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SCHIP Financing: Funding Projections and State Redistribution Issues

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SCHIP Financing: Funding Projections and State Redistribution Issues

Summary

The Balanced Budget Act of 1997 (BBA 97, P.L. 105-33) created the State Children's Health Insurance Program (SCHIP), which is authorized through FY2007. The purpose of the program is to help states pay for health coverage of uninsured children in families whose income is above the levels that would allow them to be eligible for the state's Medicaid program as of March 31, 1997.

At the time of enactment, Congress appropriated to SCHIP nearly $40 billion for the 10-year period of its authorization, with each state receiving access to a portion of the annual amount. Because SCHIP is a capped-grant program, it is possible for states to exhaust all of the federal SCHIP funds available to them in a given year.

Only two states (Alaska and Rhode Island) have ever exhausted all of their available federal SCHIP funds. Alaska faced shortfalls in FY2000 ($419,000) and FY2001 ($2,000). Rhode Island faced shortfalls in FY2003 ($30,000) and FY2004 ($19 million). These states had the option to file most of their SCHIP claims under regular Medicaid when their SCHIP funds were exhausted. By claiming under Medicaid, however, they received a 17% to 19% smaller federal payment than they would have received under SCHIP for those claims.

Six states faced a shortfall of federal SCHIP funds in FY2005 (Arizona, Minnesota, Mississippi, Nebraska, New Jersey, and Rhode Island). However, the Secretary of Health and Human Services was able to target unspent FY2002 allotments from other states to these six states' shortfalls. As a result, no state finished FY2005 with a shortfall of federal SCHIP funds.

The methodology that eliminated the FY2005 shortfalls could not cover the FY2006 projected shortfalls. For FY2006, the unspent funds available for redistribution were projected to be approximately $283 million shy of covering the shortfalls. To cover this difference, Congress appropriated $283 million in the Deficit Reduction Act of 2005 (DRA, P.L. 109-171). The Congressional Research Service (CRS) SCHIP Projection Model projects that four states will still experience shortfalls in FY2006, totaling $2.75 million. The relatively small shortfall left by the DRA funds will fall to states with SCHIP enrollees who are non-pregnant adults.

The CRS model projects that 18 states will experience shortfalls of federal SCHIP funds in FY2007. The amount of these shortfalls is projected to total $944 million, although some states may use Medicaid funds to cover some of that.

This report provides an overview of SCHIP financing and spending since the program's inception and provides state-level projections of the FY2006 and FY2007 shortfalls. The report also provides state-level projections of the impact of the SCHIP proposal outlined in the President's budget. Depending on the actual details of that plan, it may eliminate the FY2007 shortfalls. This report will be updated as new data become available that might substantially alter the results.

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SCHIP Financing: Funding Projections and State Redistribution Issues

The Balanced Budget Act of 1997 (BBA 97, P.L. 105-33) created the State Children's Health Insurance Program (SCHIP), which is authorized for FY1998-FY2007. The purpose of the program was to help states pay for health insurance coverage of uninsured children in families whose income is above the levels that would allow them to be eligible for the state's Medicaid program as of March 31, 1997.[1] States can cover SCHIP enrollees by expanding their Medicaid program or by creating a separate SCHIP program, or by a combination of both.

At the time of enactment, Congress appropriated to SCHIP nearly $40 billion for the 10-year period of its authorization, as shown in **Table 1**, with each state entitled to a portion of the annual amount.[2] Besides these annual original allotments, states may access additional funds; states that exhaust a particular year's allotment receive access to a portion of other states' unspent allotment for that year.[3]

Because SCHIP is a capped-grant program, it is theoretically possible for states to exhaust all of the federal SCHIP funds available to them in a given year. For a state to experience such a shortfall, it would have to exhaust all of its available allotments as well as the available funds that had been redistributed to it from other states. To date, only two states, Alaska and Rhode Island, have ever exhausted all of their available federal SCHIP funds.

In FY2000, Alaska planned to spend $18.1 million in federal SCHIP funds. However, its prior-year balances of $9.9 million plus its newly available FY2000 original allotment of $7.7 million were insufficient to meet the demand for funds. Thus, Alaska experienced a shortfall of approximately $419,000.

In FY2001, Alaska's amount of planned spending of federal SCHIP funds increased to $24.0 million. Even though its FY2001 original allotment ($9.0 million) was higher than the previous year's ($7.7 million), the state had no rollover of prior-year funds. Its shortfall would have been quite large, except that FY2001 was the first year that redistributions took place. After an original allotment's three-year period of availability, any unspent funds are redistributed to states that had spent all

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[1] For a more in-depth overview of the program, see CRS Report RL30473, *State Children's Health Insurance Program (SCHIP): A Brief Overview*, by Elicia J. Herz, et al.

[2] For information on SCHIP original allotments, see CRS Report RL33366, *SCHIP Original Allotments: Funding Formula Issues and Options*, by Chris L. Peterson.

[3] In this report, "balances," "spending," and "expenditures" refer only to the federal dollars available, paid or claimed through the enhanced match; state expenditures are not provided or discussed in this report.

of that particular allotment, with some exceptions discussed later. As a result, for spending in FY2001, Alaska received $15.0 million from other states' unspent FY1998 original allotments. Thus, Alaska's shortfall was only about $2,000 in FY2001. Because Alaska's SCHIP program is a Medicaid expansion, the state was able to claim its shortfalls under regular Medicaid when its federal SCHIP funds were exhausted. Thus, Alaska received federal Medicaid payments that covered 83% of its federal SCHIP shortfall.[4] Since FY2001, Alaska has not had a shortfall, even though its annual federal SCHIP expenditures have been double or triple its annual original allotment. This is because of the additional funds provided by the redistributions from other states' unspent funds.

In FY2003, Rhode Island had approximately $38.6 million in SCHIP spending, resulting in a relatively small shortfall of approximately $29,000. This shortfall was simply rolled forward to FY2004 and covered with the newly available annual distribution of federal SCHIP funds. By the end of FY2004, however, Rhode Island had a shortfall of federal SCHIP funds of $19.0 million, according to estimates provided by the state. Because much of Rhode Island's SCHIP expenditures could also qualify for payment under Medicaid, Rhode Island opted to take most of that shortfall and receive federal Medicaid funds. In doing so, Rhode Island received 81% of the federal payment it would have received under SCHIP for those claims.

On September 29, 2005, nearly the last day of FY2005, a notice in the *Federal Register* announced the final form of the redistribution of unspent FY2002 original allotments for use in FY2005. The methodology, determined by the Secretary of Health and Human Services (HHS), eliminated what would have been a shortfall of federal SCHIP funds in six states (Arizona, Minnesota, Mississippi, Nebraska, New Jersey, and Rhode Island) in FY2005.

The methodology that eliminated shortfalls for FY2005 was projected to fall short for FY2006. The pool of unspent funds available for redistribution were projected to be insufficient (by approximately $283 million) to prevent shortfalls of federal SCHIP funds in 12 states, according to the Centers for Medicare and Medicaid Services (CMS). To cover this shortfall, Congress appropriated $283 million in the Deficit Reduction Act of 2005 (DRA, P.L. 109-171). The CRS model projects that four states will still experience shortfalls in FY2006, totaling approximately $2.75 million. The relatively small shortfall left by the DRA funds will fall to states with SCHIP enrollees who are non-pregnant adults. These shortfalls are based on certain assumptions, discussed below.

The CRS model also projects that under current law, 18 states will experience shortfalls of federal SCHIP funds in FY2007, also shown in **Table 1**. The amount of these shortfalls is projected to total $944 million, although some states may use Medicaid funds to cover some of that. The SCHIP proposal in the President's Budget, depending on its details, may eliminate the FY2007 shortfalls.

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[4] As described in greater detail below, under SCHIP, states receive an "enhanced" federal matching percentage, whereas expenditures under Medicaid are reimbursed at the "regular" matching percentage, officially known as the Federal Medical Assistance Percentage (FMAP).

Table 1. National Figures on Federal SCHIP Financing
(in millions of dollars)

Fiscal year	SCHIP allotments	Spending (or projected demand)	Total amount of shortfalls	Number of shortfall states	Funds expiring
1998	$4,235	$122			
1999	$4,247	$922			
2000	$4,249	$1,929	[a]	1	
2001	$4,249	$2,672	[a]	1	
2002	$3,115	$3,776			
2003	$3,175	$4,276	[a]	1	
2004	$3,175	$4,645	$19	1	$1,281
2005	$4,082	$5,089			*$128*
2006	$4,082	*$5,981*	*$2.75*	*4*	
2007	$5,040	*$6,342*	*$944*	*18*	

Source: Congressional Research Service (CRS) SCHIP Projection Model and CRS analysis of data from the Centers for Medicare and Medicaid Services.

Note: Projected amounts are italicized.

a. Less than $1 million.

This report provides an overview of SCHIP financing and spending since the program's inception. The report then describes the CRS SCHIP Projection Model and the assumptions its results are based on. The report provides state-level projections of the FY2006 and FY2007 shortfalls as well as other key financing data. The report provides state-level projections of the impact of the SCHIP proposal outlined in the President's Budget. Depending on the actual details of that plan, it may eliminate the FY2007 shortfalls. It does so by redistributing additional funds from many non-shortfall states, the implications of which are discussed in the final section of the report. This report will be updated as new data become available that might substantially alter the model results.

If Congress intends to prevent state shortfalls of federal SCHIP funds in FY2007, legislative action will be needed. If, however, Congress decides that the intent of the original legislation was to ensure states did not treat the program as an open-ended entitlement, no action will be necessary, as the states with annual SCHIP spending well in excess of their annual allotments face the consequences of that spending through the shortfall of federal funds.

SCHIP Financing and Spending Overview

States that set up an SCHIP program are entitled to federal reimbursement, up to a cap, for a percentage of the incurred costs of covering enrolled individuals. This percentage, which varies by state, is called the enhanced Federal Medical Assistance Percentage (FMAP). It is based on the FMAP used for the Medicaid program but is higher in SCHIP than in Medicaid. In other words, the federal government contributes more toward the coverage of individuals in SCHIP (65% to 83.2% in FY2006) than it does for those covered under Medicaid (50% to 76% in FY2006).[5]

States are reimbursed for their costs up to a capped amount. Nationally, the total annual federal allotments range from $3.1 billion (FY2002) to $5 billion (FY2007). The amount available to each state is determined annually through a formula that takes into account factors such as the state's number of low-income uninsured children. State allotment amounts are published annually in the *Federal Register* for each upcoming fiscal year. States' allotments for FY2006 were published June 24, 2005.

Under current law, a state's allotment for a given year is available for use for three years. For example, each state's FY1998 allotment was available through FY2000 (September 30, 2000). At the end of the three years, if there is still a balance in that "pot" of money, BBA 97 requires that the Secretary of Health and Human Services redistribute that money to those states which had exhausted that pot. Those states that exhausted a given year's pot are called redistribution states for that year. Under BBA 97, redistributed funds are available to those states for one year, after which the money expires, reverting back to the Treasury.

Rather than leave the redistribution process up to the Secretary, Congress intervened to determine in statute how much of the unspent funds from FY1998-FY2001 states would receive. Even though BBA 97 allowed for only redistribution states to receive unspent funds, the later laws enacted by Congress permitted those states that did not spend all of their original allotments to retain a portion. These states are called retention states. When both retention and redistribution states receive access to a portion of the unspent money, the process is often called reallocation instead of redistribution, the latter implying that only redistribution states receive access to the unspent funds. Congress also gave states more than one year to spend these reallocated funds.

Redistribution states receive funds from other states' unspent original allotments based in part on their "excess spending." Excess spending is defined as the difference between a redistribution state's spending during an original allotment's three-year period of availability and the amount of that allotment. For example, at the end of FY2000, when unspent FY1998 original allotment funds were redistributed, excess spending was calculated among redistribution states as the total federal SCHIP expenditures in FY1998, FY1999, and FY2000 (that is, the FY1998 original allotment's period of availability) minus the FY1998 original allotment amount.

It is worth noting that states which exhausted a pot of money were not necessarily out of federal money altogether. For example, states that exhausted their

[5] For more information on the FMAP, see CRS Report RL32950, *Medicaid: The Federal Medical Assistance Percentage (FMAP)*, by Christine Scott, and CRS Report RS22333, *Budget Reconciliation FY2006: Provisions Affecting the Medicaid Federal Medical Assistance Percentage (FMAP)*, by April Grady.

FY1998 original allotments did so in FY1999 or FY2000, by which time the original allotments for those years were also available.

In the program's first few years, because SCHIP was new and states were just getting their programs started, much of the original allotments were unspent. In fact, there was still money left for retention states even after covering *all* of the excess spending of redistribution states.

Annual Reallocations/Redistributions

Reallocation of Unspent FY1998 and FY1999 Original Allotments (P.L. 106-554). At the end of FY2000, each state's FY1998 original allotment pot was closed. The unspent money, totaling just over $2 billion, went into a pool to be reallocated as specified in the Medicare, Medicaid, and SCHIP Benefits Improvement and Protection Act of 2000 (BIPA, P.L. 106-554). The territories (Puerto Rico, Guam, American Samoa, the Virgin Islands, and the Northern Mariana Islands) had 1.05% of that pool reserved for them. The redistribution states received access to an amount equal to all of their excess spending of nearly $700 million. The remaining $1.3 billion (65% of the total pot of unspent funds) was reallocated back to the retention states, based on their percentage contribution to the overall pool of unspent FY1998 original allotments.

Thus, at the beginning of FY2001, all states had balances available to them through the reallocation of unspent FY1998 funds. In addition, states would also have available any remaining balances from their FY1999 and FY2000 allotments, as well as the newly available FY2001 original allotment.

Typically, when states draw down federal SCHIP money, they must do so chronologically. For example, all available FY1998 funds (whether original allotments or reallocations) must be exhausted before funds from FY1999 or later can be drawn down. Once the reallocated FY1998 funds became available, those had to be drawn down before any more spending could occur out of the other available pots of federal SCHIP funds (in this case, FY1999, FY2000, and FY2001 original allotments). The exception is that the redistribution states may opt to have their redistribution pot drawn in a non-chronological order they specify. (It is still the case, however, that a pot must be exhausted before the next in the sequence can be tapped.)

Given the option to select a non-chronological order of spending, redistribution states have two primary competing incentives: (1) spend original allotment money first to ensure qualification as a redistribution state in the future, and (2) spend reallocated money first to minimize the amount of available money that expires. The order that states most commonly chose was to have spending from the FY1998 redistribution pot begin once the FY1999 original allotment pot was emptied. They generally opted to have the FY1999 pot drawn down first to ensure that they would qualify for the redistribution of other states' unspent funds from that year.

Redistribution states continued to choose non-chronological spending in which the first pot drawn down is the original allotment that will be up for reallocation at the end of the current fiscal year, followed by the reallocation(s) that will expire at the end of the current fiscal year, and then alternating between the next original allotment and the next reallocation pots, for which the expiration dates are further out into the future. For example, beginning in FY2004, when the FY2001 reallocation and the FY2004 original allotment were first made available to states, the most common order of spending selected by the redistribution states was as follows: (1) FY2002 original allotment, which was up for reallocation at year's end; (2) FY1999 and FY2000 reallocated money, which would expire at year's end; (3) FY2003 original allotment, available through FY2005; (4) FY2001 redistribution, also available through FY2005; and (5) FY2004 original allotment, available through FY2006.

The reallocation of unspent FY1999 original allotments was similar to the FY1998 reallocation. When the FY1999 allotments were closed at the end of FY2001, the redistribution states received access to an amount equal to all of their excess spending of approximately $1.6 billion. This allowed nearly $1.2 billion (42%) of the unspent pool of $2.8 billion to be reallocated to the retention states.

Reallocation of Unspent FY2000 and FY2001 Original Allotments (P.L. 108-74). At the end of FY2002, the unspent pool of FY2000 original allotments was reallocated differently, according to the State Children's Health Insurance Program Allotments Extension Act (P.L. 108-74). The territories again received 1.05% of the total unspent funds. Then each retention state was reallocated half of its unspent funds. The balance was reallocated to the redistribution states based on their percentage of the overall excess spending. For the FY2000 reallocation process, the redistribution states' excess spending totaled nearly $2.2 billion; they received half of that, $1.1 billion, in the reallocation of FY2000 funds.

The reallocation of unspent FY2001 funds was calculated as in the FY2000 reallocation, where the retention states retained access to half of their unspent funds. The redistribution states received $856 million from the FY2001 reallocation, covering 22% of their excess spending of nearly $3.9 billion.

Although BBA 97 permits redistribution funds to be available for only one year before expiring, the new laws pushed off the expiration of reallocated FY1998-FY2000 funds to the end of FY2004. This permitted these reallocated funds to be available to states for two to four years. When these pots of money expired at the end of FY2004, $1.3 billion of reallocated money reverted back to the U.S. Treasury. The FY2001 reallocation pot expired after two years, at the end of FY2005, with $72 million reverting to the Treasury.

Reallocation of Unspent FY2002 Original Allotments Onward (Reversion to BBA 97, P.L 105-33). As previously mentioned, the final notice regarding the redistribution of unspent FY2002 funds was published in the September 29, 2005, issue of the *Federal Register*. Because no law was enacted specifying otherwise, the process took place according to BBA 97, which allows the Secretary to determine the process. One limitation under BBA 97 is that the Secretary may not distribute unspent funds to retention states.

As in previous reallocations, the territories first received 1.05% of the total unspent funds. States that were projected to exhaust all of their available federal

SCHIP balances in FY2005, based on their estimated FY2005 expenditures (provided to CMS in August 2005), received redistribution money equal to that estimated shortfall. These six "shortfall states" were Arizona, Minnesota, Mississippi, Nebraska, New Jersey, and Rhode Island. The remaining balance of unspent FY2002 funds was divided among the 28 redistribution states, including the six shortfall states, based on their percentage of overall excess spending.[6] As a result, the six shortfall states received two sets of additional funds through the redistribution: (1) for qualifying as a shortfall state, and (2) for qualifying as a redistribution state. Also according to BBA 97, this reallocation pot expired at the end of one year, at the end of FY2005, with $56 million reverting to the Treasury. This amount, combined with the expired FY2001 reallocation funds, totals $128 million in federal SCHIP funds that expired at the end of FY2005.

The initial redistribution of unspent FY2003 original allotments and the allocation of the $283 million DRA appropriation for SCHIP, both of which are to be available for spending in FY2006 only, were announced by CMS in the *Federal Register* on April 21, 2006.[7] The amounts from both accounts were determined by the HHS Secretary, based on his broad discretion to allocate the funds to the FY2006 shortfall states.[8]

DRA said that "the Secretary shall allot to each shortfall State described in paragraph (2) such amount as the Secretary determines will eliminate the estimated shortfall described in such paragraph for the State." Paragraph (2) of §2104(d) defined shortfall states as those that projected their FY2006 expenditures to exceed the amounts available from (i) their balances of the FY2004 and FY2005 original allotments, (ii) the redistribution of funds from other states' unspent FY2003 original allotments, and (iii) the newly available FY2006 original allotment. Taking these funds into account, a shortfall of approximately $283 million was projected for the states. This was the basis for the $283 million appropriated in DRA.

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[6] As previously noted, excess spending is calculated as the difference between a redistribution state's spending during an original allotment's three-year period of availability and the amount of that allotment. It is worth noting that this schema causes a single year's SCHIP expenditures to be included in three years of redistribution calculations. For example, a state may have had unusually high SCHIP spending in FY2002. The FY2002 spending would have been a factor in determining whether the state qualified as a redistribution state (and the amount of redistributed funds the state would receive) in the reallocations that took place at the end of FY2002, FY2003, and FY2004. Respectively, these reallocations were of the unspent FY2000, FY2001, and FY2002 original allotments.

[7] Centers for Medicare & Medicaid Services, "State Children's Health Insurance Program (SCHIP); Redistribution of Unexpended SCHIP Funds From the Appropriation for Fiscal Year 2003; Additional Allotments to Eliminate SCHIP Fiscal Year 2006 Funding Shortfalls; and Provisions for Continued Authority for Qualifying States to Use a Portion of Certain SCHIP Funds for Medicaid Expenditures," 71 *Federal Register* 20697-20707, April 21, 2006.

[8] The funds from FY2003 available for redistribution could have gone to all redistribution states (those that had exhausted their FY2003 original allotment), but the Secretary targeted this redistribution to shortfall states, as was done in last year's redistribution.

However, DRA also included a provision that the territories would receive 1.05% of the $283 million appropriation (approximately $3 million). This percentage is consistent with the share the territories receive of the total annual original allotment and redistribution funds. The $3 million from the DRA funds for the territories means that the Secretary would not be able to eliminate the states' shortfalls altogether. In addition, the DRA funds come with limitations: "Additional allotments provided under this subsection [the $283 million] are only available for amounts expended under a State plan approved under this title for child health assistance for targeted low-income children." This prohibits states from using the DRA funds to pay for benefits of SCHIP enrollees who are non-pregnant adults.[9] Both of these factors — the DRA appropriation carved out for territories and the prohibition against it covering non-pregnant adults — raised the prospect that the Secretary would be unable to "eliminate the estimated shortfall."

To minimize the estimated shortfall, the DRA amounts were calculated first, before taking into account the redistribution of other states' unspent FY2003 funds. As stated in the *Federal Register*, "we incorporated the above definition of shortfall State under section 2104(d)(2) of the Act, except that we did not include the amount of any FY 2003 redistribution (number ii. above)."[10] Using the Secretary's broad discretion for the amounts to be distributed, the DRA appropriation to shortfall states first went to the eight shortfall states that covered only children ($142 million of the $280 million available to the states), to eliminate their shortfalls altogether.[11] The remaining $138 million was allotted to the four shortfall states that cover adults in their SCHIP programs (Illinois, Minnesota, New Jersey, and Rhode Island), taking care that the amount of the DRA funds to these states did not exceed their projected spending on children. By distributing the DRA funds in this way, the unspent FY2003 funds available to the states ($172 million), which were not limited to covered *children* only, could go entirely toward the four shortfall states that also cover adults. Using this methodology, these four states are projected to experience shortfalls totaling $2.75 million. This amount is due to the territories' portion of the appropriation that had not been taken into account when the $283 million amount was included in DRA. However, the Secretary's distribution of the funds placed the shortfall among only those states that cover adults.[12]

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[9] Pregnant women receiving SCHIP coverage may do so by virtue of the eligibility of their unborn children. The official guidance appears in 67 Federal Register 61956, Oct. 2, 2002. Because of this, pregnant women are not necessarily subject to the adult limitation under DRA, since their coverage is "for child health assistance for targeted low-income children."

[10] Centers for Medicare & Medicaid Services, "State Children's Health Insurance Program (SCHIP) ... ," 71 *Federal Register* 20700, April 21, 2006.

[11] These eight states (and their projected shortfalls eliminated by the DRA funds) were Iowa ($6.1 million), Maryland ($13.7 million), Massachusetts ($21.9 million), Mississippi ($73.6 million), Missouri ($8.0 million), Nebraska ($15.7 million), North Carolina ($2.8 million), and South Dakota ($0.5 million).

[12] In the previous version of this report, before the announcement of the distribution of the DRA funds and the unspent FY2003 funds, Minnesota and Rhode Island were projected to have FY2006 shortfalls totaling $20 million. The amounts projected for that version of the report were based on the assumption that the redistribution of unspent FY2003 funds would (continued...)

CRS SCHIP Projection Model

The Congressional Research Service (CRS) SCHIP Projection Model combines data available on federal SCHIP allotments, spending and reallocations in the program reported as of November 2005.[13] In order to make projections, these data are fed through the model's two discrete components. The first component projects individual states' and territories' demand for federal SCHIP funds for FY2006 and FY2007. Using this projected demand, the second component calculates the federal SCHIP funds that are available and drawn against each year.

Projecting Demand

Rather than just projecting *spending*, the model projects *demand* for federal SCHIP funds. If the model were to project only federal SCHIP *spending*, the maximum that a state could spend is its available balance. However, one purpose of the model is to capture the extent to which available SCHIP funds may be inadequate for a particular state. To capture this, states' *demand* for federal SCHIP funding must be projected — that is, the amount that states could be expected to spend if federal SCHIP funds were not capped.

Previous versions of the model projected demand in multiple ways. This was done partly because the estimates provided by states were only offered for the current fiscal year and the following fiscal year. As a result, the state did not provide projections through SCHIP's current authorization. Methods were then used to provide projections through FY2007. However, beginning with FY2006, which began October 1, 2006, states now provide projections through FY2007. These state projections are used in the model. Besides the previously mentioned exceptions, the state estimates used are from November 2005. These were used because they were the basis for the recently announced distribution of DRA funds and the redistribution of other states' unspent FY2003 funds.

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[12] (...continued)
be calculated *before* the distribution of the DRA funds and that the redistribution of the FY2003 funds would occur in the same way as the redistribution of the FY2002 funds in the previous year. Under that scenario, the adult limitation on the DRA funds was projected to result in the $20 million shortfall in Minnesota and Rhode Island. However, structuring the distribution of funds as was done by the Secretary in the April 21 *Federal Register* notice appears to have minimized the estimated shortfalls. Under the scenario previously projected by CRS, only two states would face shortfalls. The Secretary's distribution is expected to cause all four shortfall states that cover adults to share in the shortfall, though the total shortfall is much smaller ($2.75 million).

[13] For the CRS model, the state-level projections were updated for one state. California's amounts were updated to reflect implementation of its state plan amendment for prenatal coverage expansion (including coverage of pregnant women).

Availability of Federal SCHIP Funds: FY2006-FY2007

At the beginning of FY2006, a state could have had balances left in three original allotments — FY2004, FY2005, and the newly available FY2006 pots. These amounts calculated in the CRS model are identical to the balances published by CMS in the April 21, 2006, *Federal Register* notice. In addition, states projected to have inadequate federal funds from these three pots to cover their demand in FY2006 will also have access to funds from the redistribution of other states' unspent FY2003 original allotments, as well as from the DRA appropriation. These amounts as published in the April 21, 2006, *Federal Register* are used in the CRS model.

Based on these amounts and the projected demand for FY2006, the model draws down the available pots of money. Once that process is completed, the model calculates the amount of unspent FY2004 original allotment funds that will be redistributed and made available in FY2007. The balances that remain from the FY2005 and FY2006 original allotments, along with the new FY2004 redistribution and the FY2007 allotment, are available in FY2007.

Model Results

Current Law. Based on current law and assumptions about how funds will be allotted and redistributed, and given projected demand, the model identifies the states projected to deplete those funds in FY2006 and FY2007.

Table 2 shows the amount of DRA funds that 12 states are projected to spend in FY2006. Targeting these funds first to shortfall states that cover only children leaves the unspent FY2003 funds from other states able to go exclusively to the four shortfall states that cover adults. As a result, these states do not have any funds that they cannot spend due to the prohibition of spending on non-pregnant adults. However, the FY2003 funds available are inadequate to cover the shortfall in these four states, as previously discussed.

In FY2007, 18 states are projected to have inadequate balances in their FY2005, FY2006 and FY2007 original allotments to cover their demand for federal SCHIP funds. These states are projected to receive all of the unspent FY2004 original allotments from other states. However, the amount of these unspent funds is projected to be only $96 million. This would be the fifth year in a row in which the amount of unspent funds available for reallocation is smaller than any of the preceding years in which reallocations occurred (beginning in FY2001, with approximately $2 billion available for reallocation from states' unspent FY1998 original allotment). The shortfall among these 18 states in FY2007 is projected at $944 million, as shown in **Table 2**.

Table 2. Projected Final Distribution of DRA Funds and Projected Shortfalls of Federal SCHIP Funds, 2006 and 2007

(in millions of dollars)

State	DRA funds	2003 redistribution	Projected shortfalls	
	2006	2006	2006	2007
Alaska				$12.2
Georgia				$39.7
Illinois[a]	$56.2	$61.3	$0.98	$151.3
Iowa	$6.1			$28.0
Louisiana				$20.9
Maine				$0.9
Maryland	$13.7			$91.3
Massachusetts	$21.9			$101.4
Minnesota[a]	$7.1	$12.9	$0.21	$36.2
Mississippi	$73.6			$74.0
Missouri	$8.0			$45.6
Nebraska	$15.7			$12.2
New Jersey[a]	$50.5	$55.1	$0.88	$149.7
North Carolina	$2.8			$113.0
North Dakota				$5.6
Rhode Island[a]	$23.8	$42.3	$0.68	$46.6
South Dakota	$0.5			$6.7
Wisconsin				$8.6
Total[b]	$280.0	$171.6	$2.75	$943.7

Source: Congressional Research Service (CRS) SCHIP Projection Model and CRS analysis of data from the Centers for Medicare and Medicaid Services.

Notes: "DRA funds" refers to the $283 million for federal SCHIP funding appropriated in the Deficit Reduction Act of 2005 (P.L. 109-171).

a. States that cover non-pregnant adults.
b. Excludes projected DRA funds and shortfalls for territories.

Of the 18 states projected to exhaust their federal SCHIP funds in FY2007, four (Georgia, Minnesota, Mississippi, and North Carolina) appear to have no alternative for federal funds besides SCHIP. This is because their SCHIP programs are separate from Medicaid. In the other 14 states, some portion of the SCHIP federal funds could be paid by Medicaid, albeit at the regular FMAP instead of the enhanced rate, because these states have SCHIP programs that include, or are exclusively, a Medicaid expansion. The percentage of SCHIP expenditures that come from these states' SCHIP Medicaid expansions varies, from 10% (Illinois) to 98% (Nebraska), based on states' expenditure for FY2005.

Table 3 shows estimates of the net shortfall that would remain under current law after taking into account the federal Medicaid funds these states could draw for their Medicaid-expansion SCHIP programs. Column A of the table shows the same shortfalls as in **Table 2**. Column B provides estimates of the maximum amount of shortfalls payable by federal Medicaid funds. This was estimated by assuming states facing a shortfall would claim as much of its separate-SCHIP spending in its available SCHIP balances, maximizing the amount of shortfall funds for which Medicaid funding could be received. Under this assumption, and reflecting Medicaid's regular FMAP versus the SCHIP enhanced FMAP, column B shows that $350 million of the projected SCHIP shortfall in FY2007 could be covered by federal Medicaid funds. This would leave a net shortfall of approximately $600 million in FY2007.

Table 3. Projected Shortfalls Net of Potential Federal Medicaid Funding, FY2007

(in millions of dollars)

	A	B	C
Shortfall states	**Shortfall**	**Potential federal Medicaid funding**	**Net shortfall (A-B)**
Alaska	$12.2	$10.0	$2.2
Georgia	$39.7	$0.0	$39.7
Illinois	$151.3	$30.0	$121.3
Iowa	$28.0	$16.9	$11.1
Louisiana	$20.9	$18.5	$2.4
Maine	$0.9	$0.7	$0.1
Maryland	$91.3	$70.2	$21.1
Massachusetts	$101.4	$78.0	$23.4
Minnesota	$36.2	$0.0	$36.2
Mississippi	$74.0	$0.0	$74.0
Missouri	$45.6	$38.5	$7.2
Nebraska	$12.2	$10.0	$2.2
New Jersey	$149.7	$36.1	$113.6
North Carolina	$113.0	$0.0	$113.0
North Dakota	$5.6	$4.8	$0.8
Rhode Island	$46.6	$21.3	$25.3
South Dakota	$6.7	$5.7	$1.0
Wisconsin	$8.6	$7.1	$1.6
Total	$943.7	$347.6	$596.1

Source: Congressional Research Service (CRS) SCHIP Projection Model and CRS analysis of states' FY2005 SCHIP expenditures and FY2007 FMAP rates from the Centers for Medicare and Medicaid Services (CMS).

It must be noted that there is some uncertainty about the limitations of claiming the regular Medicaid FMAP to cover SCHIP expenditures in a shortfall situation. There is little federal guidance on the issue. The only sizeable shortfall was experienced by Rhode Island ($20 million) in FY2004. State officials had informed CRS that they were able to claim approximately 95% of their SCHIP expenditures under regular Medicaid. They stated that most of the individuals covered under their separate SCHIP program still qualified for the regular Medicaid FMAP. CRS has not been able to confirm how this can occur. If separate SCHIP spending can be funded by federal Medicaid dollars in lieu of available SCHIP balances, then the amounts payable by Medicaid could be much higher than shown in column B of **Table 3**.

President's Budget. The SCHIP proposal in the President's Budget is to reduce the period of availability of the FY2005 original allotment from three years to two.[14] There may be additional details that have not yet been announced, but the effect of reducing the period of availability of the FY2005 original allotment is the focus of this section.

As previously mentioned, the amount of unspent funds available for redistribution has been decreasing over the past several years, as shown in **Table 4**. Historically these funds have been able to forestall much of the federal SCHIP shortfalls that would otherwise have occurred. FY2005 was the last year in which the amount available for redistribution was adequate to cover states' shortfalls of federal SCHIP funds. Because the $173 million available for redistribution in FY2006 was inadequate to cover the projected shortfalls, Congress appropriated an additional $283 million to SCHIP. In FY2007, only $96 million is projected to be available for redistribution, far short of the amount needed to cover the shortfalls.

The CRS model projects that at the end of FY2007 there will be approximately $155 million in unspent FY2005 original allotments. Assuming current authorization rules continue, this would be the amount available for redistribution in FY2008. This would be the first time in several years in which the amount of unspent original allotments at the end of its applicable period exceeded that of the previous year. This is because the total original allotments for FY2005 ($4.1 billion) were markedly higher than in FY2004 ($3.2 billion), resulting in some additional monies remaining at the end of the FY2005 original allotment's period of availability.

The president's proposal would make states' unspent FY2005 original allotments available for redistribution at the beginning of FY2007 rather than at the beginning of FY2008. As a result, unspent FY2005 funds available for redistribution would total $1,142 million, shown in **Table 4**. Although the details of the plan have not been released, the CRS projections assume that only funds necessary to close states' FY2007 shortfalls ($944 million), plus the territories typical 1.05% of the total unspent funds ($12 million), would be used from the unspent FY2005 original allotments. Based on these assumptions, the president's proposal would eliminate the FY2007 shortfall, with states that had unspent FY2005 original allotments at the end of FY2006 retaining about 16% of those funds ($186 million). Column D of **Table 5**, on the last page of this report, shows the projected amount that states would have redistributed from their unspent FY2005 original allotments to other states as a result of the president's proposal. Column E of the table shows the percentage of the $956 million redistributed to other states and territories that each state contributes.[15]

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[14] The President's Budget does not provide this detailed of an explanation, but individuals in the executive branch have confirmed this description.

[15] These results are not intended to approximate a cost estimate, like those done by the White House's Office of Management and Budget (OMB) or the Congressional Budget Office (CBO). Budgetary cost estimates take into account offsets and other effects that these projections do not attempt to address.

Table 4. Annual Historical and Projected Reallocation Amounts, by Fiscal Year
(in millions of dollars)

Fiscal year	*Current-law reallocations*				*Additional reallocations due to President's Budget*			
	Fiscal year reallocated	**Total amount**	**Redist.**	**Retain**	**Fiscal year reallocated**	**Total amount**	**Redist.**	**Retain**
2001	1998	$2,034	$720	$1,313				
2002	1999	$2,819	$1,638	$1,181				
2003	2000	$2,199	$1,099	$1,099				
2004	2001	$1,749	$875	$875				
2005	2002	$643	$643	$0				
2006	2003	$173	$173	$0				
2007	2004	$96	$96	$0	2005	$1,142	$956	$186

Source: Congressional Research Service (CRS) SCHIP Projection Model and CRS analysis of data from the Centers for Medicare and Medicaid Services.

Notes: "Total amount" is the total amount of unspent original-allotment funds available for reallocation. It is the sum of the amounts redistributed to other states (and territories) and retained by states that keep a portion of their unspent original allotments. The redistributed amounts include the 1.05% of the "total amount" provided to the territories. FY2006 and FY2007amounts are projections.

Analysis and Options

SCHIP was created in BBA 97 as a capped grant program to states. Fixed annual balances of federal funds are available to states, which they can exhaust. This contrasts with SCHIP's older and much larger companion in providing health insurance to low-income individuals, Medicaid, which was created as an individual entitlement program that states cannot exhaust.[16]

Although it is theoretically possible for states to be in a chronic state of shortfall of federal SCHIP funds, this had been avoided through FY2005 using the funds in the program's original appropriation. To cover shortfalls projected for FY2006, Congress appropriated an additional $283 million. To cover the shortfalls in FY2007, an appropriation of approximately $1 billion would be required. Alternatively, Congress could alter redistributions to tap into other federal money available in SCHIP. The president's proposal appears to do this by shortening the period of availability of the FY2005 original allotment from three years to two years. This was also part of the SCHIP package in the first Senate-passed version of DRA (S. 1932), which was ultimately replaced by the $283 million appropriation targeted to FY2006 and therefore not addressing the FY2007 projected shortfall.

Redistribution and appropriation are two alternatives if the policy goal is to ensure that states never exhaust their federal balances of SCHIP funds. In addition, the SCHIP program could be turned into an open-ended entitlement, perhaps by folding it into the Medicaid program. This would spare the administration and

[16] States have to provide matching funds, though, since Medicaid is a joint federal-state program.

Congress from having to periodically rearrange funds or funding methodologies to cover shortfalls. However, states would likely oppose folding SCHIP into Medicaid if it meant reverting to the regular FMAP and following all of Medicaid's other more restrictive rules. Federal policymakers may oppose this because they believe SCHIP as an individual entitlement could result in greater federal outlays than would occur under SCHIP as a capped grant program.

Although the SCHIP program has been successful in covering millions of uninsured children, and has therefore been politically popular, more states are poised to exhaust their federal SCHIP funds as early as next fiscal year. If Congress decides to prevent these shortfalls, legislative action will be needed. If, however, Congress decides that the intent of the original legislation was to ensure that states did not treat the program as an open-ended entitlement, no action will be necessary through the end of the program's authorization, as many states with annual SCHIP spending well in excess of their annual allotments face the consequences of that spending through the shortfall of federal funds.

Table 5. Characteristics of States Projected to Have Funds Redistributed Under President's SCHIP Proposal, FY2007

	A	B	C	D	E
State	**Demand for federal SCHIP funds**	**Current-law beginning-of-year balances**	**Beginning-of-year balances under president's proposal**	**FY2005 funds redistributed under president's proposal (B-C)**	**State's portion of total FY2005 redistributed funds under president's proposal**
Arkansas	$51.2	$132.5	$103.5	$29.0	3.0%
Colorado	$53.4	$173.0	$136.6	$36.4	3.8%
Connecticut	$18.0	$113.7	$83.1	$30.6	3.2%
Delaware	$8.2	$29.3	$21.7	$7.6	0.8%
DC	$8.2	$29.7	$22.7	$7.0	0.7%
Florida	$373.9	$585.8	$561.8	$24.0	2.5%
Hawaii	$13.4	$32.8	$28.5	$4.2	0.4%
Idaho	$31.5	$57.0	$47.8	$9.2	1.0%
Indiana	$89.3	$201.4	$169.4	$32.0	3.4%
Kentucky	$78.5	$144.3	$131.6	$12.8	1.3%
Montana	$15.8	$33.5	$28.9	$4.5	0.5%
Nevada	$31.2	$134.0	$100.2	$33.8	3.5%
New Hampshire	$9.4	$29.2	$22.0	$7.3	0.8%
New Mexico	$42.7	$134.9	$100.8	$34.1	3.6%
New York	$411.1	$700.4	$623.7	$76.7	8.0%
Oklahoma	$69.9	$141.5	$130.4	$11.1	1.2%
Oregon	$30.0	$152.0	$112.5	$39.6	4.1%
Pennsylvania	$168.9	$343.8	$306.8	$36.9	3.9%
South Carolina	$62.4	$148.8	$128.1	$20.6	2.2%
Tennessee	$3.9	$258.6	$192.5	$66.0	6.9%
Texas	$409.0	$1,431.5	$1,082.9	$347.7	36.4%
Utah	$39.2	$85.5	$74.2	$11.4	1.2%
Vermont	$2.9	$15.7	$11.6	$4.1	0.4%
Virginia	$106.4	$170.8	$163.1	$7.7	0.8%
Washington	$39.5	$209.3	$155.1	$54.2	5.7%
West Virginia	$41.2	$56.4	$52.9	$3.6	0.4%
Wyoming	$8.0	$17.5	$13.9	$3.7	0.4%
Total	$2,217.0	$5,563.0	$4,607.4	$955.6	100.0%

Source: Congressional Research Service (CRS) SCHIP Projection Model and CRS analysis of data from the Centers for Medicare and Medicaid Services.

Notes: The impact modeled is that the period of availability of the FY2005 original allotment will be reduced from three years to two. It is assumed that the FY2005 funds unspent as the end of FY2006 will be redistributed as necessary to meet states' shortfalls, as well as 1.05% of the unspent total going to the territories. These results are not intended to approximate a cost estimate, like those done by the White House's Office of Management and Budget (OMB) or the Congressional Budget Office (CBO). Budgetary cost estimates take into account offsets and other effects that these projections do not attempt to address.