money that could be recouped by the state through Medicaid estate recoveries is unknown, but the state does know that a large number of individuals with income sufficient enough to make them ineligible for Medicaid have used Miller income trusts as a method of obtaining Medicaid eligibility. Furthermore, a number of seniors may be "cash poor" since many live on fixed incomes, yet "land rich" as they own their land. State data indicates a wide discrepancy between the success of estate recovery programs based on the parameters set by the state Legislature and the efficiency and aggressiveness of the various state agencies responsible.

Texas has relatively generous income limits for long-term care in its Medicaid program. Eligibility is set up to 300% of the SSI Federal Benefit Rate (\$1635/month) and individuals can become eligible by spending down their income to the eligibility level. Because long-term care constitutes such a large portion of Texas' Medicaid budget, it make sense for the state to recoup as much of that expense as possible. Furthermore, the presence of an aggressive estate recovery program in Texas may persuade those moving assets and income to become eligible for Medicaid to pay for private long-term care rather than forcing taxpayers to do so.

Texas should comply with federal law and establish an estate recovery program so as not to jeopardize federal funding for Medicaid. A proposal at the federal level designed to increase the purchasing of long-term care insurance uses estate recovery as a tool to encourage people to purchase long-term care insurance. However, there are a variety of ways the state can create an estate recovery system.

Upon the death of a Medicaid nursing home patient, or other long-term care patient, the Department of Human Services could work in conjunction with the Office of the Attorney General (OAG) to recover expenditures through the use of a Medicaid lien. The Legislature should determine what, if any, assets will be protected or what estate value will initiate the recovery process. Again, states have tremendous latitude in designing estate recovery programs.

The Department of Human Services could also perform an estate valuation upon entry of a resident into long-term care services, whereby the state would subtract the yearly value of Medicaid services from the estate value and then recoup that amount after the recipient dies or at the sale of the estate. Again, the state could cap the amount to be recaptured or protect a certain portion of the estate (a homestead exemption of sorts).

The state could mandate the purchase of long-term care insurance or demonstration of financial responsibility by all individuals at age 50. Those without private coverage would then be allowed to access services through Medicaid with the understanding that their estate will be subject to recovery. This ensures that those who are financially able will purchase long-term care insurance, while those who lack the resources will still have access to long-term care.

### **State Kids Insurance Program (SKIP)**

#### **Eliminate the State Kids Insurance Program and return the funds to General Revenue.**

The State Kids Insurance program (SKIP) was created in 1999 as an alternative to the Children's Health Insurance program (CHIP) for the children of state

employees. Children with access to certain types of health plans, like those offered by the Employees' Retirement System (ERS), are not eligible for CHIP. In an attempt to provide similar benefits to state employees at income levels similar to the parents of CHIP children, the state subsidizes the cost of dependent coverage. Cost-sharing and eligibility requirements are identical to CHIP. Unlike CHIP which has a 3-to-1 federal match rate, the SKIP program is entirely state funded with General Revenue (GR). SKIP enrollment is approximately 19,000.

CHIP was intended to provide health insurance to low-income, uninsured children. Children with access to state health plans like ERS were specifically excluded to prevent "crowd-out." In fact, SKIP has primarily served as a pay raise as virtually every child enrolled in SKIP was participating in the ERS health plan prior to SKIP.

Children of state employees were excluded from CHIP for very good reason. It is obvious that the majority of parents with children covered by SKIP saw dependent coverage as a value. The state is subsidizing health coverage for a population that already has access to comprehensive and affordable insurance.

## **HHSC Riders**

### **Repeal certain riders from the 77<sup>th</sup> Legislative Session.**

The following four riders were passed during the 77<sup>th</sup> Legislative Session and should be eliminated:

- Rider 20- Women's Health Services Demonstration Project
- Rider 21- Mental Health Services Demonstration Project
- Rider 23- Medicaid Buy-in Pilot Project
- Rider 24- Voluntary Medicaid Demonstration Project

These riders were passed as a part of the largest budget in state history and are only a few of the "extras" that contributed to the tremendous increase in the budget between 2000-01 and 2002-03. These demonstration and pilot projects become new programs that the state simply cannot afford and contribute to the growth of government and government programs. They are unnecessary and should not be funded in the next budget.

## **Nursing Home Liability**

**Enact meaningful tort reforms by placing a cap on exemplary damages and remove DHS from nursing home supervision in favor of private accreditation.**

Liability insurance rates have increased tremendously during the past five years. Survey data from nursing homes indicates that liability rates have tripled to nearly \$2,000 per bed, with some nursing homes reporting increases of up to 1000 %. Nursing home operators contend, and the Texas Department of Insurance data confirms, that litigation is the primary driver. Much of the litigation involving nursing homes is not subject to caps set on exemplary damages by the Texas Legislature in 1995. As such, the average amount of a claim involving a nursing home in Texas is nearly five times the national average.

Exacerbating the litigious environment is the current policy set by the Texas Legislature, embodied in SB 190 from the 75<sup>th</sup> Legislative Session. SB 190 established a number of regulations affecting the operation of nursing homes, the most significant of which involved the contents and access to survey reports used by the Department of Human Services (DHS). Prior to SB 190, survey reports were not available upon request, but SB 190 changed state law to provide open access to these reports, which are cited by TDI as a major reason for the liability insurance crisis facing nursing homes.

During the 77<sup>th</sup> Legislative Session, the Legislature passed SB 1839 in order to provide relief to nursing homes. SB 1839 included a number of provisions including:

- new language on the admissibility of survey reports and certain evidence in civil actions,
- expansion of eligibility in the Joint Underwriting Association (JUA) to for-profit nursing homes,
- exemption from exemplary damages for the JUA (the insurer of last resort), which applies without regard to the common law theory of recovery known in Texas as the “Stowers Doctrine”,
- a list of best practices for risk management and loss control for nursing homes which insurers may use when setting liability rates for homes, and
- a requirement that all nursing homes carry liability insurance, currently optional, by September 2003.

Since passage of SB 1839, the situation in Texas has worsened as liability rates have increased while the number of insurers has decreased. According to TDI, only seven insurers are still writing policies in Texas with five of them being surplus line companies and the other two being niche marketers (one writes only for hospitals and associated facilities and the other only for church related facilities). TDI also expects that rates will increase another 60 to 100% and that as many as 70% of nursing homes may choose to go without liability insurance coverage.

The prospect of nursing homes going without liability coverage is dangerous. Without coverage it is entirely possible that one settlement could bankrupt a nursing home, which would cause access to care problems. Additionally, it is not



good public policy for nursing home operators not to be vested in the nursing homes. Liability coverage is purchased as part of an investment in the operation and while going without it is a significant cost saver for operators, it also allows them to pull out of operation more quickly.

The cost of liability insurance rates also means that every dollar that goes to insurance is a dollar that does not go to medical care, increasing the likelihood that lawsuits will be filed for poor care or negligence. Limiting exemplary damages would immediately impact liability insurance rates and TDI estimates that a \$1 million limit would allow for a significant decrease in rates. In addition to freeing more dollars for medical care, it would also promote stability in the insurance market and allow insurers to re-enter the market and encourage competition.

The vast majority of nursing homes in Texas are classified as Tier II, on a scale of I to V with V being the worst. While they have a few claims filed against them, no major deficiencies, and provide outstanding care, these homes still feel the impact of jury awards against poor homes because those cases set the baseline for possible liability. Simply put, if nursing homes cannot make money or avoid being sued, they will cease to operate, leaving an uncertain future for the increasing number of Texans who will need long-term care. Meaningful tort reform is needed simply to allow homes to stay in business and continuing to offer care.

## **Medical Malpractice**

**Texas should enact legislation similar to California’s Medical Injury Compensation Reform Act (MICRA) and take certain additional steps to address the medical malpractice problems.**

Like nursing homes, doctors in the state of Texas are facing rising liability insurance rates and increased litigation. Litigation has been targeted as the number one culprit in the malpractice crisis and doctors point to the fact that 52% of doctors had claims filed against them in 2000 and one out of four doctors was sued. Particularly disturbing is the fact that the vast majority of claims (80-85%) are dismissed with no payment to the plaintiff. While many of the claims lack merit and do not constitute instances of malpractice, the claims still take time away from a physician’s practice and still cost money

“Litigation has been targeted as the number one culprit in the malpractice crisis and doctors point to the fact that 52% of doctors had claims filed against them in 2000 and one out of four doctors was sued. Particularly disturbing is the fact that the vast majority of claims (80-85%) are dismissed with no payment to the plaintiff.”

to defend. In fact, the average cost of settling a claim, not including the amount of any settlement or award, has jumped from \$46,000 in 1995 to \$68,000 in 2000. Unlike many professionals, doctors are not able to simply pass their costs along to their clients. The majority of business for doctors comes through managed care, which involves a pre-negotiated fixed rate of reimbursement, or through a public payer like Medicaid, Medicare, or CHIP, which involves a set payment. For many physicians the choice is either to reduce the number of procedures they perform in order to keep liability rates affordable, or turn away patients; neither is an attractive solution.

Malpractice insurance rates have jumped substantially over the last few years with some specialists experiencing increases up to 300% in just one year. These increases are in part a result of the increased number of claims, but also a result of increased jury awards, cost of settlements, reduced access to reinsurance by malpractice carriers, and increased scrutiny of medical errors. Certainly, the malpractice crisis is not solely about affordability, but availability as well. The number of malpractice insurers authorized to operate in Texas has dropped from 17 to 4 within the last year. Also tellingly, the number of doctors covered through the JUA, the insurer of last resort, has gone from 168 in 2001 to 592 through April 2002, to approximately 1000 as of August 2002. While doctors are not required to carry malpractice insurance, it is generally a requirement of managed care plans and hospitals, which makes it a virtual necessity for doctors.

While doctors around the state face increasing risks of having claims filed against them as well as increased malpractice insurance, the situation is more severe in certain pockets of the state. For example, the frequency of claims runs 40 to 60% higher in the Valley than in the rest of the state, and 70% of the doctors in the valley had claims filed against them. Certainly as doctors become more concerned about the possibility of claims filed against them coupled with malpractice insurance hikes, doctors may respond by choosing to drop out of the field or may refuse new patients, both of which create access to care problems. The Texas Medical Association projected that as of October 1 there would be no doctors from Del Rio to San Antonio to deliver babies. Additionally, there is only one pediatric neurosurgeon operating south of San Antonio. Certainly, as the state looks to doctors to provide medical care around the state, the proliferation of claims and the increased risk and cost to doctors' means that many doctors may not choose, or be able to afford, to maintain their medical practice.

Medical malpractice not only increases costs for doctors, but for the health care system as a whole as well. An April 2002 study surveyed physicians to reveal how often they act in anticipation of possible lawsuits and found that 79% of physicians surveyed said that they had ordered more tests than they would normally see necessary, 74% referred patients to a specialist more often than they would, 51% recommended invasive procedures like biopsies to confirm diagnoses, and 41% said they had prescribed more medication than they would have normally judged necessary.<sup>34</sup> Certainly, some of these services are

supported by taxpayer dollars as the government pays for some health care through programs like Medicaid, which are funded by tax dollars. The federal government estimates that the impact of medical malpractice and defensive medicine for government-paid health care increase costs by \$28.6-47.5 billion per year.<sup>35</sup> Additionally, the government estimates that if reasonable limits were placed on non-economic damages to reduce defensive medicine, it would reduce the amount of taxpayer dollars the federal government spends by \$25.3-44.3 billion per year.<sup>36</sup> Texas, like the federal government, bears part of the cost of providing health care in a litigious climate. Medical malpractice is more than a policy issue, it has a fiscal impact to the state as well.

California's Medical Injury Compensation Reform Act (MICRA) has been universally recognized as the model for medical malpractice reform. Using this as a model for Texas' reforms, the Texas Legislature should look to:

- **Placing a hard cap on non-economic damages.** Non-economic damages typically encompass things like pain, suffering, and loss of consortium, damages that are not only hard to quantify but can vary greatly when juries make these awards. There is no cap on economic damages and patients will still be entitled to recover that which they are entitled to. The challenge to the cap on non-economic damages is that in order to uphold the open courts doctrine, the legislation must carry a quid pro quo for patients, though this could be achieved by requiring doctors to carry malpractice insurance.
- **Collateral source reform.** Texas juries are not allowed to hear about other sources of payment that a plaintiff might have access to, such as disability insurance. It would be beneficial to provide this information to juries so that they can accurately determine what is necessary to make the person whole.
- **Limiting contingency fees.** California allows attorneys in medical malpractice cases to collect 40 % of the first \$50,000, 33 1/3% of the next \$50,000, and 15% of any payment that exceeds \$600,000. Limits on contingency fees would help to decrease the frequency of claims as attorneys would be forced to evaluate the merits of a claim before investing time in pursuing the claim.
- **Limiting when a minor can bring suit.** In Texas, malpractice claims must generally be brought within two years of the breach or from the completion of treatment. However, if the claim involves a minor it can be brought any time before the minor's 20<sup>th</sup> birthday. This effectively means that doctors are responsible for their patient 20 years after the treatment. MICRA limits actions on behalf of minors to three years from the date of the act or prior to the child's eighth birthday in cases involving a child under the age of six.

- **Periodic payments for future damages.** This provides that any economic damages awarded to a plaintiff should be awarded over time as needed. An individual that dies earlier than expected should not receive an award that was based on what would be necessary for an individual's entire life. This reform ensures that care is provided when needed, but allows the dollars to remain "in the system" if they become unnecessary. This provision of the California law as been pointed to as one of the most successful and should be included in any reform effort made in Texas.
- **Good Samaritan Law.** The law as written has been misinterpreted by courts and is thus ineffective. Other state have crafted Good Samaritan legislation around the duty of the doctor to provide emergency care, while Texas courts have interpreted the statute to require that a physician demonstrate prior to treatment that they expect no payment.
- **Judicial discretion.** One of the biggest sources of contention in Texas has been the claims by doctors that judges have waived statutory requirements that expert witness affidavits be filed within 180 days and that expert witnesses meet certain standards. Removing the authority of judges to waive these requirements should also be considered.
- **Arbitration/Special Courts.** Doctors are not allowed to request, let alone require, patients to sign any agreement that would require arbitration unless it is signed by an attorney representing the patient prior to treatment. Arbitration has worked well in other areas and is usually overseen by individuals who are experts in certain fields and therefore not in need of much education on the subject. Governor Perry has also suggested that special malpractice courts be established to handle claims precisely because of the technical proficiency required.
- **Bad Faith Cause of Action.** A recent appeals court ruling found that even when suits are brought maliciously and in bad faith, it is not abuse of the litigation process. The State Bar has not regulated frivolous lawsuits by its members and cannot undo harm done to doctors when frivolous lawsuits are brought against them. As proposed last session, a separate cause of action could be created to allow doctors to sue independently or as a countersuit to show that a plaintiff and the plaintiff's attorney filed or maintained a lawsuit with reckless disregard.
- **Screening panels.** Screening panels would require all medical malpractice claims to go before an expert panel to determine if the claim is valid. A plaintiff may move forward with the claim regardless of the panel's decision, but if the panel found the claim to lack merit then the plaintiff would be responsible for attorney's fees and costs of the doctor if they did not prevail at trial. If crafted incorrectly these panels could

become a testing ground for attorneys to determine whether claims should be pursued, however, the use of an expert panel has been an extremely popular idea with many doctors.

Medical malpractice is a problem statewide and does not only impact doctors. Patients all over the state need to be able to access care when it is necessary and as more doctors decide that the cost of providing medical services does not outweigh the risk, patients are sure to notice the negative impact of medical malpractice lawsuits on even the most basic medical care. Furthermore, the cost of defensive medicine has budget implications for Texas as studies estimate that defensive medicine costs the United States \$50 billion a year.<sup>37</sup> Texas is not alone in the liability crisis, and certainly shares in the total cost of providing medical care in this litigious climate. By following California's MICRA, which has widely been considered successful, Texas will allow patients access to damages they are entitled to receive while safeguarding the system from as many frivolous and unnecessary claims and exorbitant jury awards as possible.

### **Temporary Assistance for Needy Families**

**Implement the “Full Engagement” work model so that all families must participate in work and other constructive activities leading to self-sufficiency. Amend state law to remove all exemptions from work requirements and workforce orientation, and allow Choices case managers to screen participants for good cause.**

The 1996 welfare reform act granted states greater flexibility in administering the Temporary Assistance for Needy Families program (TANF). These reforms at the federal level offer Texas an opportunity to reduce costs and promote financial independence within the state program.

A single parent with two children on TANF, Medicaid, and food stamps, equates to a \$12,612 annual income, which is below the federal poverty line of \$14,640. However, with this same family, if the adult has a minimum wage, full-time job and assistance of Earned Income Tax Credit, TANF, Medicaid, food stamps, and child care, this family now has equivalent to a \$30,208 annual salary. That minimum wage job more than doubles the family's income. In addition, the Department of Human Services has shown that 46% of TANF leavers reported an average hourly wage of \$7.20, which, with benefits, equates to approximately \$32,308 annually.<sup>38</sup> The increasing additional income clearly creates a better situation for these families and helps them to become more self-sufficient.

The “Full Engagement” model would require a TANF recipient to meet with their local Choices case manager, who is equipped to help them navigate the job market and match the recipient's skills with an employer's needs. Currently, some TANF recipients are determined to be exempt before having the chance to find out if a suitable job is available; these exemptions usually last for six months.

Good cause exemptions, however, can better account for specific situations that preclude work than upfront exemptions. Good cause exemptions are more flexible than the existing exemptions, and allow the exemption to match the situation. For example, a single parent might have good cause not to work if their baby were ill, so the caseworker would follow up on the parent and once the baby was well, the good cause exemption would be invalid and the parent would have to return to work.

**Establish a pay-for-performance program for TANF recipients, or implement full grant denial for individuals who are not in compliance.**

When a family applies for TANF, the adult is required to sign a Personal Responsibility Agreement. The state assumes, on good faith, that the recipient will abide by the agreement. The agreement establishes certain requirements and sanctions, some of which are outlined in the following table:

<b>Requirement</b>	<b>Sanction</b>
Child Support	\$78, \$125, or \$165
Choices	\$78 or \$125
School Attendance-Minor Parent	\$78
Voluntary	\$25
Texas Health Steps	\$25
Immunization	\$25
School Attendance-Child	\$25
Parenting Skills	\$25
Alcohol or Misdemeanor Drug	\$25

If the TANF recipient does not comply with one or more requirements, a sanction is levied against them.

By rule, the cap on sanctions for a single parent family is \$78 per month.<sup>39</sup> For example, once a \$78 sanction has been levied for missing a job interview, the family is no longer penalized for refusing to pay child support, or to keep their children in school. The sanctions are held in place until the person complies. As of September 2002, 33% of all TANF adults with work requirements were under a work-related sanction.<sup>40</sup> As stated by TCWEC, “these numbers indicate that the state’s partial work-related sanction policy does not provide sufficient incentives for adults to comply with program requirements.”<sup>41</sup> In order to establish a path toward self-sufficiency for TANF recipients, the recommendation is to implement either “Full Grant Denial” or “Pay-for-Performance.”

A full grant denial would halt all TANF funds for an individual or an individual’s family, if an individual fails or refuses to comply with any requirement of the responsibility agreement without good cause. For a single parent with two children, the monthly TANF benefit is \$213. Under the current system, once the parent has been sanctioned, the family could still receive benefits of \$135 a month until their five year federal time limit expires; however, under a full grant

denial, all benefits would be halted until they return to compliance. Nearly forty states have a full grant denial of TANF benefits for those individuals who do not, without good cause, comply with the work requirements.

Alternatively, the state could choose a pay-for-performance method that pays recipients for their compliance. Wyoming has instituted a pay-after-performance system along with other sanctions and has reduced their caseload by 90 %, as have North Carolina and Wisconsin, with caseload reductions of 62 % and 77 %, respectively.<sup>42</sup> Texas can look to Wyoming and Wisconsin as an example in creating a pay-for-performance program in this state, and implementation of either model could result in an estimated annual savings of approximately \$25 million in monthly benefits.

According to Wyoming's Department of Family Services, Wyoming's program requires full compliance with requirements before benefits are provided.<sup>43</sup> The family must complete all requirements for the entire performance period to receive full benefits. If a family member fails to comply for even one day within the performance period and good cause has not been approved, a performance payment of \$1 will be issued to the family. Once parents comply for a full month, they can receive a full grant again; after two months of non-compliance, the case is closed and the family must reapply for future benefits.

Wisconsin's model transforms the welfare cash assistance program into a work program by compensating the recipient based on the number of hours engaged in the work program.<sup>44</sup> To fund such a program, the monthly TANF and Food Stamp benefits are combined and then converted into a wage that can only be accessed by the client if they are engaged in work or an approved work-related activity. The total value of benefits is divided by \$5.15 per hour to determine the average number of hours the individual is required to work per week. If a recipient only complies with half of the work requirement, the compensation is reduced by half for that month. Medicaid benefits, however, are not affected for the adults or children under this policy.

All people, regardless of the challenges they may face, should be given the opportunity to contribute to the workforce. Efforts to redesign the TANF program should work toward encouraging and assisting TANF parents to enter employment more quickly and pursue activities leading to a more stable financial future for their children. The pay-for-performance model offers unique incentives by mirroring the way an individual is paid for their work, and better prepares TANF recipients for eventual transition from welfare to work. Additionally, the pay-for-performance model provides an incentive for individuals to move into real jobs quicker as their food stamp allocations would no longer be diverted, but one instead be given to them directly.

TANF work requirements are not meant to create barriers to benefits, but are intended to encourage transition from welfare to work. The TANF program

provides opportunities to parents to develop their skills for work and in support of the family. While accelerating the closure of TANF cases creates a cost savings to the state, the goal is to do so by giving TANF recipients the tools to reach self-sufficiency.

### **Interagency Council on Early Childhood Intervention**

**Transfer the Interagency Council on Early Childhood Intervention into the Texas Department of Health and reduce the number of FTEs that manage the program.**

The Texas Interagency Council on Early Childhood Intervention (ECI) is responsible for serving families with infants and toddlers under age three with disabilities and developmental delays. ECI is also responsible for the management of Texas' Comprehensive Service Delivery System for the Individuals with Disabilities Education Act (IDEA) Part 3.

There is simply no reason for this activity to be managed by a single, independent agency. Many of ECI's activities have a health component that TDH is prepared to handle, and should handle as the state's agency over health. Transferring the functions of ECI to TDH would consolidate some administrative aspects and allow more effective delivery of services. Thus this change would not only result in a reduction of FTEs, but savings from greater efficiency as well.

### **Texas Cancer Council**

**Abolish the Texas Cancer Council.**

The Texas Cancer Council was established in 1985 and receives slightly more than \$4 million in general revenue funding each year to fulfill its obligations. A number of private organizations, such as the American Cancer Society, the Cancer Research Center, the American Cancer Institute for Cancer Research, the American Cancer Association, and the National Cancer Institute, all work toward virtually the same goals as the council, and do so with private funds.

As illustrated in the table below, the council's activities are largely duplicated by these private organizations as shown in the chart.<sup>45</sup>



Texas Cancer Council Activity	Other Organizations Providing Service	Notes
Provide cancer prevention and treatment information	American Cancer Society, the Cancer Research Institute, American Institute for Cancer Research, American Cancer Association, National Cancer Institute	The council contracts with the Texas Cancer Data Center, a clearinghouse on Texas cancer statistics, programs and services, in order to fulfill this activity. Much of this data is not provided by other organizations.
Provides a toll-free number for information on tobacco through Office of Smoking and Health	American Cancer Association and American Institute for Cancer Research provide similar toll-free numbers. The American Cancer Society provides phone assistance, and the National Cancer Institute has a toll-free cancer help line for both Spanish and English speakers.	
Further education of health-care professionals through oncology programs.	Texas medical schools, Cancer Research Institute, American Institute for Cancer Research, and American Cancer Society offer scholarships, teaching fellowships, meetings and films.	
Coordinate efforts of other cancer organizations in Texas.		The council has no statutory authority over organizations and each operates independently.
Implement Texas Cancer Plan		Several of these organizations indicated that they have not heard of the Texas Cancer Plan and it does not impact their efforts.

Clearly, the Council's services are duplicated by these private organizations. The efforts of these private organizations are not coordinated by the Cancer Council, and some report that they are not familiar with the Texas Cancer plan, which is justification for the bulk of the council's funding. The Council does not lead these organizations, nor does it coordinate the efforts of these organizations. The Texas Cancer Council is almost entirely duplicative and should be abolished. Furthermore, if the aim of this program is essentially to reduce instances of cancer, resources would be better directed toward cancer research than an additional state organization focusing on awareness.

The one program not administered by the council that is not duplicated by a private or non-profit organization is the Texas Cancer Data Center. The Center collects information on service providers, hospital information, and equipment information, as well as mortality and population information available without the use of private medical records. This is perhaps the only function of the council that should be preserved, and it should be moved to another agency like the Texas Department of Health, where a similar program, the Cancer Control Program, already exists.

## **Texas Health Care Information Council**

### **Abolish the Texas Health Care Information Council.**

The Texas Health Care Information Council was created in 1995 under the recommendation of various business and consumer interest groups. The rationale for the creation of THCIC was to provide quality-based information

concerning health care providers so that consumers could make truly informed decisions when considering the purchase of health care services. The legislative charge was to “implement a statewide health care data collection system to collect information on health care charges, provider quality, and health care outcomes to facilitate the promotion and accessibility of cost-effective, quality health care.”<sup>46</sup>

Seven years and \$8.4 million after the council’s creation, THCIC released its first hospital “report card” to the public. In order to create the report, THCIC has implemented rules requiring hospitals and HMOs to report data to the council, and have contracted out the maintenance of a database, which houses the data transferred from HMOs and hospitals.<sup>47</sup> The result of all of this information collected for the report card, according to the Austin American-Statesman, is that “for the first time, consumers can compare hospitals in Texas for a variety of inpatient procedures and conditions. The comparisons can be made by mortality rates or by the volume and frequency of certain procedures.”<sup>48</sup>

The next endeavor THCIC has is to publicize the information that they have captured. The Austin American-Statesman reports that in the last part of 2002, THCIC “plans to compare hospital performance in patient safety and to examine the rate of treatment of a variety of illnesses and diseases in different regions of the state.”<sup>49</sup> They also plan on adding 1999 and 2001 data to the hospital report card in Spring 2003.

The intentions behind the construction of this council may have been good, but it has provided little benefit to the citizens of Texas over the last seven years. In fact, seven years and \$8.4 million later, the THCIC has produced only one report. This one report, released in October 2002, included hospital information from the year 2000, even including hospitals that had been out of business for over a year.<sup>50</sup> Furthermore, it only reported on in-patient data, which will become less useful as the trend toward out-patient procedures continues, and listed the hospitals in alphabetical order rather than in order of performance, making the comparison process cumbersome.<sup>51</sup>

In addition, the governing statute charges THCIC with doing several worthwhile items, some of which are included in the following chart with the current status of each task:

<b>TASK<sup>52</sup></b>	<b>STATUS<sup>53</sup></b>
Make reports to the Legislature, the governor, and the public on the quality and effectiveness of health care and access to health care for all Texas citizens.	THCIC has been unable to get to this task due to lack of resources and time.
Work with DIR in developing and implementing the statewide health care data collection system and maintain consistency with DIR standards.	DIR would not work with THCIC, so THCIC is working with HHSC.
Develop criteria for evaluating drug purchasing cooperatives.	Texas does not have a drug purchasing cooperative; no action being performed.
Analyze data and make recommendations relating to Medicaid managed care.	HHSC is performing this task; HHSC takes the data the THCIC collects from hospitals and compiles it with other HHSC Medicaid data.

The council has issued one report and has done little toward fulfilling its statutory responsibilities. With this record of performance in mind, the state should abolish the council. In regard to the budget, the Legislature should transfer funding to the agencies taking over the responsibilities, as well as achieve possible savings of approximately \$750,000 annually from the simple reduction in staff and the operating budget.

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<sup>1</sup>Nicholas Eberstadt, "A Misleading Measure of Poverty," Washington Post, February 17, 2002: B7.

<sup>2</sup>"A Misleading Measure of Poverty".

<sup>3</sup> Texas Council on Workforce and Economic Competitiveness, Family Income and Assistance Model, "Annual Wage and Benefit Scenario for Single Parent with Two Children".

<sup>4</sup> Texas Health and Human Services Commission, Texas Medicaid in Perspective, Fourth Edition, p.1-1.

<sup>5</sup> Texas Medicaid in Perspective, p.5-2.

<sup>6</sup> Texas Medicaid in Perspective, p5-2.

<sup>7</sup> Heritage Foundation, The Baucus 'Work' Act of 2002: Repealing Welfare Reform, by Robert Rector, September 3, 2002, <<http://www.heritage.org/Research/Welfare/BG1580.cfm>>.

<sup>8</sup> HHSC Presentation to TCCRI Task Force on State Finances, March 19, 2002, p.17.

<sup>9</sup> National Conference of State Legislatures, Medicaid Cost Containment: A Legislator's Tool Kit, March 2002, Strategy 6, p.6.

<sup>10</sup> Texas Medical Association testimony to House Appropriations Committee and House Insurance Committee, Joint Hearing on Medicaid and CHIP, April 24, 2002.

<sup>11</sup> State of Florida, Agency for Health Care Administration, Medicaid Prescribed Drug Spending Control Program, Annual Report, January 2002.

<sup>12</sup> National Conference of State Legislatures, Medicaid Cost Containment, p.7.

<sup>13</sup> Health and Human Services Commission, "HHSC Survey: Medicaid Cost Sharing for ER" and "HHSC Survey: Medicaid Cost Sharing for Pharmacy".

<sup>14</sup> HHSC "Cost Sharing Workgroup Summary" 4/21/02.

<sup>15</sup> HHSC, "Most Adult Medicaid Recipients to Pay Copayments."

<sup>16</sup> HHSC, "Proposed Texas Medicaid Copay Policy: Two Step Approach-Implementation Fall SFY 2002 and SFY 2004" attached to letter to CMS, and "Proposed Texas Medicaid Copay Policy, Implementation Fall 2002," as proposed to MCAC.

<sup>17</sup> "Most Adult Medicaid Recipients to Pay Copayments."

<sup>18</sup> National Conference of State Legislatures, Medicaid Cost Containment, Strategy 6, p.2.

<sup>19</sup> HHSC letter to CMS, accompanying "Proposed Texas Medicaid Copay Policy: Two Step Approach- Implementation Fall SFY 2002 and Fall SFY 2004".

<sup>20</sup> HHSC Letter to CMS, Medicaid Copay Proposal, June 3, 2002.

<sup>21</sup> Letter from Jason Cooke in response to TCCRI inquiry, September 23, 2002.

<sup>22</sup> Presentation to the TCCRI State Finance Task Force, "e-Texas, Texas Performance Review, Options for Controlling Medicaid Costs," March 19, 2002.

<sup>23</sup> Presentation to TCCRI State Finance Task Force, "Options for Controlling Medicaid Costs."

<sup>24</sup> Health and Human Services Commission, Texas Medicaid in Perspective, Fourth Edition, 4-17.

<sup>25</sup> HHSC presentation to TCCRI Health Care, "Medicaid Cost Sharing", March 26, 2002.

<sup>26</sup> HHSC presentation to TCCRI State Finance Task Force, March 19, 2002, p.16.

<sup>27</sup> Pharmaceutical Care Management Association website, PBMs Deliver Value to Patients and Payers, Issue Brief, June 2002, <<http://www.pcmanet.org>>.

<sup>28</sup> Arizona Legislature website,

[www.azleg.state.az.us/issues/senate/pharmacy%20benefits%20manager.pdf](http://www.azleg.state.az.us/issues/senate/pharmacy%20benefits%20manager.pdf)

<sup>29</sup> Pharmaceutical Care Management Association, PBMs Deliver Value, p. 3.

<sup>30</sup> HHSC, Texas Medicaid in Perspective, Fourth Edition.

<sup>31</sup> Governing Magazine, Christopher Swope, July 2002.

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- <sup>32</sup> Texas Department of Human Services.
- <sup>33</sup> State of Texas, Office of the Attorney General, Letter Opinion 95-005.
- <sup>34</sup> Common Good, Fear of Litigation Study, by Harris Interactive, April 11, 2002, p. 20.
- <sup>35</sup> U.S. Department of Health and Human Services, Confronting the New Health Care Crisis: Improving Health Care Quality and Lowering Costs By Fixing Our Medical Liability System, July 24, 2002, p. 7.
- <sup>36</sup> HHS, Confronting the New Health Care Crisis: Improving Health Care Quality and Lowering Costs By Fixing Our Medical Liability System.
- <sup>37</sup> Citizens Against Lawsuit Abuse, Press Release, July 25, 2002.
- <sup>38</sup> Texas Families in Transition, January 2002, page XV of the Executive Summary.
- <sup>39</sup> Family Services Division, Department of Human Services, facsimile on November 15, 2002.
- <sup>40</sup> Texas Department of Human Services, Management Information Focus Report, September 2002, p.23.
- <sup>41</sup> Texas Council on Workforce and Economic Competitiveness, Welfare to Work Initiatives in Texas: Report 2001, p.10.
- <sup>42</sup> United States Department of Health and Human Services, Temporary Assistance for Needy Families (TANF) Program, Third Annual Report to Congress, August 2000.
- <sup>43</sup> State of Wyoming website, <<http://dfsweb.state.wy.us/p&p/powerpat.htm>>.
- <sup>44</sup> State of Wisconsin website, <<http://www.dwd.state.wi.us/wtw/>>.
- <sup>45</sup> Texas Comptroller of Public Accounts, <<http://windows.state.tx.us/tpr/atg/atghhs/hhs26.html>>.
- <sup>46</sup> HB 1048, 74<sup>th</sup> Legislature
- <sup>47</sup> Interview with Jim Loyd, Executive Director, THCIC, October 1, 2002.
- <sup>48</sup> Robert W. Gee, "Picking a hospital just got easier," Austin-American Statesman, Oct. 9, 2002.
- <sup>49</sup> "Picking a hospital just got easier".
- <sup>50</sup> "Inhospitable", Fort Worth Star-Telegram, October 13, 2002.
- <sup>51</sup> THCIC website, <http://www.thcic.state.tx.us>
- <sup>52</sup> Texas Health and Safety Code, Chapter 108.
- <sup>53</sup> Conversation with Jim Loyd.

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**ARTICLE III**  
**Education**



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# PUBLIC EDUCATION

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Public education is the largest single function funded by the state and accounts for 30% of the total budget and 40% of general revenue related spending. In the 2002-2003 biennium, the Legislature appropriated \$29.9 billion for public education, including TEA administration, of which 77% was general revenue. The responsibility for funding public education is shared by local school districts, the state, and the federal government, with the greatest portion of the bill paid for by the local property taxes. The federal government's contribution is the smallest and generally directed for specific federal education programs.

While Texas' school funding system gets the most headlines and is a contentious issue that deserves attention, the recommendations in this section of Article III reflect possible areas of cost savings in public education as it currently exists. Although the issue of school finance has budget implications that will surely be considered at some point, the issue is beyond the scope of this report. However, as a matter of discussion, the first recommendation for public education is in response to the state's emphasis on equity and the equally important goal of establishing a standard of adequacy in education. The remaining recommendations are simply an effort to look at areas of public education that need improvement and a new level of accountability.

## **Adequacy**

### **Study the cost of a thorough and efficient education.**

As a result of the findings in the Edgewood cases, Texas public school finance reforms have almost exclusively dealt with the constitutional principle of equity. Texas has made great strides in the area of equity, but it has not yet addressed the equally important principle of adequacy- that is, suitably providing for a general diffusion of knowledge. It was assumed that by continually adding resources to the current system to meet equity standards, the state had satisfied the adequacy requirements and effectively provided students with a suitable and efficient education. However, as then Supreme Court Justice Cornyn articulated in his dissent in Edgewood III, "Fiscal input alone offers no guarantee of a quality education. This is because pure 'equality of input' requirements do not require a positive correlation between dollars spent (input) and quality of education realized (output)."<sup>1</sup>

Despite Texas' detailed curriculum standards and the implementation of an advanced accountability system, there is still only a tenuous connection between legislative funding and how those dollars work in the classroom. The level of funding provided by the Legislature must have some relationship to the costs

associated with achieving certain levels of student performance. Yet, it is hard to quantify the cost of an efficient education, and thus it is difficult to determine whether a school district's failure to perform is due to lack of funding or administrative failure at the district level, and even then, it is difficult to determine how much additional money, if any, is needed to remedy those failures.

The 78<sup>th</sup> Legislature should undertake a study to determine the cost of a suitable provision of a general diffusion of knowledge. Funding for the adequacy study should come from private donations, or should be found in the current Texas Education Agency (TEA) budget. The results of the study will assist the Legislature in directing state funds to the appropriate areas in order to improve the quality of a public education. More than a dozen states have already begun this type of review, although many have done so at the direction of the state's courts. Texas has an opportunity to begin this study before any legal action directs Texas to do so.

The importance of a study of this kind cannot be overstated. Under the current system, the Legislature has not put in place a link between the ends of public education and the resources available to it. For years, Texas has struggled to ensure that every child has access to substantially equal amounts of money. This derives from the common notion that those with more resources can achieve better results. But the larger issue is what public education should achieve- that every child has access to a quality education that will provide him or her with the knowledge necessary to be self-sufficient. The only way to ensure that the children of Texas have access to a quality education is to set standards and then determine what that education costs. While Texas has seen significant successes in public education, we must link what we want to achieve to the costs associated with that goal. Only by doing this can we be assured that Texas taxpayer's public education dollars are achieving the intended result. The adequacy study is the first necessary step to preventing reckless spending in the name of school finance before the state's true needs are identified.

## **Flexibility and Local Control**

### **Relieve school districts from state mandates and grant more local control.**

Under then-Governor George W. Bush, Texas public education began an era of accountability for results, with local control of the process of education. With a historic revision of the Texas Education Code in 1995, the Legislature began moving toward this goal.

Now, Texas school districts are at a crossroads. The Legislature has required new, tougher academic exams, which will begin in Spring 2003. Although Texas test scores on the current TAAS exam and on the National Assessment of Education Progress have shown that Texas students are learning more, the bar is being raised significantly in the near future on Texas students and their



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schools. However, with greater accountability, the Legislature has not given schools greater local control to direct their resources where they need to go (and in some cases the Legislature has created even more restrictive state mandates).

At the same time, school districts are rapidly reaching their maintenance and operations tax rate caps of \$1.50 per \$100 of property value. Although property values have climbed dramatically in recent years, school districts do not keep the extra tax dollars generated by higher values. Instead, the Legislature has used the extra local wealth to give school districts a proportionally smaller share of state dollars (or for Robin Hood districts, required the local districts to send more dollars to the state) - and has used the state dollars "saved" to create new programs.

With the academic bar raising at the same time that more districts are reaching their revenue capacity, schools need more flexibility and local control to be able to direct their resources where they should go to best help their students. To this end, the Legislature should:

- **Let schools focus on academics.** Many laws mandate non-education-related functions, taking educators' time away from educating students. The Legislature could review and repeal laws that take time and resources away from educating students.
- **Help schools improve personnel resources.** Many schools must hire more and more substitute teachers, after teachers' sick leave entitlement was changed in 1995 to "personal leave." Having a substitute instead of the regular teacher disrupts students learning and costs taxpayers more money. The Legislature should return the law to "sick leave" and let districts define, provide, and monitor personal leave. In addition, for personnel in the district who are not fulltime classroom teachers, districts should have more flexibility to find appropriate personnel. For teachers, the contract law should provide more options, such as paying a teacher in lieu of an expensive due process termination proceeding or returning a teacher to probationary status in lieu of termination.
- **Grant relief on restrictions and paperwork.** Many state mandates detail how districts must spend different pots of money. For example, last session a law was enacted to restrict how districts use compensatory education funds for disciplinary alternative education programs. Other examples include audits on district effectiveness compliance and dropouts, which are time-consuming and expensive requirements that should not apply to districts performing at acceptable achievement levels.
- **Give incentives to create more choice.** To improve choice and excellence among public schools, we should free school districts to create

more campus or program charters that are voluntary for both students (at their parents' choice) and teachers. Because they would be voluntary, these charters could operate with fewer state strings. Such charters would be especially useful for online courses, where a students might need more or less time on task than is prescribed for ordinary courses.

## **Total Returns**

### **Monitor the performance of other total return funds to project long-term distributions and fund growth possibilities.**

The Texas Constitution requires that only the income (interest and dividends) from the Permanent School Fund (PSF) may be distributed to the Available School Fund (ASF), and capital gains must remain in the Fund. The intent behind this provision is to protect the corpus of the PSF so that it can continue to help pay for public education in perpetuity.

The State Board of Education (SBOE) has two primary duties regarding the PSF. First, the Fund must be managed in such a way that it generates revenue adequate to meet current distributional needs as targeted by the General Appropriations Act. This involves an investment strategy that focuses on income producing vehicles, such as bonds, but does not increase the value of the PSF. Second, the SBOE must ensure that the corpus of the fund grows enough to keep pace with inflation and an expanding student population. By investing more heavily in stocks, the SBOE is better able to reach this goal, but as a result unable to produce current income for the Fund.

A management tool based on "total return," which is an investment's annual price appreciation plus interest and dividend income, would allow the SBOE to distribute to the ASF a prudent portion of the PSF's long-term cumulative total return. Such a strategy could allow the SBOE to meet its conflicting duties and could generate greater distributions to the ASF. Given the fact that the PSF is so important to the funding of education in this state, it is prudent to watch how other "total return" funds perform in bear markets to determine if distributions and fund growth can be maintained over the long-term.

Proponents say that the adoption of a "total return" spending rule will provide greater investment flexibility, thereby potentially enhancing the performance of the fund, both now and in the future. Allowing the SBOE to make distributions based on "total returns" will provide an investment mix that relies less on bonds, which generate comparatively high interest but lower total returns, and more on investments that generate higher total returns over the long-term but perhaps less current income (stocks). By achieving higher long-term total returns, the SBOE can more effectively ensure growth of both the PSF and its annual distributions.

By basing distributions on long-term market forecasting under a “total return” spending rule, the Fund can make annual pay outs that are stable and predictable. Under the current “income” spending rule, calculating future income is complex and requires an ability to predict market returns over the short-term. As a result, the PSF has exceeded its income targets in bull markets and fallen short of its target in bear markets.

Most large public educational endowment funds are managed according to the “total return” spending rule. Currently, 97.5% of all university endowment funds utilize some form of “total return.” Every university fund valued at more than \$500 million uses this management rule. In 1999 the Permanent University Fund adopted this tool and has been able to optimize its asset mix without harming annual distributions. Furthermore, adequate safeguards can be written into the constitution to help protect the corpus of the PSF. Such provisions could set maximum spending rates and prohibit spending increases if the Fund’s purchasing power declines over the prior 10 year period.

## **Regional Education Service Centers**

**Abolish Regional Education Service Centers and redistribute any necessary functions to related agencies, or reorganize the Regional Education Service Centers to provide services and programs to targeted school districts.**

Regional Education Service Centers (RESCs) were originally created to distribute federal education funding and serve as media storage centers.<sup>2</sup> Twenty centers provide services to Texas school districts in geographic regions created in 1967.<sup>3</sup> The RESCs role has broadened to include instruction-related services, teacher training and certification testing, training for bus drivers and school board members, informational services, data processing and administering various federal and state programs.<sup>4</sup> The RESCs charge districts varying fees for their services and few, if any, of their services are free.<sup>5</sup>

Regional Education Service Centers receive funding from local, state and federal sources and charge districts varying fees for their services. Through contracting, many of TEA’s technical assistance functions have been moved to RESCs so that they function in practice as TEA satellite offices. RESCs are not state agencies, their salary and benefits are independent of the state’s salary classification and they are free to set charges for their services. Their quasi governmental status and failure to provide districts with comparative data insulates them from private sector competition, or even inter-regional competition, and gives them a stranglehold on determining how services will be provided and the fees charged to school districts. Regional educational service centers should be abolished or at least re-organized to focus on providing assistance only to needy school districts. Abolishing the service centers would eliminate their direct appropriation of \$122 million.

RESCs have played an increasing role in Texas public education, but despite sweeping changes in the roles and responsibilities of RESCs, the state has not conducted a comprehensive assessment of how RESCs fit into the overall educational delivery system in several years. There are several factors that should be cause for concern in the continued existence of these RESCs.<sup>6</sup>

First, the state has no authority over the content of RESCs materials or the program assistance they provide. The State has the responsibility for setting the policy goals of Texas' education system, but when school districts must rely on RESCs to develop the program and the state has no oversight or say into the services provided by the RESC, the RESCs become de facto policy makers.

Second, federal funding funnels through the RESCs. Their existence as semi-private, semi-public entities shields many of the federal monies they receive from oversight of TEA, the duly authorized educational agency of the state.

Third, even though RESCs are legally recognized nonprofit corporations, their ability to establish their own salary, benefit and retirement structures, and set their own fees for their services to school districts makes them essentially publicly owned for-profit entities.

Fourth, RESCs have monopolized service delivery, and school districts pay the price. As quasi-governmental entities, RESCs are property-tax free, giving them an unfair advantage over private sector entities willing to provide the service, yet the RESC sets the fee to school districts.<sup>7</sup> The RESCs also have an inside track to superintendents and have bargaining leverage over the services provided because they serve as the repository of many of the services, programs, and expertise that the school districts need.

It is troubling that the RESCs' practices and operating policies are largely hidden from public scrutiny, and although they enjoy the many benefits of being a quasi-governmental entity, they are not held accountable for the funding that they receive.<sup>8</sup> As the state works toward improving public education in the state of Texas, it is illogical that these centers would go virtually unchecked. The centers could be abolished with the necessary duties assigned to TEA or other relevant agencies, or they could simply be re-organized to better work with districts such as co-ops established by the client districts that might benefit from the expertise and services of the centers.

## **Teacher Retirement System**

Since its inception, the Teacher Retirement System (TRS) has been primarily concerned with the provision of retirement benefits to public school employees, but three major events have shaped TRS into an agency that is not only concerned with retiree benefits, but also the benefits of active and current

teachers. In the mid-1980s, TRS began providing a basic level of health insurance to retired teachers through TRS-Care, and participants now make contributions to fund their health care coverage in their future retirement. In the early 1990s, the system undertook a study of statewide health insurance for active and retired teachers, and districts were then also required by law to provide a group health insurance benefit comparable to that provided to state employees. Then last session, the 77<sup>th</sup> Legislature created a comprehensive, statewide group health insurance program for teachers called TRS-Active Care.

Participation in TRS-Active Care is mandatory for all school districts with 501-1000 employees, while districts with more than 1,000 employees may opt in beginning in 2005-06. According to TRS, effective September 1, 2002, 870 entities began participation in TRS-Active Care and another 180 would join as soon as their current insurance contracts expired. These entities include school districts, charter schools, education service centers, and other educational districts. As the benefit was passed, the funds were not dedicated strictly for health care, but were allowed to be taken as an increase in salary, and the benefits were extended to part-time employees as well.

Of course, TRS is experiencing the tremendous increases in costs that all of health care is facing, and the addition of a statewide and mandatory program has only served to strain the resources for these benefits even farther. According to a TRS presentation to the Senate Finance Committee's Subcommittee on Rising Medical Costs in September, the system's funding request for the 2004-05 biennium includes substantial increases for TRS-Care "driven principally by constitutional and statutory provisions and continued increases in health program enrollment and medical cost trend."<sup>9</sup> Increases in both TRS-Care and TRS-Active Care warrant greater cost sharing as a means induce cost sensitivity in the system. Furthermore, the task force has made recommendations to increase cost sharing in the Employee Retirement System health plans, as well as in Medicaid and CHIP.

#### **Increase prescription drug co-payments in TRS-Care.**

Prescription drug co-payments in the TRS-Care program should match the current rates in TRS-Active Care Plan 3, charging \$5 for generic, \$20 for name-brand drugs on a preferred list, and \$35 for the name-brand drugs that do not appear on a list. Mail order prescriptions may be filled for 90-days and are charged twice the rate of the retail cost. TRS estimates that implementing this plan could save \$36 million in 2004 and \$47 million in 2005.

Additionally, the Active Care Plan 3 structure is modeled after the plan for state employees under the Employee Retirement System (ERS), and thus should match the recommendations made for greater cost sharing in ERS. Plan 1 and Plan 2, can be used as models for defined benefit structure in TRS.

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**Amend provisions of TRS-Active Care to give districts greater flexibility and ensure that the program is truly a health benefit.**

TRS-Active Care, however, is truly the focus of the task force's recommendations regarding TRS. Although a statute requiring school districts to offer teachers coverage comparable to state employees existed, it was not enforced. A Teachers Retirement System (TRS) comparability study of district insurance plans indicated 202,780 employees, or 38% of reported school employees, were covered by a state employee comparable plan; only 350 employees were not offered any type of health plan.<sup>10</sup> While these numbers would indicate that the majority of Texas teachers had some level of health coverage, the state created a far-reaching plan to provide health insurance to teachers regardless of the comparability of existing plans.

The plan that was created as a result of the passage of HB 3343 in the 77<sup>th</sup> Legislative Session provides that the state pays \$900 annually per employee, and the school district pays \$150 every year for each employee.<sup>11</sup> In addition, the state pays each school district employee \$1,000 that can be used to, supplement the employee's health coverage, provide dependent coverage, be used for a health care reimbursement account, or may be used as cash.<sup>12</sup> In essence, this "employee pass-through" is a pay raise for every employee in the district, including non-education personnel. Also, the employee may receive this cash even if they elect to waive participation in a health plan. As a result of the need to provide health insurance, the state passed a plan that provided coverage regardless of whether equal or better coverage was provided by the school district and gave each school district employee a pay raise. The state now bears the bulk of the responsibility in providing teachers with health insurance, and as the costs of providing insurance rise, the school districts and the state must put additional funds toward teacher health insurance. The current plan is untenable and is disingenuous for health care; the state must address these issues to control the costs and maintain the solvency of this health plan.

Seven recommendations should be considered to improve the teachers' health plan:

- **Change the delivery of services to allow regional risk pools and competition, rather than a sole provider, and introduce patient choice through the option of a defined contribution.** The defined contribution alternative allows funds to be set aside for the employee, making the first dollar of health care coverage the responsibility of the employee. The recent federal decision allowing funds in the account to rollover from year to year gives the employee flexibility and incentive to control their health care costs, and allows the patient more control of their health care decisions when they also control the money

- **Adopt a defined contribution bill devoting funds solely to health care.** Allowing school employees to receive the health benefit as compensation rather than dedicating it solely to health care, means that health needs may still go unaddressed. TRS Active Care was created to provide health insurance for teachers, not a pay increase. All employees, including janitorial staff, got \$1,000 pay raises last year, but this money should be limited to educators and not given to non-education personnel. Also, districts should have more flexibility in budgeting at this time, as many are reaching their tax rate limits.
- **Merge ERS with TRS and separate functions.** Consider merging TRS and ERS and separating the functions, establishing one agency with jurisdiction over retirement and another over health insurance. Merging these activities would reduce the administrative duplication of each agency. Separating the agencies by function would focus the agency on one mission, rather than two unrelated responsibilities. Retirement and insurance are two entirely different responsibilities and should not be handled by the same organization. The current structure is as nonsensical and inefficient as the prospect of an insurance carrier managing a client's health insurance and 401K.
- **Offer health coverage only to full-time employees, eliminating the provision of health insurance for part-time employees.**
- **Limit the ability of large districts to enter the program based upon the financial effect their entry would have on the plan.**
- **Rescind mandated participation and extend limited ability to districts to opt out of TRS Active Care if school districts can offer evidence that they are providing their employees with a state comparable plan.** Since 1991, Texas has stipulated in statute that school districts shall provide coverage through managed or preventive care, comparable to the basic health coverage provided under the Texas Employees Uniform Group Insurance Benefits Act.
- **Provide financial relief for district already contributing the full amount to health coverage prior to implementation of the state plan.** Districts that made previous financial commitments to health coverage for employees are penalized while a "hold harmless" clause helps districts that were contributing little to nothing for health coverage.

The current teacher health insurance plan is unnecessarily cumbersome and inflexible. It is troubling that TRS voluntarily removed any competition from the system when, by board-adopted rule, it said insurance would be provided by a single provider statewide. With a single provider and mandated statewide participation, the state prevents individual districts that are best able to respond

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to the needs of their employees. Individual districts should be able to opt out of the state plan if they can provide comparable coverage. The 1991 statute already required that a comparable plan be offered, so the problem was not necessarily that teachers did not have health coverage as much as it was that the statute in place was not enforced. However, the feature that is perhaps the most concerning is the state's willingness to pass a teacher health plan that does not solely fund health insurance. Simply put, the Legislature must insist that competition be a part of the teachers' health insurance program and that the funds are specifically for health care and not for salaries of teachers and other employees. Furthermore, in keeping with the recommendations made for additional cost sharing in the Employees Retirement System plan, the TRS-Active Care Plan 3 plan should mirror any changes in ERS to keep the two plans comparable.

Furthermore, the RFP process for TRS is as prescriptive as the RFP process in ERS (See General Government). Because these areas have difficulty containing costs and because, as the ERS numbers illustrate, there are a variety of health care needs within these large pools. Without allowing innovation and creativity in the submission of proposals, the state discourages competition, makes patient choice a virtual impossibility, and further drives bidders from the market. The RFP process in TRS, like the process in ERS, should be opened up to bidders who can submit bids with plans that vary and address many needs. The prescriptive nature of this process only ensures that there will be few bidders and that patient choice will be limited.



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# HIGHER EDUCATION

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Public higher education institutions funded by the state include universities, community colleges, technical colleges and institutes, state colleges, private and public health-related institutions, and research institutions and programs with particular emphasis in areas like agriculture and engineering. For the 2002-03 biennium, the total general revenue appropriation to higher education totaled \$9.8 billion, a 13.9% increase over \$8.6 billion for the 2000-01 biennium.<sup>13</sup> Higher Education alone accounted for 15.9% of the total general revenue appropriation for 2002-03 biennium.<sup>14</sup>

Higher education plays an important role in building a competitive and educated workforce, and places importance on providing a strong higher education system to serve all students in the state. In making recommendations relating to higher education, the task force looked primarily at areas of the higher education budget that can be tightened simply by eliminating or adjusting funding for those items that do not meet their performance objectives or are not a priority expenditure, as well as ways to allow universities to better meet their financial needs by adjusting the cap on university tuition, and making changes to the funding methods of community colleges.

## **Higher Education Funding**

The two important sources of funding for the general academic higher education institutions are the Permanent University Fund (PUF) and the Higher Education Fund (HEF). The PUF and the HEF each serve different schools and have funds that mirror one another to provide funding for certain specific activities. Appendix C lists the PUF and HEF institutions, as well as which universities are eligible for funding from the various higher education funds.

### **The Permanent University Fund and Available University Fund**

The PUF fund is a public endowment that provides some funding for most institutions of the University of Texas and Texas A&M systems. The PUF fund has been constitutionally dedicated since 1876 through land grants, which now total 2.1 million acres of land located in 19 west Texas counties.<sup>15</sup> The Texas Constitution prohibits spending of PUF principal and requires that mineral income remain in the fund and not be spent.

The Available University Fund (AUF) is a constitutionally established fund for general academics, specifically for PUF institutions. Income from PUF investments provides the funding for the AUF, a separate account used for debt service at all the PUF institutions, and for “excellence” funding at UT-Austin,

Texas A&M-College Station, Prairie View A&M, and the UT and A&M system offices. In 1999, Texas voters approved HJR 17 which amended the Constitution to revise the PUF's distribution and investment practices by shifting to a total returns on all PUF investments, including capital gains for funds to be distributed to the AUF, which receives PUF monies to distribute to the higher education institutions. According to the Higher Education Coordinating Board, at the end of August 2001 the net investments of the PUF were valued at \$7.5 billion.<sup>16</sup>

#### The Higher Education Fund and Higher Education Assistance Fund

Amendments to the Constitution in 1984 and 1993 gave the Legislature the ability to provide appropriations for universities that do not share the PUF income through the Higher Education Assistance Fund (HEAF). Institutions can acquire land; construct, repair and refurbish buildings; and purchase capital equipment and library materials with HEAF funds. The Legislature appropriated \$100 million to the HEAF each year between 1986 and 1995 and increased to \$175 million a year beginning in 1996.<sup>17</sup>

The Higher Education Fund (HEF) is a constitutionally established fund for general academics, specifically for those institutions not eligible for PUF/AUF funding. This dedicated endowment fund is supported with General Revenue and receives a total appropriation of approximately \$50 million each year.<sup>18</sup> The annual appropriation is intended to build the corpus of the HEF to \$2 billion, as well as to fund the Texas Excellence Fund.<sup>19</sup> The corpus of the HEF, like the PUF, cannot be spent. Once the HEF reaches \$2 billion, the annual appropriations to the HEAF will cease, and a portion of the income from investments will be added back to the corpus of the HEF; the remainder of any HEAF income is distributed to the HEAF institutions.<sup>20</sup>

#### The Texas Excellence Fund and University Research Fund

The 77<sup>th</sup> Legislature passed HB 1839, creating the Texas Excellence Fund (TEF) and the University Research Fund (URF) to support excellence and research at general academic institutions. Each research fund was appropriated \$33.8 million for the 2002-03 biennium

The TEF is for HEF-eligible institutions and is supported by a portion of the HEF.<sup>21</sup> The \$50 million annual appropriation to the HEF endowment is reduced by the amount of interest earned by the HEF, and transferred to the TEF. TEF funds are distributed among 21 eligible institutions, which are first divided by their annual restricted research expenditures and the number of PhDs awarded, and funds allocated based on the restricted research expenditures.<sup>22</sup> Accordingly, three "comprehensive research universities" share 80% of the TEF and the other 18 HEF-eligible institutions share the remaining 20% of the fund<sup>23</sup>.

The URF is for PUF-eligible institutions other than UT-Austin, Texas A&M, and

Prairie View A&M; the eight eligible institutions are divided according to the number of master's and doctoral degrees awarded and annual restricted research expenditures. The four teaching institutions that are URF-eligible each receive \$1 million annually and the other four share the remaining funds based on restricted research funds, and master's and doctoral degrees awarded.<sup>24</sup>

**Prevent reductions in the Higher Education Fund before the \$2 billion corpus is built.**

The Constitution prohibits spending the corpus of the HEF, yet it is important for Legislators to resist temptation to find ways to dip into this fund prematurely. The Legislature should continue to demand prudent fiscal responsibility with the PUF and HEF accounts to ensure funding is available to provide resources to the state's institutions of higher education in the future. Although the current balance is far from the \$2 billion goal, building the corpus of the endowment is important to building a strong financial backbone for the non-PUF institutions of higher education.

**Repeal HB 1839 from the 77<sup>th</sup> Legislative Session, creating the Texas Excellence Fund and the University Research Fund.**

The TEF siphons money out of the HEF, which delays reaching the \$2 billion corpus in that fund. Not only are these funds a biennial drain on General Revenue, but they also costs the state the potential investment income and time lost in trying to fully fund the HEF corpus. In an effort to continue to build the HEF and be equitable to both PUF and non-PUF institutions, the legislation created in HB 1839 should be repealed and both the TEF and URF should be eliminated.

**Capital Equity and Excellence**

**Enforce the rider eliminating Capital Equity and Excellence Hold Harmless funds after the 2002-2003 biennium.**

For the 2002-2003 biennium, Capital Equity and Excellence funds are allocated general academic institutions that do not receive PUF funds, which only Texas A&M University and the University of Texas receive. The equity portion is intended to balance out funding for building and maintenance costs, which A&M and UT receive through PUF. Excellence was intended to allow an institution to pursue unique missions, such as research enhancement, student services, and recruitment. The hold harmless funds were established so that differences in allocation between the 2000-01 and 2002-03 budgets would not adversely impact schools that lost funding for these items in the recalculations

According to Higher Education Special Provision 50, Capital Equity and Excellence Hold Harmless funding is not to be continued after the 2002-03

biennium. Because the hold harmless. This rider should be enforced and will provide the state with an estimated \$12 million in savings.

## **Special Items Matching**

### **Create a matching funds ratio for special item matching.**

In Texas, the core of higher education funding is provided through formulas. Other appropriations for special needs or programs are referred to as “special items” and are often funded in a lump sum. For the 2002-2003 biennium, the Legislature approved \$258 million in special items appropriations. Creation of a matching program would allow the state to offer some support and funding for these items, while the institution and private donors must contribute the difference.

A matching program helps provide money for special interests and areas of excellence, while putting the pressure on institutions to review the necessity of the programs they fund through the matching program. The program also encourages institutions to leverage and raise funds from private sources, and provides an incentive to donors who can make a sizeable investment in the university with the prospect of stretching their dollars with the addition of matching dollars. Matching programs have proven to be successful in the twenty-four other states that have matching programs, prompting other states to look into establishing their own programs.

Nearly half of the states have created matching funds programs to encourage this practice and three other states had bills before their 2002 legislative sessions.<sup>25</sup> Evidence suggests that state matching funds generate a sizeable return on investment for both the state and higher education administrators. In FY 2001, \$117 million of state funds matched \$214 million from private sources for a return investment of 85%.<sup>26</sup>

Simply by creating a 1:1 ratio for special item matching, Texas could reduce the biennial appropriation by half from \$258 million to \$129 million, while still offering financial support and encouraging private donations that would keep the funding unchanged.

## **Institutional Enhancement**

### **Institutional enhancement should either be eliminated or cut across the board, or cut from schools with special item funding.**

Institutional enhancement is a new funding mechanism for Higher Education institutions. Because of budget surpluses in the 76<sup>th</sup> and 77<sup>th</sup> legislative sessions, extra money was given to academic institutions to use at their discretion. The total for institutional enhancement, not including the consolidated

funding of special items, is \$138 million per biennium. Each school, except those that benefit from new excellence funding or from the Permanent University Fund, receives \$2-3 million per biennium.

Individual institutions can use the institutional enhancement for any purpose they deem necessary, although generally it was expected to be spent on unique or specific program development for the individual institutions. Its purpose is to provide support to strengthen regional research, academic and extension services. The vast majority of the institutional enhancement funds have been used for faculty salaries and wages, according to Legislative Appropriations Requests submitted in August 2002. The monies have been used to both add faculty for new programs and to enhance faculty and staff salaries throughout the institutions. A small portion of the funds have been used for scholarships, graduate assistantships, and student recruitment and retention efforts.

These enhancement dollars were given to general academic institutions to enhance or develop unique programs when the state was running a budget surplus, however, the surplus no longer exists and the institutional enhancement should be cut. These funds were never intended to be added to the individual institutions' baseline budgets, and after two biennia, funds needed for capitol outlay or start up monies for any new programs or enhancements should be complete. In addition, this funding was created by virtue of surpluses and should not be funded in the upcoming biennium when the discretionary funds are not available.

## **Teaching Experience Supplement**

### **Eliminate the teaching experience supplement.**

Beginning in the 1998-99 biennium, the Legislature added a teaching experience supplement to the Instruction and Operations formula (I&O) for higher education institutions. The additional weight is added to the formula for lower and upper division semester credit hours taught by tenured or tenure-track faculty. Initially, the supplement was 5%, and doubled to 10% for the 2002-03 budget. In addition, a rider was placed in the Appropriations Act stating that "it is the intent of the Legislature that the weight shall increase by 10% per biennium, up to 50%." So, in 2004-05 it is intended that the weight will be 20% and up to 50% in the 2010-11 biennium.

For the 2002-03 biennium, the estimated cost of the supplement is \$96.8 million. If the number of courses taught by tenured track faculty, the rate in the I & O formula, and the number of semester credit hours taken remain equal, the amount for the teaching experience supplement will be \$490 million per biennium in 2010-11. However, these variable elements are expected to increase, underestimating the long-term cost per biennium.

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There is little indication that the number of courses taught by tenured or tenure track faculty has increased since the supplement has been added, and in fact, in some cases it has decreased. Without overwhelming evidence that the supplement has been successful, the monies appropriated to this program do not appear to make a dramatic difference. While encouraging tenured and tenure track faculty to increase the number of courses they teach is a worthwhile cause, the state should expect more than a marginal return for its dollar.

## **Tuition Waivers**

### **Restore non-resident tuition rates for all non-residents.**

Texas has seventeen types of tuition waivers that waive the out of state tuition for nonresidents. According to the Higher Education Coordinating Board, these tuition waivers were granted to 30,514 nonresident students in 2001, resulting in \$120 million less tuition collected.<sup>27</sup> The waivers are not only for students from other states, but from other countries as well; a few of these tuition waivers are discussed below.

Citizens of Mexico with financial need may enroll in a general academic teaching institution in a county that borders Mexico, or participate in a pilot program to attend a general academic institution anywhere in the state. Combined, these two waivers were granted to 1,942 students, waiving \$10.2 million in tuition in 2001. Neither the waiver, nor the waiver pilot program, is a priority of the state. The state of Texas has no obligation to educate a student living in another country.

The Competitive Academic Scholarship Waiver waives out of state tuition for nonresident students who receive competitive scholarships of at least \$1000 from a Texas public college or university for the academic year or summer in which they are enrolled. The number of out-of-state students receiving this waiver may not exceed 5% of the total registered at the institution for the same semester of the preceding year. Coordinating Board numbers show that in 2001, 3,913 graduate students had these waivers totaling \$16.1 million in waived tuition, while 4,794 undergraduates received the waiver, waiving \$24.5 million in tuition. This means that the state has agreed to waive a total of \$40.7 million of tuition for nonresident students that may have received as little as \$8.7 million in competitive academic scholarships. This is not a good deal for the state.

Even a nonresident with a nonacademic scholarship can get a tuition waiver. In 2001, a total of 1,086 students, only 40 of which were graduate students, received tuition waivers because they held a nonacademic scholarship. These waivers totaled \$4.8 million in uncollected tuition. Although fewer of these waivers were granted compared to the academic scholarship waivers above, at least those waivers are based on academic merit.

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Texas' taxpayers support higher education in the state, in part, so that Texas' students have the benefit of receiving a quality education in the state of Texas. The state has no obligation to provide education to nonresidents that have other options for higher education in their respective states. At a time when university tuition is an issue and higher education funding is in question, it is even more important for the state to focus on its priorities. The state's first priority should be for the provision of higher education for Texas' students- not nonresidents.

## **University Tuition**

### **Remove the cap on tuition at four-year, public universities.**

Tuition for four-year public universities is capped by the Texas Legislature. The Education Code establishes a two-pronged tuition rate; a statutory tuition rate that increases gradually each academic year until 2005-2006 when it reaches \$50, and a designated tuition rate to set by the individual university governing boards, to supplement, but not exceed the statutory rate. For the 2002-2003 academic year the statutory tuition is set at \$44 per semester credit hour, but universities may charge undergraduates up to \$88 per semester credit hour once the two tuition rates are combined. All of this tuition is for general education purposes. As of last fall, only six of the thirty one public, four-year universities were charging the maximum tuition rate: The University of Texas- Austin, The University of Texas- Dallas, The University of Texas-Arlington, The University of Texas-San Antonio, Texas A&M University, and Texas Tech University. The majority of the public four-year universities are under the tuition cap.

The state's contribution to public universities has diminished over the last decade as other areas of the budget, such as public education and health care, have seen tremendous increases. According to a recent article in the Houston Chronicle, the University of Texas System only gets about a quarter of its \$7 billion budget from state tax dollars.<sup>28</sup> With decreasing appropriations from the state, public universities are forced to find federal funding and private donations to fill funding gaps, but are unable to pass any of the increasing costs on to the students.

The Legislature should consider ways to lift or raise the cap on tuition that would allow the individual universities to respond to the needs of their particular campus. The Legislature has generally held the authority to cap tuition by setting the statutory tuition and then capping the designated tuition, creating something of a ceiling and a floor for public universities. The Legislature may continue to exert some authority by lifting the cap on the designated portion of the tuition and allowing the university regents to set that amount, while keeping the statutory tuition in place. The state will continue to appropriate general revenue to these universities ensuring that the universities still remain accountable to the Legislature. Nationally, fifteen states let institutions of higher education set

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tuition and fees, twenty states give the authority to the Legislature, and the remainder relies on some combination of those methods.<sup>29</sup>

Removing the cap on tuition allows universities to generate necessary additional revenue, which can be used to hire and retain outstanding faculty and develop and enhance educational opportunities for students. It also clears the way for free market competition among universities. Since the majority of the public universities have set tuition under the cap, there are still alternatives to those institutions that will raise their tuitions. It is appropriate for businesses to pass along their increasing costs to the consumer and the universities are no different. Placing an artificial cap on tuition will leave gaping holes in university budgets if the universities are unable to keep pace with their increasing costs.

Furthermore, removing the cap on tuition allows universities to operate and market themselves in new and innovative ways, with greater accountability to their students. Even under the current system, university enrollments are tight and it is often impossible for a university to accommodate every student that wants to attend. While financial aid and scholarships will still be available to students, it is realistic to expect that some students will be unable to afford some universities. However, it is also assumed that this will positively impact other universities that have lower tuition by comparison, yet may now struggle to enroll the most competitive high school graduates. Certainly, universities will have to be responsive to its students and its applicants, and it will encourage even the largest universities in the state to be competitive and prevent them from laying claim to the most competitive students.

The keys to a competitive and healthy higher education system, as well as a prosperous Texas, rest in the public universities' ability to operate competitively and efficiently with decreasing reliance on the state. Lifting the cap on tuition should allow universities to respond to their needs with fewer constraints from the state, while still providing Texans access to higher education. Encouraging competition in Texas' public universities will be beneficial to the state and to its students, and will also create a stronger and more competitive system in comparison to other states.

### **Eliminate the Tuition Equalization Grant Program.**

Every year the state provides private institutions of higher education with a total of \$82 million in tuition equalization grants (TEG). While these grants were necessary when the program began in 1971 in order to address the limited capacity of state universities to accommodate more students while the private schools had room to accept additional students, these grants are no longer necessary. Students in Texas now have many options to attend public universities in Texas, and the vast majority of four-year college students attend a public university. Additionally, the program requires recipients to be Texas



residents, enrolled at least half-time, and still, only 50% of TEG recipients earn a baccalaureate degree within six academic years.

The state should not be providing assistance to private universities when the vast majority of Texas' students are educated in public universities. This is a clear example of a program that is unnecessary and reflects the needs of a very different time in Texas higher education. Furthermore, students have many choices in where to pursue higher education and there are affordable alternative to private universities.

The 2002-03 appropriation for TEGs was \$82.2 million annually and \$164.4 million biennially. For comparison, the 2002 appropriation for TEGs was only \$10 million less than the total appropriation for Southwest Texas State University, and could entirely cover the total combined appropriation for multiple campuses in the University of Texas System or the Texas A&M University System, among others. Entire public universities can be funded with the money appropriated to TEGs. These grants should be eliminated in the 2004-05 budget and the Legislature should examine other grant programs in higher education to determine which grant programs create opportunities for students to pursue higher education, and which programs may be unnecessary.

## **Developmental Education and the TASP Test**

**Abolish the Texas Academic Skills Program.**

**Expend all developmental education funds at the community college level.**

Established in 1987, the Texas Academic Skills Program (TASP) Test was designed to be a diagnostic tool, placement device, and a standard for skills an entering college freshman should possess. Originally required of undergraduates in Texas' public post-secondary institutions, the test must now be taken before beginning college work. The TASP test identifies students who need developmental education to remediate any deficiencies in their preparation for college.

Students must pass math, reading, and writing sections and may repeat sections until they are successful in passing them. Unsuccessful students are required to enter and remain in appropriate remedial classes until they pass all test sections. Exemptions are allowed for high-level performance on the SAT, ACT or TAAS tests. Classes are organized by each institution, with community colleges making remediation a part of their mission, while state universities offer it as supplemental education. Some research universities require students to take the necessary remedial classes at community colleges.

Developmental education classes address deficiencies in students' academic preparation for college, and most are semester-length courses with credits not

applicable for either baccalaureate or associates degrees. Institutions charge students at the usual tuition rates and receive funding for course-based developmental education through the funding formulas; university general appropriations are reduced in relation to any tuition charged. Community colleges use formula funding for instruction and operations, and tuition for overhead costs in addition to instruction.

Remedial instruction increased the most the year after the TASP test was implemented. Since then, developmental education has remained constant at 2.8% of all lower-division instruction, increased 1.8% in community colleges, and decreased 3.9% in universities, 4.3% in the Texas State Technical College System, and 4.6% in the Lamar State Colleges. The combined effect was an overall statewide increase of 1.5%. More than 88% of development instruction occurs in two-year colleges, with mathematics accounting for 65% of the instruction and the remainder split between reading and writing.

The TASP test is one of only many tests that the traditional student takes upon graduation from high school continuing on into their education at either a two or four-year college. Many institutions have individual methods of placement testing and evaluation regardless of a student's performance on the TASP test, and many of these institutions have open-enrollment policies. The TASP test's effectiveness at evaluating a student's preparation for college is in many respects duplicative, as well as an unnecessary hurdle for a student before beginning classes. The TASP test should be abolished and placement and evaluation should be made by examination of other common test scores, or by an institution's individual policies.

Additionally, developmental education to remediate deficiencies in a student's preparation for college should be done through community colleges. The state should expend all developmental education funds at the community college level as that is where the vast majority of that instruction already occurs. Certainly the state of Texas should expect students to meet a standard of academic preparation and should not make efforts at remediation at all levels; students can be expected to complete remedial coursework at the community college level.

## **Community College Funding**

**Clarify that public community college tuition and fee revenues be used for a portion of instruction and administration costs, and amend statutes or add language to the Appropriations Act accordingly.**

**Direct the Texas Higher Education Coordinating Board to develop a contact hour-based allocation that does not depend on a biennial cost study.**

Community college funding is determined through a formula based on "contact hours" in which the Higher Education Coordinating Board (THECB) conducts a

cost study to find the per-contact hour cost of both instruction and administration. Community colleges received \$1.7 billion in appropriations for FY 2002-03, representing a 9% increase from the previous biennium. Of this increase, \$88 million is for enrollment growth of 5.7%, which reflects the change to basing enrollment growth on actual rather than projected growth, and an increase in the contact-hour formula funding of \$51 million.

The 61<sup>st</sup> Legislature in 1969 passed language that allowed for the state to appropriate money for instruction and administration (I&A) costs for community colleges, while allowing the community college districts to use local tax dollars as well as tuition and fees for construction, and the operations and maintenance of facilities. While the THECB recommended that the state pay for all I&A costs, the statute adopted used language indicating that state funding for I&A be only “sufficient to supplement”, rather than fully funding.

Community colleges assert that the legislative intent was to fully fund I&A. According to the Legislative Budget Board’s (LBB) Staff Report to the 77<sup>th</sup> Legislature, there is no historical data to support this theory. Despite this, over the years pressure for full funding has found its way into THECB recommendations to the Legislature. The LBB’s report addressed the full funding issue with respect to I&A for community colleges and recommended two changes to address the issue, which are the same recommendations outlined above. Ultimately, no action was taken on the recommendations made in the LBB report, possibly because most members of the Legislature have a significant community college presence in their district and are wary of changes that might negatively impact their community college.

However, as the backbone of the future of higher education, neglecting to clarify the full funding issue will only create additional problems in the future. Community college growth has outpaced typical four-year universities and the trends are expected to continue. This growth paints a positive picture for higher education in the state of Texas, but because of the tremendous growth, full funding of I&A would be virtually impossible for the state to maintain. Clarifying legislative intent would alleviate confusion and pressure for full funding now and in the future.

Additionally, the role of the state should be to augment local governments in their desire to create or continue local, 2-year higher education opportunities, but not to fund the entire cost of instruction and administration. Tuition, fees, and a taxing authority make community colleges independent with opportunities to address financial needs, yet significant differences exist among the institutions with respect to philosophies and the local property tax base. A funding formula should be developed that is more in-line with general academic institution formulas based on semester hours in order to omit the biennial cost study and address the specific needs of community colleges.

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- <sup>1</sup> Edgewood III; 826 S.W. 2d 489
- <sup>2</sup> Comptroller of Public Accounts, e-Texas, Recommendations of the Texas Comptroller, "Review the Role of Regional Educational Service Centers in Public Education, December 2000, ED-10, <<http://www.e-texas.org/recommend/ch06/ed10.html>>.
- <sup>3</sup> e-Texas, ED-10.
- <sup>4</sup> e-Texas, ED-10.
- <sup>5</sup> e-Texas, ED-10.
- <sup>6</sup> e-Texas, ED-10.
- <sup>7</sup> e-Texas, ED-10.
- <sup>8</sup> Texas Education Code, 8.101-8.104.
- <sup>9</sup> TRS Presentation to Senate Finance Committee, Subcommittee on Rising Medical Costs, by Charles Dunlap, Exec.Dir., and Ronnie Jung, Deputy Exec. Dir., September 5, 2002, 2.
- <sup>10</sup> Legislative Budget Board, Guide to the Texas State Employee Uniform Group Health Coverage Act (House Bill 3343), May 02, p 1.
- <sup>11</sup> Guide to the Texas State Employee Uniform Group Health Coverage Act.
- <sup>12</sup> Guide to the Texas State Employee Uniform Group Health Coverage Act,p4
- <sup>13</sup> Higher Education Coordinating Board, "Texas Higher Education Facts-2001," <<http://www.thceb.state.tx.us/reports/pdf/0445.pdf>>.
- <sup>14</sup> "Texas Higher Education Facts-2001."
- <sup>15</sup> "Higher Education Coordinating Board, "Permanent University Fund, Higher Education Assistance Fund, Overview," <<http://www.thceb.state.tx.us/reports/pdf/0434.pdf>>.
- <sup>16</sup> "PUF, HEAF, Overview."
- <sup>17</sup> "PUF, HEAF, Overview."
- <sup>18</sup> Legislative Budget Board presentation to the Joint Interim Committee on Higher Education Excellence Funding, "State Funding for General Academic Institutions of Higher Education," Feb. 2002, p. 13.
- <sup>19</sup> "State Funding for General Academic Institutions of Higher Education," p 13.
- <sup>20</sup> "PUF, HEAF, Overview."
- <sup>21</sup> "State Funding for General Academic Institutions of Higher Education," p. 15.
- <sup>22</sup> "State Funding for General Academic Institutions of Higher Education," p. 15.
- <sup>23</sup> "State Funding for General Academic Institutions of Higher Education," p. 15.
- <sup>24</sup> "State Funding for General Academic Institutions of Higher Education," p. 15.
- <sup>25</sup> "Raising Dollars for Education," State Government News, April 2002.
- <sup>26</sup> "Raising Dollars for Education."
- <sup>27</sup> Chairman Rob Junell, House Committee on Appropriations, letter to Chairman Rodney Ellis, September 17,2002
- <sup>28</sup> Janet Elliot, "UT chancellor advocates new ways to pay the bills," Houston Chronicle, December 11, 2002.
- <sup>29</sup> "Universities seek end of tuition cap," Dallas Morning News, August 13, 2002.

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ARTICLE V  
Public Safety  
and Criminal Justice

And

ARTICLE VI  
Natural Resources



# PUBLIC SAFETY and CRIMINAL JUSTICE

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Three of the largest state agencies in the state are funded through Article V of the state budget: The Department of Criminal Justice, The Texas Youth Commission, and the Texas Department of Public Safety. The task force's recommendation for Article V is simply the consolidation of an agency that is somewhat duplicative.

## **Adjutant General's Department and Texas Military Facilities Commission**

### **Merge the Adjutant General's Department and the Texas Military Facilities Commission.**

The Adjutant General's Department (AGD) was created to execute the Governor's constitutional and statutory responsibilities relating to the state's military forces, of which the Governor is Commander in Chief. The state military forces consist of the Texas Army National Guard, Texas Air National Guard, and the Texas State Guard. The Governor appoints the Adjutant General and two assistants to command the forces.

The Texas Military Facilities Commission (TMFC), formally the National Guard Armory Board, was created in 1935 and primarily rents armories and other facilities to the AGD. In 1980 the agency developed a program to renovate older armories and facilities that were designed to meet the structural integrity of building and safety codes, increase the economic value, and maintain these facilities. The agency maintained 337 facilities in over 100 locations during the 2002-2003 biennium.

The TMFC and the AGD manage several empty armories around Texas, and although there has been discussion about consolidating or closing some of the armories in the past, lack of coordination between the two agencies has prevented some of this from happening. Additionally, the two agencies maintain their offices at Camp Mabry in Austin, and there would be no cost or time associated with physically moving the agencies together, and is in keeping with a 1996 Sunset Advisory Commission Staff Report that suggested abolishing the TMFC and transferring its duties to the AGD.

Merging the agencies is a logical step given the need for greater coordination and since they are already housed together. Merging the two entities would more than likely reduce their total staff by seven for an annual savings of

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\$359,151 in general revenue, and there may be additional savings from eliminating the per diem and other incidental expenses from the members of the TMFC.



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# NATURAL RESOURCES

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Article VI, Natural Resources, encompasses a variety of different state agencies, including the Department of Agriculture, the Texas Commission on Environmental Quality, the General Land Office, and the Texas Department of Parks and Wildlife. These agencies receive the bulk of their funding through general revenue and general revenue dedicated fees. TCEQ is one of a few Article VI agencies that is primarily fee driven. Because the funding is financed primarily through dedicated funds, finding easily accessible cost savings is difficult, though passage of some legislation might help to free up dollars.

The task force recommendations for Article VI are an attempt to clearly direct funds to a particular account in order to stay in compliance with federal law, an evaluation of state priorities that would leave two small programs without funding in the upcoming biennium. A final recommendation regarding the General Land Office addresses a mechanism for evaluating and appraising state properties that could be sold or leased, and presenting those options to the state outside of the Governor's list, which currently allows the Governor to select land that is unused or underutilized.

## **Texas Commission on Environmental Quality, Air Programs**

**Create a Title V fund specifically for Air Emissions Fees used to run Title V programs.**

Fund 151 is the Texas Commission on Environmental Quality's (TCEQ) account that funds all air programs in Texas. As a result of dwindling revenue coupled with stable or increasing air program costs, the TCEQ Sunset Bill, as well as agency reviews and independent reports, project that Fund 151 will be depleted in the near future. Within Fund 151 is the Title V program, which is a specific program designated by the United States Environmental Protection Agency (EPA) to fund particular air programs. The EPA requires states to do emission inventory of industries that charge Air Emissions Fees to cover the administrative costs of the Title V program. Additionally, the EPA mandates that Title V cannot be funded through general revenue- only through emissions fees. Likewise, funds from Title V cannot be spent on other air programs.

In 2002, TCEQ began considering a fee increase on industry to fund Title V programs. This prompted concerns among industry that revenue from Title V was being spent on other air programs to make up for the deficiency in Fund 151. The primary question is this: Is there enough revenue from Air Emissions Fees to run Title V programs? If so, why should the state increase fees on industry? Although in May 2002 the agency commissioned an independent report by Sidney Hacker of SBH consulting to study this matter, TCEQ still has yet to

sufficiently answer this question. If in fact the agency is using Title V Air Emissions Fees to fund programs in Fund 151, this is a violation of the Clean Air Act.

Creating a Title V fund, separate from Fund 151 and routing air emissions fees directly to the Title V fund would ensure compliance with EPA standards. Separating the funds will also help TCEQ maintain accurate accounting records of Title V man-hours, which has been a source of concern in the past. Furthermore, this action would lend TCEQ more credibility with fee payers.

## **Lower Colorado River Authority**

### **Privatize the Lower Colorado River Authority.**

The Lower Colorado River Authority (LCRA) is a conservation and reclamation district in Central Texas, operating on revenues from wholesale electric power services, electric transmission services, water services, and community services in 58 counties. The LCRA supplies electricity to more than a million Texas through 42 wholesale customers, including 9 electric cooperatives and 33 cities. It also serves numerous water customers including cities, certain agriculture industries, and municipal utility districts, and operates six dams and around 40 recreational parks.

The LCRA receives no tax dollars and sells electricity, electric transmission services, and water services at cost, and is generally exempt from paying taxes.<sup>1</sup> According to the LCRA, nearly three-quarters of FY 2002 revenues, totaling \$570.3 million, were from electric sales.<sup>2</sup> LCRA is an attractive candidate for privatization due to its prime assets, existing infrastructure, and share of the market. The state should privatize the LCRA, allowing private enterprise to pursue profits and allow the market to govern its business practices, as well as add the assets to the local tax roles that they are currently exempted from. Sale of the LCRA could reasonably expect to bring in more than one year of the LCRA's annual earnings. This an opportunity for the state to not only generate revenue, but do so in an effort to allow private enterprise to take over a function that the state does not need to fulfill.

## **State and Local Parks**

### **Withhold appropriations for grant assistance to local governments for local parks, using half of the savings to fully fund state parks.**

In the 2002-03 biennium, the Legislature appropriated \$49.9 million toward local parks, which as distributed, are matched by the local governments requesting the grant. Essentially the program allows local governments to fund half while the state spends half as well. Funding for the grant program comes partially from the sporting goods sales tax, and the other portion comes from a dedicated fund, all

of which is considered general revenue. The state would probably save somewhere on the order of \$15 million if the appropriations are withheld, and could potentially find additional savings if the dedicated fund were release to the state through statute.

On balance, the state has priorities that outweigh the need for the state to appropriate GR to local governments in support of local parks. Local government should balance their local priorities with funding local parks, and the state should only be responsible for funding the state parks. Local parks are a local issue, providing benefit primarily to local residents, and thus should be funded by local revenues according to the priority placed on parks. While parks may enhance a community's appearance and may even be an important quality of life issue, the state has other needs that should be put ahead of local parks.

### **Adopt-A-Beach**

#### **Turn the adopt-a-beach program over to local entities.**

Since the first cleanup in 1986, more than 292,000 volunteers have picked up 5,388 tons of trash along 200 miles of Texas beaches through the Adopt-A-Beach program. This program strives to raise awareness, educate, and generate public support for state, national and international action to clean up coastal waters. This all-volunteer effort is dedicated to preserving and protecting Texas beaches. The program's success is due to the generous efforts of dedicated volunteer county coordinators, coastal community leaders, sponsors and citizens.

Local governments, businesses, or organizations can coordinate these activities. The state may have given the program credibility or raised its profile in its infancy, but the state does not need to provide a volunteer coordinator of sorts for this activity. Local entities can certainly run the program, and perhaps even further develop the program with better ability to organize at the local level.

### **Oil Spill Response**

#### **Consolidate the oil spill response activities within one agency.**

Currently there are three agencies that handle some aspect of oil spill response duties: the General Land Office (GLO), the Railroad Commission (RRC), and the Texas Commission on Environmental Quality (TCEQ). Each agency has jurisdiction over particular areas depending on the type of spill, the location of spill, and the magnitude of the spill. The state contingency plan for dealing with spills indicates that generally, the RRC has authority over crude oil spills resulting from oil exploration and production operations, the GLO would handle an oil spill in the coastal areas from an oil tanker or offshore rig, and TCEQ is the lead agency in spill response to certain inland oil spills, all hazardous substance spills,<sup>3</sup> and spills of other substances that may cause pollution or impact air quality.

There are exceptions to these rules, however, and other agencies may have additional peripheral responsibilities in case of a spill.

These divisions in responsibilities are needless. The duties delegated to the GLO neglect to recognize that in the case of an oil spill in the Gulf of Mexico, the United States Coast Guard will respond and have clean-up responsibilities as well and would be nearly duplicative of the GLO's responsibilities. The Memorandum of Agreement between the Coast Guard and the GLO suggests that the GLO mostly plays a secondary role in any oil spill response or prevention activities with the Coast Guard taking the lead, and it seems that there are no duties which only the GLO could fulfill in comparison to the other state agencies with some oil spill response duties.<sup>4</sup> Certainly the threat of spills and leaks is an area of state concern, but it is questionable whether three agencies are necessary to handle such occasions. Concentrating the response efforts in one location cuts out needless contacts in multiple agencies within the state and would allow a more swift response in coordinating clean-up efforts with the federal government. Charging each agency with part of the duties is wasteful and duplicative, and the state should consolidate these efforts into one agency that could best handle these needs.

### **Energy Conservation and Alternative Fuels**

#### **Abolish the State Energy Conservation Office and transfer oversight of oil overcharge settlement funds to the Texas Building and Procurement Commission.**

The State Energy Conservation Office (SECO) was created in 1975 and was most recently transferred to the Comptroller's office by the 76<sup>th</sup> Legislature. Funding for SECO primarily comes from court settlements from federal oil overcharge settlements, which are used to promote and support energy efficiency and renewable energy sources. The management of oil overcharge settlement funds should reside with the TBPC, as it is the state agency that has responsibility for facilities management. The Comptroller's office is not the appropriate place to oversee any state energy conservation activities or manage these funds, particularly when the state has an agency with the express purpose of managing such activities.

#### **Abolish the Alternative Fuels Research and Education Division and conduct an interim study on state alternative fuels programs.**

The state currently promotes the use and development of alternative energy sources and subsidizes many of the efforts of this industry. The Railroad Commission has an entire division, the Alternative Fuels Research and Education Division, dedicated to education and promotion of alternative fuels, including the development of an alternative energy science curriculum supplement that correlates with statewide tests for public school students. These

types of activities simply are not necessary functions of state government and the state should not be involved in promoting or giving preference to one natural resource over another; marketing and education for alternative fuels should be left to those businesses with an interest in alternative fuels. Furthermore, the research and education division of the RRC received slightly under \$6 million in the 2002-03 biennium, yet it has no truly meaningful performance measures. While alternative fuels programs may be a politically attractive way to address the environment, these programs should be held to a measurable standard that allows legislators to evaluate the success of such programs. The Legislature should immediately abolish the Alternative Fuels Research and Education program at the Railroad Commission and thoroughly review all of the state's alternative fuels programs and evaluate the impact of such programs.

### **General Land Office**

**Do not limit the sale or lease of state-owned properties to land that is unused or underutilized; consider additional ways to determine whether state land should be for sale.**

Consider the sale of state property, regardless of whether the land is included on the unused or underutilized report.

Each year the General Land Office (GLO) produces a report to the Governor on state owned property that is unused or underused. Statute allows the Governor ninety days to approve or disapprove the recommendations, after which time the Land Commissioner is authorized to conduct the approved transactions. Once recommendations are approved, the statute freezes the ability of land-owning agencies of land-owning state agencies to change the use or dispose of properties that have recommended transactions.

Some property has remained on the list and approved since 1995, for a variety of reasons. The changing market conditions may make selling or leasing land difficult, or opposition may exist in attempts to sell park lands for construction. In addition, the relocation costs of moving an agency may outweigh the potential savings of moving the agency to another location. As an example, the Starr office building on 6<sup>th</sup> Street in Austin is still used by the Comptroller's office, yet it was approved for sale or lease in 1996.

However, limiting the sale or leasing of lands to only those properties that are unused or underused neglects to address properties that could be turned into financial assets. According to a study by the American Legislative Exchange Council, the Reason Foundation estimates that cities and states own more than \$226 billion in assets that could be sold to the public.<sup>5</sup> Selling these assets could allow the state to not only generate revenue off the sale or leasing of these lands and the subsequent tax revenue, but may allow the state to realize additional savings as a result of moving to a cheaper location and less expensive labor.

As an example, the Texas School for the Blind is located on 45<sup>th</sup> Street in Austin, which was once on the outer edges of Austin, but is now surrounded by business and residential areas that are now in the central part of Austin and a prime area for commercial development. This land is valuable and offers opportunity for residential or business development, and, in addition to the revenue generated from the sale of the land, putting this land on the tax rolls adds an additional source of revenue. The state could move such a facility to an area that might suitably meet the needs of the residents at a lower cost, and could potentially become an important employer in an area. Regardless of the value of the land and whether services could be provided better and at less cost, this property will never appear on the Governor's list if it continues to be fully utilized. The state should have an opportunity to evaluate these properties on something other than the use of land.

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<sup>1</sup> LCRA website, "LCRA Financial Highlights," <<http://www.lcra.org/about/finance.html>>.

<sup>2</sup> "LCRA Financial Highlights.

<sup>3</sup> Texas Natural Resources Conservation Commission, State of Texas Hazardous Substances Spill Contingency Plan, May 1999, 2-2.

<sup>4</sup> Texas General Land Office website, "Memorandum of Agreement on Pollution Prevention and Response Between the Eighth Coast Guard District and the Texas General Land Office," <<http://www.glo.state.tx.us/oilspill/moa.pdf>>.

<sup>5</sup> American Legislative Exchange Council, Show Me the Money, by William Eggers, July 2002, p.6.

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ARTICLE VII  
Economic Development

And

ARTICLE VIII  
Regulatory





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# ECONOMIC DEVELOPMENT

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State agencies working in support of economic development in the state of Texas are funded through Article VII. These agencies include the Texas Department of Economic Development, the Texas Department of Housing and Community Affairs, The Lottery Commission, the Texas Department of Transportation, and the Texas Workforce Commission.

## **Texas Department of Economic Development**

**Abolish the Texas Department of Economic Development and redistribute some of its functions to appropriate agencies.**

The Texas Department of Economic Development was established in 1997 with the goal of marketing Texas and assisting communities with their economic development opportunities in a global market.<sup>1</sup> Working toward these goals, TxED has had five core functions: tourism marketing, Market Texas, economic information, business incentives, and Smart Jobs incentives. The largest program managed by the agency was the Smart Jobs program, which has been phased out and expired at the end of 2001.<sup>2</sup> The tourism duties, which are funded from a portion of the hotel/motel tax, are regarded as the agency's shining jewel and enjoy industry support. However, all of the agency's duties could be handled by other state agencies that would either provide better opportunities for success, or that are already responsible for related aspects of TxED's responsibilities.

For instance, the Office of International Business exists to help Texas companies expand in foreign markets. Primarily, the department attends and organizes trade shows and missions, yet it has proven to be ineffective in gaining sufficient trade leads for Texas businesses. The real work that is accomplished in lead development is done through the Small Business Development Centers (SBDCs) and the Regional Export Assistance Centers. These centers do not receive much from the department in the way of leads, training, or resources, though they are effective in supporting international trade efforts in the state. Funding that presently goes to the Office of International Business would be better spent assisting these entities in their endeavors in international trade.

Since the days of the Department of Commerce, Texas has been unable to make business development work at the statewide level in a stand alone agency. The state's tax and regulatory structures mitigate against that. Therefore, the agency only acts as a liaison between the local communities and the prospective businesses. Most endeavors to attract large business ventures require the governor in cooperation with the local communities to take an active role.

Similarly, international trade functions would benefit from the visibility that leadership from the Governor's Office or the Secretary of State would bring to those efforts. Smaller funds that the agency deals with can be relocated in other relevant agencies and other programs such as the clearinghouse (a web portal with links) can be maintained by the Secretary of State, or Governor's office. The tourism functions are well supported by industry and its functions, and while important, the program is essentially contract management with the advertising agency handling the program. These activities can be managed through the Governor's office with an eye toward privatizing many of the functions, or the entire program could be managed by the Texas Hotel and Motel Association, which has already agreed to tax its consumers to pay for the advertising program.

The department has had a long and turbulent history as illustrated through reports from the State Auditors Office and the Sunset Commission. A January 2000 report found gross fiscal mismanagement in Smart Jobs, the department's largest program, with specific findings that the department lacked oversight to ensure that the funds they provide to employers are used appropriately and that contract requirements are met and that the grant distribution process is not competitive.<sup>3</sup> In the department's Sunset Review in 2001, the Sunset staff concluded that "the Department had yet to succeed as an effectively run state agency and cited numerous management and oversight concerns, as well as poor coordination of the state's tourism efforts."<sup>4</sup> The Sunset Commission at the time recommended that the department be continued for a probationary period of two-years, and in its most recent recommendations the commission suggests restructuring the department and directly linking it with the Governor's office, with some functions being assigned to the Comptrollers office and through the State Agency Tourism Council. The Sunset Commission has identified that this restructuring would create a savings of \$795,000 and a reduction of 14 positions, plus additional savings through better efficiency that cannot be quantified.

## **Texas Aerospace Commission**

### **Abolish the Texas Aerospace Commission.**

The Texas Aerospace Commission was created in 1987 in order to foster the development of the commercial space industry in Texas. That industry consists of private companies that launch satellites into space. State law directs the commission to:

- Promote economic development by fostering the commercial space industry
- Analyze space-related research
- Assist local communities in establishing a spaceport

The commission operates on an annual appropriation of \$212,815. The 77<sup>th</sup>

Legislature appropriated an additional \$1.57 million for grants to assist local communities with developing commercial spaceports.

The Aerospace Commission is undergoing sunset review in the 78<sup>th</sup> Legislative Session. In its staff report from August 2002, the Sunset Advisory Commission notes that the Aerospace Commission “lacks the organizational capacity and necessary controls to operate efficiently as a state agency.” The report also states that the commission’s economic development and research activities are duplicated by other federal, state, and local entities. Additionally, the report recommended that the administration of the Spaceport Trust Fund be transferred to the Texas Department of Transportation’s Aviation Division. Spaceport initiatives should be handled exclusively by the Texas Department of Transportation.

While the savings from abolishing this agency is minimal, the Sunset review makes the case that the Aerospace Commission is not a necessary entity for the state. In keeping with the Sunset Commission’s recommendations the Aerospace Commission should be abolished, and should furthermore be abolished immediately, rather than in September 2004 as recommended under the terms of the Sunset Act. This agency serves no purpose and ultimately is a priority of the federal government and should receive federal funding at the behest of Texas’ Congressmen. The Aerospace Commission is not a priority of the state of Texas and the state should not continue to fund an unsuccessful program such as this.

### **Texas Department of Transportation**

#### **Eliminate appropriations to the Texas Department of Transportation for tourism.**

According to the Appropriations Act, the 77<sup>th</sup> Legislature appropriated \$37.8 million to the Texas Department of Transportation (TxDOT) to support and promote tourism, and makes additional provisions and appropriations through Rider 5 and Rider 35 for the publication and distribution of travel information, such as the Texas Highway Magazine and the Texas State Travel Guide. These appropriations are unnecessary given the tourism functions already under the Texas Department of Economic Development, or another entity when TxED is reorganized in the Governor’s office, and clearly falls outside of the priorities and scope of TxDOT. Travel guides and magazines already exist, and further efforts to highlight Texas as a travel destination may be done through the “Market Texas Travel” strategy under TxED. While encouraging economic development by promoting travel to Texas may be of interest to the state, it is certainly not a priority of the state’s transportation agency and funds currently appropriated for these activities are unnecessarily duplicative.

## **Abolish the Texas Automobile Theft Prevention Authority.**

The Texas Automobile Theft Prevention Authority (ATPA) receives roughly \$30 million in biennial appropriation to help the state combat automobile theft. The ATPA has distributed theft prevention grants totaling \$139 million to cities, counties, and regions around the state.<sup>5</sup> In addition to administering these grants, ATPA works to create public awareness on auto theft prevention, provides funding for a statewide vehicle registration program, and establish a program to prevent stolen vehicles from entering Mexico. The program is “self-funding” in that the General Revenue appropriated to TxDOT for these is first collected from a portion of a \$1 fee assessed for each year of insurance on policies delivered, issued for delivery, or renewed.

These efforts are simply a law enforcement activity and not the responsibility of TxDOT. The Legislature should not use General Revenue to fund ATPA.

## **Transportation Funding**

**Undo the past county fee switch. Support county road assistance from the state with a portion of vehicle sales taxes, and return current vehicle registration fees to the state highway fund for infrastructure needs.**

Many transportation changes took place during a special session in 1992. The Texas Legislature increased the state gas tax from 15 cents per gallon to the current 20 cents per gallon. This five-cent increase was argued as a transportation “need” stemming from population growth and increased support for the North American Free Trade Agreement (NAFTA). However, one might question the “need” when realizing that transportation never saw one cent of the increase. All of the new revenue was diverted to other programs and never appropriated for transportation projects.

First, the Legislature changed the category of state funds available to counties for road work. Prior to 1992, counties received General Revenue funds in the form of vehicle sales taxes for county road work. In 1992, in tandem with the nickel gas tax increase, Texas counties began receiving State Highway Fund dollars rather than General Revenue for local road work. The highway funds that counties now receive are equivalent to the amount of General Revenue (5% of vehicle sales taxes) they received prior to 1992, making the appropriations modification revenue-neutral for counties. This county fee switch, coupled with other diversions of the gas tax increase, resulted in no new state or county road work and played a key role in negating any potential for increased investment in transportation services from the nickel tax increase.

The result of these diversions is a subsidy by state highway funds for programs that should be supported out of general revenue. The Legislature should establish an honest taxing structure where dedicated funds are spent for their

dedicated purpose and tax increases are not pushed for one reason while they are devoted to others. The Legislature should undo the past county fee switch. County road assistance from the state should be supported from a portion of vehicle sales taxes (pre-1992 funding source) and the current vehicle registration fees should be returned to the state highway fund for state infrastructure needs.

Two arguments exist for undoing the county fee switch: honesty in taxation and a critical need in transportation funding. The Legislature has a duty to be honest with its citizens. When it passes a tax increase for a stated purpose, then those monies should be devoted to that purpose. This argument is bolstered when the constitution actually devotes certain taxes to a specific purpose. When the 1992 gas tax increase was sold on the basis of providing needed infrastructure funding but resulted in no net increase in transportation funding, the legislature violated this duty of honesty to its citizens. The end result was a subsidy of programs that should be supported by general revenue at the expense of our infrastructure. The Legislature should undo this slight of hand and deal with the programs supported by general revenue honestly.

Our infrastructure funding cannot afford to lose money to subsidize other programs. Our current revenue sources can only fund 36% our transportation need. Since 1980, transportation spending per capita in Texas has fallen 34%, and now trails the national average by 12% ranking Texas 46th out of the 50 states in highway spending per capita. Spending per vehicle mile traveled in Texas is now 18% below the national average. Texas ranks third nationally for allocating nearly 35% of its dedicated funds to non-highway programs. Even when you remove the 25% for the available school fund, the remaining 10% ranks higher than the national average.

Some argue that paying for county road assistance from motor vehicle registration fees is appropriate and undoes a general revenue subsidy of transportation programs. This argument fails for two reasons. First, when the county fee switch is coupled with other diversions it is clear that the maneuvers were to use transportation needs and a five cent gas tax increase to subsidize general revenue programs. Second, the constitution dedicates motor fuels taxes and vehicle registration fees to transportation, it does not bar general revenue from being spent on transportation needs. It is entirely appropriate for general revenue to supplement transportation spending.

### **Use dedicated highway funds for infrastructure spending only.**

The Legislature appropriates highway user fees to the DPS to administer programs such as driver license issuances and driver record information services. This practice would not be considered unacceptable if the fees generated by these programs were appropriated to transportation services, instead of to the General Revenue Fund.

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Appropriating revenues generated from driver license issuance and driver records requests to the state's General Revenue Fund is wrong. The main purpose of driver licenses is to provide Texans access to the public road system. This is the nexus that allows the program to be funded with highway user fees. However, the use of a driver license for purposes other than driving does not justify depositing the fees into the General Revenue Fund, as this destroys the nexus and admits that transportation fees should not be used to fund the entire cost of the program. The same rationale applies to driver records. Driver license issuance and driver records programs require more than \$59 million per year to administer, with approximately 95% coming from constitutionally dedicated highway funds. In turn, they generate \$171 million in revenue deposited to the state's general fund with not so much as a reimbursement of the constitutionally dedicated highway funds used to operate the programs.

The current system uses dedicated highway funds to generate revenue for the General Revenue Fund. The Legislature should recognize that money generated from the use of constitutionally dedicated funds should be spent within constitutionally dedicated parameters. As a consequence, the Legislature should devote the fees generated from these programs to infrastructure spending. At a minimum the cost of operating these programs should be reimbursed to the highway fund or devoted to other infrastructure programs.

Public Interest groups would be outraged if the Legislature appropriated money generated from health insurance premiums to pay for highway construction while the level of health care services declined. The same should apply to dedicated transportation funds. When dedicated monies are used to raise additional funds, the additional funds should be devoted to the same service and so these fees should be returned to the transportation arena.

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# REGULATORY

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Regulatory agencies under Article VIII include the many licensing arms of the state, as well as provisions for the general oversight and regulation of state business. Many of the licensing bodies are fee driven as they collect on license applications and renewals and receive comparatively small amounts of state funding. The recommendations from the task force look at agency policies for travel as well as issues relating to the business of several of the licensing bodies.

## **Texas Mutual Insurance Company**

**Authorize the sale of the state's worker compensation insurance fund, the Texas Mutual Insurance Company.**

In 1991, the Texas Legislature chartered the Texas Workers' Compensation Insurance Fund with the task of stabilizing the workers' comp system. In 2001, the Legislature redesigned their charter and changed the name to the Texas Mutual Insurance Company (TMIS). The fund is part of a regulated insurance system to pay medical bills and lost wages of employees that sustain work-related injuries or illnesses. TMIC is the main provider of insurance for small businesses, and also serves as an insurer of last resort. TMIC operates like a private insurance company with strict regulation. The fund has developed a surplus of around \$575 million, which shows that this is a profitable enterprise, and is an asset which would be valuable to private insurance providers.

An e-Texas report from 2000 estimated that the fund would have netted the state around \$300 million. That amount may be a little less today, since the surplus has decreased by about \$31 million, but provides an estimated value of such a sale. Operating a profit-making insurance company does not fall within the scope of government, and such an asset should be sold into the private market.

## **Personal Vehicle Usage Policies**

**Require each agency to review personal vehicle usage policies to determine if renting a car is more cost efficient than providing reimbursements.**

The 76<sup>th</sup> Legislature tasked the Texas Building and Procurement Commission's Office of Vehicle Fleet Management with drafting a statewide vehicle fleet management plan. The plan was adopted and approved by the State Council on Competitive Government in October 2000, and was codified into law by the 77<sup>th</sup> Legislature.

The plan provides overall recommendations to improve the administration and operation of the state's vehicle fleet; however, there are several state agencies, particularly small regulatory agencies and members of the Health Professions Council, that do not have access to state vehicles but are required to do frequent traveling for inspection purposes. Thus, many of these agencies direct staff to use their personal vehicles and be reimbursed for mileage. Recently, the Funeral Service Commission analyzed its mileage reimbursement expenses and determines that renting a car for the purpose of providing inspections is more cost effective than reimbursing mileage for private vehicles.

The state's mileage reimbursement rate is 34.5 cents per mile, set by the Comptroller's office. The state's rental car contract rates with Advantage, Avis, and Enterprise through December 31, 2002, offer Economy through Intermediate class vehicles ranging from \$28 to \$36 a day, depending on time of year and rental location.

State agencies that allow employees to use personal vehicles for state travel and be reimbursed for mileage should perform a cost analysis of its mileage reimbursement expenses to determine whether renting a vehicle under the state contract would be more cost efficient. If the analysis shows that renting a vehicle, including the cost for fuel, is more cost effective, the agency must adopt a travel policy reflecting the cost efficiency.

### **Information Resources Manager**

**Direct the Funeral Services Commission, the Board of Examiners of Psychologists, and the Executive Council of Physical Therapy and Occupational Therapy Examiners to share an Information Resources Manager through interagency contracts.**

The Funeral Services Commission, the Board of Examiners of Psychologists, and the Executive Council of Physical Therapy and Occupational Therapy Examiners are members of the Health Professions Council (HPC). The HPC currently employs a network manager to assist member agencies in setting up and maintaining their networks and hardware, however, the network manager is not equipped to help agencies resolves specific information resources (IR) problems, such as software consultation, website design, e-mail, viruses, and daily technical support.

Several of the larger HPC member agencies have sufficient fee-generated funds to hire their own information resources manager (IRM), and other agencies are beginning to search out innovative ways to procure information resources support. The Texas Optometry Board hired an IRM, and in an effort to share cost and services, the Board of Veterinary Medical Examiners entered into an interagency contract to purchase 40 % of the IRM's position.



Many small agencies continue to expend funds on contractors for information services. In the current fiscal year alone, the Funeral Services Commission has spent over \$18,000 for a contractor just to maintain the commission's daily information resources functions, excluding any updates, support, or new program development. The commission's Chief Financial Officer currently updates the agency's website and performs minor troubleshooting. The Board of Examiners of Psychologists' accountant currently handles the agency's information resources matters, and the Executive Council of Physical Therapy and Occupational Therapy Examiners spent \$15,500 in the current fiscal year on website support and implementing mandated upgrades.

Since e-government has come to be an expectation, it is more important than ever to have a cost efficient approach to information resources. Allowing these agencies to share an IRM would allow the agencies to enjoy greater support and increased efficiency without creating a financial burden on the individual agencies. Most small agencies have a web site that they would like to expand, and need to do so in order to comply with the Legislature's mandate to transition licensing agencies to online renewals and applications. Following the precedent set by the Optometry Board and the Veterinary Medical Examiners, the Legislature should allow small licensing and regulatory agencies to contract with like agencies to share an information resources manager.

## **Cosmetology Commission and Barber Examiners**

### **Consolidate the Cosmetology Commission and the Barber Examiners.**

The State Board of Barber Examiners and the Cosmetology Commission share virtually all the same duties, and as a result of the 77<sup>th</sup> Legislative session, they office in the same building in Austin. Consolidating these agencies is a natural step toward efficient government by reducing duplicative staff under each agency and reducing unnecessary costs of overhead for two such similar agencies. Consolidating the agencies should not result in any difficulty for the barbers and cosmetologists the agencies license, but may in fact result in more of their licensees being able to receive joint licenses. The barbers and the cosmetologists will each continue to bring in general revenue through their licensing and renewal fees and share in the administrative costs that are now separate.

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<sup>1</sup> Texas Department of Economic Development website, [www.tded.state.tx.us](http://www.tded.state.tx.us)

<sup>2</sup> Sunset Advisory Commission, Texas Department of Economic Development, Staff Report, November 2002, p.1.

<sup>3</sup> State Auditors Office, An Audit on the Department of Economic Development, Number 00-008, Jan 2000.

<sup>4</sup> Sunset Advisory Commission, Texas Department of Economic Development, Staff Report, November 2002.

<sup>5</sup> Texas Automobile Prevention Theft Authority, Press Release, October 18, 2002.



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# Appendix



## Appendix A Comparison of State Plan to Private Industry Plans

Source: Employees Retirement System of Texas, Presentation to Joint Meeting of House Appropriations Committee House Insurance Committee, May 22, 2002

### Comparison of Health Select Programs Under the Uniform Group Insurance Program with Private Industry Plans

Plan Description	Texas Health Select	Private Industry				
		HEB	SW Airlines	IBM	Motorola	Dell
Type of Plan	POS	PPO	PPO	PPO	PPO	PPO
Employer Premium Share						
Employee Only	100%	80%	100%	80%	87%	80%
Dependents	50%	80%	2%	80%	87%	80%
Retirees	100%	Note (1)	0%	0%	0%	0%
Retiree Dependents	50%	Note (1)	0%	0%	0%	0%
Waiting Times for Coverage	None	None	30 Days	None	None	None
Network Co-Insurance Level	90%/10%	90%/10%	85%/15%	100%	90%/10%	90%/10%
Calendar Deductible	None	\$200	\$150	None	None	\$300
Office Visit Co-payments						
Primary Care	\$15	\$0	85%/15%	\$15	\$10	\$15
Specialist	\$15	\$0	85%/15%	\$15	\$10	\$15
Calendar Year Stop Loss	\$500	\$1700	\$1725	\$1500	\$2000	\$2300
Hospital <small>(addl. Co-pay or ded.)</small>						
Inpatient						
Co-pay	\$0	\$0	85%/15%	90%	\$0	\$0
Deductible	\$0	\$0	\$0	\$0	\$0	\$0
Outpatient						
Co-pay	\$0	\$0	85%/15%	90%	\$0	\$0
Deductible	\$0	\$0	\$0	\$0	\$0	\$0
Emergency Room						
Co-pay	\$50	\$0	\$100-\$300	\$50/90%	\$0	\$75
Deductible	\$0	\$0	(85%/15%)	\$0	\$0	\$0
Drug Benefit						
Separate Deductible	\$0	\$0	\$0	\$0	\$0	\$0
Co-Pay Retail	\$5/\$20/\$35	\$5/\$13/\$23(2)	\$7/\$15/\$30	20% to \$25	\$10/\$20/\$40	\$7/\$15/\$30
Co-Pay Mail <small>(90 Day Supply)</small>	\$10/\$40/\$70	None(2)	\$15/\$30/\$60	20% to \$25	\$15/\$30/\$60	\$14/\$30/\$60
Annual Drug Max	None	None	\$750 PP/Pyr	None	None	None
Lifetime Drug Max	N/A	N/A	N/A	N/A	N/A	N/A
Lifetime Maximum Benefit	Unlimited	\$1,000,000	\$2,000,000	Unlimited	\$2,000,000	Unlimited
Out of Network Benefits:						
Individual Deductible	\$500	\$4,700	75%	\$300	90% of R&C*	\$300
Family Deductible	\$1,500	\$14,100	75%	\$900	90% of R&C*	\$750
Stop Loss	\$1,500	\$14,100	75%	\$2,500	90% of R&C*	\$2,000
Co-Insurance Level	70%	70%	75%	70%	90% of R&C*	70%
Lifetime Maximum	\$1,000,000	\$1,000,000	\$2,000,000	\$1,000,000	\$2,000,000	Unlimited

\*R&C- Reasonable and Customary

**Note (1).** Based on hire date of February 1992 and before there is a corporate contribution up to age 65. At age 65 coverage is cancelled. Other hires after February 1992 have very limited contribution if any.

**Note (2).** Co-pays for employees with salary under \$40K. Employees with salary over \$40K the co-pays are \$5/\$18/\$33. There are limited medications available for a 90 day supply at 1½ retail copays.

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## **Appendix B**

### **Services Covered by Texas Medicaid**

*Source: Texas Health and Human Services Commission,  
Texas Medicaid in Perspective, Fourth Edition, April 2002*

#### **Mandated Services**

Federally mandated services that all state Medicaid programs must pay for:

Regular medical and dental checkups for minors and treatment of any conditions identified by the Texas Health Steps program or a medical provider and medically necessary under the state's definition.

- Ambulance
- Family planning/genetics
- Federally Qualified Health Centers
- Home health care
- Inpatient and outpatient hospital
- Renal dialysis
- Lab and X-ray
- Medical transportation (non-emergency) to Medicaid-covered health care services
- Nursing-facility care
- Rural Health Clinics
- Physicians
- ICF/MR Dental
- Dentists (when providing physician services)
- Certified Nurse Midwife
- Certified Family Nurse Practitioner
- Certified Pediatric Nurse Practitioner

#### **Optional Services**

Federal law allows the state to cover certain optional services. All federally allowable and medically necessary services must be provided to persons under age 21. Texas provides the following optional services:

- Birthing center (limited)
- Case management for people with chronic mental illness, women with high-risk pregnancies and infants, persons with mental retardation and related conditions, and blind or visually impaired adolescents
- Certified Registered Nurse Anesthetists
- Chiropractic (limited)
- Christian Science Sanitarium
- Day activity and health services
- Dental care (for persons under age 21)
- Durable medical equipment (for persons under age 21)

- Emergency medical
- Licensed Professional Counselor
- Licensed masters of Social Work/Advanced Clinical Practitioner
- Licensed Marriage and Family Therapists
- Hearing instruments and related audiology
- Hospice Care
- Intermediate Care Facilities for people with Mental Retardation or Developmental Disabilities (ICF/MR)
- Institutions for Mental Disease (IMD) (for persons under age 21 and elderly 65+)
- Maternity Care Clinics (limited)
- Medically necessary surgery and dentistry (not routine dentistry)
- Optometry and eyeglasses
- Personal care services in the home
- Physical therapy
- Podiatry
- Prescription drugs (three per month; unlimited drugs for nursing home residents, persons under 21 and managed care)
- Psychology
- Private duty nursing (for persons under 21)
- Rehabilitation: limited to chronic mental illness, chronic medical conditions, day activity and health services, daily rehabilitation services
- In-home respiratory care
- In-home tube feeding (enteral)
- Total parenteral hyperalimentation
- Advanced practice nurse
- Targeted case management
- Telemedicine
- School Health and Related Services
- Certified Registered Nurse Anesthesiologist

Texas does *not* cover the following optional services:

- Christian Science Nurses
- Clinic services (except for limited maternity care clinic and family planning services)
- Routine Dental Care
- Dentures
- Diagnostic, screening, preventive, and rehabilitative services not specifically described above
- Durable medical equipment such as wheelchairs, walkers and crutches, except when provided by a Medicaid home health agency
- Occupational hearing, language, or speech therapy

## Appendix C Higher Education Funding

*Sources: The Texas Higher Education Coordinating Board, "Permanent University Fund, Higher Education Assistance Fund, Overview," and the Legislative Budget Board, "State Funding for General Academic Institutions of Higher Education."*

### **PUF Institutions:**

The University of Texas at Arlington\*

**The University of Texas at Austin**

The University of Texas at Dallas\*

The University of Texas at El Paso\*

The University of Texas of the Permian Basin\*

The University of Texas at San Antonio\*

The University of Texas at Tyler\*

**Texas A&M University**

Texas A&M University- Galveston\*

**Prairie View A&M University**

Tarleton State University\*

Texas A&M University Services Agencies

The University of Texas SWMC- Dallas

The University of Texas Medical Branch- Galveston

The University of Texas HC- Tyler

The University of Texas HSC- Houston

The University of Texas MD Anderson Cancer Center

The University of Texas HSC- San Antonio

Texas A&M University System HSC

**The University of Texas System Administration**

**Texas A&M University System Administration**

Bold type indicates those institutions that receive AUF Excellence and Debt Service, all others receive debt service only.

\*denotes institutions that receive URF funding. Note that this funding is limited to general academic institutions, other than UT Austin, Texas A&M, and Prairie View A&M.

### **HEAF Institutions:**

Lamar University\*

Lamar State College- Orange

Lamar State College- Port Arthur

Sul Ross State University\*

Sul Ross State University- Rio Grande

Angelo State University\*

Sam Houston State University\*

Southwest Texas State University\*

Texas A&M University- Corpus Christi\*

Texas A&M International University\*



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Texas A&M University- Kingsville\*  
Texas A&M University- Commerce\*  
Texas A&M University- Texarkana  
West Texas A&M University\*  
University of Houston\*  
University of Houston- Clear Lake\*  
University of Houston- Downtown\*  
University of Houston- Victoria  
The University of Texas- Pan American\*  
The University of Texas at Brownsville\*  
Texas State Technical College System  
Midwestern State University\*  
Stephen F. Austin University\*  
Texas Southern University\*  
Texas Woman's University\*  
Texas Tech University\*  
Texas Tech University Health Sciences Center  
University of North Texas\*  
University of North Texas Health Science Center

\*denotes the institutions that receive TEF funding. Note that this funding is for 21 general academic institutions that are HEF-eligible.

# Addendum

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## **Require generic rebate parity in the Medicaid Vendor Drug Program.**

Pharmaceutical manufacturers who sell branded products to the Texas Medicaid Vendor Drug Program currently pay a rebate of approximately 25% back to the state. This rebate amount is calculated based on a federal formula (OBRA 90) that sets the amount at a minimum of 15.1% plus an added amount that is indexed to price increases above the Consumer Price Index (CPI) plus a “best price”. The CPI index penalty requires branded manufacturers to pay back to the Medicaid program any amount of price increases over the CPI. The “best price” provision requires branded manufacturers to sell to the Medicaid Program the product at the lowest price it is offering the same product anywhere in the country-whether the customer is in the private or public sector.

Generic manufacturers are only required to rebate a flat 11% thus providing them no incentive to hold price increases at or near the annual CPI. In fact, many generic manufacturers have increased prices in the range of several hundred percent and even up to 2000% based on the market environment and raw product availability. Under current law, if a generic drug manufacturer raises its prices it does not receive an inflation penalty.

More than half of prescriptions paid for by Medicaid are generic. If generic manufacturers paid the same federally required rebate as research and development based manufacturers, the state could collect an additional \$22.8 million per fiscal year.

## **Adjust the dispensing fees Medicaid pays for prescriptions.**

The State of Texas pays one of the highest Medicaid dispensing fees in the nation. In fiscal year 2002, the dispensing fee for each of the 30 million prescriptions filled in Texas Medicaid was approximately \$6.10 per prescription. The national average was just over \$4 per Medicaid prescription. The same Texas pharmacist contracts with other state agency customers for much less for the exact same service. In FY 00, Texas pharmacist contracted with ERS (HealthSelect Only) for \$2.65, TRS for \$1.43 and the Texas A&M University System for \$1.78 in dispensing fees per prescription.

Estimated general revenue savings from a reduced Medicaid Vendor Drug Program pharmacy dispensing fee that is more consistent with other state agencies is as follows:

Fiscal Year	<u>Reduce fee to \$1.45</u>	<u>Reduce fee to \$2.45</u>	<u>Reduce fee to \$3.45</u>
2004:	\$ 58 million	\$ 46 million	\$42 million