



**Losing Jobs, Losing Income, and Worsening the Deficit?**

***The Economic Impact of Connecticut's Hospital Tax***

***& Reimbursement Policies***

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#### **Summary**

This brief analysis looks at the impact of the State of Connecticut progressively moving away from the commitments made in FY2011 in conjunction with the imposition of a tax on hospitals. The promise was that, to offset the impact of the tax, the state would sustain and then expand its support for the hospitals, support that would in turn generate significant federal reimbursements (50% in FY 2011-13; 67% in FY 2015-17). Hospitals, while incurring a \$33 million loss in state support annually compared to FY2010, would thereafter be “held harmless,” with no further reductions. The State would benefit with increasing contributions to the General Fund generated largely from the federal reimbursement. But the State has significantly reduced its support to hospitals—and thus foregone nearly \$200 million in federal reimbursement in FY 2015, in the false belief that reducing the offset to the hospital tax would generate additional enhancement to the General Fund. That simple accounting approach fails to take into account the dynamic economic interactions that the growing cuts to the hospitals generates—lost jobs, lost wages, lost tax revenues. Under the assumptions described below, the evolving structure of the hospital tax, state transfers to hospitals, and federal reimbursements are cutting state employment by more than 4000 jobs, personal income by nearly a quarter of a billion dollars, and may in fact be hurting the State budget, not helping.

The data on which this analysis relies comes from the Connecticut Hospital Association; CHA provided this data at the request of CCEA. CCEA has not confirmed the data's accuracy.

## The Analysis

Table 1 summarizes the initial commitments that were made when the State adopted the hospital tax. From 2012 on, hospitals incurred an annual reduction in state support of \$33 million, but the General Fund enjoyed systematic growth, driven by the Federal reimbursements. This looked to be a constructive approach to taking full advantage of Federal support on offer.

**Table 1: The Promise of the Hospital Tax (Millions \$)**

	Hospital Taxes	Hospital Receipts from the State	Federal Payment to the State	Net Benefit to (Tax on) Hospitals	Annual Help to Hospitals from the State Losses due to the Hospital Tax	Net Benefit (Cost) to General Fund
2011	0	83	42	83		(42)
2012	349.1	399	200	50	(33)	149
2013	349.1	399	200	50	(33)	149
2014	349.1	399	234	50	(33)	183
2015	349.1	399	268	50	(33)	217
2016	509.7	560	375	50	(33)	325
2017	509.7	560	375	50	(33)	325

But as Table 2 shows, the reality of State funding to the hospitals has shrunk every year to date, to only \$96 million in 2015. Federal reimbursements were 50% of state transfers to the hospitals 2011-2013, with the rate then rising to 67% for 2015-2017. But because State transfers have fallen systematically, Federal reimbursements have fallen sharply. If the structure of 2012 had remained in place, Federal reimbursements would now be \$268 million, rather than the \$64 actually in hand.

**Table 2: The Reality of the Hospital Tax (Millions \$)**

	Hospital Taxes	Hospital Receipts from the State	Federal Payment to the State	Net Benefit to (Tax on) Hospitals	Annual Help to Hospitals from the State Losses due to the Hospital Tax	Net Benefit (Cost) to General Fund
2011	0	83	42	83		(42)
2012	349.1	399	200	50		149
2013	349.1	323	161	(26)	(77)	188
2014	349.1	245	143	(104)	(154)	247
2015	349.1	96	64	(254)	(304)	318
2016	509.7	241	162	(269)	(319)	430
2017	509.7	241	162	(269)	(319)	430

The difference in the flow of funds results from subtracting the numbers in the second table from those in the first: Table 3 captures the results of this exercise. Because Federal transfers flow through the state and because CCEA models state revenues to balance, in-line with legal requirements, the net changes to state expenditures amount to the federal transfers that the state is no longer receiving less the differences in the net benefits to the general fund.

**Table 3: Shortfalls on Promises of the Hospital Tax (Millions \$)**

	Hospital Taxes	Hospital Receipts from the State	Federal Payment to the State	Net Benefit to (Tax on) Hospitals	Annual Help to Hospitals from the State Losses due to the Hospital Tax	Net Benefit (Cost) to General Fund	Net Changes in State Expenditures
2011	0	0	0	0	0	0	0
2012	0	0	0	0	33	0	0
2013	0	(77)	(38)	(77)	(44)	38	0
2014	0	(154)	(90)	(154)	(121)	64	(26)
2015	0	(304)	(204)	(304)	(271)	100	(103)
2016	0	(319)	(213)	(319)	(286)	105	(108)
2017	0	(319)	(213)	(319)	(286)	105	(108)

Two economic implications of the cutbacks to state support of the hospitals are clear under a balanced budget constraint: State expenditures fall \$26 million in 2014 and by higher amounts thereafter, reaching \$108 million in 2016 and 2017. Second, hospital revenues fall by the combined cuts in state and federally funds, rounding to \$531 million in 2016 and 2017, with somewhat smaller amounts in the earlier years.

Relative to the promised trajectory at the time the hospital tax was imposed, the counterfactual that the CCEA examines involves the hospitals raising rates to recoup the reductions in government funding, resulting in a shift in household expenditures; consumers spread those cuts across the panoply of other goods and services. This approach also recognizes the net changes in state expenditures inclusive of the impacts of the cuts in federal transfers.<sup>1</sup>

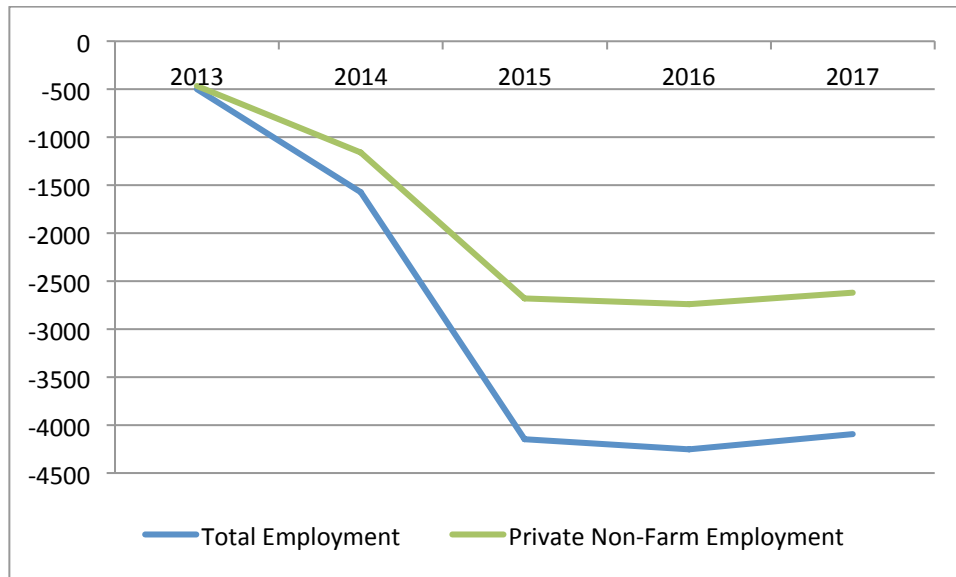
This approach differs from the strictly accounting approach in Tables 1 and 2 because it picks up on the economic impacts of the policy imposed constraints on both consumers and the state resulting from the State’s failure to meet its promises associated with its hospital tax.

<sup>1</sup> These fee hikes would affect insured patients more indirectly through higher premiums to accommodate the higher hospital costs so even with this complication consumers’ incomes after covering health costs, actual or anticipated, will be impacted at some juncture.

## Economic Impacts

CCEA estimated economic impacts for 2013 to 2017. They are particularly adverse on employment in both the private and public sectors, as Figure 1 reveals.

**Figure 1: Job Impacts: Total and Private (# Jobs)**

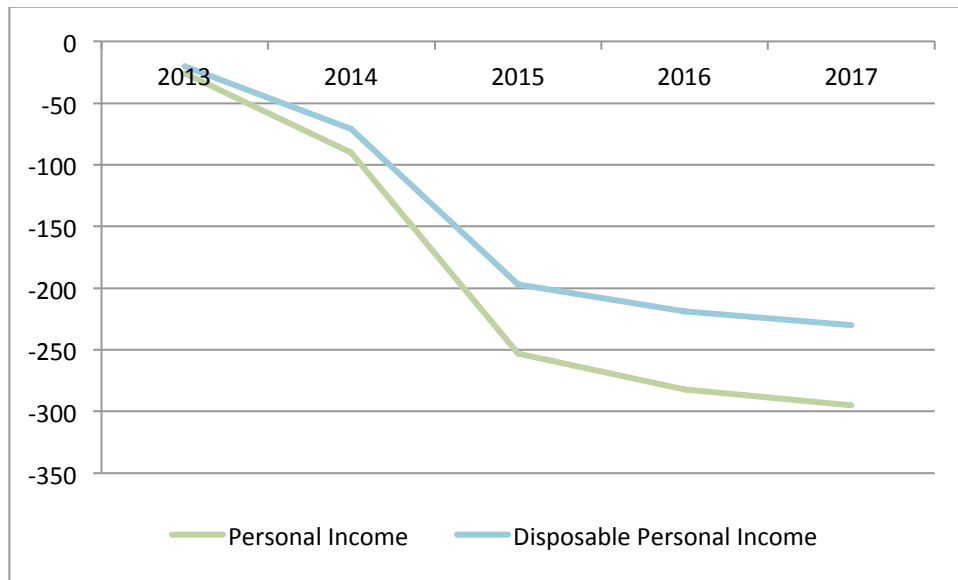


Total job losses exceed 4,000 annually from 2015-2017. This is hardly surprising; given the scale of reductions in support, the fallout necessarily falls on employment. The majority of the jobs lost, in excess of 2,600 in each of the three years, are in the private sector, with another 1400+ lost in the public sector.

## Personal Income Impacts

The cutbacks and resulting job losses necessarily reduce personal incomes. The CCEA analysis estimates annual personal incomes falling by a quarter of a billion dollars or more from 2015 onward, reaching a shortfall of nearly \$300 million in 2017. Personal disposable incomes—after tax income--falls by \$197 million to \$230 million from 2015-2017, with government revenues absorbing the balance of losses.

**Figure 2: Personal Income Impacts: Total and Disposable (\$ Millions)**



The differences between the two income measures, \$35 to \$57 million annually 2015-2017, are cutbacks to governments, mostly the result of lower income tax revenues, of which about 23-24% flow to the State of Connecticut (much of the rest is a reduction in Federal tax payments).

### **Economic Impacts on the State Revenues**

The total net economic impacts on the State revenues are adverse, as noted in the sixth line of Table 4; State revenue *falls* by \$145 million. These estimates are only partial because the REMI model can capture easily the adverse impacts on only two sources of State revenues. A more comprehensive analysis would likely increase the scale of negative outcomes; alternative assumptions (scenarios) would also impact the scale, but not the direction, of these outcomes. The last line of the table contains the estimate of the net improvement in the state budget using simple direct accounting measures. Differences between the two methodologies approaches *a quarter of a billion dollars* by 2016-2017; think of this as the State's budgetary process making a \$250 million error. While it might appear that the changes in the hospital tax/state transfer/federal reimbursement scheme is helping the State budget, this analysis argues it is making the situation in Connecticut worse, resulting in significant job losses, reductions in household incomes, and budget shortfalls.

This analysis underlines how critical it is for the budget process to include dynamic economic modeling: it would help frame policy discussions with an appreciation of the complex interactions that flow from the policy choices. To emphasize this, consider how failures to model the implications of policy choices fully can lead, as it appears to be doing here, to serious missteps that come at the expense of lower employment, falling standards of living, and

unnecessary constraints on the capacity of governments to capture the revenues they need to deliver the services their citizens need and deserve.

**Table 4: Impacts on State Government Net Revenues (Millions \$)**

	2013	2014	2015	2016	2017
Cuts in state income taxes	-1.4	-4.4	-12.9	-14.5	-15.0
State sales tax cuts	-4.0	-9.2	-20.2	-21.4	-21.7
Total of the two tax revenues	-5.4	-13.5	-33.1	-35.9	-36.7
Changes in transfers to the state less accounting gains	0	-26	-103	-108	-108
Cuts in state revenues	-5.4	-39.8	-136.4	-144.3	-145.0
Claimed Net Benefit to the General Fund	38	64	100	105	105

A final consideration is that, in this instance, there has also been almost certainly an adverse impact on human health. If hospitals were not able to recoup government cuts through increased fees, hospital services would need to be curtailed, staff over-extended, or other consequential adjustments made. Similarly, from a client perspective, if hospital services are too expensive, clients may choose to avoid procedures, leading to longer term adverse health impacts and increase private as well as social costs. No account has been taken in this analysis of these more complex but inevitable outcomes.